# A Golden Currency Board

**Until early in the 20th century, gold played a central role in the world of money. Gold had an incredible run – almost three thousand years. And why not? After all, Professor Roy Jastram convincingly documents in The Golden Constant just how gold maintains its purchasing power over long periods of time.**

But, since President Richard Nixon closed the gold window in August 1971, gold has not played a formal role in the international monetary regime. Today, the "regime" is characterized by many as a chaotic non-system.

In the past decade, gold prices have surged and there have been noises in some quarters that gold's formal role should be re-established in the sphere of international money. In 1997, Nobelist Robert Mundell went so far as to predict that "Gold will be part of the structure of the international monetary system in the twenty-first century." Today, there are many proposals to re-introduce gold into the world of money, including a Swiss parliamentary initiative (11.407 "Establishing a Gold Franc").

### Automatic Currency Boards

One foolproof way to transform Professor Mundell's prediction into a reality is via gold-based currency boards. Currency boards have existed in more than 70 countries and a number are still in operation today. Countries with such monetary institutions have experienced more fiscal discipline, superior price stability, and higher growth rates than comparable countries with central banks.

An orthodox currency board is a monetary institution that only issues notes and coins. These monetary liabilities are freely convertible into a reserve currency (also called the anchor currency) at a fixed rate on demand. The reserve currency is a convertible foreign currency or a commodity chosen for its expected stability. For reserves, such a currency board holds low-risk, interest-earning securities and other assets payable in the reserve currency.

By law, a currency board is required to maintain a fixed exchange rate with the reserve currency and hold foreign reserves equal to 100 percent of the monetary base. This prevents the currency board from increasing or decreasing the monetary base at its own discretion. Nor does a typical currency board influence the relationship between the monetary base and the money supply by imposing reserve ratios or otherwise regulating commercial banks. An orthodox currency board system is passive and is characterized by automaticity.

In the past, currency boards have issued monetary liabilities that were fully backed by gold and were fully convertible into gold at a fixed rate on demand. The following abridged gold-based currency board law is presented to indicate how a modern, independent, gold-based currency board could be established and would operate (the full version is available in Hanke 2012). As drafted, the law would allow for the creation of a government-owned entity. But, with slight amendments, the draft law could support the establishment of a purely private currency board.

### A Gold-Based Currency Board Law

1. The Currency Board of Country *X* ("the Board") is hereby created. The purpose of the Board is to issue notes and coins denominated in a gold currency unit, and to hold foreign reserves sufficient to maintain them fully convertible at a fixed exchange rate into gold.
2. The Board shall have its legal seat in Switzerland and shall be subject to the laws of Switzerland.
3. The notes and coins issued by the Board shall be fully convertible into gold on demand. The Board shall charge no commission for exchanging its currency into or out of gold. The notes shall be printed outside Country *X*.
4a. The Board may not increase its monetary liabilities without gold or foreign reserves equal to 100 percent of the amount of the increase.
4b. The Board shall hold its reserves in gold or in highly rated and liquid securities either denominated in gold or fully hedged against changes in the fiat-currency price of gold. These reserves shall be on deposit at the Bank for International Settlements or at an internationally certified gold warehouse.
5. The Board shall remit to the Government of Country *X* all net seigniorage beyond that necessary to maintain 110 percent foreign reserves.
6. The Board may not perform banking services for the Government of Country X, and it shall not be responsible for the financial obligations of the government.
7. Failure to maintain the fixed exchange rate with gold shall make the Board and its directors subject to legal action for breach of contract according to the laws of Switzerland. This provision does not apply to attempts to redeem embezzled, mutilated, or counterfeited notes, coins, and deposits.
8. Existing laws that conflict with this law are void.
9. This law takes effect immediately upon publication.


**References**

- Steve H. Hanke. "A Gold-Based Currency Board, Please," *Globe Asia*, May 2012. http://www.cato.org/publications/commentary/goldbased-currency-board-please.
- Steve H. Hanke. "Currency Boards," *Annals of the American Academy of Political and Social Science*, Vol. 579, January 2002. http://www.cato.org/pubs/articles/hanke_annals.pdf.


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