

Introduction

How can the exchange rate of a currency be fixed, and for sound economic reasons? Shunning foreign exchange controls and bureaucratic intervention, the currency board system is an option in the modern context. A currency board regime (CBR) may be viable and optimal, if the **credibility** of a set of clearly defined **monetary rules** that incorporates the currency board system can be established.

Such monetary rules serve two crucial functions. First, they impose discipline on the behaviour of the authorities and limit the extent of official discretion (or indiscretion). Second, they enable the operation of automatic and transparent adjustment mechanisms under the currency board system (involving in particular the arbitrage activity of market participants) that would cause the market exchange rate to converge to the official parity and restore macroeconomic equilibrium at minimised costs.

Credibility is a complicated issue. In so far as the majority of the market participants believe in the

- (a) **sanctity;**
- (b) **effectiveness; and**
- (c) **appropriateness**

of the monetary rules, and hence willingly engage in self-interested arbitrage activities, the currency board regime will function smoothly without the need for direct government intervention.

How is credibility for the monetary rules to be established? Since credibility depends partly on sanctity, or the **commitment** of the authorities (the other two factors being effectiveness and appropriateness of the rules, as said), one obvious way to enhance credibility is for top government officials to repeatedly affirm adherence to those monetary rules. The results of such an “informal”

approach may vary. In the case of Hong Kong in the pre-1997 era, the commitment to the linked exchange rate of HK\$7.80/US\$ seemed “natural” for all walks of life because of the over-riding concerns of transitional stability. Nevertheless, if the “commitment” is just governmental rather than society-wide in nature, an alternative in more difficult situations is to **legislate** the monetary rules, or parts of them, i.e. turn them into laws. The merit of this option is that the commitment is formalised.

However, there are two potential problems for this legal route. First is the credibility of the law-making body itself. In rather extreme situations, even this could be in doubt. The proposal to adopt a currency board system, floated in Indonesia in 1997-98, was apparently rejected by the IMF in view of acute political instability. Another example is that of Bosnia and Herzegovina in 1997. A foreigner was appointed by the IMF as the first Governor of the Central Bank (for a six-year term) to launch a currency board regime, in order to top up credibility for a new country arising from ashes (Article VII of the Constitution of Bosnia and Herzegovina).

The second problem is that a law is rather rigid and may take a long political process to formulate, enact, revise or exit from. So what part(s) of the monetary rules should be included in legislation? Even for the obviously critical core of the rules, i.e., the convertibility undertaking by the monetary authority on the exchange rate, Argentina and Lithuania have chosen to be legally asymmetrical, although effectively, the undertaking is two-way in daily operations. Also, controversy remains on what else should be brought within the ambit of law, especially concerning the operations of a modern currency board regime with regard to liquidity management and lender of last resort facilities.

This paper presents a general survey of the legal frameworks of the major currency board regimes (CBRs) now operating in the world. It looks at three key aspects of such frameworks, namely,

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- (1) The legal setting covering the relationships between the currency board system and the monetary authority/central bank, which may be explicit, implicit, or non-defined;
- (2) The extent of legal commitment to a backing rule and the convertibility undertaking; and
- (3) Legal coverage of other aspects of currency board operations, including,
 - (a) the lender of last resort function;
 - (b) lending to government; and
 - (c) pursuit of transparency.

Six CBRs are analysed in the paper. They include Argentina, Bosnia-Herzegovina, Hong Kong, Bulgaria, Estonia and Lithuania. **Annex A** provides a tabular summary of the key legal features of these regimes.

Varieties of Legal Setting: Unitary, Separate and Loose Frameworks

Existing CBRs have adopted a variety of legal frameworks. A central bank is in operation in all major CBRs, which by definition has to carry out more functions than a pure currency board system. A question thus arises as to whether the currency board system and the central bank should be legislated separately or under one single law. Basically, there are three approaches:

- (a) Unitary approach: through which the central bank is directly legislated as a means to implement a currency board system; e.g., the case of Bosnia and Herzegovina and that of Bulgaria;
- (b) Separate legislation: whereby the currency board system or the Backing Rule/Convertibility Undertaking is under a different law from that of the Central Bank Law; e.g., Argentina, Estonia and Lithuania;
- (c) Loose frameworks: where there are no clear legal commitments to a currency board system or specific laws on central banking; e.g., Hong Kong.

Unitary Approach (Bosnia-Herzegovina and Bulgaria)

In the Dayton Peace Agreement on Bosnia and Herzegovina and the country's Constitution, explicit references were made to the establishment of the Central Bank of Bosnia and Herzegovina (CBBH), operating as a "currency board" (Article VII of the Constitution). Article 02.1 of the Law on the CBBH, which came into operation on 11 August 1997, states:

"The objective of the Central Bank shall be to achieve and maintain the stability of the domestic currency (Convertible Marka) by issuing it according to the rule known as a currency board."

However, the Constitution of Bosnia and Herzegovina provides an apparent flexibility after the initial six-year period. Article VII.1 stipulates that

"The Central Bank's responsibilities will be determined by the Parliamentary Assembly. For the first six years after the entry into force of this Constitution, however, it may not extend credit by creating money, operating in this respect as a currency board; thereafter, the Parliamentary Assembly **may** give it that authority." (our emphasis)

Bulgaria also has a unitary legal framework for its CBR. Although the Law on the Bulgarian National Bank (LBNB) passed in 1997 does not explicitly mention the term "currency board", its provisions are very specific. Article 28.1 obliges the BNB to maintain foreign exchange reserves to cover its monetary liabilities – a hallmark of modern CBRs. In Article 29, it is clearly stated that the Bulgarian currency, lev (BGL), is to be pegged to the Deutschemark.

Moreover, Article 19 of the LBNB states that three "basic departments" shall be established at the BNB: an Issue Department, a Banking Department and a Banking Supervision Department. Article 20(1) further pronounces that "(t)he main function of the Issue Department shall be to maintain full foreign exchange cover for the total amount of monetary liabilities of the Bulgarian National Bank, by taking actions needed for the

efficient management of the Bank's international foreign exchange assets." The Issue Department is legally equivalent to the "currency board".

Separate Legislation (Argentina, Estonia and Lithuania)

The Law of the Republic of Estonia on the Security for Estonian Kroon (LRESEK) became effective from June 1992 onwards. It is a very concise piece of law, with only six clauses. The basic principle of a modern CBR is established in Clause 1, under which the monetary liabilities of the central bank are to be "secured" by gold and convertible foreign exchange reserves. Clause 2 stipulates that the currency is to be pegged to the German mark. However, the term "currency board" is not referred to in the Law.

The Law on the Central Bank of the Republic of Estonia (LCBRE) was enacted in 1993. It institutes the Eesti Pank as the "legal successor" to the Central Bank of the Republic of Estonia, as established in 1919. There is however no reference in it to the LRESEK. Moreover, the LCBRE does not put forward any clear provisions on currency board operations.

In Argentina and Lithuania, a central bank existed before the enactment of a law effecting a CBR or a convertibility undertaking. Argentina's Convertibility Law (CL) came into effect in April 1991, which fixed the domestic currency against the US dollar. It was intended to be a legalised approach to remedy the aftermath of hyperinflation in the 1980's, in a bid to regain market confidence. Likewise, the Law on the Credibility of the Litas (Lithuania's currency) was passed by the Lithuanian Seimas (Parliament) and became effective on 1 April 1994. It stipulated that the "official exchange rate of the Litas shall be established against the currency chosen as the anchor currency" (Article 3). However, the US dollar was not specified as the "anchor currency".

Then the existing law on the central bank had to adjust in both countries. In Argentina, the Central Bank (BCRA) Charter of 1992 was passed to facilitate the commitments of the Convertibility

Law. In Lithuania, the Law on the Bank of Lithuania came into effect on 1 December 1994.

It is interesting to note that the central bank law caters to different extents to the CBR/convertibility undertaking in these two countries. In both cases, no explicit reference is made by the former to the latter. The Charter of the BCRA is more compliant. In its Article 3, it is stated that

"The primary and essential mission of the Central Bank of Argentine Republic is to preserve the value of the currency.

The Bank shall develop a monetary and financial policy in order to secure the function of money as value reserve, unit of account and instrument of payment to settle monetary obligations, in full compliance with such legislation as the Honorable National Congress may pass."

One such legislation is of course the Convertibility Law of 1991, but it is not mentioned in the BCRA Charter.

In the case of Lithuania, the Law on the Bank of Lithuania of 1 December 1994 again made no reference to the Law on the Credibility of the Litas of 1 April 1994. Article 7 on "The Principle Objective of the Bank of Lithuania" states:

"The principal objective of the Bank of Lithuania shall be to achieve stability of currency of the Republic of Lithuania.

Implementing the principal objective, the Bank of Lithuania must:

- (1) ensure the reliable functioning of the currency market and the system of credit and settlements; and
- (2) support the economic policy carried out by the Government of the Republic of Lithuania, provided the said policy is in compliance with the principal objective of the Bank."

That seems a less vigorous compliance to the CBR/convertibility undertaking.

Loose Frameworks

In the case of Hong Kong, Article 111 of the Basic Law requires that the issue of Hong Kong currency be backed by a 100% reserve fund, without specifying the reserve assets. There is no central bank law. The only other relevant statutory provision in Hong Kong's CBR is Section 4 of the Exchange Fund Ordinance, which covers the Certificates of Indebtedness for issuing bank notes. Section 4(1) of the Ordinance stipulates full backing for Hong Kong dollar bank notes issued. Again, no specific assets in foreign currency are referred to.

The Backing Rule and the Convertibility Undertaking

The basic principle of a modern CBR is that the monetary authority should have sufficient foreign exchange reserves to cover its monetary/financial liabilities. As the discussion in the last section made obvious, all six regimes surveyed, including Hong Kong, have some legal provisions on such a **Backing Rule**. They are summarised in **Annex A**.

Even with sufficient foreign reserves backing, which should boost confidence in the domestic currency, the central bank may or may not be required to adhere to different forms of legal commitment to the **Convertibility Undertaking**. That undertaking can involve explicit promises to allow banks and citizens to engage in exchange transactions with the central bank at the fixed exchange rate. In existing CBRs, several approaches to undertaking convertibility are observed:

- (a) Legal two-way: the cases of CBBH and the Bulgarian National Bank (BNB);
- (b) Legal one-way (but operationally two-way): Argentina;
- (c) Loose legal one-way (but operationally two-way): Lithuania;
- (d) Non-legal: Hong Kong

Legal Two-way

In the unitary Law on the CBBH, the commitment to parity against the Deutsche mark is unequivocal and two-way. Articles 0.2.3 cum 0.2.3a state:

- “3. The basic tasks of the Central Bank performed under the authority of its Governing Board shall be:
 - a. to formulate, adopt and control the monetary policy of Bosnia and Herzegovina by issuing the domestic currency (Convertible Marka) at a one to one exchange rate with the Deutsche mark with full backing in freely convertible foreign exchange, and through its other functions as defined in this Law;”

According to Article 30 of the Law on the Bulgarian National Bank (LBNB), covering the assets and liabilities of the BNB,

“On demand, the Bulgarian National Bank shall be bound to sell and purchase Deutschemarks against leva up to any amount within the territory of this country on the basis spot exchange rates, which shall not depart from the official exchange rate by more than 0.5 percent, inclusive of any fees, commissions and other charges to the customer.”

That constitutes a clear two-way convertibility undertaking with a 0.5% spread.

Legal One-way (but Operationally Two-way)

The Convertibility Law of Argentina (CL), enacted in 1991, stipulates that the national currency is pegged to the US dollar at a fixed rate. Article 2 of CL requires the central bank, BCRA, to sell foreign exchange for peso at the official rate; but Article 3 permits the BCRA to purchase foreign exchange at the market rate.

However, the market exchange rate has allied closely around the official rate. Hence in effect the

undertaking turns out to be two-way in daily operations.

Loose Legal One-way (but Operationally Two-way)

The Law on the Credibility of the Litas (LCL) of Lithuania in 1994 initiated a CBR, but in a loose manner. Indeed, the LCL does not spell out the US dollar as the “anchor currency”. Article 3 states:

“The official exchange rate of the Litas shall be established against the currency chosen as the anchor currency.

The official exchange rate of the Litas and the anchor currency shall be established or changed by the Government of the Republic of Lithuania upon co-ordination with the Bank of Lithuania.”

The Law has been criticised by currency-board purists for the lack of binding force because of the loose provisions of this Article 3, which implies that both the anchor currency and the official exchange rate may be changed by a “co-ordination” between the Bank of Lithuania and the Government. To critics, this sounds too loose a statutory commitment.

Article 4 of the LCL states:

“The Bank of Lithuania shall guarantee to the extent of its gold holdings and foreign exchange reserves free exchange of the Litas specified in Paragraph 2 of Article 2 into the anchor currency according to the official exchange rate of the Litas, as well as free exchange of the anchor currency into the Litas within the territory of the Republic of Lithuania.”

In a strictly legal sense, that implies a one-way convertibility undertaking, as the Law leaves open the rate at which the free exchange of the anchor currency into the Litas is to be conducted. Again, like in Argentina, the market exchange rate has allied closely around the official rate. Hence the undertaking is effectively two-way in daily operations.

Non-legal

In Hong Kong, the only statutory provision that underpins the CBR is Section 4 of the Exchange fund Ordinance. As said, it covers the Certificates of Indebtedness. Even that is phrased in very general terms, and can be consistent with any exchange rate regime. Section 4 (1) states:

“The Financial Secretary is authorised to issue to any note-issuing bank, to be held as cover for bank notes lawfully issued in Hong Kong, a certificate of indebtedness in the form of the Schedule and to require such bank to pay to him for the account of the Fund the face value of the notes so issued, or the equivalent in such foreign currency and at such rate of exchange as may be determined by the Financial Secretary, to be held by the Fund principally for the redemption of such notes and may be used for such purposes in the event of a note-issuing bank being wound up in Hong Kong or elsewhere.”

In lieu of a clear legal backing for Hong Kong’s CBR, top officials, including all the Financial Secretaries since 1983, have been confirming the Government’s unequivocal commitment to the linked exchange rate of 7.80. This contrasts with the situation in Lithuania, whether the central bank’s reservations about a rigid CBR have become quite obvious.

Legal Coverage of Other Aspects of the CBR

Other than the backing rule and the convertibility undertaking, the legal coverage of the other aspects of the CBR varies across countries and territories. Again, in the case of Bosnia and Herzegovina, legal discipline is the strongest. As said above, the principle of a currency board (Article 1.1) and the one-to-one official parity (Article 2.3.a) are explicitly stated in the Law on the CBBH. Moreover, in defining the objectives and basic tasks of the central bank, constant references are made to Article 2.3.a. For example, Article 2.3.d states,

“d. to issue regulations for the implementation of the activities defined in paragraph a of Article 2, section 3 of this Law;”

Articles 2.3.f and 2.3.h further stipulate,

“f. to execute the monetary policy in accordance with paragraph a of Article 2, section 3 of this Law;

.....

h. to put into and to withdraw from circulation the domestic currency (Convertible Marka), including legal tender banknotes and coins, adhering strictly to the currency board rule defined in paragraph a of Article 2, section 3 of this Law.”

Such an explicit legalisation is rare among CBRs. As pointed out above, neither Argentina’s nor Lithuania’s central bank law makes any direct reference to the legal convertibility undertaking. In Argentina’s BCRA Charter, Article 3 states that the BCRA will comply with legislation by the Congress; but otherwise, the Charter looks very similar to any conventional central bank law.

Lender of Last Resort Function

In fact, there are provisions in the BCRA Charter that may be regarded as deviations from classical currency board principles, particularly regarding the lender of last resort (LOLR) function. For Example, Article 33 states that “(u)p to one third of the freely available reserves held as a(n) ordinary pledge may be paid with public bonds at market price”. Moreover, although Article 19 prohibits the BCRA from acting as a general lender of last resort, Article 17 clearly spells out ways under which it can provide LOLR facilities.

“The Bank is empowered to:

.....

b. grant rediscounts to financial institutions on account of temporary lack of liquidity, for periods not exceeding thirty (30) running days, up to a maximum amount per institution equivalent to the equity capital thereof;

c. grant overdrafts to financial institutions due to temporary lack of liquidity, for periods not exceeding thirty (30) running days, collateralised by public bonds or other securities, or by a special or general guarantee or allocation over certain assets, provided that the total amount of rediscounts and overdrafts granted to a single institution is not, under any circumstance, over the limit determined in the previous paragraph.”

The situation in Lithuania is similar. Article 8.11 of the Law on the Bank of Lithuania states that the Bank “shall act, in accordance with the procedure established by law, as the lender of last resort in the bank system”. Article 26 deals with “Open-Market Operations” and the Bank is authorised to “buy and sell debt instruments (securities) issued by the Republic of Lithuania” and to “perform rediscount operations”. Moreover,

“In exceptional cases, pursuant to the decision of the Board of the Bank of Lithuania, bills of exchange and other obligations of commercial operations may be accepted for rediscounting provided that they have a maturity not exceeding six months and bear the signatures of two guarantors and warrantors of which at least one is a bank.”

Article 27 on Credit Operations also stipulates that, given defined guarantees and pledged assets, the Bank “may make credits to banks and other credit institutions of the Republic of Lithuania that hold their required reserves with (it). The amount of credit may not exceed 60 per cent of the liabilities of a given commercial bank or other credit institution in litas or foreign exchange”.

Even in Bulgaria, some flexibility is allowed. According to Article 33 of the Law on the Bulgarian National Bank (LBNB), the BNB should not extend credits to banks except where the emergence of a liquidity risk may affect the stability of system. In any case, there are restrictions on the maturity and the required collateral, and such liquidity assistance is limited to the excess of foreign exchange reserves over the monetary liabilities of the BNB.

In the case of Hong Kong, the Exchange Fund Ordinance stipulates the use of the assets of the Exchange Fund for defending the exchange rate of the Hong Kong dollar and for the maintenance of the stability and integrity of the local monetary and financial systems. Operationally, the provision of liquidity to individual banks is determined on a case by case basis and there are no statutory references.

Lending to Government and Pursuit of Transparency

Classical currency boards prohibited the monetary authority from lending to the government to cater for fiscal needs. In the six regimes surveyed, three have explicit provisions in the central bank law forbidding such lending. They are Argentina, Bulgaria and Estonia. In the case of Argentina, however, the central bank is allowed to buy at market prices negotiable instruments issued by the Treasury.

As to the pursuit of transparency, the Law on the Credibility of the Litas requires the Bank of Lithuania to publish on a monthly basis statistics on the litas in circulation and Lithuania's foreign exchange reserves (Article 6). The Law of the Republic of Estonia on the Security for Estonian Kroon asks the Eesti Pank to do the same for the kroons in circulation and the country's foreign exchange reserves (Clause 5). According to the Law on the Bulgarian National Bank, the balance sheet of its Issue Department, which is the nearest entity to the "currency board" in the system, has to be published weekly. At the same time, financial information of the whole BNB is to be published monthly (Article 49).

Although there are no legal requirements in Hong Kong, the HKMA has been moving towards greater transparency through daily publication of figures on the monetary base and regular publication of the Currency Board Account and the records of discussion of the meetings of the EFAC Sub-Committee on Currency Board Operations.

Concluding Observations

There is a notable variety of the legal frameworks for the operation of CBRs, ranging

from the "loosest" (Hong Kong) to the "strictest" (Bosnia and Herzegovina). The different modes adopted were often dictated by specific internal and external circumstances surrounding the birth of the CBR. In Bosnia and Herzegovina, the post-war situation apparently demanded the highest degree of commitment and monetary discipline by the government. In Hong Kong, the successful launching of the link in October 1983 simply diverted market participants' attention from the legal fine points, or the lack of them. The less than ideal economic situations in Argentina and Lithuania, on the other hand, have resulted in legal provisions that may be regarded as inconsistent with classical currency board principles.

All in all, the credibility of a CBR depends not just on the implicit or explicit commitment of the authorities, which may be legalised in various manners and to different extents, but also on the effectiveness and appropriateness of the underlying monetary rules. The lack of full legalisation of currency board commitments may in some cases enhance confidence in so far as these two latter considerations are concerned, and contribute to the overall credibility of the CBR. In other words, a legally rigid pledge to some ineffective mechanisms or inappropriate principles may not be credible. Hence even the Constitution of Bosnia and Herzegovina allows for some flexibility in its CBR after an initial six-year period. By the same token, most CBRs provide leeway for the central bank to perform the lender of last resort function, which may be regarded as a deviation from the classical design.

A final remark is that this paper has been based on a survey of the legal documents and other relevant material available from the six CBRs. Legal interpretations, on such a basis, may be a hazardous business. The author, who is an economist rather than a lawyer, bears full responsibility for any inaccuracy, deficiency and misjudgement. ☹

STATUTORY PROVISIONS IN SIX CURRENCY BOARD REGIMES Argentina, Bosnia-Herzegovina, Hong Kong, Bulgaria, Estonia and Lithuania

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
Law governing the Currency Board Setup	Convertibility Law of 1991 (CL).	Constitution of Bosnia and Herzegovina (Article VII); Law on the Central Bank of Bosnia and Herzegovina of 1997 (CBBH).	No legislation dedicated to the currency board setup.	Law on the Bulgarian National Bank (LBNB).	Law of the Republic of Estonia on the Security for Estonian Kroon (LRESEK). The law for the establishment of the Eesti Pank (LCBRE) makes no reference to the law providing for currency board system (LRESEK).	Law on the Credibility of the Litas (LCL).
Anchor Currency	US\$	Deutschemark	US\$	Anchor currency of Deutschemark is stipulated (Article 29, LBNB). When Euro becomes the legal tender of Germany, the anchor currency will be changed to Euro.	Anchor currency of Deutschemark is stipulated (Clause 2, LRESEK).	US Dollar. Article 3 of LCL states that in the case of extraordinary circumstances, the Bank of Lithuania upon co-ordinate of the government, may change the anchor currency or the official rate of Litas.

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
Official Exchange Rate	1 peso = US\$1	1 Convertible Marka = 1 Deutschemark	HK\$7.80 = US\$1	Official exchange rate of BGL1000 to DEM1 is stipulated (Article 29, LBNB). When Euro becomes the legal tender of Germany, the official exchange rate of lev to Euro will be determined by multiplying the official exchange rate to conversion rate of Deutschemark to Euro (Article 29.2, LBNB).	1 DM = 8 kroon. Official exchange rate is determined by Eesti Pank. Eesti Pank can only revalue the kroon exchange rate, but has no right to devalue the kroon (Clause 2, LRESEK).	US\$ 1 = 4 Lit. Official exchange rate is determined and can be changed by the Government "upon co-ordination with the Bank of Lithuania" (Article 3, LCL).
Backing Rule	Article 4 of the CL specifies a minimum of 100% backing of the Monetary Base.	Articles 0.2.3 and 0.2.3a state that the domestic currency will be issued with full backing in freely convertible foreign exchange. Article 31 provides a detailed rule for issuing currency.	Article 111 of the Basic Law required that the issue of HK currency must be backed by a 100% reserve fund. Section 4(1) of Exchange Fund Ordinance also specifies the requirement of full backing, in face value of the notes so issued, or in foreign exchange at the exchange rate determined by the FS, of the bank notes issued.	BNB is obliged to maintain foreign exchange reserves to cover its monetary liabilities (Article 28.1, LBNB).	Eesti Pank is obliged to maintain foreign exchange reserves to cover its monetary base (Clause 1, LRESEK). In addition, Eesti Pank can only change the kroon in circulation with a correspondent change in foreign exchange reserves (Clause 4, LRESEK).	Bank of Lithuania is obliged to maintain foreign exchange reserves to cover the litas in circulation (Article 1, LCL). In addition, Bank of Lithuania can only change the litas in circulation with a corresponding change in foreign exchange reserves (Article 2, LCL).

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
(a) coverage of monetary base	Operationally, the monetary base is defined as the sum of cash in circulation and deposits of financial entities with the Central Bank.	No information.	Operationally, both the stock and flow of the monetary base are fully backed by foreign reserves.	Monetary liabilities consist of all bank notes and coins in circulation, account balances held with the BNB (Article 28.2, LBNB).	Monetary base includes cash in circulation, currency and in accounts of a fixed date (Clause 1, LRESEK).	Litas in circulation includes bank notes and coins in circulation, account balances held with Bank of Lithuania and litas-denominated securities and other promissory notes of the Bank of Lithuania (Article 2, LCL).
(b) eligible assets for backing	Article 4 of CL specifies that reserves are to be invested in deposits, other interest-bearing transactions, or in national or foreign public bonds payable in gold, precious metals, US\$ or other foreign exchange. The Central Bank Charter; however, allows a maximum of 1/3 of backing assets to be provided in the form of US\$ government bonds ('Bonex').	No information.	The entire backing portfolio backing the monetary base is made up of US\$ assets. None of these assets are claims on the domestic government. A non-statutory requirement.	Eligible backing assets include (1) foreign currency denominated bank notes and coins, (2) foreign currency funds held with foreign financial institutions, (3) SDRs, (4) debt instruments issued by foreign institutions, (5) forward or repo agreements with foreign institutions and (6) gold (Article 28.3, LBNB).	Not specified.	Foreign exchange reserves include foreign currency denominated bank notes and coins, foreign currency deposits held in foreign institutions and foreign currency denominated securities held by Bank of Lithuania (Article 2, LCL and Article 31, LBL).

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
Convertibility Undertaking	Legally one-way although two-way in practice. Articles 1 and 2 of the CL require the central bank to sell foreign exchange for peso at the official exchange rate. Article 3 permits the BCRA to purchase foreign exchange at the market price.	Article 0.2.3a specifies that domestic currency will be issued at a one to one exchange rate with Deutschemark.	Section 4(1) of the Exchange Fund Ordinance stipulates the issue and redemption of Certificates of Indebtedness, as cover of bank notes, at the exchange rate determined by the Financial Secretary. Operationally, a one-way Convertibility Undertaking in respect of the Aggregate Balance is also provided to the licensed banks in Hong Kong. In other words, licensed banks can convert their HK\$ balance in their clearing accounts into US\$ with the HKMA at the Convertibility Rate.	The BNB is bound to sell and purchase Deustchemarks against levs at the spot exchange rate which should not depart from the official exchange rate by more than 0.5 percent (Article 30, LBNB).	There are no provisions obliging Eesti Pank to convert the kroon into foreign exchange, or vice versa. Nevertheless, Eesti Pank guarantees the free exchange of the kroon to foreign exchange, according to the official rate of Eesti Pank (Clause 3, LRESEK).	Bank of Lithuania guarantees the free exchange of litas into anchor currency according to the official rate of litas. In the opposite direction, the Bank guarantees free exchange of the anchor currency into Lit as without specifying the applicable exchange rate. (Article 3, LCL).

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
Role of Central Bank	Central Bank functions are governed by the CB Charter. Article 3 specifies that the primary function of the central bank is to preserve the value of the currency and the monetary and financial policy have to be in full compliance with legislation passed by the Congress.	Central bank functions are governed by the same CBBH. Articles 0.2.1 clearly specifies that 'the objectives of the Central Bank shall be to achieve and maintain the stability of the domestic currency by issuing it according to the rule known as a currency board' for the initial six years.	No separate legislation governing central bank functions. Operationally, the primary function of the HKMA is to maintain currency stability within the framework of the linked exchange rate system.	The establishment of the Bulgarian National Bank (BNB) and the currency board system are provided in one single legislation - the LBNB. In addition, the Department, Banking Department and Banking Supervision Department are separated (Article 19, LBNB). The function of the Issue Department to maintain full foreign exchange cover for monetary liabilities of the bank is specified to make currency board operations distinct from other functions of the bank (Article 20, LBNB).	The law for the establishment of the Eesti Pank (LCBRE) makes no reference to the law providing for the currency board system (LRESEK).	The law for the establishment of the Bank of Lithuania (LBL) makes no reference to the law providing for the currency board system (LCL).

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
Lender of last resort function	Article 19 of the CB Charter prohibits the central bank from acting as the general lender of last resort but Article 17 permits it to grant rediscount and advances to financial institutions in temporary illiquidity.	No information.	The Exchange Fund Ordinance stipulates the use of the assets of Exchange Fund for defending the HK\$ exchange rate and for the maintenance of stability and integrity of the monetary and financial systems in HK. Operationally, the provision of liquidity to individual banks in stress will be determined on a case by case basis.	The BNB is not allowed to extend credits to banks except where emergence of a liquidity risk that may affect the stability of the banking system. Restrictions on maturity and collaterals are also stipulated. Such liquidity assistance is limited to the excess of foreign exchange reserves over the monetary liabilities of the BNB (Article 33, LBNB).	Eesti Pank is empowered to carry out monetary operations and grant loans to credit institutions without detailed restrictions (Article 14, LCBRE).	Bank of Lithuania can act as the lender of last resort (Article 8, LBL). It is empowered to carry out open market operations and perform rediscount operations (Article 26, LBL). It can also extend credits to banks and other credit institutions with a maximum amount of 60% of the liabilities of the given institution (Article 27 and 32, LBL).
Lending to Government	Article 19 of the CB Charter prohibits the central bank from lending to the national government, provinces and municipalities but Article 20 permits the central bank to buy at market price negotiable instruments issued by the Treasury.	No information.	No statutory specifications. Operationally, the government exercises fiscal discipline and has accumulated over HK\$400 bn of fiscal reserves.	The BNB cannot extend credits to the state or state agencies (Article 45, LBNB).	Eesti Pank is prohibited from granting credits to the state or local authorities. Neither can it buy securities issued by the Government (Article 16, LCBRE).	No special provisions.

	Argentina	Bosnia-Herzegovina	Hong Kong	Bulgaria	Estonia	Lithuania
Pursuit of Transparency	No information.	No information.	Operationally, the HKMA has been moving towards greater transparency through regular publication of the monetary base, the currency board account, and records of discussion of the EFAC Sub-Committee on Currency Board Operations, etc.	Balance sheet of the Issue Department of the BNB has to be published weekly, while financial information of the BNB is published monthly (Article 49, LBNB).	Eesti Pank has to publish statistics on kroons in circulation and foreign exchange reserves on a monthly basis (Clause 5, LRESEK).	Bank of Lithuania has to publish statistics on litas in circulation and foreign exchange reserves on a monthly basis (Article 6, LCL).

Footnote: The following abbreviations are used in this Annex:

- Argentina: Convertibility Law of 1991 - CL
Central Bank Charter - CB Charter
- Bosnia-Herzegovina: Law on the Central Bank of Bosnia and Herzegovina of 1997 - CBBH
- Bulgaria: Law on the Bulgarian National Bank - LBNB
- Estonia: Law on the Central Bank of the Republic of Estonia - LCBRE
Law of the Republic of Estonia on the Security for Estonian Kroon - LRESEK
- Lithuania: Law on the Bank of Lithuania - LBL
Law on the Credibility of the Litas - LCL