

Testimony of  
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Chairman  
e-Gold Group, Inc.  
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Subcommittee on Oversight and Investigations  
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Mr. Chairman, members of the Committee on Energy and Commerce Subcommittee on Oversight and Investigations: thank you for the opportunity to participate in these hearings. The problem of child pornography on the Internet is a serious one, and I am pleased to see the full involvement of the federal government, nongovernment organizations, and private industry. Working cooperatively will certainly help us all in the goal to eradicate this heinous crime from the Internet.

I would also like to applaud Ernie Allen and the National Center for Missing & Exploited Children (NCMEC) who have spearheaded the effort to bring together this financial coalition. Our aim, along with the NCMEC, is to curb the flow of payments to these criminals and to help identify perpetrators and their activity so that law enforcement can take appropriate action. We strongly support the NCMEC's goal to eradicate child pornography on the Internet, and I would like to add my thanks to my colleagues in this coalition.

I would like to take the opportunity to introduce you to e-gold. Though e-gold is approaching its tenth anniversary in November of this year, we recognize that we are still not well known in circles that do not make extensive use of the Internet for commerce. e-gold, Ltd. is a Nevis, West Indies company. It is operated by Gold & Silver Reserve (G&SR), headquartered in Melbourne, Florida. Gold & Silver Reserve also operates a service for the purpose of buying or selling e-gold, branded as OmniPay.

Gold & Silver Reserve's primary mission is to establish e-gold as a viable and credible medium/mechanism for Internet payment transactions, allowing an easy, safe, and secure means to receive payment via the Internet.

### **Overview**

e-gold<sup>®</sup> is a unique alternative system that mobilizes the value of gold for Internet payments. e-gold is designed to provide a complementary payment system for secure and final Internet transactions that minimizes exchange risk. Following charge cards, e-gold has the world's second largest reach as an online payment system behind PayPal, and it is far more global. Comparative analysis by websites that measure Internet activity show PayPal and e-gold first and second respectively in web traffic on payment system sites.

e-gold differs from every other existing payment system in that a quantity of e-gold constitutes a liability that, by virtue of a 100% reserve of physical gold, perfectly embodies the value of gold in allocated storage. e-gold is denominated in weight units. Transfers from account to account occur by book entry on dedicated database servers. E-gold is a closed system; that is, it is impossible for a user to send value into the system. Increases or decreases of the overall quantity of e-gold in circulation can be effected by bailment or redemption of physical gold by a credentialed entity, either a gold bank or other primary dealer designated by the issuer, e-gold, Ltd.

e-gold has over 3 million accounts in more than 165 countries and has the credibility of significant tenure, having been in operation online for almost 10 years. During e-gold's 10-year history, numerous other payment mechanisms have attempted to penetrate the online payment and remittance market, spending hundreds of millions to do so. PayPal, clearly the market leader, burned through \$275 million of losses before their acquisition by eBay. e-gold established its position almost entirely through the personal investment of its founder and a close circle of family and friends and has carefully continued its progress, relying on internally generated funds. e-gold has survived and thrived where most others have failed, due to a sound and coherent business model and robust, evolving self-governance as described below. This financing approach has not allowed the speed of growth that, for example, PayPal has achieved, but it has allowed e-gold to stay firm to its original mission. Classical market analysis would show organizations such as PayPal, Western Union, and credit card companies as competitors. In actuality, however, every seeming competitor would benefit from a strategic embrace of e-gold, taking advantage of e-gold's inherently global reach and non-repudiable settlement protocol to extend their own market penetration, reduce direct costs, and thereby offer a better service to their customer base. These same efficiencies, combined with e-gold's ever more refined capabilities for detection and interdiction of illicit payment transactions, would provide substantial benefit to official institutions that accept payment online and/or which themselves offer remittance and related services, like the U.S. Postal Service,.

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.

All e-gold in circulation is backed 100% by a reserve of physical gold in London Bullion Market Association member repositories. Currently, reserves amount to nearly 3.6 million

Fine Grams of gold, which would place e-gold 76th among countries for the value of gold reserves. At today's gold exchange rates, this reserve is valued at over \$68 million USD.

## **Vision**

e-gold was established in 1995 as a viable and credible medium/mechanism for Internet payment transactions, allowing an easy, safe, and secure means to make account-to-account transfers of value on the Internet by anyone, anywhere in the world.

e-gold's governance and transaction model derives from the dual imperative to assure finality of settlement and freedom from default 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 with a governance model that precludes even its management and founders from having the power to subvert it.

## **Governance, Security, and Visibility**

e-gold has a firm governance model to protect its users, is highly secure, and offers unprecedented visibility of activity to its users.

e-gold remains independent of its Operator and any “exchangers” of e-gold, a separation of roles that further aids in assuring e-gold’s freedom from default risk and finality of settlement. The operating guidelines are governed by the e-gold Account User Agreement which can be found on the e-gold website. The physical gold, stored in London Bullion Market Association recognized depositories in allocated storage, is titled to the “e-gold Bullion Reserve Special Purpose Trust,” a purpose trust holding these physical assets for the exclusive benefit of e-gold account holders. The gold is not under the control of the owners or operators of e-gold.

Transfers within e-gold are account-to-account, with immediate settlement by book entry on dedicated servers.

e-gold payments are made in a weight-based unit of (typically) gold. This medium of payment makes e-gold less subject to extreme fluctuations in currency exchange rates, especially for customers in countries with unstable currency. The asset portfolio backing e-gold, consisting entirely of physical gold, is free from the financial risks that pertain to securities or other debt instruments.

Freedom from default and finality of settlement are essential features that set e-gold apart from other payment systems and have led to e-gold’s firm position in the market. For e-gold to continue to grow and achieve its original vision, it is imperative that it maintain its low-risk model and operate at the highest level of integrity.

The e-gold system is very secure. All transactions occur online. Account login requires an account number, a pass phrase, human recognition of a Turing number, and a system verification of the user’s IP address. The only instances e-gold has encountered with compromised accounts are those in which a user in some manner surrendered both their

account data and access to their personal email to an unknown party. e-gold maintains significant information on its website to educate users to the various schemes used to gain account information.

e-gold abides by an unparalleled standard of transparency. The “Statistics” and “Examiner” links on the e-gold website publish real-time data on payment volume and other system usage data as well as the detailed inventory data for each repository. This transparency is unique among all online payment systems, including other precious metal-backed sites. We believe it is of fundamental importance that our customers fully understand e-gold’s size, growth, and gold backing to establish the credibility for safe, ongoing use.

Very favorable critiques have been received from respected business journals. Both *Barron’s* in April 2001 and *Grant’s Interest Rate Observer* in June 2003 reported favorably on the e-gold system. *Barron’s* noted: “The ideal e-currency might even be backed by gold. Encrypted digital units of the precious metal could in principle be used to pay for anything.....One company, E-gold already allows on-line users to settle payments using its currency, which is 100% backed by gold.”

### **e-gold’s Commercial Advantages**

e-gold offers numerous advantages to both online merchants (recipients of payment) and to online consumers (payers). (With e-gold, this traditional merchant/consumer distinction is obsolete—e-gold is bi-directional, meaning every account can make or receive payments.) Merchants benefit from fees that are significantly lower than any other online payment system. All payments are immediate and final: there are no chargebacks and the possibility of fraudulent payments is eliminated. e-gold is the most global of all payment systems, with easy-to-use interfaces, including a shopping cart. Since e-gold itself is immune to credit-related risks such as default by a user, recipients of e-gold payments are

free of the costs and risks that other systems are forced to pass to their payment recipients.

Consumers do not need to share personal information across the Internet to make a payment. This feature is a great advantage in reducing identity theft. Payment is immediate, final, and fully automated, enabling the purchased product or service to reach the consumer faster. Low transaction fees, coupled with elimination of costs associated with chargebacks can provide merchants a competitive edge by enabling cost savings to be passed back to the buyers. All transactions are fully traceable: if a debate ensues about a sale, there is a clear and unimpeachable record of the payment. And importantly, the e-gold payment system is easy to use.

#### **e-gold “Exchange”**

e-gold does not accept “money” (or any other transfer of value from the public) directly into the system. The only way to obtain e-gold is from someone who already has it. Many users will buy and sell their e-gold through a third-party “exchanger.” These are organizations completely independent of e-gold that operate around the world. The “exchangers” will accept payment for e-gold in a number of ways, but most typically accept wire transfers or certified checks. Any entity performing exchange realizes a business necessity to “know their customer” in order to avoid fraud losses due to failed or reversed payments transmitted via legacy (conventional credit-based/bank mediated) mechanisms.

Gold & Silver Reserve’s OmniPay serves as an exchanger and is the primary source of e-gold, buying from or selling to other exchangers as the market requires. OmniPay has implemented significant controls on how and to whom they buy or sell e-gold. When a new user profile is created, it requires e-mail validation followed by confirmation of the postal address. The user is also required to prove control of any e-gold account to or from which

the user intends to transact with OmniPay. User profiles are screened against OFAC and similar lists upon creation and with each exchange transaction that exceeds a threshold.

OmniPay will only sell e-gold upon confirmed receipt of a bank wire, further guaranteeing “know your customer” considerations. Upon selling e-gold, OmniPay will transmit by bank wire or a check delivered to the validated postal address.

All bank wires are reviewed to assure the transmitter name matches the name of the OmniPay user that entered the “exchange” order, and a permanent file of wire notifications is maintained. OmniPay restricts daily exchange from one party to \$100,000. If a larger amount is necessary, OmniPay requires significantly more due diligence, including notarized residence documents and copies of a government-issued photo ID. Inbound wire transfers are reviewed to ensure that the sending bank is not proscribed by U.S. Treasury guidelines.

### **e-gold is Not Hospitable to Illicit or Criminal Activity**

All online payment systems are subject to the attempts of individuals to use them inappropriately, whether for acceptance of illegal funds, money laundering, or other illicit activity. e-gold’s unique features and investigative protocols make it the poorest choice a criminal could make.

Two fundamental elements coupled with numerous programmatic processes and controls eliminate the possibility of e-gold serving as a source of indirection or successful obfuscation of money trails.

1. The public is incapable of sending “money” into the system. e-gold, Ltd. has no bank accounts and no capability of accepting payment or holding value in the form



of any national currency. Value can be added (via the bailment of good delivery bars into the Trust) only by an entity that has been fully vetted by one of the gold banks that comprise membership of the LBMA. Currently, only G&SR is credentialed to bail additional precious metal reserves into the system. A normal account user can obtain a quantity of the circulating medium (e-metal) only by receiving it in payment from another account user who already has some.

2. Value in the system is fully traceable. Transfers are executed by book entry, creating a permanent record of the lineage of every particle of value within the system. Records are maintained perpetually: the details of any transfer since the beginning of e-gold are available.

One of duties of the e-gold Operator (G&SR) is to conduct investigations pursuant to lawfully executed subpoenas or court orders. The organization of e-gold as a closed system where all transfers settle by book entry and all transactions capture supplemental information of potential forensic value eliminates the possibilities of a miscreant successfully using the system in an anonymous or untraceable fashion, even if false contact information has been provided. Upon its creation, an e-gold account contains no value and can only be "funded" by receiving payment from another user, thereby linking the newly funded account to a web of counterparties, some of whom inevitably will have provided correct and discoverable contact information. There has never been an investigation (over 75 performed per year) where the e-gold investigative staff has failed to identify the true identity of a suspect.

A new user may create an account online. The prospective user is required to provide contact information, including name, e-mail address, postal address, and telephone number. To validate the e-mail address, the system sends a welcome message to the specified e-mail address, also notifying the account-holder of the assigned account

number. Each day, e-gold's due diligence and investigative staff screens all accounts created since their previous screening session to locate accounts with false or inadequate contact information. The screening is assisted by a series of pre-configured database queries that flag suspicious patterns that have been found to be associated with false information. Accounts suspected of false identities are immediately blocked, rendering them incapable of receiving e-gold transfers.

Whenever a transaction occurs or a user update of contact information is committed to the database, the system captures a permanent record of the IP number and timestamp. This vital data is key to investigative techniques that require linking accounts in a constellation quietly controlled by a single entity seeking to mask their identity.

In 2004, e-gold implemented a countermeasure to mitigate phishing exploits (a form of identity theft). The e-gold system keeps track of the IP number and browser agent data from which a user logs into their e-gold account. If a login attempt is made from a different IP number or computer, the system will not allow access and will issue a challenge, e-mailing a one time PIN to the e-mail address registered with the account. This e-mail serves the dual purpose of notifying the rightful user of an unauthorized attempt to access their account and alerting them to the fact that their account information may have been compromised. The system also captures a permanent record of the IP number from which the attempt was made.

e-gold users are encouraged to supply complete and accurate information when they establish their account and to update their information if the contact data does change. If an account holder loses their passphrase, this contact data is required before a new one will be issued.

Of particular importance is e-gold's Right-of-Association in the e-gold User's Agreement. e-gold reserves the right to refuse to do business with individuals and entities at the sole discretion of e-gold. This right enables e-gold, Ltd. to refuse an active account to any entity suspected of engaging in illicit activities. This right is imposed by blocking the suspected account, preventing it from receiving transfers. Blocking an account still allows a user to spend the existing value in their account. A feature implemented in 2005, however, enables account users to refuse to accept Spends from blocked accounts. In the case of suspected child pornography, accounts are frozen outright, pending full investigation, thereby stopping all account activity.

e-gold has initiated a major system improvement to change from an account-based login process to a user-based login. With the implementation of this change e-gold will dramatically streamline the ability to capture only accurate user identity information and further reduce the already poor hospitability of e-gold for illicit activity. This change is significant requiring substantial programming and implementation switchover processes, and is expected to be deployed early in 2007.

### **e-gold is not a major payment system for Child Pornography**

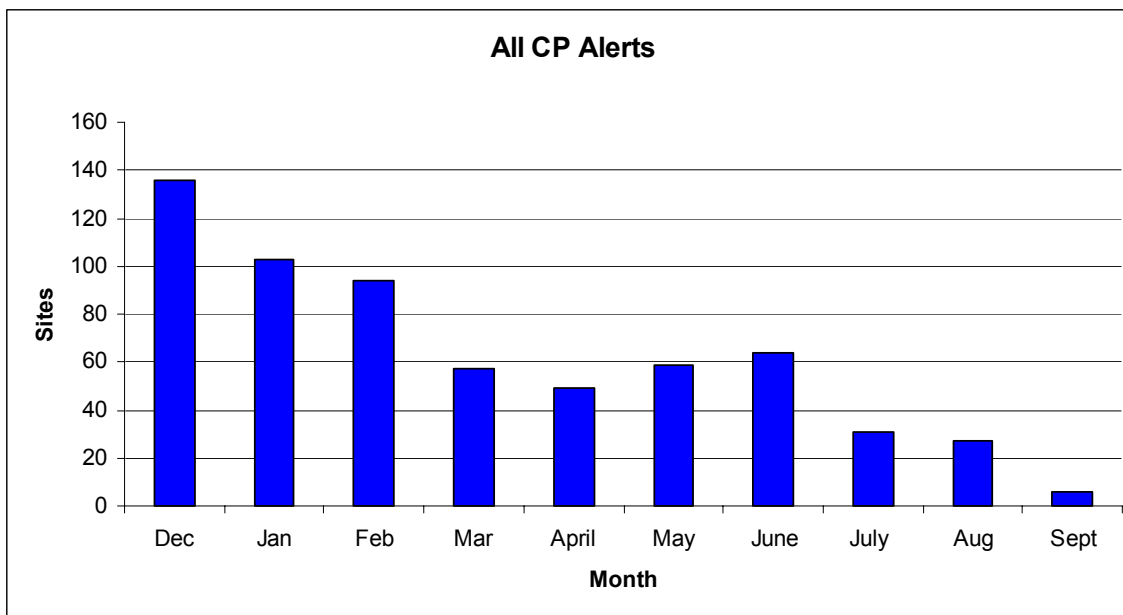
e-gold first experienced the possible use of e-gold for CP payment in early 2003. Those indications proved to be "phishing" sites using the bait of CP to learn account data of e-gold users, suggesting CP availability though apparently not actually selling it. e-gold blocked those accounts from further use of e-gold as well as all associated accounts.

At the beginning of 2004, e-gold investigators received a small number of third-party reports that proved to be real cases of CP sites accepting e-gold. As these sites were identified, they were blocked, along with all associated accounts. Recognizing the problem was real and growing, e-gold began to reach out to third-party watchdog organizations to

help in the alert process. This reaching out was frankly very difficult: e-gold was not well known or understood, and often, responses from these third parties were limited. e-gold did increase its in-house investigative activities and continued efforts with law enforcement. In mid 2005, the National Center for Missing and Exploited Children initiated their work that led to this financial coalition, which has helped significantly. e-gold is very proud to be one of the founding members of this very worthwhile coalition.

During this time period, e-gold received adverse press that came close to implying complicity in this problem, but it was press that was not justified. Based upon the financial size of the CP trade identified by the NCMEC and our review of historical transactions, e-gold has been the payment mechanism abused in less than one hundredth of one percent of the CP payment dollar volume since this problem surfaced. The NCMEC CyberTipLine sends alerts to Financial Coalition members, and alerts are received from other third-party sources as well. Since collaborative efforts started, the activity has decreased dramatically. When an alert is investigated, 95% of the time the account has already been identified and blocked through e-gold's own internal investigative efforts, almost always detected upon the first payment or before a single payment has been received.

The following chart represents all CP alerts from all sources since December 2005.

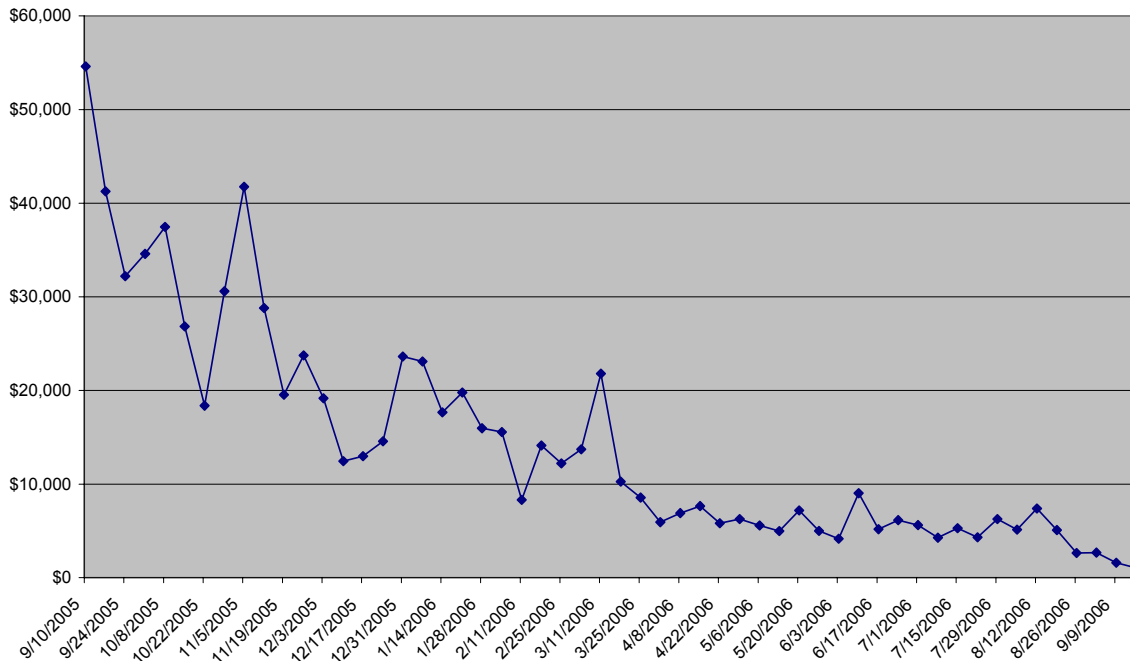


e-gold investigators estimate that 90-95% of the alerts received are for CP websites for which e-gold has already blocked the applicable account.

The very favorable trend shown in the chart is not an accident. e-gold continues to refine its protocols to detect and interdict CP payments. Investigative protocols are routinely upgraded as more is learned about the behavior of the perpetrators and enormous personnel resources are applied. e-gold's cost for investigative and preventive actions to stop the use of e-gold for illicit activity, especially CP, is the single largest element of expense in its business. e-gold will continue to apply this attention and resource until the problem no longer exists.

The following graph illustrates the declining dollar volume that, unfortunately, has escaped detection before the accounts were ultimately identified and blocked. It is evident that the visibility we gained from our association with NCMEC in the fall of 2005 was a turning point in our efforts to prevent e-gold being used at all for CP payment. The declining value depicts the evolving capability of our investigative techniques and show we have reduced e-gold abuse to a marginal level.

**Abuse of e-gold for Child Pornography  
Payment Volume per Week**



e-gold is not limiting its efforts to its own data base. Whenever a CP buyer account is identified, e-gold investigators alert the exchange provider from whom the perpetrator purchased their e-gold. The exchange providers are proving very helpful in suppressing CP from the demand side. It has been highly encouraging to see how strongly these organizations are supporting efforts to deter this crime.

As low as the escape payments have become, we will still remain vigilant: we know full well that these criminals will not stop until the risks of their activity outweigh any possible commercial incentive. We will continue to strenuously support the NCMEC and law enforcement until the problem is gone.

### **Justice Department Investigation**

In a spirit of full cooperation and disclosure, it is fair to inform the Committee that Gold & Silver Reserve is under investigation by the United States Justice Department. G&SR

remains confused as to why this investigation was undertaken, why it continues, and why G&SR and its founder, Dr. Douglas Jackson, have been treated in such an abusive manner.

In December of 2005, the Secret Service conducted a “raid” of the Gold & Silver Reserve offices and Dr. Jackson’s home. Bank accounts were frozen, and company funds were seized. In an emergency hearing in U.S. District Court on January 13, 2006, the freeze order on Gold & Silver Reserve's bank accounts was lifted. Though numerous criminal claims had been made in obtaining the search and seizure warrants, the government made no attempt to sustain such allegations. The only claim at that time and continuing now is a contention that G&SR is operating as a currency exchange without the proper license. G&SR had previously proposed to the Government that e-gold be classified for regulatory purposes as a currency, enabling G&SR to register as a currency exchange. In a Treasury report released January 11, 2006, however, the Department of Treasury reaffirmed their interpretation of the USC and CFR definitions of currency as excluding e-gold.

As early as 2001, Gold & Silver Reserve attempted to make contact with the United States Secret Service to explain how the e-gold system works and to illustrate the advanced protocols for interdiction and investigation of potential criminal use. Dr. Jackson, e-gold and Gold & Silver Reserve’s founder and CEO, scheduled meetings to meet with the Secret Service in Washington—meetings which were postponed and subsequently canceled by the USSS. These rebuffs by the Secret Service continued during the time period when an investigation of the Shadow Crew, a carder ring, was made public approximately a month before the raid. At no time did the Secret Service engage with e-gold investigators, even though the company volunteered to assist the Secret Service by obtaining information to assist in their investigations under proper subpoena. Throughout

this period, Gold & Silver Reserve cooperated with numerous other U.S. and international law enforcement agencies and expeditiously answered subpoenas.

G&SR, for nearly a year, had been engaged with an agency of Treasury in a BSA (Bank Secrecy Act) compliance examination it had voluntarily initiated for the purpose of determining how Gold & Silver Reserve, Inc. should be regulated.

In order to obtain the subpoena allowing the search and seizure in December, it would also have been necessary to show the court that there existed a high probability of flight or destruction of records. Dr. Jackson, his wife, and their two children have lived in Melbourne, Florida for the past 14 years. Gold & Silver Reserve has regularly cooperated with all law enforcement in the United States as well as with non-U.S. governments, regularly providing information to law enforcement under due process. As noted earlier, Gold & Silver Reserve had contacted the Secret Service repeatedly to explain the system, the data it held, and how Gold & Silver Reserve and law enforcement could cooperate.

Online payment systems, credit cards, money transfer systems, and banks are all subject to attempts by criminal elements to use them for moving illegally obtained funds. No one is exempt from the threat. Extensive public scrutiny has recently been provided to a U.S. government program to review international Swift transactions of major financial institutions, a program seen as important and necessary, looking for money laundering activity. In the Shadow Crew case itself, public pronouncements identified other systems, including well-known PayPal and Western Union. From Gold & Silver Reserve's own investigation, it is certain many large U.S. banks have had illegal funds processed into and out of their accounts. Gold & Silver Reserve does not know why it has been singled out for investigation when the other larger institutions have not, especially considering Gold & Silver Reserve has possibly the best ability to track payments and identify those making transactions and had made repeated offers to assist if provided with proper legal direction.



In December 2005, the Secret Service confiscated all records and documentation from the e-gold system and Gold & Silver Reserve's offices. It has the entire history of every e-gold transaction ever made. As of December, e-gold had processed over 55 million individual financial transactions—the greatest majority from U. S. citizens. Since the December 2005 government actions, e-gold has cooperated fully with the government. Despite the fact that the U.S. government has all the records, Gold & Silver Reserve has continued to support government investigations and respond to individual subpoenas. This assistance includes supporting an investigation of this same carder ring by other agencies of the U.S. government.

Gold & Silver Reserve regrets being in this conflict situation with a service of the United States government and does not understand why. Seized funds continue to be held, pending what appears to be a never-ending investigation we now believe to be over two years long. These funds were designated for ongoing improvements of the e-gold system, which would have the effect of making the e-gold system even less hospitable for criminal abuse. Employees and contractors of Gold & Silver Reserve have had their lives interrupted, being called from Florida to Washington for testimony, having never been interviewed previously. The ongoing legal issue is depleting resources for Gold & Silver Reserve's defense against apparently uncertain claims since the Government itself has deemed e-gold not a currency, thereby rendering the claim of not being licensed as an exchange service unfounded. e-gold continues to labor under a cloud of unwarranted suspicion, which is clearly impacting business operations and its ability to reach out with marketing initiatives to natural strategic partners, such as the very financial institutions that participate in this coalition.

Gold & Silver Reserve hopes this issue is settled quickly, that seized funds are returned, and that proper attention be given to the investigation, apprehension, and prosecution of the criminals now operating at will. G&SR will continue, as always, to obey the law and support law enforcement through every possible means to stop true criminal activity.

### **e-gold's Future**

e-gold, despite unwarranted adverse press and intense government investigation, is remaining true to its initial vision. With the ever-increasing online commerce and globalization, the need for a cross border, risk free, low-cost payment and remittance system is growing. The ability to provide a service to individuals from all backgrounds and economic conditions will serve to simplify increasing world commerce and allow the migrant worker to perform his business in one country and then buy goods or send money home across a border easily and inexpensively. This ability can only serve to bring all the economic interests and people across the world closer together.

Historically, e-gold has been viewed by some as presenting a potential risk, possibly facilitating improper cross border movement of funds. It has been difficult to fully educate everyone involved in a rapidly changing economic online world. This risk, however, is clearly not the case. It is more important that a proper focus be given to e-gold's ability to better monitor and control those cross-border transactions while providing enhanced service to individuals.

Multiple U. S. government agencies could benefit from using e-gold, including the U.S. Postal Service, the Internal Revenue Service, and the U.S. Mint. Low transaction fees, finality of settlement, and transaction traceability are all positive features supporting agency adoption. For example, the U.S. Postal Service deals in Postal Money Orders and a cross-border remittance program. The inherent risks of money laundering would be

significantly reduced by encouraging a combination of the USPS' over-the-counter cash functions with the flexibility of user-directed transfers via e-gold. Rather than outlawing informal value transfer systems or leaving the unbanked no alternative to monopolistic remittance processors, this flexible combination with permanent records on a single database would capture significant market share while eliminating a potential channel for terrorist funding or money laundering.

### **Summation**

e-gold is a business, but within its mission is also a fervent desire to bring a benefit to the world. It is not now nor ever has been a suitable vehicle for persons engaged in illicit activity. With the full cooperation of law enforcement, e-gold is, in fact, one of the least hospitable systems a criminal could use. The NCMEC's Financial Coalition is demonstrating how a strong level of cooperation can lead to the reduction and, hopefully, elimination of crime on the Internet.

It is certainly e-gold's objective, working with the NCMEC and our coalition partners, to completely eradicate child pornography on the Internet.

Again, thank you for the opportunity to participate in your Committee's hearings. We remain willing to help in any manner possible.