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Use of Parallel Currencies

The phrase “parallel currencies” tends to sound rather novel and experimental to us today, living in the United States. However, most people in the world are using parallel currencies today. Many of us have found that, when traveling to some foreign countries, that shops and restaurants are happy to accept U.S. dollars in return for their goods and services. Often, people there also use U.S. dollars among themselves, in their own commerce and business dealings. In this case, the U.S. dollar is serving as a parallel currency, alongside the currency issued by the domestic government, such as Costa Rican colón or Vietnamese dong.

In such places, the U.S. dollar is used not only by sidewalk vendors, but often by the largest corporations in the country. Throughout Latin America, until only a few years ago, large corporations would typically finance their operations with loans or debt denominated in U.S. dollars. Indeed, the governments of these countries themselves borrowed in dollars, issuing dollar-denominated government bonds. After many decades of bad experience, nobody would buy a bond denominated in the local currency, which the government could devalue at a whim. Before the introduction of the Euro in 1999, German marks were popular throughout Europe. During the 1990s, governments with a history of poor currency management, such as that of Greece, issued government debt denominated in German marks.

It is perhaps only in the United States, and more recently in the eurozone, that people are not already accustomed to using a variety of currencies in their daily business and commerce. Large U.S. corporations regularly do business in a variety of currencies, and investors commonly buy or sell foreign stocks or bonds using foreign currencies. For most of us, however, we have no reason to use the Ukrainian hryvna in our daily affairs. We would much rather use dollars.

Ukrainians, at some points in their history, have also preferred to use U.S. dollars. Why is that? It is because the dollar has consistently been one of the best-managed, highest-quality currencies in the world. For 182 years, from the founding of the United States in 1789 to 1971, the United States government adhered to the principle of a gold standard for the dollar, even if, in practice, it deviated from that ideal from time to time. The United States was following the example demonstrated by the best European governments, especially Britain, whose gold standard system can be traced to 1698.

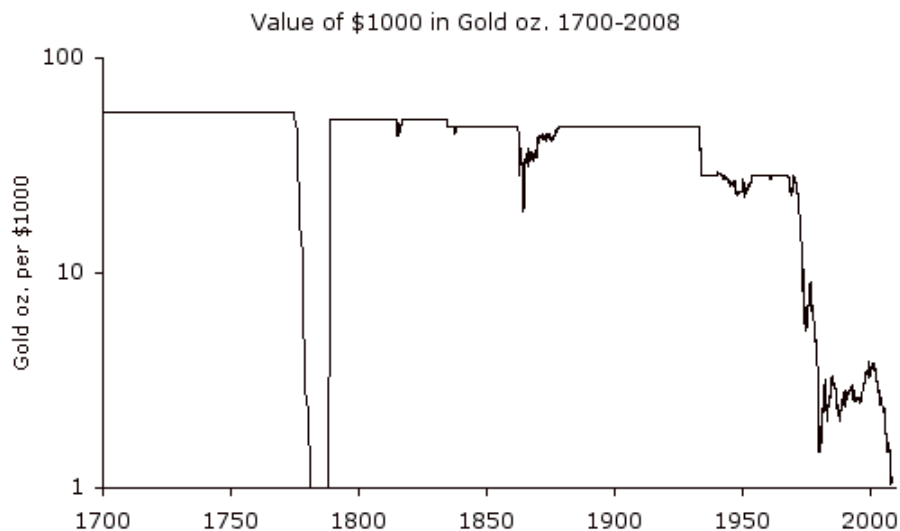
However, during the 20th century, those European governments made a mess of things numerous times, and their currencies became unreliable. The British pound, like most of the currencies of Europe, became a floating currency at the onset of World War I, and soon depreciated in value. People didn't even know if France or Britain would exist after the war.

In the early 1920s, more European currencies became unreliable, with the hyperinflation of the German mark perhaps the best remembered example. By 1926, Europe had mostly reconstructed the world gold standard system that existed before the war, just in time for the chaos of the Great Depression. During the Great Depression, currencies everywhere were devalued, led by Britain in 1931. Also, we tend to forget today that several European governments also defaulted on their sovereign debt during the 1930s, including Austria, Germany, Greece, Hungary, Poland, Romania and Turkey.

By the end of World War II, the U.S. dollar, which had been considered an emerging-market currency in 1900, had proved to be the most reliable currency in the world. It thus became the parallel currency of choice worldwide, and U.S. tourists in the 1950s found that they could spend their dollars throughout Europe. The British pound still had some fans, but after a devaluation in 1949 and again in 1967, few people were willing to give Britain any more chances.

In 1971, the United States abandoned its then nearly two-century-old commitment to the gold standard system. At this point, historically, currencies were often discarded for whatever the highest-quality, most reliable alternative was, which in practice meant a gold standard currency from a large developed country. However, a consequence of the U.S.'s abandonment of the gold standard in 1971, due to the nature of the Bretton Woods system, was that other governments' currencies left gold too. There was no gold standard alternative in the world.

Since 1971, the value of the U.S. dollar has fallen from 1/35th of an ounce of gold to about 1/1600th of an ounce today. The dollar today is worth only 1/46th of its value during the Kennedy administration. As bad as this is, the alternatives have been even worse. This is why the U.S. dollar remains the most popular currency in the world, and serves as a parallel currency in many, if not most, countries today.



After several centuries of stability, the dollar became a floating fiat currency in 1971. Since then, it has fallen to about 1/46th of its prior value. The decline in the 1780s represents the hyperinflation of the Continental dollar.

Use of parallel currencies in the U.S. today

Today, there are no particularly onerous barriers against using a parallel currency in the United States. People are free to do business in euros or Russian rubles if they choose to. It would be easier if there were no tax consequences from this, such as a capital gains tax. This is the case in Switzerland or Hong Kong, where people can do business in the currency of their choice without tax issues. At least one country, Zimbabwe, has no official currency, but rather a formal multi-currency policy where people can do business using any currency the like. In practice, this has turned out to be primarily U.S. dollars, with some use of South African rands.

Historically the preferred currency of business, in any country, is one based on a gold standard system. British pounds, and later U.S. dollars, became the preferred parallel currency throughout the world for this reason. It was the currency people chose to use instead of their own government's fiat junk.

Some people today, including myself, think that the United States should return to the monetary principles of the country's first 182 years – in other words, a gold standard system. However, that idea remains contentious, particularly among those who believe that a currency should be used as a tool for economic manipulation. Our present chief currency manager, Benjamin Bernanke, spent his academic career arguing for the merits of economic manipulation via currency manipulation. A gold standard system would prevent such things.

However, even among academics who share Mr. Bernanke's viewpoints, the idea of letting people choose whatever currency suits them best remains a popular one. The concept of parallel currencies, including those based on gold, within the United States seems to be relatively uncontroversial among the economic mainstream.

Today, there are over 150 currencies in the world, all of which could conceivably be used as parallel currencies within the United States or other countries. However, all of them are floating fiat currencies, generally of lower quality than the U.S. dollar or euro. There is hardly any reason to introduce another. Thus, the most meaningful new parallel currency to be introduced, in the U.S. or in another country, would be one based on gold.

Difficulties of using gold- and silver-based parallel currencies in the U.S. today

Although the use of other countries' national currencies is largely accepted in the U.S., the issuance of alternative currencies within the U.S. can run afoul of what are collectively known as "legal tender laws," both *de jure* and *de facto*. Beginning in 1998, a private businessman, Bernard von NotHaus, issued a system of coinage and paper bills called Liberty Dollars that represented warehouse receipts for gold and silver bullion. The notes and coins bore no resemblance Federal Reserve Notes or U.S. Mint coins. About 250,000 people apparently participated in the system. Although other alternative currencies have existed, such as "Phoenix dollars," Baltimore's "BNote," "BerkShares," "Ithaca Hours," and "bitcoin," this was apparently the only such system based on gold and silver.



Liberty Dollar notes and coins.

In 2006, the U.S. Mint issued a press release stating that the U.S. Justice Department had determined that using Liberty Dollars was a Federal crime. The press release stated:

Under 18 U.S.C. § 486, it is a Federal crime to pass, or attempt to pass, any coins of gold or silver intended for use as current money except as authorized by law. ...

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. § 486, and is a crime.

In 2007, the Federal Bureau of Investigation (FBI) raided the warehouse used by the Liberty Dollar system at the Sunshine Mint in Coeur D'Alene, Idaho, confiscating a reported \$7 million of gold and silver bullion. The seizure warrant was for money laundering, mail fraud, wire fraud, counterfeiting, and conspiracy.

In 2009, von NotHaus was arrested and charged with: one count of conspiracy to possess and sell coins in resemblance and similitude of coins of a denomination higher than five cents, and silver coins in resemblance of genuine coins of the United States in denominations of five dollars and greater, in violation of 18 U.S.C. § 485, 18 U.S.C. § 486, and 18 U.S.C. § 371; one count of mail fraud in violation of 18 U.S.C. § 1341 and 18 U.S.C. § 2; one count of selling, and possessing with intent to defraud, coins of resemblance and similitude of United States coins in denominations of five cents and higher, in violation of 18 U.S.C. § 485 and 18 U.S.C. § 2; and one count of uttering, passing, and attempting to utter and pass, silver coins in resemblance of genuine U.S. coins in denominations of five dollars or greater, in violation of 18 U.S.C. § 486 and 18 U.S.C. § 2.

In 2011, von NotHaus was convicted on several counts, and faced up to 15 years of jail time. In 2011, von NotHaus was labeled a domestic terrorist by the FBI.

Conceivably, people today could do business using gold coins produced by the U.S. Mint, such as the popular American Eagle gold and silver coins. However, they too would face unusual difficulties. Despite its long history as the foundation of monetary systems in the United States and elsewhere, gold today is regarded as a "collectible," and subject to a different system of taxation than if one were to do a similar transaction using foreign currencies such as euros or Canadian dollars. The capital gains tax rate on "collectibles" held for one year or longer is 28%, compared to 15% for stocks and bonds.

For example, if a house were purchased using U.S. Mint gold coins, the transfer of the coins to the seller would be regarded as a "sale" of gold bullion for tax purposes, and subject to capital gains taxes. If the same transaction were done with euros, no such taxes would

apply. (Capital gains taxes would apply to the eventual sale of the house, and if the euros were converted back to dollars.)

In addition, purchases or sales of small quantities of gold are subject to sales taxes in many states. California, for example, charges sales tax on bullion sales of less than \$1,500. Thus, a businessman who wished to pay employees using a 1/10th ounce U.S. Mint gold bullion coin, or one-ounce U.S. Mint silver coins, may face sales taxes on his “sale” of the bullion coins to the employee. (No such sales taxes apply to purchases of euros.)

Also, transactions in gold bullion are now subject to onerous surveillance, which does not apply to similar transactions in foreign currencies. To give an idea of the present state of affairs, here is some information from bullion dealer metallixdirectgold.com:

4. COMPLIANCE WITH GOVERNMENT AGENCIES; RECORDED CONVERSATIONS.

A. Documentation for Payment. Several states require that we obtain your driver’s license number or other government-issued identification and a sworn statement from You as to the Merchandise and compliance with applicable law before we process any payment to You. Certain localities require completion of forms and a waiting period for a transaction in precious metal. If merchandise contains by weight or volume 50% or more of precious metal and is valued at more than \$3,000, federal anti-money laundering laws obligate us to obtain certain completed forms and identity information from you before we process the transaction (such local, state and federal documentation, “Compliance Documents”). You agree to supply such Compliance Documents to us upon our request. . If You fail to provide such Compliance Documents to us within 5 Business Days after the date of our notice to You requesting such information, we have the option to terminate the proposed Transaction and return your Merchandise in the form in which You furnished it to us or in a different form in accordance with this Agreement without providing You with additional notices.

Thus, in practice, the U.S. Federal Government makes a powerful effort to suppress the introduction and use of alternative gold- and silver-based currencies today.

This state of affairs has become intolerable to many. In 2011, the State of Utah declared that it would consider U.S. Mint gold and silver coins (and monetary instruments based on these coins) to be legal as currency. This included the removal of all state-level taxes on transactions in gold and silver bullion. The Utah example has been widely followed. Twelve other state legislatures have had similar bills proposed¹. The Utah example could serve as a

¹ South Carolina, North Carolina, Alabama, Virginia, Tennessee, Missouri, Idaho, California, Colorado, Washington, Indiana and Minnesota.

template for similar Federal-level legislation to legalize gold and silver (and associated monetary instruments) as currency within the United States.

Parallel Currencies Issued by National and State Governments

In the last decade, some governments have taken steps to introduce gold-based parallel currencies, intended to circulate alongside their existing currencies, and to be used internationally.

In 2002, the prime minister of Malaysia proposed the introduction of a gold dinar currency, for use throughout the Islamic world. In 2006, gold dinar coins (containing 4.25 grams of gold) were introduced by the government of the Malaysian state of Kelantan. This was followed by the state of Perak in 2011. The coins have been quite popular. However, the effort to create a usable international currency based on the gold dinar has been hindered, in my opinion, by the fact that small denomination banknotes and coins have not yet been issued. Gold coins are much too valuable (have a high denomination) to be useful in small daily transactions by themselves. Also, banking arrangements based on the new currency have apparently not been established yet.



Malaysian gold dinar and silver dirham coins, produced by the state of Kelantan. In 2002, the prime minister of Malaysia stated the intent to create a gold dinar system to serve the entire Islamic world.

In 2011, the Swiss Parliament began discussions on the creation of a gold franc, which would be issued by the Swiss national government and circulate in parallel with the existing Swiss franc, a floating fiat currency. The initiative is part of the “Healthy Currency” campaign sponsored by the conservative Swiss People’s Party.

Governments of the Gulf States have discussed a common currency tentatively named the khaleeji, which some have speculated would be based on gold. In August 2011, the Dubai Multi Commodities Center introduced a gold coin, called the khalifa, intended to serve as legal currency. The DMCC is in talks with the central bank of the UAE to designate the coin as legal tender throughout the UAE and Middle East.



Proposed khalifa coin, intended to serve as legal currency in the Gulf States region.

What if the U.S. Federal government itself issued a parallel currency, in particular one based on a gold standard system? It could be quite popular both in the U.S. and abroad. The U.S. Federal government already has a long history of this. From 1882 to 1933, the Federal government issued gold certificates – a form of banknote, or paper money, redeemable for gold bullion – that constituted a major part of the U.S. currency system. During that time, both U.S. Treasury gold certificates and National Bank Notes issued by a menagerie of private banks circulated alongside. The gold certificates were more popular, due to their uniformity and the fact that people trusted the reliability of the Federal government far more than the small commercial banks of the day. In 1914, gold certificates accounted for 32% of circulating currency in the United States.



U.S. Treasury Gold Certificate, series 1922. These gold certificates circulated alongside many other types of banknotes, including Federal Reserve Notes and National Bank Notes. People were free to choose which banknote they preferred.

If the Federal government does not wish to undertake such a program, a state government, such as the State of Utah, could conceivably issue its own parallel currency.

Historically, before 1971, there was little reason for national governments to issue their own parallel currencies, because their primary currencies were already operating on a gold standard system. However, there is at least one example: in 1922, the Russian government introduced the gold-based chervonets currency, to circulate alongside the ruble, which at the time was a floating fiat currency. By 1947, the ruble itself had been pegged to gold, thus negating any need for a parallel gold-based currency. Thus, the chervonets was retired.



1937 Russian gold chervonets banknote. The chervonets was introduced by the Russian national government as a parallel currency to the floating fiat ruble in 1922.

A similar example comes from Germany. In November of 1923, a new currency based on gold, the rentenmark, was introduced to replace the hyperinflated Reichsmark. For a short period, the two currencies circulated alongside, the rentenmark pegged to gold and the reichsmark continuing its plunge into oblivion. The rentenmark was quickly adopted by all, and the Reichsmark in effect disappeared from circulation.



German rentenmark banknote. The rentenmark was introduced by the nationally-sanctioned Rentenbank as a gold-based parallel currency, at first circulating alongside the hyperinflated reichsmark.

Gold and silver have reportedly been declared legal currency in China, and major state-owned commercial banks there now offer gold- and silver-denominated bank accounts.²

Significance of gold-based parallel currencies today

The discussion today around parallel currencies is part of a broader discussion: whether to have a currency that can be manipulated for economic effect, or to have a currency which is as stable and reliable as possible, free of human intervention. Traditionally, these have been known as “soft money” and “hard money,” and, in practice, have meant either a floating fiat currency, or a gold standard system. The two options are, for the most part, mutually exclusive: it is not possible to have a gold standard system and a policy of monetary manipulation together for any length of time.

Both options have been used, by one government or another, for literally thousands of years. We have a lot of experience in these matters. For the entire post-medieval history of capitalism -- stretching from the Italian city-states of the Renaissance era, through the heyday of Amsterdam as the world’s financial center in the 17th century, through the entire history of the Industrial Revolution with London as the world’s financial center in the 19th century, into the 20th century with the U.S. as the leader of the capitalist world – a gold standard system was the preferred monetary foundation.

The worldwide transition to floating fiat currencies, or “soft money,” in 1971 reflected the increasing popularity of currency manipulation ideas beginning in the 1930s. However, it also reflected simple incompetence. It was an accident. In 1971, the Bretton Woods gold standard system had delivered twenty years that were among the most prosperous in

² See for example: <http://businesstimes.com.vn/chinas-banks-use-gold-as-legal-currency/>

world history. There was no reason to change it. President Nixon himself said that the end of the gold standard in August 1971 would be temporary. Indeed, he tried to reinstate it with the Smithsonian Agreement in December 1971, which he called “the most significant monetary agreement in the world.”

Thus, it is not surprising today that we are again trying to find a way back to the world gold standard system, which worked so well for literally centuries.

Rather than endlessly debating the merits of one system or another, a simpler method is to make both options available, and allow people to choose which they prefer. Just as people in Turkey today choose to do business either in the Turkish lira or euros, as suits their needs, people in the U.S. or elsewhere could choose to do business either in floating fiat dollars or some gold-based alternative.

According to a study of 775 floating fiat currencies by Michael Hewitt³, no floating fiat currency has ever maintained its value. In 20% of cases, they were destroyed in hyperinflation; 21% were destroyed by war; 12% disappeared in independence; 24% underwent a monetary reform; and 23% exist today, awaiting their final outcome. The average life expectancy of a floating fiat currency was found to be 27 years.

The U.S. dollar, which has been a floating fiat currency for 41 years now, is thus an unusual example of longevity. However, today’s extreme reliance upon “easy money” approaches to deal with economic problems – with the Federal Reserve promising unprecedented zero percent policy rates for years, and “real” interest rates deeply negative – suggests to many that the floating fiat dollar does not have a long or successful future. Unfortunately, with world currency arrangements still very dollar-centric, the management of the dollar has consequences for everyone. Governments of China, Russia, the Gulf States and others have complained about the potential consequences of today’s aggressive “soft money” techniques -- not only at the Federal Reserve but also the European Central Bank, Bank of England, and Bank of Japan -- and have made preliminary steps toward a future alternative.

³ Hewitt, Michael. “The Fate of Paper Money,” dollardaze.org, January 7, 2009.
http://dollardaze.org/blog/?post_id=00405



At a G8 meeting in July 2009, Russian President Dmitry Medvedev illustrated his call for a supranational currency to replace the dollar with a coin that he called a sample of a “united future world currency.” The coin is half-ounce gold bullion coin. Such a “supranational currency” would be, in effect, a parallel currency, used alongside national currencies.



*The coin held by President Medvedev.
source: futureworldcurrency.com*

On the international scale, a parallel gold-based currency, or many such currencies, would help ease this transition, and form the basis of a new monetary order if that should become necessary. Each individual would be free to make increasing use of the gold-based alternative, as it best suited their interests. There would be no great day of transition, but a smooth extended process perhaps over years. The existence of a high-quality alternative could help people avoid much of the potentially disastrous consequences if today’s floating fiat currencies meet the same end as the 599 floating currencies that no longer exist.

If the United States government wishes to retain its leadership role in world monetary affairs, I suggest that this alternative be created in the United States – either by federal or state governments themselves, or by allowing private institutions to do so. Otherwise, governments that are clearly establishing the foundation for a future dollar alternative, likely based on gold, will take that role in the future.