I. The Problem

John Maynard Keynes once stated that "There is no subtler, no surer means of overturning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million is able to diagnose." Such a situation is exactly what faces this country today, as the Federal Reserve seems hell-bent on destroying what little purchasing power remains of the U.S. Dollar.

Money is what allows civilization to flourish. Without money, consumers must barter their goods, hoping to exchange their products for those produced by others, and relying on a double coincidence of wants. Money enables man to rise above barter and makes exchange less burdensome. Once money comes into existence, businessmen can calculate profit and loss, homemakers can compare prices among different grocery stores, and individuals can begin to save and invest.

Money as a medium of exchange should always satisfy certain properties. It should be durable, not wearing out easily; it should be portable, easily carried; it should be divisible into units usable for everyday transactions; it should be recognizable and uniform, so that one unit of money has the same properties as every other unit; it should be scarce, in the economic sense, so that the extant supply does not satisfy the wants of everyone demanding it; it should be reproducible, so that enough units of money can be created to satisfy the needs of exchange; and most importantly, it should be stable, so that the value of its purchasing power does not fluctuate wildly.

Unfortunately, monetary developments over the past century have eroded the stability of the monetary unit. The roots of this instability date back to the mid-19th century, when the government sought to establish a monopoly on the issuance of money. Until that time, gold and silver from numerous countries and private mints circulated as money. At this country's founding, there was no government-controlled national currency. While the Constitution established the Congressional power of minting coins, it was not until 1792 that the US Mint was formally established. In the meantime, Americans made do with foreign gold and silver coins such as the silver Spanish milled dollar, which was understood at the time of the Constitution's drafting to be the basis of our dollar system. Even after the Mint's operations got underway, foreign coins continued to circulate within the United States and did so for many decades. Since the dollar was variously defined as a specific weight of silver (or gold) it was relatively easy to determine the value of non-U.S. currency in dollars. Perhaps more importantly, the Coinage Act of 1792 ensured that the purchasing power of United States currency would remain stable, as debasement of the currency was punishable by death.

As with most monetary malfeasance throughout history, the United States government's drive to monopolize the issuance of money came about during a time of war. In order to fund its military operations during the 1860s, the federal government for the first time in its history issued paper currency which was unbacked by any commodity and was to be accepted at face value as a legal tender. These “greenbacks” quickly declined in value against gold-backed notes, and the government undertook numerous measures to eliminate competition and ensure that individuals would have to accept greenbacks. While some measures, such as banning futures trading in gold, were quickly repealed, other laws that banned the private minting of coinage remain in force today.

Since that time, the government slowly but surely tightened its grip over the issuance of money in this country. Resumption of gold redemption led to gradual acceptance of the federal government's paper currency, and then to Federal Reserve Notes. Once paper currency drove gold out of everyday use, the government was the able to ban private ownership of gold in the 1930s. Eventually the gold window for foreign governments was closed in 1971, thus severing once and for all any link between the dollar and gold. For the past 40 years we have lived in a world in which the issuance of money is completely at the discretion of governments and central banks, and we are reaping the consequences. The fiat money standard has led from one financial crisis to another, as each attempt to inflate out of the previous bubble only sows the seeds for the next crash. Real wages remain stagnant or decrease, while price increases resulting from inflation of the money supply force American households to go ever deeper into debt in order to maintain a constant standard of living.

Economics teaches that monopolies produce fewer goods and sell them at a greater price than in a competitive market. This leads to inefficiency, deadweight losses, and over time complacency on the part of the monopolist. Most mainstream economists fail to extend the theory of monopoly to the market for money. Government monopolization of the issuance of money fails to produce the sound money the market demands. The poor-quality money that is issued continues to lose its value, and the American people must work longer and harder for money that continues to decline in purchasing power. Meanwhile, government agencies and the banking system benefit from the first use of that money, being able to spend it and lend it before it circulates through the rest of the economy and before prices increase in reaction to this inflation.

The only way to counteract this problem is to break the government monopoly on the issuance of money. The Constitution does not grant the federal government this monopoly, a fact which was not in dispute for nearly a century after this country's founding. The federal government has become complacent, forgetting the need for sound money, and the only way to break this complacency is to break the monopoly. HR 1098, the Free Competition in Currency Act, intends to do just that.

II. The Solution

Over millennia of human history, gold and silver have been the two metals that have most often satisfied the market's demand for money and gained the trust of billions of people. Gold and silver are difficult to counterfeit, a property which ensures they will always be accepted in commerce. It is precisely for this reason that gold and silver are anathema to governments. A supply of gold and silver that is limited in supply by nature cannot be inflated, and thus serves as a check on the growth of government. Without the ability to inflate the currency, governments find themselves constrained in their actions, unable to fund either the welfare state or the warfare state.

On the desk in my office I have a sign that says: “Don't steal – the government hates competition.” Indeed, any power a government arrogates to itself, it is loathe to give back to the people. The history of this nation is filled with examples of increasing and unconstitutional centralization of power by the federal government. Militias, letters of marque and reprisal, and declarations of war have gone by the wayside; the postal monopoly drove out private competition; and a market-driven system of competing currencies was suppressed by the creation of a government-supported banking cartel that monopolizes the issuance of currency. In order to return to sound money, it is necessary to undo the legal obstacles that forbid other currencies from competing against the dollar.

The first step consists of eliminating legal tender laws. Article I, Section 10 of the Constitution forbids the States from making anything but gold and silver a legal tender in payment of debts. States are not required to enact legal tender laws, but should they choose to, the only acceptable legal tender is gold and silver, the two precious metals that individuals throughout history and across cultures have used as currency. There is nothing in the Constitution that grants Congress the power to enact legal tender laws. Congress has the power to coin money, regulate the value thereof, and of foreign coin, but not to declare a legal tender. Yet, there is a section of US Code, 31 USC 5103, that purports to establish US coins and currency, including Federal Reserve notes, as legal tender.

Historically, legal tender laws have been used by governments to force their citizens to accept debased and devalued currency. Gresham's Law describes this phenomenon, which can be summed up in one phrase: bad money drives out good money. An emperor, a king, or a dictator might mint coins with half an ounce of gold and force merchants, under pain of death, to accept them as though they contained one ounce of gold. Each ounce of the king's gold could now be minted into two coins instead of one, so the king now had twice as much “money” to spend on building castles and raising armies. As these legally overvalued coins circulated, the coins containing the full ounce of gold would be pulled out of circulation and hoarded. This same phenomenon occurred in the United States in the mid-1960s when the US government began to mint subsidiary coinage out of copper and nickel rather than silver. The copper and nickel coins were legally overvalued, the silver coins undervalued in relation, and silver coins vanished from circulation.

These actions also give rise to the most pernicious effects of inflation. Once the public realized that the king debased his currency by 50%, prices would eventually double, as it would now take two coins to purchase what used to require only one. The king who debased his currency spent his new money immediately, before prices rose, and thus gained the benefit of that new money. Most of the merchants and peasants who received the devalued currency felt the full effects of inflation, the rise in prices and the lowered standard of living, before they received any of the new currency. By the time they received the new currency, they had long since had to suffer doubled prices, and the new currency they received would give them no benefit. In the absence of legal tender laws, Gresham's Law no longer holds. If people are free to reject debased currency, and instead demand sound money, sound money will gradually return to use in society.

The second step to legalizing currency competition is to eliminate laws that prohibit the operation of private mints. One private enterprise which attempted to popularize the use of precious metal coins was Liberty Services, the creators of the Liberty Dollar. The government felt threatened by the Liberty Dollar, as Liberty Services had all their precious metal coins seized by the FBI and Secret Service in November of 2007.

The sections of US Code which Liberty Services is accused of violating are categorized as anti-counterfeiting statutes, when in fact their purpose was to shut down private mints that had been operating in California. California was awash in gold in the aftermath of the 1849 gold rush, yet had no US Mint to mint coinage. Even establishment of a US Assay Office failed to provide enough coinage, as the only coins they produced were too large to be used in everyday transactions. Foreign coins filled the void, but even still there was insufficient coinage, and these coins circulated at a value higher than their inherent metal value. The public clamored for smaller denominations of coins, and private mints stepped into the breech to fulfill this demand. The private mints were eventually accused of circulating debased coinage, and with the supposed aim of providing government-sanctioned regulation and a government guarantee of purity, federal laws were enacted which banned private mints from producing their own coins for circulation as currency.

The final step to reestablishing competition in currency is to eliminate capital gains and sales taxes on gold and silver coins. Under current federal law, coins are considered collectibles, and are liable for capital gains taxes. Coins held for less than one year are taxed at the short-term capital gains rate, which is the normal income tax rate, while coins held for more than a year are taxed at the collectibles rate of 28 percent. These taxes on coins actually tax monetary debasement. The purchasing power of gold remains relatively constant, but as the nominal dollar value of gold increases due to the weakening of the dollar by the Federal Reserve, the federal government considers this to be an increase in wealth, and taxes accordingly. Thus, the more the dollar is debased, the more capital gains taxes must be paid on holdings of gold and other precious metals.

Just as pernicious are the sales and use taxes which are assessed on gold and silver at the state level in many states. Imagine having to pay sales tax at the bank every time you change a $10 bill for a roll of quarters to do laundry. Inflation is a pernicious tax on the value of money, but even the official numbers, which are massaged downwards, are only on the order of 3-4% per year. Sales taxes in many states can take away 8% or more on every single transaction in which consumers wish to convert their Federal Reserve Notes into gold or silver coins. Americans should not be penalized through punitive taxation merely for desiring to hold or use one type of currency, nor should they be penalized for exchanging Federal Reserve Notes for US Mint-produced coins.

I hope that this hearing will start a vigorous discussion of currency competition, sound money, and how to return to a sound dollar. HR 1098 is certainly not a panacea, as there remain significant structural problems in our banking and monetary system that still need to be addressed. But allowing for competing currencies will enable Americans to choose a currency that suits their needs, rather than the needs of the government. The prospect of Americans turning away from the dollar towards alternate currencies will provide the necessary impetus to the US government to regain control of the dollar and halt its downward spiral. Restoring soundness to the dollar will remove the government's ability and incentive to inflate the currency, and keep us from launching unconstitutional wars that burden our economy to excess. With a sound currency, everyone is better off, not just those who control the monetary system.