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THE STATE OF U.S. COINS AND CURRENCY

HEARING

BEFORE THE

SUBCOMMITTEE ON
DOMESTIC MONETARY POLICY
AND TECHNOLOGY

OF THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

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THE STATE OF U.S. COINS AND CURRENCY

Tuesday, July 20, 2010

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON DOMESTIC MONETARY
POLICY AND TECHNOLOGY,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:33 p.m., in room 2128, Rayburn House Office Building, Hon. Melvin L. Watt [chairman of the subcommittee] presiding.

Members present: Representatives Watt, Sherman, Green, Cleaver; Paul, Castle, Lucas, and Lance.

Chairman WATT. I will convene this hearing of the Subcommittee on Domestic Monetary Policy and Technology of the Financial Services Committee, and the hearing will come to order. We will start by having 10 minutes per side of opening statements, or up to 10 minutes per side, and I will recognize myself for the first opening statement.

In general, the purpose of this hearing is to examine the current state of coins and currency in the United States. The U.S. Mint, the Bureau of Engraving and Printing, the Federal Reserve, and the U.S. Secret Service are jointly responsible for the circulation of all U.S. coins and currency and anticounterfeiting measures to protect the U.S. money supply.

There are several specific issues we would like to explore in some detail in this hearing. First, how effective are the government's anticounterfeiting measures? Some have estimated that in 2009, the amount of counterfeit notes passed was approximately $70 million, an amount that has been increasing in recent years. There have also been reports from the United Kingdom that 1 and 2 British pound coins are being counterfeited at an increasing rate. So, we need to know what steps are being taken by the U.S. Mint to prevent counterfeiting of U.S. dollar coins, and what is the government's plan going forward to combat the increasing counterfeiting of notes that cost taxpayers millions of dollars per year.

Second, what is the government's response to the worldwide rise in the price of metals used to manufacture coins? Some reports suggest that it actually costs more to manufacture the penny and the nickel than these coins are now worth. The Administration has proposed legislation to amend 31 U.S.C. Section 5112 to allow the Treasury Secretary to prescribe the metal composition of all circulating coins, including the penny, nickel, dime, quarter, half dollar, and $1 coin. However, some have raised concerns about this pro-

posal because, by statute, only Congress has the authority to prescribe the metal content of circulated coins.

We need to evaluate alternatives, such as perhaps granting the U.S. Mint research and development authority to research alternative metals and report these researched findings back to Congress, while perhaps retaining the authority of Congress to determine the metal content of coins.

Third, is there an oversupply of certain coin denominations? Some reports suggest that there are up to $1 billion in dollar coins and other low-denomination coins being stored in large quantities by the Federal Reserve and partner companies. We need the Fed to either confirm or refute these reports; and if the reports are confirmed, we need to know what efforts the Fed is taking to reduce these coin surpluses and more efficiently manage the Nation's money supply.

Fourth, some dealers and collectors of numismatic coins have indicated that the U.S. Mint is not keeping up with the demand for numismatic coin products. Current statutes require that all refined gold and silver must be used first to meet bullion demand. We need to evaluate whether it would be a good idea to divert refined gold and silver from the bullion program to meet demand for numismatic products and what impact this would likely have on the supply of bullion products.

While there are many other important issues related to the state of U.S. coins and currency, the four issues I have outlined above should allow for a robust exchange.

While we are not attempting to address this issue today, one other important topic that we need to explore in the future is the issue of equal access to U.S. currency by the visually impaired. The Bureau of Engraving and Printing has issued a proposed rule that is open for public comment until mid-August, and the Bureau expects to issue a final rule in the fall of 2010. While I thought it would be inappropriate to put the BEP in the awkward position of commenting on a proposed rule while the rule is in the comment period and before the rule is finalized, when the final rule is issued, it would certainly be appropriate to have a hearing on this and related issues. Of course, it is important for the visually impaired to have equal access to U.S. currency and for the Congress to ensure that the Bureau's final rule accomplishes that result.

With that, I will now recognize the ranking member, the gentleman from Texas, Mr. Paul, for up to 5 minutes.

Dr. PAUL. Thank you, Mr. Chairman. And I welcome the panel.

I remain opposed to the Mint's current effort to gain greater power in determining the composition of circulating coinage. It is unconstitutional to delegate a determination of the metal content of our coinage to the Secretary of the Treasury. Under Article I, Section 8, of the Constitution, the Congress is given the power to coin money and regulate the value thereof. It is a shame that Congress has already unconstitutionally delegated its coinage authority to the Treasury Department, but that is no reason to further delegate our power and essentially abdicate congressional oversight.

While I sympathize with the aim of saving taxpayer dollars by reducing the cost of coinage, it is disappointing that our currency has been so greatly devalued as to make this step necessary. At the

time of the penny's introduction, it actually had some purchasing power. Based on the price of gold, that one penny would have purchased in 1910 what requires 57 cents today. It is no wonder that few people nowadays would stoop to pick up any coin smaller than a quarter.

One of the witnesses on our second panel mentions the importance of the Mint's production of bullion coinage and the danger of counterfeit collector coins that may or may not be minted from silver or gold. It is a shame that instead of protecting the value of the dollar to ensure that precious metals coins could still circulate as money, or enforcing counterfeiting laws to stop the flow of clearly fraudulent coins, the Federal Government insists on printing trillions of dollars out of thin air and prosecuting individuals who attempt to create precious metal currencies to compete with the devalued U.S. dollar.

The topics discussed in today's hearing exemplify how far we have fallen not just since the days of the Founders, but only in the last 75 to 100 years. We could not maintain the gold standard or the silver standard. We could not maintain the copper standard, and now we cannot even maintain the zinc standard. Paper money inevitably breeds inflation and destroys the value of the currency, which harms all Americans. I wait for the day that we have a committee hearing when we talk about once again reinstituting sound money for our people.

I yield back.

Chairman WATT. I thank the gentleman for his opening statement. I will just remind him, I am one of those people who still picks up pennies, especially when the head is up. That is supposed to be lucky.

Mr. Sherman from California is recognized for 3 minutes.

Mr. SHERMAN. Commenting on the Executive Branch's desire to control what is in the metal that is used to make coins, I would think if you had a good proposal, we could pass it. It would be a delightful break from renaming post offices; and the fair deal ought to be we will let you guys rename a couple of post offices, and we will keep control of what metal is in the coinage, unless there is a real agenda you have here to move to another metal and you figure Congress wouldn't pass it if we actually knew what you were going to use the power for.

As to counterfeiting, my whimsical suggestion is that we retaliate against North Korea by counterfeiting some of their currency. I realize this would not fully compensate us for what they are doing to ours, but it would be nice for us to be on offense for a change.

There are two major issues in this area: should we phase out the paper dollar; and should we eliminate the penny? There are those who think that the amount of value in a dollar should be represented by a piece of paper. When I was growing up, that amount of value was a quarter or less, and you had a metal coin called a quarter that was sufficient in value to buy a quarter pounder and a drink. And so I don't see why we need to have the Federal Government go through the expense of making and replacing paper money for an amount of value that has traditionally in this country been represented by a coin.

This would help dramatically reduce costs for our transit systems and our vending machine operators. As long as there is a paper dollar, the metal dollar will not take hold. And we could reduce dramatically the costs of a lot of transactions if we had a coin dollar that was in wide circulation. We could also save a lot of paper and a lot of ink because these coins last a lot longer.

That might go hand-in-hand with abolishing the penny. I am sure that we could figure out other ways to honor President Lincoln and President Washington, who appears on the paper dollar, perhaps by including these folks in some of the dollar coins that we create. Abolishing the penny would mean every cash register would have a place where you could put a coin dollar; that is to say, in the tray. We would save a lot of zinc. We would save a little copper. We would save some money.

But there are consumers who think that, when I buy something for 99 cents, I want to be able to pay just 99 cents. The fact is every transaction—I say this as in my former life, I used to have the largest sales tax agency in the country—is actually rounded up or down. If you buy something for 99 cents in a State with a sales tax of 5 percent, then you are actually paying at the cash register $1.03.95, which is rounded up to $1.04. So you already have all the rounding. And if you want, you can buy a certain amount of 99-cent items so the merchant will have to round down, rather than up; and if that is important to you, you would now round down to the nearest nickel and save almost 2½ cents.

So I would hope that we could abolish the penny, which is really not a unit of value anymore. Mel will pick one up, not for the value, only for the luck, and I assure you, those nickels will be just as lucky.

I yield back.

Chairman WATT. The gentleman's time has expired.

I recognize the gentleman, Mr. Lucas, for 3 minutes.

Mr. LUCAS. Thank you, Mr. Chairman. I appreciate the opportunity to be a part of this panel discussion today, and I look forward to the comments from our witnesses, too. It is an esteemed and very knowledgeable group.

The comment has been made about the obsolete coins, the 1-cent pieces. How many dollar coins are piled in a vault somewhere? I would look forward to the comments from the Fed as to just how many dollar coins we have stacked up in the vaults, and do they anticipate ever again in my lifetime actually ordering half dollars from the Mint for circulation? Does the half dollar fall in the same category as the 1-cent piece? Something I look forward to comments, too, here, and also representatives from the law enforcement side of the equation.

Counterfeiting is a very sensitive issue not only for the integrity of the American economy on large notes and other kinds of coins, but also from the perspective of counterfeiting numismatic-type items, coins of more than just face value, more than just metal content. Many of us have read public accounts how in the 1950's and 1960's and 1970's, in certain parts of the Middle East, there was an ongoing business of producing counterfeit U.S. gold coins, most often full weight, full metal content, but nonetheless stamped out in a way to harvest that numismatic value to coin collectors. Many,

many reports appear from some of the most prominent press in both numismatic circles and nonnumismatic circles about literally what seems to be one of the biggest growth industries in places like China, where it is not just counterfeiting low-value coins just to sell to tourists nice shiny pieces of eight, so to speak, but also using the very best technology, the very best techniques to sell coins that are of great sometimes numismatic value to unsuspecting collectors and even counterfeiting the packages that the certification services produce to try and protect the consumer from counterfeiters. I would like to hear a little bit of a discussion about that, about how aggressive we are and how aggressive we need to be to protect collectors and consumers in general.

With that, thank you, Mr. Chairman, for this opportunity.

Chairman WATT. I thank the gentleman.

The gentleman from Texas, Mr. Green, is recognized for 2 minutes.

Mr. GREEN. Thank you, Mr. Chairman.

I am concerned about one aspect of the state of U.S. coins and currency that deals with its very existence. As we move into this age of technology and plastic, I am curious as to what the prognostication is for the distant future in terms of whether we will actually have coins and currency. Is it something that we absolutely will have here, or is it something that the rest of the world needs when it deals in dollars and in the currency of the United States of America?

I would be interested in hearing your views on how coins and currency will actually impact the economic order in the not-too-distant future. But I can see that with the technology being what it is, we are moving away from coins and currency to plastic, it seems.

I yield back.

Chairman WATT. I thank the gentleman for his comments.

The gentleman from New Jersey, Mr. Lance, is recognized for 1 minute or more, unless Mr. Castle comes in.

Mr. LANCE. Thank you, Mr. Chairman.

And good afternoon to the panel. I look forward to your testimony. I will review your testimony carefully.

Initially, my viewpoint is that the Congress should not delegate further authority to Executive Branch agencies based upon the constitutional clause cited by Ranking Member Paul. I certainly want to listen to your testimony, but I would much prefer that any suggestions you have come to us in Congress, where we might review them and enact them into statutory law.

Thank you, Mr. Chairman. I yield back the balance of my time.

Chairman WATT. I think that exhausts our requests for time for opening statements from those who are present. And I would just say that, without objection, all members' opening statements will be made a part of the record. So if any other members come in and wish to submit opening statements, we will certainly put them in the record.

I will now briefly introduce the panel of witnesses. Without objection, their written statements in their entirety will be made a part of the record and each of them will be recognized for a 5-minute summary of their testimony. Of course, the lighting system is there

in front of you. It goes green for 4 minutes, yellow for 1 minute, and red at the end of 5 minutes. So while we won't be absolutely stringent on that, we would ask you to comply with that as best you can.

Our first witness today on panel one will be the Honorable Edmund C. Moy, who is the Director of the United States Mint. Our second witness will be Mr. Larry Felix, the Director of the Bureau of Engraving and Printing. Our third witness will be Ms. Louise Roseman, the Director of the Division of Reserve Bank Operations and Payment Systems at the Board of Governors of the Federal Reserve System. And our final witness on the first panel will be Mr. Ken Jenkins, Deputy Special Agent in Charge of the Criminal Investigative Division at the U.S. Secret Service.

Mr. Moy, you are recognized for 5 minutes.

STATEMENT OF THE HONORABLE EDMUND C. MOY, DIRECTOR, UNITED STATES MINT

Mr. MOY. Thank you, Mr. Chairman. And I would also like to greet Ranking Member Paul and the members of the subcommittee. I appreciate being invited to be here today. I welcome the opportunity to discuss operational results and demonstrate the need for immediate passage of the Coinage Materials Modernization Act, which is the Administration's proposal offering a potential savings of billions of dollars.

First, I would like to provide a short summary of our operations and programs. At the end of Fiscal Year 2009, the United States Mint transferred $440 million to the Treasury General Fund, which has been the lowest seigniorage in the most recent 5 years. This is attributable to higher metal costs that have caused this decrease. We have also minted and issued 5.2 billion circulating coins, which is a 45-year low. This low production was due to low coin demand and high inventories at the Federal Reserve Banks. We also minted and issued 27 million ounces of gold, silver, and platinum bullion coins, which is triple the amount of recent years.

Regarding the 2010 circulating coin programs, we have complied with our statutory obligations to identify, analyze, and overcome obstacles to the robust circulation of the $1 coin; however, despite our considerable efforts, we have had limited success while the Federal Reserve Banks have accumulated an inventory of approximately 1 billion $1 coins, which is a level that is of great concern to us. We believe that the key to robust circulation is greater use of this coin at the cash register, but are unsure as to whether or not we can cost-effectively achieve significant and sustainable increases in $1 coin circulation.

High existing Federal Reserve Bank inventories are also affecting production levels of the new 12-year America the Beautiful Quarters Program. Thus far, production levels are a fraction of those of the 50 State Quarters Program.

Turning to our gold, silver, and platinum bullion coin programs from Fiscal Year 2009, bullion coin sales approached $1.7 billion, which is an all-time high and nearly 80 percent above previous year's sales. We have increased both planchet acquisition and production to meet rising demand.

Consequences from increased worldwide bullion demand were threefold. Orders for bullion from authorized purchasers exceeded supply for all of Fiscal Year 2009. Planchet diversion to meet public demand for bullion coins meant that we could not mint and issue the very popular American Eagle 1-ounce gold and silver proof coins in 2009. Annual purchasers of these products were very disappointed.

I am encouraged that the subcommittee is exploring the possibility of an amendment that would afford the Secretary the authority to approve the minting and issuance of the American Eagle Silver Proof and uncirculated coins even when we are unable to meet the public's demand for the bullion versions of these coins. Our many customers would welcome such a change. We can mint 200,000 coins per month; and if we begin production by September, we can meet collector demand for the remaining months of 2010.

Finally, I would like to address the Coinage Materials Modernization Act. Per-unit cost for the penny and nickel have exceeded their face values in 2009 as they have since 2006. The expense of current coinage metals is a needless waste of hundreds of millions of dollars. We know how to stop this waste.

The government has acted twice before in the last 50 years to protect taxpayers from bearing the increased costs of coinage materials. In 1965, Congress changed the composition of the dime, quarter, and half dollar from silver to cupro-nickel clad. In 1974, Congress granted the authority to the Secretary of the Treasury to vary the copper-zinc alloy of the penny. Thirteen years ago, Congress passed the $1 Coin Act of 1997, granting the Secretary of the Treasury sole discretion to select materials for the $1 coin.

Our proposal builds on these precedents. Support and encouragement from Congress to save billions has resulted in the Administration's proposal, which is called the Coinage Materials Modernization Act. This proposal provides the Secretary of the Treasury the flexibility to respond quickly to changing market conditions. It ensures fair and efficient management of highly technical evaluations and selection of alternate coinage materials. We would, of course, use a competitive, transparent, open, deliberative, and market-driven process that will consider the views of the public and commercial interests.

So in conclusion, delegating the authority to evaluate and select alternative materials to the Secretary of the Treasury is a proven approach. Since 1982, taxpayers have realized savings of more than $71 billion from the change from silver to clad. Today, we can pass the Coinage Materials Modernization Act and achieve similar savings.

Thank you, Mr. Chairman. I look forward to answering the committee's questions.

[The prepared statement of Director Moy can be found on page 84 of the appendix.]

Chairman WATT. I thank you for your testimony.

Mr. Felix, you are recognized for 5 minutes.

STATEMENT OF LARRY R. FELIX, DIRECTOR, BUREAU OF ENGRAVING AND PRINTING (BEP)

Mr. FELIX. Thank you, Mr. Chairman. Thank you, Ranking Member Paul, and members of the subcommittee. Thank you for inviting me to testify about ongoing initiatives at the Bureau of Engraving and Printing.

The mission of the Bureau of Engraving and Printing is to design and manufacture high-quality security documents that meet customer requirements for quality, quantity, and performance, including counterfeit deterrence. The BEP is the government's security printer, and it provides technical assistance and advice to other Federal agencies in the design and production of security documents, which, because of their inherent value or other characteristics, require counterfeit deterrence. The BEP also reviews the cash destruction and unfit currency operations of Federal Reserve Banks.

Although the BEP produces security documents on behalf of Federal agencies, our primary product is the Federal Reserve note. Our operations are financed by means of an industrial revolving fund, and on average, the BEP produces approximately 7 billion notes per year.

The BEP works collaboratively with the Board of Governors at the Federal Reserve, the United States Secret Service, and the Department of the Treasury to improve the security of Federal Reserve notes. In 1982, by charter, the Advanced Counterfeit Deterrence Steering Committee was established to recommend designs to the Secretary of the Treasury for Federal Reserve notes. And as a general guideline, the Committee recommended that the government redesign notes every 7 to 10 years to deter counterfeiting and anticipate advances in reprographic technologies.

Consequently, in the mid-1990's, the U.S. Government introduced the first major redesign to U.S. currency in 65 years. The design changes were needed to combat the emergence of a new category of counterfeiters who were increasingly relying on computers, scanners, color copiers, and other emerging technologies to replicate notes.

The goal of staying ahead of technological threats to currency rather than simply responding to existing threats requires that the U.S. Government plan ahead in its development of new currency. This means that a new currency must be in development for several years before the counterfeiting threat is projected to materialize.

In April of this year, the U.S. Government unveiled the last banknote in the most recent currency design series. The redesigned $100 will enter circulation in February of next year. This latest redesign series contains an array of counterfeit-deterrence security features, some of which are visible and easily recognizable to the public, and some of which are covert and machine-readable.

Overall, counterfeiting U.S. currency remains at a low level, primarily due to a combination of improvements in the notes' security designs, aggressive law enforcement, and an effective public education effort. According to the U.S. Secret Service, less than 1/100 of 1 percent of all the value of circulating U.S. notes is a counterfeit.

The BEP began implementing its strategic plan that will significantly change its currency manufacturing process; and over the next few years, the BEP will continue to retool and retrofit its production by purchasing new equipment that will allow the agency to migrate to a higher capacity and capability manufacturing environment. Updating this equipment is essential. The aging manufacturing equipment at the BEP no longer meets the performance requirements demanded in today's dynamic currency manufacturing environment. The new equipment will provide a rapid response and the flexibility, productivity, and technology necessary to support the manufacture of the increasingly complex currency designs, including an array of possible features for the blind and visually impaired.

In May of this year, the BEP posted a notice in the Federal Register to announce recommendations that it intends to propose to the Secretary of the Treasury for moving forward and providing meaningful access to the blind and visually impaired to denominate currency. The BEP expects very shortly to make recommendations to Secretary Geithner as to the best possible manner to provide that meaningful access.

Our recommendations currently consist of raised tactile features; large, high-contrast numerals; and a supplemental currency reader program. Additionally, the BEP is continuing its efforts to explore emerging technological solutions, such as the development of software to enable blind and visually-impaired individuals to denominate currency. Other initiatives on the way at the BEP include employee training, product quality, cost reduction, and a modernization of our technology.

By leveraging efficiencies in new innovations, the BEP recognized that we were overstaffed in certain positions. We requested and were granted permission for early-outs and buyouts. By the end of 2014, the BEP expects to have a 10 percent overall reduction in its staff. Since 2005, staffing has declined by 338 positions.

The BEP strives to provide its customers with superior products and is continuously looking for ways to manufacture efficiently without compromising quality.

Mr. Chairman, this concludes my remarks, and I am happy to respond to any questions.

[The prepared statement of Director Felix can be found on page 53 of the appendix.]

Chairman WATT. Thank you for your comments and testimony.

Ms. Roseman is recognized for 5 minutes.

STATEMENT OF LOUISE L. ROSEMAN, DIRECTOR, DIVISION OF RESERVE BANK OPERATIONS AND PAYMENT SYSTEMS, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Ms. ROSEMAN. Chairman Watt, Ranking Member Paul, and members of the subcommittee, thank you for inviting me to discuss the Federal Reserve's perspectives on issues relating to currency and coins. I will focus my comments this afternoon on trends in currency demand, strategy for currency redesign, and our recent experience managing dollar coin inventories. Additional matters are addressed in my written statement.

The growth rate for U.S. currency began to moderate during most of the past decade, compared to the strong growth of the previous 30 years. The recent financial crisis, however, spurred a substantial increase in demand for U.S. currency in late 2008 and in 2009, driven largely by foreign demand for the $100 note. International demand for U.S. currency tends to increase during times of economic and political uncertainties, and this was no exception. While domestic demand surged briefly in the fall of 2008, it quickly returned to normal patterns as the government took steps to restore confidence in the banking system, such as increasing FDIC insurance limits. Overall, currency in circulation increased from about $775 billion at the end of 2007 to almost $900 billion by the end of last year.

Let me now turn to activities surrounding the design of currency. While currency designs remained unchanged for most of the 20th century, rapid changes in copying and printing technologies now require us to change designs more frequently to stay ahead of counterfeiters and keep counterfeit levels low. Maintaining confidence in U.S. currency requires a combination of effective security features in the notes, public education, and law enforcement. This requires a strong collaborative interagency effort.

The Treasury Department, the BEP, the Secret Service, and the Federal Reserve participate on a joint steering committee that monitors ongoing counterfeit threats and advancements in banknote security features and recommends currency design changes to the Secretary of the Treasury. The current design family began with the issuance of the new $20 note in 2003, and will conclude with the new $100, which was unveiled in April. The Federal Reserve will begin distributing the new $100 next February 10th. We are currently engaged in an important program to educate users in the United States and around the world about the design and security features of the new note before it begins circulating.

The subcommittee expressed interest in better understanding the demand for Presidential dollar coins and the effect of this program on Federal Reserve inventories. Demand for dollar coins remains quite low, especially when compared to dollar notes, and appears to come largely from collectors. Banking industry representatives have indicated that transactional demand for dollar coins has not increased materially since the start of the Presidential $1 Coin Program, and they generally do not expect demand to increase significantly in the future.

Federal Reserve inventories of dollar coins have been growing substantially, from less than 70 million in 2006 to more than 1 billion today. We estimate that our dollar coin inventories may reach 2 billion by the end of the Presidential $1 Coin Program. This inventory growth is due in large part to the legislative requirement that the Reserve Banks make each new Presidential design available to their customers for an introductory period. I should note that we have no such requirement for any other coin. Therefore, the Federal Reserve must continue to order each new Presidential design from the Mint even though it already has more than ample inventories to meet demand.

Exacerbating this problem is the legislative requirement that at least 20 percent of total dollar coins the Mint issues each year is

a Native American design. While the Federal Reserve is not currently ordering these coins due to our large inventory levels and the lack of banking industry demand, many of the coins the Mint is issuing directly to the public are deposited in the banking system and ultimately make their way back to the Federal Reserve. These legislative requirements are resulting in steadily rising Reserve Bank inventories and the associated costs of dealing with them.

In conclusion, I would like to assure the subcommittee that the Federal Reserve will continue to work to meet the public's demand for currency and coin in an efficient and effective manner. I appreciate this opportunity to discuss these issues with you and would be pleased to answer your questions. Thank you.

[The statement of Director Roseman can be found on page 98 of the appendix.]

Chairman WATT. I thank you for your testimony.

And, Mr. Jenkins, you are recognized for 5 minutes.

STATEMENT OF KENNETH JENKINS, DEPUTY SPECIAL AGENT IN CHARGE, CRIMINAL INVESTIGATIVE DIVISION, U.S. SECRET SERVICE

Mr. JENKINS. Good afternoon, Chairman Watt, Ranking Member Paul, and distinguished members of the subcommittee. I would like to thank you for providing the Secret Service the opportunity to discuss currency issues.

The Secret Service is perhaps best known for protecting our Nation's leaders. We were established in 1865 to investigate and prevent the counterfeiting of U.S. currency. Congress continues to recognize the Secret Service's 145 years of investigative expertise in financial crimes, and over the last 2 decades, has expanded our statutory authorities to include access device fraud, identity theft, computer fraud, and bank fraud.

As you are aware, the Secret Service officially became part of the Department of Homeland Security in March of 2003. Though our agency is no longer a component of the Department of the Treasury, we continue to maintain our historic ties and our robust partnership in safeguarding our currency and other payment systems.

The Secret Service strongly believes that economic security is an essential element of homeland security. Therefore, the safeguarding of our financial infrastructure and monetary framework continues to be a paramount objective of our worldwide investigative efforts.

As new technology continues to emerge, the challenges facing law enforcement are significant. These advancements mean counterfeit currency and other obligations can be reproduced quickly and effectively. Today's criminals need relatively little knowledge or specialized training to print counterfeit currency or other financial obligations. Utilizing equipment ranging from inexpensive digital devices, such as scanners, computers, and multifunction devices, to large commercial presses, a counterfeiter or criminal organization can flood a region with counterfeit currency.

The Secret Service is aggressively combating the production and circulation of counterfeits on several fronts. With our partners in the Department of the Treasury and the Federal Reserve, we are continuing with the redesign of our currency. As a member of the

Advanced Counterfeit Deterrence Steering Committee, an interagency currency design committee, we have an active role in the research, design, and introduction of new currency. The Secret Service continually evaluates the methods currently employed by counterfeiters and studies cutting-edge anticounterfeiting technologies to enhance further redesigns of the U.S. currency. This partnership was highlighted on April 21, 2010, with the unveiling of the redesigned $100 Federal Reserve note. The new design for the $100 note not only retains the effective security features from previous designs, but also contains two new security features, the 3-D Security Ribbon and Bell in the Inkwell. These security features included in the $100 note will hinder a potential counterfeiter from reproducing high-quality notes that deceive consumers and merchants.

Due to the dollar's value and widespread use overseas, it continues to be a target for transnational counterfeiting activity. Of the approximately $908 billion of genuine U.S. currency in circulation, roughly two-thirds of that amount circulates outside of our borders, making the U.S. dollar a truly global currency.

Recent trends indicate a growing globalization in the production and distribution of counterfeit notes. For Fiscal Year 2009, the Secret Service received approximately $69 million in counterfeits that was passed to the American public. Additionally, approximately $108 million in counterfeit U.S. currency was seized prior to distribution last year by the Secret Service and other authorities worldwide. Currently, more than 38 percent of all counterfeits passed domestically was printed outside of the United States using traditional printing techniques, predominantly offset printing. In contrast, 62 percent of the counterfeit currency passed domestically last year was produced within the United States by individuals using digital technology, such as computers, scanners, printers, and multifunctioning devices.

The Secret Service has observed the counterfeit notes produced on bleached paper are both a domestic and international concern. Domestic counterfeiters as well as counterfeiting operations based in Colombia, Nigeria, and Italy have produced significant quantities of counterfeit notes still printed on bleached genuine U.S. currency paper.

Today, the Secret Service continues to target locations throughout the world where significant counterfeiting activity is detected through joint task forces with our foreign law enforcement partners. Our investigative history has proven that the effect of suppression of counterfeit operations requires a close partnership between our domestic and international field offices and their law enforcement counterparts, as well as an immediate response by the law enforcement community.

The Secret Service's permanent presence overseas has been essential in establishing the required relationships to successfully suppress foreign-based counterfeit operations. For example, Project Colombia is a continuation of the Secret Service efforts to establish and support Vetted Anticounterfeiting Forces. Since its inception in 2001, Project Colombia partners have seized approximately $239 million in counterfeit U.S. currency, arrested more than 600 suspects, suppressed nearly 100 counterfeit printing plants, and re-

duced the number of Colombia-originated counterfeit passed within the United States by more than 80 percent.

As a collateral effect of our investigative successes in Colombia, the criminal element has relocated to other parts of South America. For example, from Fiscal Year 2008 to Fiscal Year 2009, the Secret Service noted an 156 percent increase in worldwide passing activity of counterfeit U.S. currency emulating from Peru. These counterfeit notes, referred to as the Peruvian Note Family, have emerged as one of the leading domestically passed notes in the last 18 months. In response to this increase in passing activity of the Peruvian Note Family, which is second only to domestic passing of digital counterfeit in Fiscal Year 2008, the Secret Service formed a temporary Peruvian Counterfeit Task Force in collaboration and partnership with Peruvian law enforcement officials. Since opening in Peru on March 15, 2009, the task force yielded 38 arrests, 17 counterfeit plant suppressions, and seizure of more than $20.6 million in counterfeit U.S. currency.

Chairman WATT. Mr. Jenkins, can you wrap up?

Mr. JENKINS. Yes, sir.

The Secret Service, in concert with established partners, both private and public, domestic and international, law enforcement and civilian, will continue to play a critical role in preventing, detecting, and investigating the effects of increasingly complex financial and electronic crimes.

Chairman Watt, Ranking Member Paul, and distinguished members of the subcommittee, this concludes my prepared remarks. I am pleased to answer any questions at this time. Thank you.

[The prepared statement of Deputy Special Agent Jenkins can be found on page 69 of the appendix.]

Chairman WATT. Thank you.

We will now recognize the members of the committee for 5 minutes of questioning each. And since Mr. Jenkins was in the middle of telling us about all the anticounterfeit stuff, I will give him the opening to go back to some of that by just asking him, you would think if $70 million a year is being counterfeited, that you would hear a little bit more about prosecutions and the things that you are describing to us. We don't seem to hear much about that. Why is that?

Mr. JENKINS. I am sorry. The last part of that, sir?

Chairman WATT. We don't seem to hear much about prosecutions, or investigations, or blowing up these counterfeiting rings. Why are we not hearing more about that?

Mr. JENKINS. Sir, a lot of these investigations begin overseas through our 22 international field offices. I believe in Fiscal Year 2009, through our investigative measures overseas, we seized over $100 million in counterfeit currency. We continue to work with the U.S. Attorney's Office as well as the district attorney's office domestically to fight counterfeiting. It is just not our stance to publicize our cases in the media, and that is probably one of the reasons why you haven't heard—

Chairman WATT. So you are saying the bulk of it is taking place outside of the United States? It is not a major problem inside our own borders?

Mr. JENKINS. That is correct, sir. The bulk of the counterfeiting is emanating out of Peru.

Chairman WATT. Okay. Mr. Moy, some of our Financial Services Committee members are somewhat concerned about the amount of money we are spending to promote the Presidential $1 Coin Program. And as part of our request for this hearing, we asked you to provide information about the costs that are being incurred for that program, and we did not receive that. So I hope you will provide that, if you don't have it with you today. We need that information.

Generally, I guess, the question would be with this program not being very successful in getting people to acquire these dollar coins, why are we spending so much money to promote something that people obviously are not taking to, and what is the rationale for that?

Mr. MOY. Yes. Mr. Chairman, first of all, we are doing a detailed accounting. And once that is done, I would like to submit that for the record so that you would have your answer.

To answer your question directly, the United States Mint, for the Presidential $1 coin, has spent $30 million to raise the awareness and to try to get this coin integrated into circulation. That money has been spent through an awareness program familiarizing Americans with the dollar coin, to pilot programs that adequately stock the banks, making sure retailers use it, and consumers are aware of it. All those programs have met with limited success. We have had success—

Chairman WATT. Is there some reason that we want to push this coin if the American people don't—what are the policy reasons that we would be pushing a coin?

Mr. MOY. The authorizing legislation said that it was the United States' mission with the dollar coin to analyze, identify, and remove all barriers to robust circulation. We have been attempting this now for 3 years. We have had limited success. For example, transit systems, like subways, are big users of the dollar coin. But, by and large, the dollar coin has not been received well in just cash register transactions. And at this point, we have tried every major idea that we can come up with, with limited success. And so the question is, how much more should we be trying with this?

Chairman WATT. We understand that we are shipping gold to Australia to be made into blanks, with the fabricated blanks shipped back to the United States for production. Is this efficient? Why can't the processing of these blanks be done in the United States?

Mr. MOY. It is efficient in that this is the easiest way to get the greatest volume of blanks that meet our specifications so we can make the bullion coins to satisfy investors' demand. We have tried to expand our ability to acquire planchets by requesting the limited number of suppliers to—we have gotten a greater percentage of what they produce. We have helped those suppliers increase their capacity, and we have constantly put out procurement requests for any suppliers, including domestic, to supply those planchets and blanks for us.

Since this effort, we have increased the number of companies supplying domestically by one, with one currently in process of con-

tracting. So we have increased our domestic suppliers, but they do have to meet our stringent standards because we are making so many of these things, and they do have to offer us an adequate supply of planchets so that it is cost-efficient for us.

Chairman WATT. Okay. The red light is on. That means my time has expired. And I recognize the gentleman from Texas, the ranking member, for 5 minutes.

Dr. PAUL. Thank you, Mr. Chairman. I want to follow up on that very subject with Mr. Moy, because I had some questions myself.

Has the Mint ever made planchets? Is that something they have ever done?

Mr. MOY. The Mint has made planchets in its past, but it got out of the business a decade ago mainly because of the extreme cost of doing it, the environmental hazard for doing it, and it was determined at that time that there were other private entities who could make it more cheaply and safely than the United States Mint could.

Dr. PAUL. Okay. And because of the shortage, you didn't have—and you had a mandate. You had to put them into the nonproof coins, that is correct; and you are asking now for authority to say that you can take some of that money out or coinage out and make proof coins.

Now, is this the first year that you have missed making proof coins in 2009?

Mr. MOY. Yes. This is the first year that we have missed.

Dr. PAUL. If the problem were corrected, is there such a thing as minting coins a year late? Because some of those collectors are thinking, oh, why can't I have a 2009 coin?

Mr. MOY. The Mint is required to basically sell the coins that are minted in the year that they are made. So if the date is 2009, we sell 2009 coins in 2009.

Dr. PAUL. The 2009 will be missing?

Mr. MOY. Is missing, and what we are trying to do is prevent 2010 from missing.

Dr. PAUL. It still baffles me that we can't make a planchet. I don't know anything about the equipment or what is necessary, but doesn't this country make jewelry and make complicated jewelry out of gold? Isn't this just pretty simple? This just really is confusing to me why this can't be accomplished.

Instead of looking for more planchets, you are saying, give me more authority so I can make a few of these proof sets, rather than figuring this out. What would a businessman do about this? Would he always resort to going to Australia to do this? It just seems so bewildering that a problem that seems rather simple, that we couldn't have had an easier solution for this. Right now, we don't even have a solution.

Mr. MOY. A businessman has to weigh two things. On one end, to make the planchets ourselves, we need to make capital investments in order to develop the smelters, the chemical processing, take care of the environmental hazard of getting rid of the chemicals, all those issues. And on the other side, you have a limited amount of planchet makers around the world who don't want to increase their capacity unless they get guarantees from government

that we will continue buying at such a high rate for some foreseeable future so that they can spread out their capital investment.

So those are the two choices. And right now, it is the most efficient choice to be able to expand the quantity of planchets that we are getting from the various suppliers.

Dr. PAUL. Now, there are private companies making, not coinage, but they make medallions, and I have never heard of them running out of planchets. Do you think they have that problem?

Mr. MOY. They don't, because they are not in a business of being the largest bullion maker and supplier in the world. Last year, we sold 28 million ounces of these. This year, we are headed to 32 million ounces. On an average year, the Mint might make 8 million ounces of this. So, the other people don't have to deal with the volume issues that the United States Mint does.

Dr. PAUL. This is awfully disturbing. What are we going to do when we go on the gold standard? We won't even be able to make the gold coins. You can't even keep up with a few collectors.

Mr. MOY. By that time, my term at the Mint will be done, and I will start a planchet-making company to pick up the excess.

Dr. PAUL. I don't know what it is, but it seems to me that there has to be a market answer for this. And maybe it is the promise to take these no matter how many they make. Maybe that would help. They are not going to lose their value, like it is a risky thing. But you are dictated by law that you have to promise these private sources on how many you can take?

Mr. MOY. We are not dictated by law, but just by business practice. When a company invests in expanding their capacity, they are going to want to make sure that investment gets paid off over time, and they are not willing to do it unless they get a commitment from their buyers to buy up all their excess capacity.

Dr. PAUL. It sounds like they don't trust the government. I don't know. Thank you.

I yield back.

Chairman WATT. You have another problem for the gold standard that we have identified.

The gentleman from Missouri, Mr. Cleaver, is recognized for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman.

To the first three panelists, it would seem to me that one of the things that you would want to sell with this proposal is the sustainability. If a $1 note lasts for approximately 21 months, and a $1 coin lasts for 30 years, it would seem to me that there is a very clear and real issue of sustainability.

Mr. MOY. Excuse me, sir. Is that question directed at me?

Mr. CLEAVER. Yes, to any of you.

Mr. MOY. Coins, because they are made of metal, are harder and last longer. We engineer our coins to make sure that they have a usable surface for at least 30 years. Many of our coins end up lasting 40 or more years. So there is an advantage for using dollar coins.

But Americans are creatures of habit. So they are very used to using the bill. They are not used to using coins in regular retail transactions.

One thing that we have seen some utility for is when you use it in a vending machine, without dollar coins, if you buy a $1 soda for $5, you get 16 quarters back. People find it a little more convenient to get four $1 coins back. But that has not been enough to change behavior.

So we are a little bit vexed, given the current co-circulation of both the dollar bill and the dollar coin, for how to make inroads for sustained utilization of the dollar coin.

Mr. CLEAVER. So, let's say a $1 bill has a life span of 21 months, how long would it take to phase out the $1 bill?

Ms. ROSEMAN. Actually, the $1 bill now lasts longer than 21 months. There have been efforts that both BEP and the Federal Reserve have taken over the years to extend the useful life of dollar bills.

Mr. CLEAVER. For how long?

Ms. ROSEMAN. It is about 3.5 years. We are planning to make further changes to Federal Reserve processing operations to extend the useful life even further. It won't approach the 30 years for the dollar coin, but I think there are a number of considerations that we need to take account of in weighing the dollar bill versus the dollar coin.

There is, as you alluded to, the cost to government. I think we also need to look more broadly at the cost to society in general, particularly to businesses that handle coin and currency and the differential cost to them.

There is also the issue that I think was brought up earlier with respect to public preference. Today, Americans have a strong preference for dollar notes. That may evolve over time. But that is the case for today.

Mr. CLEAVER. But the GAO says that they have that preference until you follow with a second question dealing with the fact that it would save a half billion dollars.

Ms. ROSEMAN. It is unclear—and I know the GAO, and we are also and I think others are looking at, in today's environment, what would be the savings to the government from looking at the dollar coin and the dollar bill. That study is just getting under way.

Mr. Jenkins would be able to address the counterfeit deterrence and detection features of coins versus notes, and if there was counterfeiting, how readily it would be detected.

And also, I think one of the other things we would need to take into consideration is the use of the dollar in other countries. Now, most use of the U.S. dollar in other countries has been more in the high denominations, but there are some economies that use the U.S. dollar for transactional purposes, as well. They are either dollarized economies, or they have the U.S. dollar co-circulate with their local currency. And as part of the cost equation, will U.S. currency be as attractive to them if the dollar coin were to replace the dollar note?

I am not clear at this point what the answer is, but I think those are all things that would need to be weighed in doing that evaluation.

Mr. CLEAVER. Mr. Jenkins, I think my time is up. So if you can do a small response.

Mr. JENKINS. Sir, it definitely would be an educational process for us to reeducate the American public on the detection of counterfeit coins. Currently, right now, through our 138 field offices and 22 international offices, we go out and educate the consumers out there on what to look for in counterfeit currency for all paper notes. So we would have to reeducate the general public on the detection of counterfeit coins if we did make that switch.

Mr. CLEAVER. Thank you.

Chairman WATT. I thank the gentleman.

The gentleman from Delaware, Mr. Castle, is recognized for 5 minutes.

Mr. CASTLE. Thank you very much, Mr. Chairman. I am pleased to be here. Unfortunately, my schedule is such that I am dancing around a little bit in terms of where I am going to be.

But I would like to welcome Michael Clark—who will be on the second panel—a coin expert and a friend of mine from Delaware. I deal with him on a regular basis.

And pursuant to that, Mr. Jenkins, I want to ask a question of something he had in his written testimony, which you haven't heard yet. I will read it to you. It says, "Our industry believes that Congress needs to take swift action to protect consumers from the increasing and systematic counterfeiting and subsequent marketing of collectible, numismatic, rare and investment-grade legal tender United States coins. As a first step, we ask that Congress direct the Treasury Department's Inspector General to conduct a thorough investigation of the sources and extent of such counterfeiting and report back to Congress on the results of that investigation 270 days after enactment."

In your mind, is that—I realize that it may be a little bit off of your department, but is that a reasonable request to be made by Congress?

Mr. JENKINS. Sir, to be quite honest with you, we don't see many cases involving counterfeit coins. I think, in the past 2 years, we have seen less than 100 cases related to counterfeiting coins, and 99 percent of those cases deal with collectors where one collector has made a purchase from another collector, and there is a discrepancy there. In cases where we do deal—

Mr. CASTLE. It is a discrepancy, but it is not a counterfeit?

Mr. JENKINS. It is one collector saying it is counterfeit, and the other collector saying it is genuine. What happens then, sir, is that it will be referred to the Secret Service. We will investigate it, and we will bring it into our labs here in Washington, D.C., to determine if it is counterfeit or not. And then, we will refer it out to one of our field offices. At that point, they will conduct the investigation. And then, we refer it to either the U.S. Attorney's Office for prosecution or the District Attorney's Office, and they would make the decision on whether there will be a prosecution or not.

Mr. CASTLE. I think I will drop that particular subject and go to something else, although I am not sure we have a complete answer at this stage.

I wanted to ask Mr. Moy a question about the America the Beautiful Quarters Program and how it is coming along. We all know the 50 State Quarter Program worked extraordinarily well. It may have produced seigniorage, I think in the area of $3 billion or

something of that nature. But I am not sure exactly where we are with the America the Beautiful Quarters Program in terms of production. Is production sufficient? I am not hearing as much about it as I did the 50 State Quarter Program. I would be interested in the Mint's views on that program and where it seems to be right now.

Mr. MOY. The short answer is that the program was launched late this spring. There have been two quarters that have come out, both the Hot Springs and Yellowstone. The orders for these quarters from the Federal Reserve are enough to meet demand, but the demand overall for quarters—not just these—is relatively low. So, for both Hot Springs and Yellowstone, the average Federal Reserve coin order has been about 50 million of these quarters. And that is compared to, at the end of the 50 State Quarter Program, when both the Mint and the Federal Reserve figured out what the right amount is, that right amount was between 350 million and 550 million quarters per issue. That is compared to early on in the 50 State Quarter Program, States like Virginia—at that time, nobody knew what the demand was going to be. So in order to meet anticipated demand, both the Federal Reserve and the Mint made about 1.6 million of Virginia State quarters.

So, comparatively speaking, the program is starting out slow because these quarters are much more difficult for consumers to get. As a result, the United States Mint has worked with the Federal Reserve to find alternate distribution mechanisms that don't tread on the Federal Reserve's responsibilities, such as allowing people to buy bulk bags, meaning bulk is 200,000 coins or $50,000 at the face value, which they can purchase directly from the Mint and pick them up at either the Denver or the Philadelphia Mint.

Mr. CASTLE. My time is about up. Did you say 50 million versus 350 million to 500 million?

Mr. MOY. That is correct, per issue.

Mr. CASTLE. Is that an economic issue in the terms of the need for quarters in general?

Mr. MOY. Yes, we believe so.

Mr. CASTLE. Thank you.

I yield back, Mr. Chairman.

Chairman WATT. The gentleman from Texas, Mr. Green, is recognized.

Mr. GREEN. Thank you, Mr. Chairman.

And I thank the witnesses for appearing. The information is greatly appreciated.

I am going to go into this line of questioning that deals with what I am calling an electronic cash society. There are other names, alternative transactions, for this.

But I noted from your testimony, Ms. Roseman, that from 1980 to 2009, the circulation increased to an average of 7 percent per year from 124.8 billion to 888.3 billion. And this is driven by demand that—much of which is international. I also noted in your testimony that the Federal Reserve estimates that as much as two-thirds of the currency is circulated abroad, which is a significant amount.

And I have not come to any conclusions about this. I really am interested in the answers. I am very much inquisitive, as you

might well expect, given that I personally use electronic transfer for most of my transactions. I understand the use of the debit card and how that is impacting society, the credit cards. Checks are still being used.

And then there are persons who are attracted to these plastic cards or other alternative transactions simply because of the interest-bearing nature of the currency. To hold currency is to lose money if you hold any large amount of it when you can have it in some sort of account wherein you actually are making money on your money.

So my concern or question—perhaps I should not say concern. My question has to do with whether or not we will find at some point that we will move aggressively or with some greater amount of speed to a society wherein we really do rely more on plastic than on the Federal notes that we carry and the coins that we carry but not quite as much, it seems to me, as we used to—we seem to lean more toward currency than coins for obvious reasons. But with that said, your thoughts, please, ma'am, in terms of our moving into what I am calling an electronic cash society.

Ms. ROSEMAN. The use of different payment mechanisms in this country is something that we have been very interested in tracking. We have tracked over time the use of noncash payment mechanisms. It is more challenging to determine how pervasively cash is used for transactional purposes because it is more difficult to count the number of cash transactions than it is for card transactions, checks, or wire transfers.

There is clearly evidence that there is some substitution taking place. Transactions that used to be done primarily in cash may be performed more frequently with debit cards and credit cards these days. Fast food restaurants, Starbucks, or other outlets that 10 or 15 years ago were largely cash-only, now have a growing portion of their transactions using cards.

But we are not sure whether actually the number of cash transactions in this country has started to decline. If it is still growing, it is growing at a very small rate, where electronic transactions are growing at a much higher rate.

So I do think that you are right, that over time there will be a continued substitution away from cash towards electronic payments. It is just unclear at this point how fast market forces will go in that direction. But I think the trend is as you suggest.

Mr. GREEN. Thank you.

I will just leave you with this comment. Perhaps you might want to respond. It seems that the technology is driving it simply because it is becoming so easy now to do this and to acclimate to it.

At one time, it was somewhat alien to us, but the vending machines now will accept credit cards and debit cards. Almost everything in life seems to be moving in this direction. I am talking about in terms of the necessity to use cash.

So it just seems that at some point, we will see an exponential increase once the technology becomes so pervasive that it is immediately available and accessible.

Would anyone else care to respond? If so, I am all ears.

Mr. MOY. Yes, sir. Given the Mint's experience, what we have seen in electronic transactions, the larger rate of growth has main-

ly come at the expense of checking. And so, when you take a look at checking's market share, that has dramatically shrunk and continues to shrink, whereas, what impacts a lot of the Mint's coin demand is retail sales.

What we have been able to extrapolate from cash used, dollar amount-wise, represents about one-third of all retail transactions. But over the last 5 years, it has been stable, one-third for 50 years. And in the last 5 years, that has eroded to about 29 percent. So you begin seeing that substitution in there. And when you anecdotally test that, you will find that customers are feeling more comfortable with it, but you have old guys like me who don't want to use a credit card for a $3 transaction.

Mr. GREEN. Thank you. My time has expired.

Thank you very much. Thank you, Mr. Chairman.

Chairman WATT. The gentleman's time has expired.

Mr. Lucas is recognized for 5 minutes.

Mr. LUCAS. Thank you, Mr. Chairman.

I come at the panel with several questions from several different directions.

First, Director Moy, it is always a pleasure to see you again. And to tee off with what my colleague from Texas was discussing about the planchette business, we get occasional reports here in Congress that there are entities in this country, manufacturers who would like to produce and provide those planchettes and that they believe they don't have an opportunity to compete. I know you will comment on that in just a moment.

But I would also note that I realize that the Mint got out of the business of making planchettes and assaying gold and silver in the 1960's. But you do have that cavernous, huge Mint building in Philadelphia that was designed for this very purpose. Maybe some of those rotating fund dollars you have, maybe they should be spent on what I suspect you have already done, which is a study to determine, is it more effective for the Mint to produce these products, the same kind of study that would project for the years to come how many planchettes that you would need, because, as you said, we are the biggest bullion sellers? We could provide some certainty here. And I think Mr. Paul and I probably would help you with the directive for the appropriations process if you need it to do this study. Let's apply that businessperson sense, and let's just see what the economics are.

To turn to Ms. Roseman, we have talked about dollars, and we have talked about 1 cent coins, so let's talk about the half dollar for a moment. Off the top of your head, how long has it been since the flow of half dollars out of the Federal Reserve Banks has been greater than the flow of half dollars from the public into the Federal Reserve Banks?

Ms. ROSEMAN. Each year since 2000, we had more half dollars deposited with the Reserve Banks than were ordered from the Reserve Banks.

Mr. LUCAS. So, essentially, 10 years since you have ordered new half dollars for circulation from the Mint. Any idea how many halves you have in the inventory system? You mentioned a billion of the dollar coins. How many half dollars?

Ms. ROSEMAN. We have 197 million half dollars.

Mr. LUCAS. But it has been 10 years since the flow has been greater out than the flow coming back in?

Ms. ROSEMAN. I am sorry. I have been corrected by my colleagues. Until 2004, we had a greater flow out than in.

Mr. LUCAS. One year out of 10, and yet it has been a decade since you have ordered new circulation pieces from the Mint. So, basically, it is a functioning obsolete denomination, too, along with the 1 cent, for all practical purposes, and the problems of the dollar coin.

Turning to Mr. Jenkins, discussing the counterfeiting stuff, I guess I have a couple of technical questions you may or may not be able to answer. But tell me, how many trained agents do you know that the Secret Service has who have the experience to be able to detect and work with counterfeit coins? By the way, since 1865, you have an awesome history of addressing counterfeit paper currency. How many folks do you have who really know anything about counterfeit coins?

Mr. JENKINS. Thank you for your question, sir.

We have a counterfeit lab here in D.C., where if we do get coins that are suspected of being counterfeit, we will actually analyze the coin to see the makeup of the coin to determine whether it is counterfeit or not. Any counterfeit coins that would come in would come into our lab here in D.C.

Mr. LUCAS. The reason I ask that, agent, is there are reports that come to us that Secret Service offices and, on occasion, field agents around the country tell members of the public and perhaps even some other law enforcement officers that they are really too busy chasing the paper fraud and the other paper currency fraud and the other things going on around to worry about counterfeit U.S. coins. I would hope that is just urban legend. I would hope that we are not telling people we don't have time to mess with counterfeit coins. Any comments on that?

Mr. JENKINS. Sir, I can assure you that the men and women of the Secret Service will investigate, whether it is a counterfeit coin or whether it is counterfeit currency on paper.

Mr. LUCAS. And there have been no directives of, "Don't waste your time on the coin side, focus only on paper?"

Mr. JENKINS. Absolutely not, sir. We just haven't seen the demand.

Mr. LUCAS. Thank you very much.

Now, we are supposed to be protected in this country, folks who are interested in coin collecting and the numismatic areas, by the Hobby Protection Act, which requires that copies be stamped with the word "copy" to make it very clear that they are not actual U.S. coins, that they are reproductions or whatever.

But one of the issues that again occasionally comes up in my discussions with folks who care about this is that because the Federal Trade Commission has jurisdiction or primary jurisdiction over the Hobby Protection Act, that confuses the chain of responsibility in pursuing these kind of cases for counterfeit coins and the selling of them in the U.S. markets. Do you have any insights? Is it more complicated because that particular issue involves the FTC versus perhaps a more straight-up issue about counterfeiting on currency?

Mr. JENKINS. To be honest with you, sir, I would have to research that further due to the lack of demand that I have seen from counterfeit coins that have come in to us. As mentioned previously, I think it is less than 100 cases we have in the last 2 years.

Mr. LUCAS. Mr. Chairman, will you indulge me with one more question?

Chairman WATT. Yes, sir.

Mr. LUCAS. I would also note, I think, by the reports that come to us, there are areas in the world where there are industrial-level efforts at manufacturing counterfeit U.S. coins. And not just ones that go through the vending machine down at the corner store, but pieces that are worth substantially more than the metal content. They are numismatic value. They are historic value, things copied from the 1790's and the 1800's and all this sort of stuff.

This is not the first time that this has gone on. There are reports that in the 1950's, 1960's, and 1970's that certain places in the Middle East counterfeited in great quantities U.S. gold coins, full weight, full metallic value simply because having Uncle Sam's stamp on the front provided a substantial surcharge. If that was the case, then that was most unfortunate. And those are still floating around.

There are reports in certain Asian countries, perhaps one of the biggest Asian countries, that this level of industrial counterfeiting is going on now. If that is indeed the case, then we are seeing the potential defrauding of many people who are purchasing these items unknowingly as legitimate investments or because of great appreciation for the perceived value. We need to do something about that.

And with that, I yield back my time to the Chair.

Chairman WATT. I thank the gentleman, and I thank this panel. I am not sure I want to go to a second round because we have a second panel. But it does seem to me that we have raised a substantial number of questions here that raise some issues that I think would cause me to ask this question with the unanimous consent of my colleagues here. Yesterday, the Washington Post ran this pretty extensive article about all of the proliferation of activities in response to terrorism and various entities not knowing what the others are doing and duplication and multiplication. And it seems to me that these four entities that are represented at the table here, some of these issues would be worth some collaboration on and—such as—we have reports, for example, that a number of studies have demonstrated that eliminating the penny, for example, would have a substantial regressive impact on poor people because they are—is anybody studying this? Is anybody talking about it, to give Congress advice about it?

This issue that Mr. Lucas raised, what kind of collaboration is going on between these four entities here? This is not all of the different entities that I saw in the Washington Post yesterday dealing with terrorism. This is four entities basically. How much are you all talking to each other? And what kind of authority do we need to be giving—do we need to be setting up a study commission to study some of these issues? Who is studying these issues so that they can make recommendations to Congress? If we have the statu-

tory authority to do this, we need to do it on an informed basis. We don't need to keep producing quarters that nobody is using. We don't need to keep producing dollar coins that nobody is using. We don't need to be producing more and more pennies unless there is some policy reason for it. Who is studying this? Is there a collaboration going on between the four entities? And what kind of authorization do you need to study some of these issues now that we have identified them?

Can somebody answer that for me? Mr. Jenkins? And then, we will go right down the line. And maybe then, we will close this panel out, unless somebody else has questions.

Mr. JENKINS. Mr. Chairman, in terms of communication, I think we all have a strong partnership together and we are on two committees where we meet on a regular basis to discuss issues that may be coming up, whether it is dealing with counterfeit currency trends or other issues that my other partners may have. So there is strong communication between the four entities at this table.

Chairman WATT. And out of that communication, is anybody communicating these recommendations of any kind to Congress so that we can act on them or do they not require congressional action?

Mr. Jenkins, that is the second part of my question, so then we will go right down the line.

Mr. FELIX. In terms of the currency design, the Secretary of the Treasury has that authority. It is not an authority that—it is a legislative authority. But to further Mr. Jenkins' point, we meet on a monthly basis to talk about some of the issues that impact not only counterfeiting, designs. At the Treasury Department, there are conversations and dialogues going on about the coin boundary mix and also about some of these issues. But certainly, the Federal Reserve has a major role and a major voice in this discussion, as well.

Ms. ROSEMAN. I would agree with respect to the level of collaboration among our four agencies. From the Federal Reserve's perspective with respect to studying certain issues, we wouldn't need additional legislative authority. I think that there may be opportunities in some laws to make changes to be able to address increasing inventories and other matters, some which we have raised in past reports to Congress, for example, on the Presidential Dollar Coin Act.

Chairman WATT. Mr. Moy?

Mr. MOY. Yes. I agree with my colleagues and further add that there are ways that we communicate the results of our collaboration, whether through reports on the Presidential dollar coin that are required on an annual basis to—during my confirmation hearings, one of the questions that was asked of me was—being 2006, that was the first year that making the coins exceeded their face value and what was I going to do about it as Mint Director. So that has spurred an initiative within Treasury Department to think of what the best solutions to that are. And as a result, you got that as a budget proposal in the Administration's Fiscal Year 2011 budget. So there are ways that we can communicate that to you. And based on the discussions here of the potential of the Mint doing a study on whether we should get back into the planchette

business, that is something we are going to explore when we get back.

Chairman WATT. The Chair notes that some members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

So maybe we will try to frame some kind of comprehensive question to ask you all to collaborate on and to give us some recommendations. This hearing kind of comes at a—this is July of the second year of the House term because we have been basically devoting most of our attention to the financial services meltdown in our committee. And who knows who will be the chairman or ranking member of the subcommittee in the next term of Congress. It could be anybody up here, on this side.

So, perhaps, the problem is one of continuity as much as anything else. But these questions do cry out. This is the medium by which we conduct business in this country. And I suppose all these people sitting in this audience are not here just by happenstance. They are here because they want to know what is happening with their dollars. And we need to be making good decisions about these issues. So with that—unless there are other questions—this panel will be excused. We thank you very much for your testimony, and we would encourage you to respond to any written questions that may be submitted to you either collectively or individually as we go forward. So thank you so much.

And the second panel, if they will come up promptly, so we don't get caught by votes at some point this afternoon. And while the second panel is coming up, I would ask unanimous consent for the following statements to be submitted into the record: number one, a statement by Mark Weller, the executive director of Americans for Commonsense—I think he has a perspective on the one penny; number two, a statement by James Mulroney, director of coin services of Brinks, Inc.; and number three, a Federal Reserve chart that explains parts of Ms. Roseman's testimony.

Without objection, those items will be made a part of the record.

We will now proceed with the second panel, the members of which I will introduce in abbreviated form. My apologies for not giving your long bios. We will put them into the record, but we don't want to get caught by votes and not have the opportunity to hear your testimony.

Our first witness on the second panel is Mr. Craig Hesch, chairman of the National Automatic Merchandising Association. Our second witness is Mr. Michael B. Clark, the president of Diamond State Depository. And our final witness will be Mr. Gary Marks, chairman of the Citizens Coinage Advisory Committee.

And you were present, I hope, when we gave the instructions about the lighting system to the first panel: green for 4 minutes; yellow for 1 minute; and then red means 5 minutes has expired, and we would ask you to wrap up as promptly as you can.

So, Mr. Hesch, we recognize you for 5 minutes for your testimony, being aware that your entire written statement, will be made a part of the record, so we would ask you to summarize.

STATEMENT OF CRAIG A. HESCH, CHAIRMAN, NATIONAL AUTOMATIC MERCHANDISING ASSOCIATION

Mr. HESCH. Thank you, Mr. Chairman. Mr. Chairman, and members of the committee, I am Craig Hesch, volunteer 2010 chairman of the board for National Automatic Merchandising Association, your vending machine people of the United States.

In addition, I am the chief financial officer of A.H. Management Group, a family business, my family and our third generation of business. It started out as a mom-and-pop operation and grew to the size that we are now. We provide vending snacks and beverages to companies throughout the Chicago land area.

Our national association, NAMA, is the trade association for the food and beverage companies, coffee service, and food service management industries. Our membership is comprised of service companies, equipment manufacturers, and suppliers of products and services. We have 34 affiliated State councils encompassing 36 States.

The vending industry is a $40 billion a year business, employing approximately 700,000 people who work at an estimated 13,500 companies. According to The Vending Times Census of the industry, there are approximately 5.3 million food and beverage machines in the United States.

Since 100 million Americans will use a vending machine each day, any changes in coins or currency will directly impact our membership and our customers. The industry could lose jobs if dramatic changes are made to coin or currency. To understand why jobs could be lost, it is important to understand the costs of a modern coin and currency acceptance system.

The coin and bill validator costs between $250 and $475 each. I have with me examples of a coin and a bill validator. This mechanism costs $450 and takes 20 minutes to install. If it needs to be reprogrammed to accept the new designs of a new U.S. Federal Reserve note or new metal content of a U.S. coin, it will cost, at a minimum, $100 per device, and take 20 minutes for a trained technician to travel to the location and reprogram the device. So changes could result in an estimated cost of at least $530 million just to this industry.

But an estimate of the cost may be much more complicated. For example, one NAMA member estimated that it would cost the industry billions of dollars when you consider all of the unattended point-of-sale locations. In addition to an estimated 5.3 million food and beverage machines, there are approximately 1.3 million amusement machines; 750,000 to 1 million gaming devices; 1.5 million to 2 million retail, car wash, and other specialty devices; 2 million, in addition, parking meters; and millions of coin and cash handling or currency counting devices in banks and retail locations currently.

And the more drastic the change to the coin and currency, the greater the cost of the engineering. If the unit is older and it requires new hardware or potentially an entirely new device, then the jump in cost is an additional $100 for low-end devices to $500 in the higher-end devices, such as you see here. The most common cost would be $300 to $400, in that range.

Examples of change which would require more costly upgrades would include coin size changes or notes that significantly differ in width and length from our current bills.

Regarding changes to the metal content of coins, we recognize that there is an increased cost of mining coins; however, changing the composition alloy, size, or weight of the coins could very well lead to expensive modifications to coin mechanisms by the vending industry.

NAMA generally opposes coins manufactured from multilayer plated materials, especially for higher value coins. Multilayer plated steel construction or other material changes to coins could have similar electronic metal signatures which may not allow coin validators to distinguish coins directly.

We also strongly oppose mechanical changes to coins, such as shapes, sizes or weights.

In my closing, because my time is up, in regards to currency, we support reasonable changes to U.S. currency to accommodate the visually impaired, but we must ensure that currency readers in vending machines can validate the currency. NAMA opposes any changes which will unnecessarily burden the thousands of small businesses which operate vending machines or to our customers, sir.

[The prepared statement of Mr. Hesch can be found on page 61 of the appendix.]

Chairman WATT. Thank you for your testimony.

Mr. Clark, you are recognized for 5 minutes.

STATEMENT OF MICHAEL B. CLARK, PRESIDENT, DIAMOND STATE DEPOSITORY

Mr. CLARK. Chairman Watt, Ranking Member Paul, and members of the subcommittee, thank you for the opportunity to address you today. I appear before you this afternoon as president of Diamond State Depository in Wilmington, Delaware, a subsidiary of the Dallas-based Dillon Gage group. Dillon Gage is one of the 12 authorized purchasers of the American Eagle Silver Bullion Coin from the United States Mint.

I also represent the industry council for tangible assets, the National Association for Rare Coins, Precious Metals and the Tangible Asset Industry.

This afternoon, I wish to discuss three issues, all related to coinage: first, the market impact of the Mint's continuing difficulties in keeping pace with the market demand for its American Eagle Gold and Silver Bullion programs; second, the desire among collectors and investors alike for an American Eagle palladium bullion coin; and third, the growing presence of counterfeit coins in the marketplace.

When Congress authorized the minting of the gold and silver bullion coins with the Gold Bullion Act of 1985, it created a wildly successful program for investors and hobbyists interested in the advantages that precious metals can offer in diversifying and stabilizing one's investment portfolio.

Today, the American Eagle Bullion Series, which includes gold, silver, and platinum products, is the dominant provider of bullion and coin investment products to the global market. The coinage

program has provided investors with a convenient manner by which to invest in silver, gold, and platinum bullion. Of course, these coins are also prized by collectors for their beauty. Strong investment demand, coupled with the global economic turmoil we have experienced in recent years, has paved the way for a bull market in precious metals investments.

In the past 3 years, the U.S. Mint has sold unprecedented volumes of American Gold and Silver Eagle Bullion Coins. Demand for these products has been so robust in recent years that the Mint at times has suspended the production of both its fractional Gold Eagle Bullion Coins, which are produced in 22 carat, and its 24-carat Buffalo Gold Bullion Coin.

Moreover, in late 2008, production of the American Eagle Gold and Silver Proof and Uncirculated Coins was suspended because of the exceptionally strong demand for the bullion coins. The Mint has allocated all available gold and silver bullion blanks to the production of the American Eagle Gold and Silver Coins because the United States is required by law to produce these coins "in quantities sufficient to meet public demand." As a result, collectors that prize the Proof and Uncirculated Coins are being denied the opportunity to purchase these products.

While the Mint's inability to keep pace with demand has had a negative and unnecessary impact on the investment and hobby community, it has also caused frustration among the Mint's main marketers, its authorized purchasers. On many occasions, the Mint has had to ration coins amongst the purchasers, causing havoc in the distribution system.

At the heart of the problem is the Mint's inability to sort sufficient blanks from multiple producers. Its reliance on just three suppliers is flawed. Moreover, there is some irony in the fact that Congress requires the Mint to procure gold for the Bullion Eagle Coins from newly mined U.S. deposits, but then the Mint shifts the gold to Australia, as we have heard, to have them made into blanks. Then, the fabricated blanks are subsequently shipped back to the United States for production of the coins. The inefficiency of this system is obvious. It seems that we should be able to create jobs at home by sourcing these blanks in the United States and eliminate the cost for the intercontinental shipping.

We wish to recommend that Congress take the following actions: one, authorize the Mint to produce both Proof and Uncirculated versions of the Gold and Eagle—Silver Eagle Coins, regardless of the demand requirements for the bullion coins to ensure an uninterrupted supply to the market; two, direct the Government Accountability Office to undertake a review of the Mint's procurement process for blanks and to seek its recommendations on what can be done to improve it; and three, require the Mint procure the blanks for its bullion programs with sources within the United States by 2014.

Our industry also believes that Congress should broaden the offerings of the American Eagle Bullion Coin Program by authorizing the Mint to produce a palladium bullion coin investment coin. While principally an industrial metal, much like silver, platinum and palladium, palladium is also favored by investors because of its rarity. Palladium is similar to platinum in composition and appear-

ance. Palladium is mined in only a few nations, and the United States is the fifth largest producer of this rare white metal. A 1-ounce palladium coin would offer the precious metals investor an interesting price point for entry, as gold trades currently at about $1,200; platinum over $1,500; and palladium at about $450 an ounce.

Lastly, a palladium bullion coin would create or maintain U.S. mining and refining jobs. In addition to mining jobs in Montana, palladium is refined in New Jersey, California, and South Carolina.

Unfortunately, I have run out of time. I was going to speak about the counterfeiting issue, but my time is up. So it is in my submitted testimony, of course.

I thank you for the opportunity to address the subcommittee, and I would be happy to answer questions at the conclusion.

[The prepared statement of Mr. Clark can be found on page 47 of the appendix.]

Chairman WATT. I suspect you will get some questions in the question-and-answer period. It will give you an opportunity to elaborate on that.

Mr. Marks, you are recognized for 5 minutes.

STATEMENT OF GARY MARKS, CHAIRMAN, CITIZENS COINAGE ADVISORY COMMITTEE

Mr. MARKS. Chairman Watt, Ranking Member Paul, and distinguished members of the subcommittee, thank you for the opportunity to address the matter of design quality for the coins and metals produced by the United States Mint.

I am the chairman of the Citizens Coinage Advisory Committee, commonly known as the CCAC. In 2003, Congress created the CCAC to advise the Secretary of the Treasury on any theme or design proposals relating to circulating coinage, bullion coinage, Congressional Gold Medals, and national and other medals produced by the Secretary of the Treasury, in accordance with Section 5111 of Title 31 of the United States Code.

As a committee designed specifically to advise the Secretary of the Treasury, the CCAC serves in an independent capacity from the United States Mint. Over the past 3 years, members of the CCAC have expressed concerns to Mint officials that the design proposals for various metals and for circulating and commemorative coinage have at times lacked the appropriate quality for the United States of America.

Specifically, the lack of design quality has been evidenced in designs that are cluttered and lack focus—and I have included these exhibits along with my submission—the use of design devices that are so small they cannot be readily discerned by the naked eye, and the use of what I call storyboard depictions that attempt to illustrate design themes in literal terms rather than through the use of allegorical or symbolic devices. And historically, some of this Nation's most acclaimed coin designs have been achieved through the effective use of allegory and symbolism.

In other instances, the CCAC has been provided a single design proposal for a medal and asked to make a recommendation. If the CCAC finds the design unacceptable or lacking, production

timelines are often so tight that the Mint is unable to provide alternate designs for review.

In a similar vein, the CCAC was recently provided a set of three proposed designs for the obverse of the silver dollar for the 2011 Medal of Honor Commemorative Coin Program. All three designs were virtually the same, except for a few very small variations.

When the choices we are asked to make become nearly meaningless for the lack of variation or because only one design is proposed, the ability of the CCAC to effectively administer its advisory role is severely diminished.

In a recent review of the 2011 United States Army and Commemorative Coin Program, the CCAC was presented with a design showing a United States soldier pointing a rifle in the direction of a United States Army helicopter, giving the unintended and unfortunate appearance of trying to shoot it down. In another example, the Army emblem was rendered with inscriptions reversed from their official position.

Despite these examples, members of the CCAC have been hopeful that necessary changes would be made and, in fact, that a renaissance in United States coinage design would occur.

This hope has been founded in a vision articulated by Mint Director Edmund C. Moy, in 2007. During the Art Medal World Congress held in Colorado Springs in September of 2007, Director Moy issued a stirring call "to spark a neo-renaissance for coin design and achieve a new level of design excellence."

I count myself as a strong supporter of the vision to bring about a neo-renaissance, as the Director has called for, and I know many of my fellow members on the CCAC share the same or similar convictions and desire to see a true modern revival of excellence for the designs of our Nation's coinage, yet nearly 3 years after the Director's call for design excellence, members of the CCAC continue to express dissatisfaction with the Mint's design proposals.

Let me be very clear. It is not my intent to find blame or point fingers, but rather to identify what must happen going forward to bring about the positive change we desire.

Let me also be very clear that the Mint's art staff is highly skilled and very capable of producing high-quality designs. I have seen moments of genius in these artists, and I believe the answer will be found when we discover what changes in the process need to be made to liberate them to perform at their full potential.

Therefore, acting in my statutory role as the CCAC's chairman, I recently appointed a Subcommittee on Coin Design Excellence comprised of five members of the committee. I have given the subcommittee the task of investigating the Mint's design processes, identifying what changes would lead to improved designs and, subsequently, to develop recommendations designed to further these changes.

It is my intent that such changes would be issued by the full committee to the Secretary of the Treasury within the next several months. Once the committee has issued its design quality recommendations, I would be pleased to provide copies to this committee or any members who might be interested.

The CCAC's Fiscal Year 2009 annual report has just been released, this document here, and it is available to all interested parties in the room if you would like to know more about us.

Thank you for the opportunity to report to you on the design quality issue and the CCAC's recent efforts to develop recommendations for improvement. I would be very pleased to answer any questions you might have.

[The prepared statement of Mr. Marks can be found on page 76 of the appendix.]

Chairman WATT. Thank you for your testimony.

And I thank all three witnesses for their testimony.

I will now recognize the members for questions.

And, Mr. Marks, I was thinking, apropos to my closing comments on the first panel, that the CCAC might be the appropriate body to be doing some of this. But it sounds like you all are being marginalized to some extent, and maybe that wouldn't be the appropriate body if you get marginalized.

Do you see the kind of consultation on a number of these issues going forth, or is your portfolio only with the design of coins and currency?

Mr. MARKS. Our statutory role is limited to design and themes for designs. I think, essentially, the Mint is a manufacturing operation, and because of that, there are production schedules. And I think that dictates a lot of what happens with the Mint.

In recent years, the last decade or so, there has been a flourish of legislation with various commemorative programs, both circulating and more of the numismatic type that I think have taxed the capacity of the Mint. That is my personal observation.

And unfortunately, groups like mine, the CCAC and the Commission on Fine Arts, typically are at the end of the design process. So, by the time a design reaches us, having sufficient time in the production schedule to react to our input I think sometimes is very limited, and sometimes, as I have indicated in my testimony, we are somewhat marginalized.

Chairman WATT. I assume both Mr. Hesch and Mr. Clark, you would support giving the Mint and/or other bodies, the four who appeared on the first panel, greater research and development authority on alternative metal compositions for circulating coins and, I suppose, numismatic coins also. Do you have any comments to make in this area?

Mr. CLARK. Thank you, sir.

I believe our industry feels as though the present system is probably best. I like one idea that I heard I think from Congressman Paul.

Chairman WATT. The present system being—

Mr. CLARK. That Congress has the authority.

But the recommendation earlier, the suggestion earlier that the Mint and its resources be brought to bear to bring about recommendations for the Congress to consider seems it would be the most logical approach in our minds, I believe.

Chairman WATT. I think that was actually my opening statement comment as a suggested alternative.

Mr. Hesch?

Mr. HESCH. NAMA definitely supports the idea of giving the U.S. Mint and the Bureau of Engraving the authority to do research and conduct research.

However, we do hope that Congress will retain the authority to allow such changes.

Chairman WATT. And that is so that it doesn't get made regularly and have an adverse impact, I suppose, on your industry?

Mr. HESCH. Yes.

And we do have a very good working relationship with both, I might add, but again, the costs associated to dramatic changes or any changes are so large to our industry that we want to be able to monitor them.

Chairman WATT. Mr. Hesch does your industry have a position on whether we should retain the statutory requirement that refined gold and silver must first be used to meet bullion demand as opposed to being used in numismatic—

Mr. HESCH. Our association has no position on that at this point in time.

Chairman WATT. I take it, Mr. Clark, you have a bigger dog in that fight?

Mr. CLARK. We do, sir, yes. We believe that the Mint should be authorized to produce the Proofs and Uncirculated along with the bullion coins. And it would seem logical that it could be done in some proportion. But under the current system, the collectors of the Proofs and Uncirculated Coins are sort of being shut out of the market, quite honestly, because there are no products for them to buy from the Mint.

Chairman WATT. Is the collection of numismatic coins a profit center for—we are obviously encouraging collection, but wouldn't the primary role of these agencies be to deal with the circulation and economic value as opposed to collection?

Mr. CLARK. Part of the U.S. Mint's mission, as I understand it, is to satisfy the demands and desires of the collector community as well as provide circulating coinage at the same time. So I don't think their mission—that they are mutually exclusive requirements.

Chairman WATT. One final question. This palladium suggestion that you have made, would that help to solve—how much of the undersupply would that help to solve, in your estimation?

Mr. CLARK. We do believe it is an ideal price point for many investors. And as a result of producing a palladium coin, we believe it would have the effect of reducing the burden on the Mint for Silver Eagle production because the Silver Eagle coins are priced roughly at $20 to $21, $22 right now, whereas the palladium bullion coin would be in the $450 market—price range, excuse me. And it would no doubt attract some of the investors who forego the higher priced $1,200-plus gold bullion coin and the $1,500-plus platinum coin. It would provide us an excellent alternative for the lower-priced coin investors.

Chairman WATT. My time has expired. I was tempted to ask you about the value of all of these Kennedy half dollars I have in my safety deposit box, but I won't do that on the record.

My colleague, the ranking member, is recognized for 5 minutes.

Dr. PAUL. Thank you.

Chairman WATT. Diminishing value, I take it.

Dr. PAUL. They may have some silver left in them.

I have a question for Mr. Clark. Why do you think the Mint only uses three suppliers to provide these planchettes?

Mr. CLARK. I would like to be able to understand that, but I have no firsthand knowledge.

Dr. PAUL. If you know the business, are there other people who can make them in the country?

Mr. CLARK. I believe there are other companies out there that are very interested in offering their services to the Mint.

Dr. PAUL. And I understand that they are not restricted by the law to these three individuals. They have the authority to do it.

If we get the palladium coin, we are still going to have that same problem; where are we going to get the planchettes? Because they can't even supply the demand right now.

Now, you suggested that we get the GAO involved and take a look at all of this and see if we can get recommendations. And I am just wondering how much we really need this. Is there any other way to get some professional or political advice on this without an audit? Or do you see the audit as something very, very important?

Mr. CLARK. Are we talking about the planchettes or the palladium coin, sir?

Dr. PAUL. Your recommendation for the audit to review the Mint's procurement processes for the blanks.

Mr. CLARK. We thought an outside agency looking at their process and why—to answer your question, why they are restricting sources to only three separate entities, someone with a separate set of eyes and kind of a fresh look might be able to determine that there is a better way to go about it. That is why we are making the recommendation.

Dr. PAUL. And your other recommendation was that we require all the planchettes be made here in this country.

Mr. CLARK. We believe there is sufficient capacity within the U.S. borders to do so.

Dr. PAUL. Do you think there is a lot of difference, a net difference in making these coins if we didn't require that the gold came from this country? Isn't gold generally pretty fungible? Does that make a big difference?

Mr. CLARK. I think the interest in—Congress' interest at the time they passed that requirement, of course, back in 1985, was to promote the sale, the job creation amongst American mining companies that domestically produced gold be used for the American bullion coin programs.

But you are right, obviously, gold is fungible, and conceivably it could be acquired anywhere. I don't think that is part of the problem. I think there is a sufficient gold supply. It is just the actual fabrication of the planchettes for some reason is limited to three separate sources at the current time.

Dr. PAUL. Yes. It just seems to me, like I mentioned earlier in our hearing, that this problem seems to be unique to government. If the private industry is doing this, they just don't run into this. Some of this, I think, just like the emphasis in 1985 to—I use domestic gold and all, I can understand that. But it certainly is—we

are a long way away from a business person adjusting for supply and demand and doing it at the best price. There is no way that the government can compete with private industry in even making a coin these days. But I was just wondering about how strongly you felt about that. But I really don't have any other questions, and I am going to yield back my time.

Chairman WATT. I thank the gentleman.

The gentleman from Texas is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. I thank the witnesses as well.

Mr. Hesch, your testimony was very insightful. You provided a lot of intelligence that I think a good many people were just not aware of in terms of the costs associated with making a transition from one coin to another. Your industry went for a very long time without accepting currency within the automated machinery, and then you made that transition to currency. And currently, I assume, if you—not all have, but you are making a transition now to plastic or alternative forms of promoting these transactions. How rapidly is this taking place from the coinage, to the currency, to what I am going to call plastic?

Mr. HESCH. It kind of depends upon what generation you are from, to be quite honest. What we have experienced is the younger generation obviously does not carry cash and coin. I have two daughters, 28 and 26, and they don't carry cash with them. I understand that. Our industry is definitely moving toward a cashless or a credit-based system.

Up until not that long ago, it was very expensive for microtransactions to take place on the cost that we had to issue back for the credit card usage. So as that barrier has been breaking down, we have becoming more intrigued and putting out more credit card acceptance devices on equipment. It is a cost that we encumber both on the up-front charge as well as on the back-side charge.

But we have to obviously take care of all of our customers. So, yes, cash and credit are coming on every machine. As far as acceptance, that is kind of tough. It depends upon the generation.

Mr. GREEN. I understand that. I think I am with your daughter's generation. I rarely carry cash; I use credit cards, for various and sundry reasons.

Now, you talked about the costs associated with making the change. Do you have an adequate means by which you can convey your concerns to those who have the hands-on experience with making the change? Is this the means by which you communicate your message, primarily through us in hearings like this? Or is there some other means by which you can adequately convey your message?

Mr. HESCH. Actually, both; here in front of you to convey our message to you, who actually are telling or are letting them do what they want. But we do have a working relationship with the BEP as well as the Mint. We know both gentlemen very well as far as our President. We do work on both sides, if you will, sir.

Mr. GREEN. And to this end, you made mention of the costs associated with this. Are you of the opinion that these things are given consideration when changes are made such that your industry is

not adversely impacted to some astronomical degree? I am confident that you are always adversely impacted.

Mr. HESCH. Absolutely, sir. We did go through. When the BEP did come up with the new bills, our industry did get them for a period of time to be able to test them, to be able to find out what changes needed to be made on our currency acceptors, etc. So, yes, we do have a working relationship.

As far as coins, we haven't gotten to that point yet. Obviously, we don't take pennies; we take nickels and above. But the electronic signature is of concern to us because not only will we have to accept what we currently have, we will have to accept potentially what is being manufactured. And again, in my statement, the alloy is a concern, not as much of a concern on the lower denominational coin, but when you start talking size, shape, diameter, that impacts our industry on a much more larger level, much more larger.

Mr. GREEN. My final question would be this: In making the transition to what I am calling plastic or electronic credit, if you will, what is the most significant obstacle that you are having to deal with that we here in Congress might have an opportunity to give some assistance with?

Mr. HESCH. We are talking to Members of Congress as far as initiatives that we are looking at for equipment investment to be able to do certain things, such as credit card acceptance. Not only do we have that, we also are on the green side, if you will, because we are bringing something to people at either where they work or a place where they are at. We are bringing a convenience to them so that they don't have to go somewhere else. So in reference to that, we are trying to look for places through initiatives here in Congress to be able to get some capital to be able to improve what we are able to offer.

Mr. GREEN. Thank you, Mr. Chairman. My time has expired.

Chairman WATT. Thank you.

And the gentleman from Oklahoma, my friend Mr. Lucas, is recognized for 5 minutes.

Mr. LUCAS. Thank you, Mr. Chairman.

Mr. Hesch, I apologize for being out of the room for part of your oral testimony. But reading your statements here, in an earlier panel, I inquired about the nature of what would be defined as obsolete coins and what is not. You are the best example of an industry that is using them each and every day.

Mr. HESCH. Yes, sir.

Mr. LUCAS. What percentage would you guess that go through your machines are half dollars, quarters, dimes, nickels?

Mr. HESCH. The majority of the coinage that goes through our machines would be quarters.

Mr. LUCAS. Followed by dimes?

Mr. HESCH. Followed by dollar coins. I would say quarters, dimes, dollar coins, nickels. No half dollars. We don't even take half dollars, sir. I am sorry.

Mr. LUCAS. Absolutely. And you make the point in your testimony that whatever we do, it is important to maintain that consistent alloy, that electronic signature that you referred to.

Mr. HESCH. Consistency is key.

Mr. LUCAS. So, in fact, thinking to the earlier discussion, if the 1-cent piece went away, the half dollar went away, your folks wouldn't notice it at all—minimally.

Mr. HESCH. Minimally. If the penny went away, no.

Mr. LUCAS. And on the 5-cent piece, which we have had much discussion here, historically we have not always used this particular combination, this particular size in the past. The 5-cent piece was of the same alloy as the larger ones. Fair enough.

Let me turn to Mr. Clark and anyone on the rest of the panel. Let us expand for just a moment on the counterfeit issues. I think, Mr. Clark, in your testimony, you mentioned that the estimation on sales of products that were alleged to be legitimate U.S. legal tender, perhaps defined as collector coins but not, could be as high as $5 billion?

Mr. CLARK. Yes, sir. By some industry estimates, it could be as high as $5 billion.

Mr. LUCAS. Could you expand for a moment on that problem? Since we are talking about not just a few thousand dollars or a few hundred thousand dollars, but billions, could you expand on that issue and what your folks are encountering and seeing?

Mr. CLARK. There have been written reports and discussions at our gatherings, estimates made of as many as 1 million counterfeit in numismatic coins being brought into the U.S. marketplace last year. They come primarily from the Far East, as you mentioned earlier. There are some very sophisticated and extensive capabilities in certain parts of the Far East, where it is legal to produce replicas, which we would probably consider as counterfeits once they come into this country. And the issue is critical within our industry, because even our own experts sometimes have a difficulty distinguishing an authentic coin from a replica or a counterfeit.

Mr. LUCAS. And, Mr. Clark, I have seen reports that on occasions these pieces come into the country packaged or encapsulated in what are purported to be systems to verify the authenticity by third-party grading services not only counterfeiting the coin, but counterfeiting the package that implies the coin is real. Have you seen those reports?

Mr. CLARK. We have. And this is correct. It is happening. There have been reports of the exact same coin with the exact same serial number.

Mr. LUCAS. As long as they have a verification package.

Mr. CLARK. Yes, exactly, on the package having been replicated. The two most well-known services are NGC, the Numismatic Grading Company, and PCGS, which is the Professional Coin Grading Service, are the most widely recognized throughout the world actually, and are the most replicated in that country, counterfeited in ours. And we have seen multiples of the same replicated coin packaged in the exact same container, bearing even the same serial number, but they are so good and they are so authentic looking, as I said, it is sometimes difficult for the experts to distinguish between the two.

Mr. LUCAS. And for the benefit of the panel, Mr. Clark, we are talking about things that, by creating this appearance, by adding the appearance of this packaging, we are not just talking about a $20 gold piece selling for whatever an ounce of gold is selling for,

we are talking about potentially for thousands of dollars above and beyond metallic value.

Mr. CLARK. Yes. They can range from several thousand dollars to—I have seen certified coins in excess of $1 million in value, in market value.

Mr. LUCAS. So clearly, this is an area where law enforcement and all of the appropriate entities need to be aggressive. And this is not just selling to tourists on the street somewhere, these are Internet marketers, these are a variety of sources moving this product. Is that a fair statement?

Mr. CLARK. That is correct. Yes, sir, I agree with that.

Mr. LUCAS. Thank you, Mr. Chairman.

Chairman WATT. The gentleman's time has expired.

Mr. Cleaver is recognized.

Mr. CLEAVER. Thank you, Mr. Chairman.

This is an amazing place to be, because if somebody had told me that there was an Automated Merchandising Association in the world, I would have challenged it. Since I have been here, I have never seen anything that does not have an association. And I also would contradict your industry.

I am in an industry where people leave their change at a higher level. I am in the church, and more change is left in the church than in any of the machines. People are adverse to a silent offering in church.

The other thing is that—and I don't want to be insensitive, but most of the industries, when we proposed seat belts, the automobile industry said, this is going to collapse our industry. And then when we required air bags, they said, this is going to do it for sure. And in any industry, we always hear that. So I don't mean to suggest that there won't be costs involved, because obviously there will be.

And the other issue—and I said this to the last panel—it would seem to me—and you did speak on the issue of sustainability, I think, for a lot of people, certainly for me, is a much more sellable issue if the coins could be melted and then reformed into strip metal for making new coins. And it seems to me that is something that we ought to be involved in. I wouldn't be surprised if some of the Treasury stimulus money does not deal with sustainability, even in the coins.

My question is, I have a stack of coins. My grandfather used to give us silver dollars for Christmas. And my generation, which is the younger generation—you earlier suggested that this might not be it, but this is it, the younger generation. We got silver dollars for Christmas. It was a big deal. And so, I am wondering about the Peace silver dollar and then the one with Eisenhower and the Liberty Bell on the back. I am wondering, what are we going to—this is a question for the people who left, but I am just hypothetically just throwing it out. What do we do with all of those coins? How would your industry deal with all those coins?

Mr. HESCH. As far as the coins that are not in true circulation, those actually go to the bank, and the bank either deposits them through the Fed or retains them. That is how our industry deals with them.

Mr. CLEAVER. With a $1 value.

Chairman WATT. You need to ask Mr. Clark, because they may be valuable.

Mr. CLEAVER. Do I have more money coming?

Mr. CLARK. The question is, what happens to the coins if new coinage was to be introduced?

Mr. CLEAVER. Yes.

Mr. CLARK. Undoubtedly, they would become collector's items.

Mr. CLEAVER. Worthless?

Mr. CLARK. Collector's items, meaning they might be worth more than their face value, depending on things like the mintage, the number produced in any given year, the condition of those coins. But if they are no longer being produced or circulated, they will find their way into hobbyists' collections and just amateur collectors.

Mr. CLEAVER. I am for this, Mr. Chairman. That is my last question. Thank you.

Chairman WATT. You should give up now. I just made you a millionaire, see?

The Chair notes that some members may have additional questions for this panel, which they may wish to submit in writing. And without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record. If everything has been done for the good of the order, I think I will thank these gentlemen for your testimony and encourage you to respond, if you get written questions, as promptly as you can.

The hearing is adjourned.

[Whereupon, at 4:50 p.m., the hearing was adjourned.]

A P P E N D I X

July 20, 2010

OPENING STATEMENT OF REP. MELVIN WATT

Hearing Entitled, "The State of U.S. Coins and Currency"

Tuesday, July 20, 2010

In general, the purpose of this hearing is to examine the current state of coins and currency in the United States. The U.S. Mint, Bureau of Engraving and Printing, Federal Reserve and U.S. Secret Service are jointly responsible for the circulation of all U.S. coins and currency and anti-counterfeiting measures to protect the U.S. money supply.

There are several specific issues we would like to explore in some detail in this hearing. First, how effective are the government's anti-counterfeiting measures? Some have estimated that in 2009, the amount of counterfeit notes passed was approximately $70 million, an amount that has been increasing in recent years. There have also been reports from the United Kingdom that £1 and £2 British pound coins are being counterfeited at an increasing rate. So we need to know, what steps are being taken by the U.S. Mint to prevent counterfeiting of U.S. dollar coins and what is the

government's plan going forward to combat the increasing counterfeiting of notes that costs taxpayers millions of dollars per year?

Second, what is the government's response to the worldwide rise in the price of metals used to manufacture coins? Some reports suggest that it actually costs more to manufacture the penny and the nickel than these coins are now worth. The Administration has proposed legislation to amend 31 U.S.C. §5112 to allow the Treasury Secretary to prescribe the metal composition of all circulating coins, including the penny, nickel, dime, quarter, half-dollar and $1 coin. However, some have raised concerns about this proposal because by statute only Congress has the authority to prescribe the metal content of circulating coins. We need to evaluate alternatives, such as perhaps granting the U.S. Mint research and development authority to research alternative metals and report these research findings back to Congress, while retaining the authority of Congress to determine the metal content of coins.

Third, is there an oversupply of certain coin denominations? Some reports suggest that there are up to $1 billion in dollar coins and other low-denomination coins being stored in large quantities by the Federal Reserve

and partner companies. We need the Fed to either confirm or refute these reports and, if the reports are confirmed, we need to know what efforts the Fed is taking to reduce these coin surpluses and more efficiently manage the nation's money supply.

Fourth, some dealers and collectors of numismatic coins have indicated that the U.S. Mint is not keeping up with the demand for numismatic coin products. Current statutes require that all refined gold and silver must be used first to meet bullion demand. We need to evaluate whether it would be a good idea to divert refined gold and silver from the bullion program to meet demand for numismatic products and what impact this would likely have on the supply of metals for bullion products.

While there are many other important issues related to the state of U.S. coins and currency, the four issues I have outlined should allow for a robust exchange. While we are not attempting to address this issue today, one other important topic that we need to explore in the near future is the issue of equal access to U.S. currency by the visually impaired. The Bureau of Engraving and Printing has issued a Proposed Rule that is open for public comment until mid August and the BEP expects to issue a Final Rule in the

Fall of 2010. While I thought it would be inappropriate to put the BEP in the awkward position of commenting on a Proposed Rule while the Rule is in the comment period and in the process of being finalized, when the Final Rule is issued it would certainly be appropriate to have a hearing on this and related issues. It, of course, is important for the visually impaired to have equal access to U.S. currency and for the Congress to ensure that the BEP's Final Rule accomplishes that result.

Michael N. Castle

Opening Statement of Michael N. Castle
Hearing on Coins and Currency

Thank you Mr. Chairman.

I have been a proponent of many important programs involving coins over the years, and have sponsored legislation to create the 50 State Quarters Program and the new America the Beautiful Quarters. I became involved in this effort when coin collectors presented a great idea for a new program to feature each of the 50 states on the quarter. I was not thrilled with the idea of getting rid of the traditional George Washington featured quarters until, I found out that the program would actually make money: as seigniorage would return millions, if not billions, to the General Treasury.

Earlier this year, the U.S. Mint issued their report on the success of the 50 State Quarters Program, which found that the program brought in $8.6 billion in revenue, generating $6.3 billion in seigniorage ($3 billion more than regular quarters would have produced). It is my hope that the America the Beautiful program, which began this year, will enjoy the same success of its predecessor.

...I am also pleased to welcome Michael B. Clark of Wilmington, Delaware, who is a witness on today's second panel. Mr. Clark has had a long career in precious metals as evidence by his work in managing Wilmington Trust's Precious Metals Services Division, to establishing the Delaware Depository Service Company LLC, to his current role as President of Diamond State Depository. His service and many contributions to the precious metals and certified coin industries over the years, earned him the Industry Council for Tangible Assets' first annual "Chairman's Award" in 2008.

Thank you Mr. Chairman, I yield back.

Congressman Ron Paul
Financial Services Committee
Subcommittee on Domestic and International Monetary Policy, Trade, and Technology
The State of US Coins and Currency
Statement for the Record
July 20, 2010

I oppose the Mint's current efforts to gain greater power in determining the composition of circulating coinage. It is unconstitutional to delegate the determination of the metal content of our coinage to the Secretary of the Treasury. Under Article I Section 8 of the Constitution, the Congress is given the power to coin money and regulate the value thereof. It is a shame that Congress has already unconstitutionally delegated its coinage authority to the Treasury Department, but that is no reason to further delegate our power and essentially abdicate Congressional oversight.

Oversight by members of Congress, who have an incentive to listen to their constituents, ensures openness and transparency. Legislation to delegate added authority to the Mint would eliminate that process and delegate it to unelected bureaucrats. The Secretary of the Treasury would be given sole discretion to alter the metal content of coins, or even to create non-metal coins. Given the history of Congressional delegation and subsequent lax oversight on issues as important as the conflict in Iraq, it would be naïve to believe that Congress would exercise any more oversight over an issue as unimportant to most members as the composition of coins.

While I sympathize with the aim of saving taxpayer dollars by reducing the cost of coinage, it is disappointing that our currency has been so greatly devalued as to make this step necessary. At the time of the penny's introduction, it actually had some purchasing power. Based on the price of gold, what one penny would have purchased in 1910 requires 57 cents today. It is no wonder then that few people nowadays would stoop to pick up any coin smaller than a quarter.

Congress' unconstitutional delegation of monetary policy to the Federal Reserve and its reluctance to exercise oversight in that arena have led to a massive devaluation of the dollar. If we fail to end this devaluation, we will undoubtedly hold future hearings as the metal value of our coins continues to outstrip the face value.

One of the witnesses on our second panel mentions the importance of the Mint's production of bullion coinage, and the danger of counterfeited collector coins that may or may not be minted from silver or gold. It is a shame that instead of protecting the value of the dollar to ensure that precious metal coins could still circulate as money, or enforcing counterfeiting laws to stop the flow of clearly fraudulent coins, the federal government insists on printing trillions of dollars out of thin air, and prosecuting individuals who attempt to create precious metal currencies to compete with the devalued US dollar.

The topics discussed in today's hearing exemplify how far we have fallen, not just since the days of the Founders, but only in the last 75 to 100 years. We could not maintain the gold standard nor the silver standard. We could not maintain the copper standard, and now we cannot even maintain the zinc standard. Paper money inevitably breeds inflation and destroys the value of the currency.

Statement
of
Mr. Michael B. Clark, President
Diamond State Depository

Before the

U.S. House of Representatives
Committee on Financial Services
Subcommittee on Domestic Monetary Policy and Technology

The State of U.S. Coins and Currency
July 20, 2010

Chairman Watt, Ranking Member Paul and Members of the Subcommittee, my name is Michael Clark. I appear before you this afternoon as President of the Diamond State Depository, located in Wilmington, Delaware, a subsidiary of the Dallas-based Dillon Gage Group, Inc. Dillon Gage is one of 12 current Authorized Purchasers of American Eagle Silver Bullion Coins from the United States Mint. I have over 30 years experience in the precious metals and tangible assets industries, working for industry leaders such as Deak Perera, Wilmington Trust Corporation (NYSE: WL), and now Dillon Gage. I am a past Chairman, and remain a Director, of the Industry Council for Tangible Assets (ICTA), Inc., the national industry association for the rare coin, precious metals and tangible assets industry, which is headquartered in Severna Park, Maryland.

It is a pleasure to speak with you today on the state of U.S. Coins and Currency. My purpose in appearing today is to address three issues, all related to coinage:

1. The market impacts of the U.S. Mint's continued difficulties in keeping pace with market demand for its American Eagle Gold and Silver Bullion coinage programs;
2. The desire among collectors and investors alike for an American Eagle Palladium Bullion coin; and
3. The growing presence of counterfeit coins in the marketplace.

Impact of Planchet Shortages on American Eagle Gold and Silver Bullion Coin Markets

When Congress authorized the minting of gold and silver bullion coins in 1986[1] with the Gold Bullion Act of 1985, it created a widely successful program for investors and hobbyists interested in the advantages that precious metals can offer in diversifying and

[1] The Congressionally authorized American Eagle Bullion Coins were launched in 1986, following a 1985 Executive Order by President Ronald Reagan banning the further importation of South African-produced Krugerrand gold bullions coins to signal disapproval of apartheid.

stabilizing an investment portfolio. Today, the American Eagle Bullion Coin series (gold, silver, platinum) is the dominant provider of bullion coin investment products to the global market. This coinage program has provided investors with a convenient manner in which to invest in silver, gold and platinum bullion. Of course, the coins also are prized by collectors for their beauty.

Strong investment demand, coupled with a wounded global economy, has paved the way for a five-year-plus bull market in precious metals investments. The introduction in 2004 of exchange-traded funds backed by physical precious metals[2], coupled with the global economic crisis that began in 2007, has caused demand for precious metals to skyrocket. Gold has risen by 160% since 2005, while silver has shot up 141%, platinum rose 77%, and palladium 131% during the same period.

In the past three years, the U.S. Mint has sold unprecedented volumes of American Gold and Silver Bullion Coins. For example, demand for the U.S American Eagle Silver Bullion Coin reached record highs in 2009, with over 30 million sold. To put 2009's performance into context, over the 1986-2008 period, U.S. Silver Eagle minting averaged 7.7 million coins per year. Looking at the gold product, last year the Mint produced 1.3 million one-ounce Gold American Eagle coins, up from nearly 800,000 in 2008. In the first six months of 2010, demand for these products is on pace to equal last year's demand.

Demand for these products has been so robust in recent years that the Mint has at times suspended production of both its fractional Gold Eagle Coins and its 24-carat Buffalo Gold Bullion Coin (the Gold Eagle is produced in 22 carat). Further, beginning in late 2008, production of American Eagle Gold and Silver Proof and Uncirculated Coins has been suspended because of exceptionally strong demand for these coins. The Mint has allocated all available gold and silver bullion blanks to the American Eagle Gold and Silver Bullion Coin Programs because the U.S. Mint is required by Public Laws 99-61(Silver) and 99-185 (Gold) to produce these coins "in quantities sufficient to meet public demand . . . ." Proof and uncirculated coins are prized by collectors, who pay a premium for these coins.

The Mint's inability to keep pace with demand has had a negative and unnecessary impact on the investment and hobby community. At the heart of the problem is the Mint's inability to source sufficient planchets (or blanks) from multiple producers. Its reliance on just three suppliers is flawed. Moreover, there is some irony in the fact that while Congress requires the Mint to procure the gold for its Eagle bullion coins from newly mined U.S. deposits, the Mint then ships that gold to Australia to be made into blanks. Then, the fabricated blanks are later shipped back to the United States for the production of the coins. The inefficiency of this system is obvious, and it seems that we

[2] Since November 2004, the Securities and Exchange Commission (SEC) has permitted the registration of securities representing equity interests in trusts holding precious metal bullion, including the first-to market SPDR Gold Shares, for listing on registered stock exchanges. Today, over 40 billion dollars is invested in just two funds, iShares Silver Trust ETF (NYSE: SLV) and SPDR Gold Trust (NYSE: GLD).

should be able to create jobs at home by sourcing these blanks in the United States and eliminate the costs of inter-continental shipping.

Robust demand aside, there is a level of frustration among investors and collectors alike as gold and silver bullion coin production shortages continue and, in some cases, coin production stoppages occur. There is also frustration amongst the Mint's main market makers, its Authorized Purchasers. On many occasions, the Mint has had to ration coins amongst its Authorized Purchasers. These frustrations are being leveled almost entirely at the doorstep of the U.S. Mint since the Mint has not yet addressed the manufacturing issues surrounding the production of blanks needed to manufacture the coins. This production crisis first arose in 2008 and while the Mint has made public proclamations promising to address this issue, no significant action has taken place.

We wish to recommend that Congress take the following actions:

1. Authorize the Mint to produce both proof and uncirculated versions of the Gold and Silver Eagle Coins, regardless of the demand requirements of the bullion coins, to ensure uninterrupted supply to the market;

2. Direct the General Accountability Office to undertake a review of the Mint's procurement process for blanks, and seek its recommendations on what can be done to improve it; and

3. Require that the Mint procure the blanks for its bullion programs from sources within the United States by no later than 2014.

Palladium American Eagle Bullion Coin

Our industry believes that Congress should broaden the offerings of the American Eagle Bullion Coin Program by authorizing the Mint to produce a palladium bullion investment coin.[3] While principally an industrial metal, much like silver and platinum, palladium is also favored by investors. According to GFMS, Ltd, a leading precious metals research firm, there is a history of palladium investing that has been largely concentrated in the United States and Japan.[4] An American Eagle Palladium Coin would fill an important market void. Canada already produces palladium investment coins.

Palladium is a precious metal similar to platinum in composition and appearance but currently about one-third of its cost per troy ounce. Palladium is mined in only a few nations, and the United States is the fifth largest producer of this rare, white metal.[5]

Mined in Montana, palladium is used for numerous applications including use as an industrial catalyst; for the composition of automotive catalytic converters, dentistry, and jewelry; as well as in the production of surgical instruments and electrical contacts.

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[3] In 1996, Congress authorized the Mint to produce Platinum Bullion coins.

[4] GFMS Limited, *Platinum and Palladium Survey 2009*.

[5] Ibid.

The value of palladium is driven not only by its practical use, but also by its role as a store of value. Investment options include coins, bars, and exchange-traded funds. As the price of commodities has risen, investing in gold and platinum bullion coins is increasingly cost-prohibitive for many investors.

A one-troy ounce palladium coin would offer the precious metals investor an interesting price point for market entry. While gold presently trades around the $1,200 level, and platinum over $1,500, palladium is trading in the spot market in the range of $460 – $475.

Further, the introduction of a palladium coin may absorb some of the demand for the Silver Eagle, and reduce some of the Mint's production burden for that coin. There are ample reports in the marketplace that many investors are opting for silver bullion coins rather than the highly priced gold and platinum bullion coins the Mint also offers.

Lastly, a palladium bullion coin would create or maintain U.S. mining and refining jobs – in addition to mining jobs in Montana; palladium is refined in New Jersey, California and South Carolina.

Counterfeit Rare U.S. Collector Legal Tender Coinage

A growing problem in the marketplace today is counterfeit rare U.S. legal tender collector (numismatic) coins – generally the older coins whose value derives from their rarity and desirability for collectors, such as Morgan and Peace Silver Dollars.

Increasingly these coins are being counterfeited outside the U.S. and sold principally on online auctions. This poses a significant financial threat to American consumers. Last October, five of the country's most influential rare coin organizations issued an advisory to warn the public of the danger and the need for consumers to educate themselves.[6]

These counterfeit coins, the majority of which are believed to originate in the People's Republic of China, are often of extremely high quality. Hobby periodicals have reported that more than one million counterfeit coins manufactured in China have been sold in the United States. Unchecked, these counterfeits will cause significant financial harm to the American public.

Many of these "coins" are produced as replicas of authentic legal tender coins and are sold online. The U.S. Hobby Protection Act, (Public Law 93-167 15 US Code §2101 et seq) requires manufacturers and importers of imitation numismatic items to mark them plainly and permanently with the word, "COPY". While thousands of coins described as "copy" or "replica" are listed for sale in online auctions every day, there also are numerous reports of replica coins being exported from China without the word, "COPY," incused in the surface as the law requires. One respected industry weekly reported last year that 99% of the "replica" items sold into the U.S. market do not contain the required

[6] October 12, 2009 joint press release issued by American Numismatic Association, Industry Council for Tangible Assets, Numismatic Guaranty Corporation, Professional Coin Grading Service, and Professional Numismatics Guild. See: http://www.pngdealers.com/item.php?item_id=120&category_id=2

"COPY" markings. One counterfeiter in China told the publication he already has produced and sold more than one million coins.[7] Unfortunately, many of these counterfeit items are resold in the market place to unwitting consumers, in online auctions and at flea markets and other venues, as authentic rare legal tender U.S. coins.

While federal law addresses the matter of counterfeiting legal tender coinage, enforcement seems to be lacking, in part because these counterfeiters tend to be based in China, and are for all intents and purposes beyond the reach of U.S. law enforcement agencies. The industry organizations cited above have sought help from the Federal Trade Commission, U.S. Secret Service, U.S. Postal Service, and Immigration & Customs Enforcement with no apparent success. Because these counterfeits are arriving on U.S. shores principally via small, individual purchases, these government agencies are either unable or unwilling to investigate this fraud, which is endangering our country's numismatic legacy and resulting in significant loss to consumers.

Moreover, our industry has also consulted with eBay regarding policing its sellers, but eBay's stance is that its policies are being followed because the seller clearly state on their auction site that their coins are copies; and the photographs of these coins advertised for sale are clearly marked "COPY." But, as noted above, the vast majority of consumers are being delivered items devoid of the mandated "COPY" marking.

The primary relevant criminal statute is 18 U.S.C. §485, which prohibits manufacture of "any coin ... in resemblance or similitude of any coin of a denomination higher than 5 cents" and passing or importation into the U.S. "any false, forged, or counterfeit coin or bar, knowing the same to be false, forged, or counterfeit, with intent to defraud ... or attempts the commission of any offense described in this paragraph." Even possession of counterfeits of U.S. coins, or "any token, disk, or device in the likeness or similitude as to design, color, or the inscription thereon of any of the coins of the United States or of any foreign country issued as money", with the intent to sell is a crime punishable by fine (18 U.S.C. §489).

Further, the online sale of counterfeit coins, whether they are described as genuine or as "replicas" but nonconforming with the Hobby Protection Act, is fraudulent and, because it is in interstate or foreign commerce, violates the federal mail and wire fraud statutes. The mail fraud statute, 15 U.S.C. §1341, prohibits "any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, or to sell ... or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, security, or other article", if in executing such a scheme anything is placed in the U.S. Postal Service or any private or commercial interstate carrier.

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[7] Susan Headley, "Chinese Counterfeits Deceptive," *Coin World* http://www.coinworld.com/articles/chinesecounterfeit/part1.aspx

Our industry believes that Congress needs to take swift action to protect consumers from the increasing, and systematic counterfeiting and subsequent marketing of these counterfeit numismatic, rare and investment-grade legal tender United States coins. As a first step, we ask that Congress direct the Treasury Department's Inspector General to conduct a thorough investigation of the sources and extent of such counterfeiting and report back to Congress on the results of that investigation.

Specifically, we believe that the report should cover such topics as where the counterfeiting takes place; whether such counterfeiting is either sponsored by, or condoned by, a government, or enabled by specific laws or lack thereof; the marketing channels used domestically and overseas; the effect of any such counterfeiting on hobbyists, numismatists and on the investment opportunities for bullion or numismatic coins produced by the United States Mint; whether and to what extent such counterfeiting extends to the counterfeiting of third-party coin grading protective materials in such a way that might imply that the counterfeit inside had been examined and authenticated by a reputable third-party coin-grading firm; an estimate of the annual value of such fraudulent acts domestically and worldwide; the trends in value and the effects such fraud has on markets in general; and any recommendations the Inspector General may determine to be appropriate to curtail or forestall any such counterfeiting.

Thank you for the opportunity to address the Subcommittee. I would be pleased to answer any questions you may have about these matters.

Larry R. Felix
Director
Bureau of Engraving and Printing
US Department of the Treasury
Testimony before the Subcommittee on Domestic Monetary Policy and Technology

Chairman Watt, Ranking Member Paul, Members of the Subcommittee, thank you for holding this hearing and inviting me to testify before you today about initiatives underway at the Bureau of Engraving and Printing (BEP).

Mission/Vision

The mission of the BEP is to design and manufacture high quality security documents that meet customer requirements for quality, quantity, and performance, including counterfeit deterrence.

The BEP is the security printer for the United States Government, and it provides technical assistance and advice to other Federal agencies in the design and production of security documents, which, because of their inherent value or other characteristics, require counterfeit deterrence. The BEP also reviews cash destruction and unfit currency operations at Federal Reserve Banks. As a free service to the public, the BEP processes claims for the redemption of mutilated paper currency. Other BEP activities include engraving plates, dies and manufacturing inks.

The vision of the BEP is to maintain its position as a world-class securities printer, providing customers and the public with superior products through excellence in manufacturing and technological innovation.

Overview

The BEP produces security documents on behalf of other federal agencies; however our primary product is Federal Reserve notes. The BEP began producing currency in 1862. Authority conferred upon the Secretary of the Treasury under 31 U.S.C. 321(a)(4) and § 5114 allows the BEP to engrave and print currency and other security documents. BEP operations are financed by means of an industrial revolving fund, which was established in 1950 in accordance with Public Law 81-656. This fund is reimbursed through product sales for direct and indirect costs of operations including administrative expenses. In 1977, Congress amended the law, in Public Law 95-81, to authorize the BEP to include an amount sufficient to fund capital investment and to meet working capital requirements in the prices charged for products.

The BEP has a diverse workforce, which operates in two locations – Washington, DC and Fort Worth, Texas. Each BEP facility is capable of producing all banknote denominations. On average the BEP produces approximately seven billion Federal Reserve notes per year.

The BEP works collaboratively with the Board of Governors of the Federal Reserve System, the United States Secret Service and the Department of the Treasury to improve the security of Federal Reserve notes. In 1982, by charter, an Advanced Counterfeit Deterrence Steering Committee was established to recommend designs to the Secretary of the Treasury for Federal Reserve notes. As a general guideline, the committee recommended that the Government redesign Federal Reserve notes every seven to 10 years to deter counterfeiting by anticipating advances in reprographic technologies.

Currency Redesign Program

Consequently, in the mid-1990s the US Government introduced the first major redesign of US currency in 65 years. The design changes were needed to combat the emergence of a new category of counterfeiters who were increasingly using computers, scanners, color copiers and other emerging technologies to replicate notes. The goal of staying ahead of technological threats to our currency, rather than simply responding to an existing threat, requires the US Government to plan ahead and regularly develop new designs for currency. This means that new currency must be in development several years before the counterfeiting threat is projected to materialize.

On April 21, 2010, the US Government unveiled the last banknote in the most recent currency redesign series. Redesigned $20, $50, $10 and $5 notes were introduced into circulation in 2003, 2004, 2006 and 2008, respectively. The redesigned $100 note will enter circulation in February 2011. The redesign of the $100 note marked the completion of a multi-year initiative to implement the most ambitious currency redesign in the US. The innovative security features in the new note are the fruit of more than a decade of research and development to protect US currency from counterfeiting. While still retaining the traditional look of US currency, the new $100 note incorporates advanced technology to combat counterfeiting. There are a number of security features in this redesigned $100 note, including two new features: the 3-D Security Ribbon and the Bell in the Inkwell. The 3-D Security Ribbon is a blue ribbon on the front of the $100 note with images of bells and 100s. When holding the note and focusing on the blue ribbon, the bells change to 100s. When the note is tilted back and forth, the bells and 100s move side-to-side. If you tilt the note from side to side, the bells and 100s move

up and down. This security feature is woven into the paper, not printed on it. The Bell in the Inkwell is a color-shifting bell, inside a copper inkwell, on the front of the note. The inkwell and bell are both copper until you move the note. When tilted the bell changes from copper to green, an effect which makes the bell seem to appear and disappear within the inkwell. The BEP's latest assessment indicates that the 3-D Security Ribbon and the Bell in the Inkwell are effective counterfeit deterrence measures for threats posed to the $100 note.

This latest redesigned series, including the new $100 note, contain an array of counterfeit deterrent security features, some of which are visible and easily recognizable to the public (microprinting, raised printing, symbols of freedom, a watermark, security thread and color shifting ink) and some of which are covert or machine readable only. The driver for these redesigned notes is a digital counterfeit deterrent system that was developed under the auspices of the Central Bank Counterfeit Deterrence Group, in cooperation with major digital printer and software manufacturers. The US effort on this initiative was led by the Board of Governors of the Federal Reserve System. The digital counterfeit deterrent system, which is being used in a number of countries, relies on a hidden 'marker' embedded in the note's design that can be read or detected by new technology deployed in digital printers and software. This systemic design feature heralds a vibrant and growing partnership between the public and private sector to protect US currency, and is intended to thwart increased counterfeiting of currency using digital reprographic technology. This is a significant investment in the future of currency, and will greatly assist in preventing counterfeiting as digital technology becomes dominant in the marketplace. All of these security features work collectively to create layers of complexity that make these redesigned notes, including the new $100 note, difficult to counterfeit, but easy to authenticate.

The BEP, along with its collaborative partners, launched global public education programs with the unveiling of each redesigned currency note. A successful public education program is crucial to the anti-counterfeiting effort. The unveiling of the redesigned $100 note was the first step in a multi-government agency global public education program to educate those who use the $100 note about its changes before it begins circulating on February 10, 2011. The public education program offers training materials to inform users about the latest currency designs and how to authenticate US currency. These informational materials are available online and can be downloaded from the BEP's 'new money' website – www.newmoney.gov. The goal of the public education program is to build an adequate threshold of awareness to support commerce and ensure seamless, "business as usual" transitions as new currency designs are introduced to the public. The public is the first line of defense in combating

counterfeiting, and paper money users must be aware of new security features in genuine US currency when the new designs are introduced.

Overall, counterfeiting of US currency remains at low levels – due primarily to a combination of improvements in the notes' security design, aggressive law enforcement and public education efforts. According to the US Secret Service less than 1/100th of one percent of the value of all circulating US currency is reported as being counterfeit.

Strategic Plan

In December 2009, the BEP awarded a contract for the development of a facility feasibility study at the Washington, DC facility. The purpose of this study is to provide the BEP with sufficiently documented data to define and determine the preferred alternative of renovation and/or relocation that will most favorably meet BEP and our strategic partners' requirements. The study results are due at the end of this month.

The BEP is also implementing its strategic plan that will significantly change the currency manufacturing process. Over the next few years, the BEP will continue to retool and retrofit the production process by purchasing new processing, printing and inspection equipment, which will allow the agency to migrate to a higher capacity and capability manufacturing environment. The BEP's strategic plan will serve as a roadmap to guide the agency toward the goal of creating a new environment that will ensure cost-effective and flexible business operations for years to come. While the BEP is committed to meeting the many challenges of implementing innovative technology, we remain resolute in producing quality currency, controlling costs, being environmental stewards, and working safely as we move towards our vision – to continue to be the world's preeminent banknote producer.

The BEP's retooling transition began several years ago with the addition of six Simultan offset presses, which allowed us to incorporate color into our currency. The next phase was the installation of Super Orlof Intaglio (SOI) presses. Eight SOI presses are in operation; four at each BEP facility. Both of these presses provide the BEP with greater manufacturing flexibility and expanded functionality. Beginning this September, the BEP will have the first of three processing machines installed. Two of the machines will be installed at the Fort Worth Facility, and the third installed at the Washington, DC Facility. These multi-tasking machines perform functions at the back end of currency production such as overprinting serial numbers and seals, and cutting and packaging. These machines were designed specifically for the BEP, and they too will increase production flexibility and efficiency. Updating this equipment was essential. The aging manufacturing equipment at the BEP no longer met all the performance requirements

demanded in today's dynamic currency manufacturing environment. The new equipment will provide the rapid response, flexibility, productivity, and technology necessary to support the manufacture of increasingly complex currency designs, including an array of possible features for the blind or visually impaired.

Meaningful Access

In January 2008, the BEP commissioned a study, to address options to enable the blind and visually impaired to better denominate US currency. The study consisted of three phases:

- Phase 1: Was to gather data about the demographics of the visually impaired and the usefulness of various accommodations.
- Phase 2: Was to review features currently available to improve access to the visually impaired via discussions with the international banknote community and experts in vision loss and tactility.
- Phase 3: Was to conduct a cost-benefit analysis on the alternatives identified in the first two phases. This included considering the benefits to the visually impaired and the costs to the government, industry and the general public.

Additionally, the study provided a decision model, by which the BEP can evaluate various potential accommodations. Based on the study results, the BEP, in consultation with the Department of the Treasury, the Board of Governors of the Federal Reserve System, drafted proposed recommendations to the Secretary of the Treasury, who by statute has the sole authority for approving designs of US currency. The Advanced Counterfeit Deterrence Steering Committee approved these proposed recommendations. The recommendations consist of the use of a raised tactile feature; use of large, high contrast numerals; and a supplemental currency reader program.

As part of the next currency redesign to assist individuals that are blind or visually impaired to denominate US currency, the BEP plans to develop and deploy a raised tactile feature that builds upon current tactile feature technologies. The tactile feature will be unique to each Federal Reserve note denomination that may lawfully be changed, and will provide users with a means of identifying each denomination by way of touch. A BEP research group has visited several banknote printers to gather information on their progress in developing a tactile feature. Testing is underway at the BEP to determine which process and feature works best in producing the volumes needed for US currency. Based on experience, independent research, and the commissioned study, the BEP believes it can develop a raised tactile feature that is

reasonably durable, and can be incorporated into its existing manufacturing systems at a reasonable cost.

The BEP will continue with its current practice of adding large, high-contrast numerals and different and distinct color schemes to each denomination that it is permitted by law to alter in order to further assist visually impaired citizens. By law, the Department of the Treasury is not permitted to redesign the $1 note.

Meaningful Access Status

In May of this year, the BEP posted a notice in the Federal Register to announce the recommendations it intends to propose to the Secretary of the Treasury for moving forward in providing meaningful access to the blind and visually impaired community in denominating currency, and to request public comments about the agency's recommendations. In June, the BEP held simulcast, public forums at both facilities to hear comments from the public. Earlier this month, the BEP once again participated in the national conferences for both the American Council of the Blind and the National Federation of the Blind. After the public comment period the BEP expects shortly to be in a position to make recommendations to Secretary Geithner on the best manner in which to provide meaningful access to US currency.

The most recent redesign of the currency commenced in 2003, and the final denomination in that series of currency is in production. It is somewhat difficult to provide a specific date or time frame as to when the redesign of a new family of currency will be completed; however, if approved by the Secretary, some variation of a tactile feature, a large high-contrast numeral, and distinct colors will be included in future generations of US currency to provide meaningful access for individuals that are blind or visually impaired.

Meaningful Access – Interim

In the interim, the BEP also proposes to recommend to the Secretary of the Treasury a supplemental currency reader program that will provide access to US currency. This measure would involve a process to loan and distribute currency readers to the blind and visually impaired at no cost to them. The BEP believes that this process will ameliorate difficulties stemming from the transition that will occur during the co-circulation of notes with and without a tactile feature and large, high contrast numerals, a transition which will persist for many years after the introduction of the tactile-enhanced note.

Additionally, the BEP is continuing in its efforts to explore emerging technological solutions such as the development of software to enable blind and visually impaired individuals to denominate US currency. Some of the options include the development and deployment of assistive software to enable banknote denomination recognition using cellular telephones, computers, and imaging and reading devices. Initial design specifications for the cellular phone application have been completed, and a functioning preliminary prototype has been produced and made functional. An image recognition engine has been selected and the BEP contractor is working through algorithm refinement. A target release date is anticipated later this year. This is the first of several government sponsored cellular phone applications aimed at assisting the blind and visually impaired community.

Other Initiatives

Other initiatives currently underway at the BEP include employee training, product quality, cost reduction efforts, and the modernization of the BEP's information technology systems. Through our Human Capital Strategic Plan, we are creating an environment that supports, nurtures, and sustains a high caliber workforce that ensures we efficiently accomplish our mission. By leveraging the efficiencies of the new innovations and technologies we recognized we were overstaffed in certain positions as we modernized; therefore, we requested and were granted authority from the Office of Personnel Management to offer optional early-outs and buy-outs to specific positions where we were overstaffed, based on a projected five-year staffing analysis. By the end of 2014, the BEP expects to have at least a 10% overall staff reduction. Thus far, 39 employees accepted the early-out, buy-out offer for an estimated $1.5 million in savings. In addition, staffing has continued to decline over the past several years through prior early-out and buy-out offers as well as normal attrition – for example in 2005 staffing declined from 2,282 FTEs to 1944 FTEs in 2009, reduction of 338 FTEs. Each year, the BEP analyzes the number of positions to ensure that the organization has the right number and mix of employees in place to achieve its mission requirements.

The BEP strives to enhance the effectiveness of recruitment and retention to ensure that the agency continues to meet its critical mission requirements, establishes itself as an employer of choice, and moves into the top 50% of Best Places to Work in Government by the end of FY 2014. Along with innovative, cutting-edge designs, BEP will maintain its focus on producing quality security products in the most cost effective manner possible. It will continue to pursue process improvements as required of an ISO 9001 certified organization, a designation that indicates to current and prospective customers that the BEP employs a rigorous quality management program.

Continuous process improvements will be the catalyst for world class quality and improved cost performance through streamlined processes and low spoilage. In addition to quality certification, the BEP attained ISO 14001 certification in 2007 for its environmental management systems, institutionalizing its commitment to sound environmental stewardship.

The BEP strives to provide its customers with superior products and continuously looks for ways to manufacture efficiently without compromising quality. The BEP is modernizing its business information technology system, which is more than 25 years old. Over the next five years, nearly all of the BEP's production related business decisions will be driven by near real-time manufacturing performance metrics. The upgraded business information system will provide an integrated platform that will simplify and standardize the integration of disparate information technology systems and applications used in the BEP to optimize the timely collection and reliability of all available data. The new business information system will use modern software with built-in longevity and upgrade paths. This project will span the next several years, and it will be a companion modernization effort to the new equipment that the BEP is acquiring.

Conclusion

Mr. Chairman, this concludes my remarks about initiatives at the BEP. I will be happy to respond to any questions you or other members of the Subcommittee may wish to ask. Thank you.

Serving the Vending, Coffee Service and Foodservice Management Industries

To the House Subcommittee on Domestic Monetary Policy and
Technology of the U.S. House of Representatives
Committee on Financial Services

STATEMENT OF THE NATIONAL AUTOMATIC MERCHANDISING ASSOCIATION

By
Craig A. Hesch
Chairman

Hearing: July 20, 2010

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Mr. Chairman and members of the committee, thank you for this opportunity to attend this hearing and offer testimony on the subject of coin and currency. I sincerely appreciate the chance to visit with you about critical issues to our industry.

My name is Craig Hesch, and I am the 2010 volunteer national chairman of the National Automatic Merchandising Association (NAMA). In addition, I am the Chief Financial Officer of A.H. Management Group of Rolling Meadows, IL. Our company is a third generation small business which is a full line vending operator. We provide vending snacks and beverages to companies throughout the Chicago area. We also provide music and gaming vending machines to our customers. So while I will visit with you today about coin and currency issues related to the food and beverage vending industry, I can discuss the impact on other vending channels as well.

Our national association, NAMA, is the trade association of the food and refreshment vending, coffee service and foodservice management industries including on-site, commissary, catering and mobile. Our membership is comprised of service companies, equipment manufacturers and suppliers of products and services to operating service companies. The basic mission of the association, to collectively advance and promote the automatic merchandising and coffee service industries, still guides NAMA today as it did in 1936, the year of the organization's founding.

While we will spend the majority of our time in this hearing discussing coin and currency issues, it is important to first note that our association, and our industry, has recognized the national problem with obesity. We share the administration's concern about obesity, and are also working to try and solve this problem.

Our members understand that childhood obesity is a serious issue that must be addressed. It is a complicated problem and the solution requires better education about nutrition and increasing physical activity.

Vending machines can provide healthy options. For example, the Alliance for a Healthier Generation reports that a school district in Florida recently purchased 60 vending machines which are providing students and faculty with "organic items, nutrition and sports bars, fresh fruits and vegetables, low fat milk and dairy selections such as yogurt and cheese sticks, fresh sandwiches, soymilk, bottled beverages and more." Vending can provide healthy "grab-and-go" solutions to meals through refrigerated vending machines which vend breakfast products such as low fat milk and single servings breakfast bars and breakfast cereals.

We have always supported the federal government's "competitive foods" regulation requiring that foods of minimal nutritional value not be sold in school cafeterias when the lunch is being served.

Vending machines are retail locations which provide a variety of snacks and beverages. For example, in addition to standard snacking choices, vending machines are available which sell fresh fruit, fresh vegetables, salads, milks and a wide variety of healthy meal choices. They

provide similar products which are found at other retail locations such as convenience stores, grocery stores and even in the al a carte line in school cafeterias. Like these other retail locations, vending machines can provide what customers want, whether it's a traditional snack or a healthy alternative.

Vending provides a very valuable service to those who work irregular hours, or who may not have full-service meal alternatives. For example, federal workers in the White House and Eisenhower Executive Office Building in Washington, DC use vending for healthy between-meal snacks and for salads after hours. The 24 hour work cycle of these and other government facilities such as congressional office buildings necessitate innovative solutions which vending does provide.

To address the issue of obesity, NAMA developed the Balanced For Life and Fit Pick programs to assist in the issue of providing "healthier for you" choices in vending. Across the country, school and work vending accounts look to our industry and association to partner with them on health and wellness issues. Our voluntary program components help vending operators with tools to help and truly be part of the solution. In addition, because our nutritional programs are a stand-alone resource, each vending operator can easily implement the program he or she thinks is best suited to a particular location.

We agree that childhood obesity is a serious problem that must be addressed and applaud the intent of those working so hard to protect our children. Our members are mothers and fathers ourselves, and certainly want to protect our children's health and future well-being. When we help our children truly understand the elements of a balanced diet and the importance of being physically active, we can have a lasting impact on their lives, protecting and enhancing their futures.

We also recognize that obesity may be related to a lack of healthy options in geographic areas called food deserts. Our solution is to encourage our operators to place healthy choices in vending machines in under-served communities.

NAMA is working to try and test vending machines that will vend Supplemental Nutrition Assistance Program (SNAP) foods in machines which will accept Electronic Benefit Transfer (EBT) cards to help those with public assistance benefits. It is our hope that as convenient retailers, we can assist in solving the problem of food deserts and help reduce obesity.

As a corporate trade association working on these and other issues, we represent the companies which make vending machines, companies which make the snacks, and the companies, like mine, which are the operators of the vending machines.

We have 34 affiliated State Councils encompassing 36 states.

As background, the vending industry is a $40 billion a year industry, employing approximately 700,000 people who work at an estimated 13,500 companies.

Vending is a major component of the food service industry. According to the industry research group Technomics, vending and office coffee service represents 4.8% of the U.S. food service industry. This is twice the size of Convenience Stores (2.0%) and larger than Supermarket Foodservice (3.4%), Primary / Secondary schools (3.2%) and Colleges / Universities (2.4%)

According to The Vending Times Census of the Industry 2009, there are approximately 5.3 million food and beverage vending machines in the United States.

An estimated 100 million Americans will use one of these vending machines each day, so any changes in coins or currency will directly impact our membership and our customers. It is important to note that while many vending machines accept credit or debit cards, the vast majority of vending machines operate on cash transactions only. Therefore any changes to coin or currency will dramatically affect our industry.

The overall cost of these modifications and of potential refused sales will be significant. And with an industry of small business operators, such increased cost could easily cause businesses to fail and jobs to be lost.

To understand why jobs could be lost it's important to understand the function and costs of a modern coin acceptance system.

Costs:

In current widely used electronic coin acceptors, a coin passes between a pair of sensors; one that transmits a magnetic field and the other that receives a magnetic field. As the coin rolls by, it alters the magnetic field and the variation is interpreted by the acceptor's computer algorithm. Differences in size, shape, or metal content produce different, very precise electronic signatures that determine coin type and denomination. The coin acceptor may be measuring the diameter, the thickness, the alloy and, for certain coins, also the embossing features. Another method of validation uses a series of optical sensors to gather data along the coin path for size and width. The acceptor will then compare that data against preprogrammed criteria. In both cases, a motor or solenoid is used to open and accept the coin into the correct denomination tube or slot. Upon acceptance, the product is vended. Such machines can track sales, make change and reject unacceptable coins. Newer systems even have a "learning mode" which allows the coin acceptors to recognize standard deviations, wear patterns and coin usage to increase the percentage of accepted coins.

Modern coin validator systems that accept, verify, provide security and pay out coins, cost between $250 and $475.

For example, I have brought with me today a coin and bill validator. This mechanism costs $450, and takes 20 minutes to install. If it needs to be reprogrammed to accept the new designs of a new U.S. Federal Reserve Note, it will cost $100 and take 20 minutes for a trained technician to reprogram the device, in addition to travel time to the location.

With approximately 5.3 million food and beverage vending machines in place today, a $100 upgrade would cost the industry $530 million dollars.

But an estimate of the cost may be much more complicated. For example, one NAMA member estimated that it would cost the entire vending industry billions.

First, companies would have to spend millions of dollars on design and development to even identify equipment that is capable of handling the changes. The more drastic the changes, the greater the cost of engineering.

Cost to convert currency equipment can be as low as $100 if the validator unit is fairly modern and has programmable memory. Some companies supply simple and "free" upgrades, but that does not include the cost to locate, travel to, update and test the device at each machine. A typical estimate would be around $100 per machine for a simple reprogramming.

If the unit is older and requires new hardware or potentially an entirely new device, then the costs jump an additional $100 for low end devices to $500 for higher end devices. The most common costs would be in the $300 - $400 range.

If the changes in the currency impact either the size or electronics required to detect and handle the bills then the units would have to be replaced. Again, this would be at a cost ranging from $100 to $500. Examples of changes which would require more costly upgrades would include coin plating technology or Federal Reserve bank notes that significantly differ in width and length from our current notes. Mechanical changes to the size or weight of coins would also dramatically increase costs, and the coin validators would have to be re-engineered.

In addition to 5.3 million food and beverage vending machines, there are approximately 1.3 million amusement machines, 750,000 to 1 million gaming devices, 1.5 to 2 million retail, car wash and other specialty devices, 2 million parking meters, and millions of cash handling or currency counting devices in banks and retail locations.

So if you consider the total number of mechanical devices which handle coins and currency, one member estimates that the cost to replace or reprogram coin and currency validators could be in the billions of dollars. Again, the more dramatic the changes to coins or currency size, shape or weight, the more expensive the cost to the industry.

Coin Changes:
We are prime customers when you have a discussion about changes to coins and currency. On the issue of coins, the National Automatic Merchandising Association (NAMA) in 2008 supported H.R. 5512 which provided that the alloy content of future coins, while reducing production costs for the taxpayer, must work in existing coin-acceptance equipment in our country's vending machines and anywhere where coins are used without modification to that equipment.

Regarding changes to the metal content of coins, thanks to the superb quality control program of the United States Mint, Americans confidently make vending a frequent choice in retail shopping. The industry has a very high trouble-free vend rate thanks to consistency in coin, currency and new coin validation technology. However, rising prices for copper, nickel and zinc

have pushed the cost to make pennies and nickels above their face value and have reduced the profit the government makes on dimes, quarters, half dollars and dollar coins.

We recognize this increased cost of minting these coins. And as American taxpayers, we understand the importance of reducing the federal deficit. However, changing the composition of coins could very well lead to expensive modifications to coin mechanisms by the vending industry.

When the Sacagawea dollar coin was introduced, the mint successfully worked with the industry in finding an alloy that met the requirements of the Mint in color and size, yet still resembled the electronic signature of the Susan B. Anthony dollar coin. When the U.S. Mint introduces new quarter designs, we have had no problems with acceptance rates. For the newly designed America the Beautiful National Park quarter dollar coins, we have had no problems with acceptance in our coin validators.

This is due to successful partnerships we have had with the Mint and with their very professional staff.

It is critical that future alloy changes follow a similar path to ensure that any changes don't impact our industry.

With fluctuation in metal commodity prices, we encourage the U.S. Mint and decision makers to continue to consider the vending industry – a prime customer – in any changes in coin composition. For example, if the Mint were to produce steel coins or plated steel coins, such as being considered by other nations, we would argue that we as prime customers would be severely harmed. Any such changes would cost the industry jobs.

NAMA, the World Wide Vending Association and national vending associations from around the world generally oppose coins manufactured from multilayer plated materials especially for higher value coins.

Using multilayered plated material in coins could cause numerous problems. For example, multilayer plated steel construction could have similar Electronic Metal Signatures which may not allow coin validators to distinguish coins correctly. Manufacturing variability and wear in circulation could additionally lower the reliability rate of vending machine equipment. Also, plating facilities are very widespread around the world for many other common applications, making any combination of materials readily available and creating a huge potential supply for criminals. It is important that any changes in alloy content or composition of coins take into consideration that we do not want our coins to become an attractive target for counterfeiting.

It is very important that any changes in alloy or material be allowed only in low value coins such as a penny or nickel. In addition, it is critical that any alloy and any steel must come from a very controlled source or comply with highly consistent technical standards.

And most importantly, while it may be less expensive to mint coins with different alloys, there will be a significant cost associated with the upgrade of the coin validators used in vending, and

indeed in all other industries that use electronic coin validation. In all situations a trained staff member will be required to visit each coin validator to carry out the modifications to the coin sensor limits. In addition, some coin validators may not be able to be upgraded to discriminate new coins satisfactorily and will have to be replaced with more capable versions.

For example, if changes to the metal content occur, this will require expensive reprogramming of most coin validators. Such reprogramming requires a technician to visit all vending machines and transfer new data to the coin validators.

If mechanical changes are made to the coins, such as changes in sizes or weights, then these changes will require even more expensive changes to our coin validators. Expensive entire redesigns to the coin validators in addition to reprogramming will be required. We would strongly urge the committee to oppose any mechanical changes to coins.

We are also concerned that changes in coinage would change the acceptance rates of coins. It is possible that coin validator manufacturers may increase the verification security level of coins thereby restricting and lowering the acceptance rate of the genuine coins to protect against counterfeiting or misreading of the coins. However, customer dissatisfaction may occur because too many apparently good coins will be rejected and vending sales will be affected.

Currency Changes:

Regarding changes to currency, we also applaud the Bureau of Engraving and Printing for outstanding quality control programs. The BEP is a very responsible partner. They regularly make confidential advanced copies of currency available to the industry so that we can evaluate new currency to accommodate and update our bill validators.

We also call to the attention of the committee that our members who manufacture coin and currency validators are committed to providing their customers with the best products, technology and services which are available. They have a long and distinguished record of providing very effective tools to process coins and currency to ensure accurate transactions.

The Bureau of Engraving and Printing will soon implement changes to the currency to accommodate the blind and visually impaired in distinguishing currency denominations. BEP is responding to the U.S. Court of Appeals decision that the Department of Treasury failed to design, produce and issue paper money to assist those who can't distinguish bill amounts. BEP studied changes in sizes (length and width), three tactile features (cluster pattern of raised dots, notches cut into the currency, and heavy intaglio raised print bars) and three commercially available currency readers.

We support reasonable changes to U.S. currency to accommodate the visually impaired, but we must ensure that currency readers in vending machines can validate the currency without undue burden to the millions of customers who purchase vended products every day. NAMA also opposes any changes to the currency which will unnecessarily burden the thousands of small businesses which operate vending machines. With approximately 5.3 million food and beverage vending machines in use today, any changes which would require replacement, modification or

reprogramming will harm the industry. These costs could result in job reductions and price increases, thereby creating an unfair disadvantage for our industry versus other retail channels.

As an example, anecdotally, when European nations switched from their currency to the Euro, all coin and bill validators had to be modified. This was enormously expensive for vending operators across Europe. We understand that since operators spent all their capital on new coin and bill validators, that very few other vending equipment, such as new machines or energy efficient equipment, was purchased. This dramatically harmed vending operators who couldn't increase costs to recover these new expenses.

We would specifically oppose changes to the size of the currency as this could dramatically change the physical design of our mechanism. This may be the most costly change which could occur. We would also oppose notches or cuts which might make verifying currency very difficult. As unattended retailing, trouble free validation ensures ease of use for our customers, but also easily rejects counterfeit or tampered currency. For example, when bills are refused, sales are lost and customers are upset. Dramatic changes to the physical design such as size changes, notches, punches or cuts could result in increased costs to replace equipment, and could result in more bills being refused, resulting in lost sales.

So we strongly encourage the committee and the Bureau of Engraving and Printing to continue to partner with our members and with our association as any changes are discussed. In fact, we recommend that an advisory group be formed to assist with the technical matters related to any changes.

Our members are experts in the field of validating coins and currency. So our expertise could be invaluable to ensure that any changes are properly implemented.

We also recognize the debate about how changes in coins and currency should take place. We generally support allowing the U.S. Mint and the Bureau of Engraving and Printing the authority to conduct research and development on potential changes. But we hope that Congress will retain their authority to allow such changes.

It is critical that there is sufficient time, prior to the introduction of new coins or currency, for the industry to review and have access to any changes. It will take many months to accommodate changes. So such research and development may allow additional time for industry input on the potential economic impact of coin and currency changes.

Mr. Chairman and members of the Committee, thank you for this opportunity. We are honored to be able to make these comments and welcome the opportunity to work with you on these issues in the future.

STATEMENT OF MR. KENNETH JENKINS

Special Agent In Charge

Criminal Investigative Division

United States Secret Service

Before the Subcommittee on Domestic Monetary Policy and Technology

Committee on Financial Services

U.S. House of Representatives

July 20, 2010

Good afternoon, Chairman Watt, Ranking Member Paul and distinguished members of the Subcommittee. I would like to thank you for providing the U.S. Secret Service (Secret Service) an opportunity to discuss U.S. currency issues.

While the Secret Service is perhaps best known for protecting our nation's leaders, we were established in 1865 to investigate and prevent the counterfeiting of United States currency. As the original guardian of the nation's financial payment system, the Secret Service has a long history of protecting American consumers, industries, and financial institutions from fraud. Congress continues to recognize the Secret Service's 145 years of investigative expertise in financial crimes and over the last two decades has expanded our statutory authorities to include access device fraud (18 USC §1029), which includes credit and debit card fraud. Congress has also given the Secret Service concurrent jurisdiction with other law enforcement agencies for identity theft (18 USC §1028), computer fraud (18 USC §1030), and bank fraud (18 USC §1344). We take our mission to combat these crimes seriously and as a result, the Secret Service is recognized worldwide for our investigative expertise and innovative approaches to detecting, investigating, and preventing financial crimes.

As you are aware, the Secret Service officially became a part of the Department of Homeland Security in March of 2003. Though our agency is no longer a component of the Department of the Treasury, we continue to maintain our historic ties and a robust partnership in the safeguarding of our currency and other payment systems. The Secret Service strongly believes that economic security is a central element of homeland security; therefore, the safeguarding of our financial infrastructure and monetary framework continues to be a paramount objective of our investigative efforts.

New Federal Reserve Notes

Rapid and continual technological advancements have enabled criminals to more easily conduct and expand a variety of crimes. These advancements mean counterfeit currency and other obligations can be reproduced quickly and efficiently. Today's criminals need relatively little knowledge or specialized training to print counterfeit currency or other financial obligations. A counterfeiter or criminal organization can utilize equipment ranging from inexpensive digital

devices such as scanners, computers, printers and multi-function devices, to large commercial presses, to flood a region with counterfeit currency.

The Secret Service is aggressively combating the production and circulation of counterfeit currency on several fronts. With our partners in the Department of the Treasury and the Federal Reserve, we are continuing with the redesign of our currency. As a member of the Advanced Counterfeit Deterrence Steering Committee (ACD) and the Interagency Currency Design Committee (ICD), we have an active role in the research, design, and introduction of new currency. The Secret Service continually evaluates the methods currently employed by counterfeiters and studies cutting-edge anti-counterfeiting technologies to enhance future redesigns of U.S. currency. This partnership was highlighted on April 21, 2010, with the unveiling of the redesigned $100 Federal Reserve Note. The new design for the $100 note not only retains the effective security features from the previous design but also contains two new security features: the 3-D Security Ribbon and the Bell in the Inkwell. The 3-D Security Ribbon is woven into the paper and shifts from *100s* to *bells* depending on how you tilt the paper. The Bell in the Inkwell feature includes a color-shifting bell in a copper inkwell. The bell changes from copper to green, an effect which makes the bell seem to appear and disappear within the inkwell. These advanced security features will hinder potential counterfeiters from producing high-quality notes that can deceive consumers and merchants.

Trends in Counterfeiting

Due to the dollar's value and widespread use overseas, it continues to be a target for transnational counterfeit activity. Of the approximately $908 billion dollars of genuine U.S. currency in circulation, roughly two-thirds of that amount circulates outside of our borders.

Despite our considerable success in reducing the amount of U.S. counterfeit currency in circulation, recent trends indicate a growing globalization in production and distribution of counterfeit notes. While it is difficult to determine precise figures detailing the amount of counterfeit U.S. currency passed annually overseas, as not all nations report that information, the Secret Service received approximately $69 million in counterfeit that was passed to the American public in FY 2009 alone—a combination of money the Secret Service has seized within the United States that has been passed to the public, as well as money that has been processed through the Federal Reserve system. Additionally, approximately $108 million in counterfeit U.S. currency was seized prior to distribution last year by the Secret Service and other authorities worldwide. Of this amount, approximately seven percent was seized within the United States.

Currently, more than 38 percent of all counterfeit currency passed domestically was printed outside of the United States using traditional printing techniques, predominately offset printing. The rest of the counterfeit currency passed domestically last year was produced within the United States by individuals using digital technology such as computers, scanners, printers, and multi-function devices. The most commonly passed counterfeit note domestically is the $20, whereas the most commonly passed note overseas is the $100.

The Secret Service has also observed that counterfeit notes produced on "bleached" paper are both a domestic and international concern. The "bleaching" process consists of the counterfeiter taking a lower denomination genuine U.S. note, usually a $5 bill, and removing the printed ink through a labor-intensive process commonly referred to as "bleaching." This "bleaching" process creates a blank note of genuine U.S. currency paper that retains many of its "distinctive counterfeit deterrents" and is, of course, made of the "distinctive paper" adopted by the Treasury Department. The counterfeiter then transfers an image of a higher denomination U.S. note, usually from a $100 bill, onto the "bleached" genuine paper. Domestic counterfeiters, as well as counterfeiting operations based in Colombia, Nigeria, and Italy have all produced significant quantities of counterfeit notes that were printed on "bleached" genuine U.S. currency notes. Counterfeiters have also targeted foreign currency, using "bleached" Venezuelan and Iraqi currencies to produce counterfeit U.S. $100 bills.

Counterfeit currency also continues to be associated with organized crime and drug trafficking. In one example, in October 2009, the U.S. Drug Enforcement Administration's Organized Crime Drug Enforcement Strike Force (OCDESF), located in New York, New York, contacted the Secret Service's New York Field Office with information concerning counterfeit currency. An OCDESF investigation had yielded reliable information that counterfeit Federal Reserve Notes (FRNs), would be accompanying a shipment of illegal narcotics, expected to arrive via commercial aircraft from Cali, Colombia. Working with the Colombian National Police and a confidential source, OCDESF and Secret Service agents were able to arrest the suspect with a suitcase containing illegal narcotics and a laptop computer bag containing over $150,000 in counterfeit FRNs concealed in the liner and charge him in U.S. District Court, Eastern District of New York.

Counterfeit Suppression

Today, the Secret Service continues to target strategic locations throughout the world where significant counterfeiting activity is detected through joint task forces with foreign law enforcement partners. Our investigative history has shown that the effective suppression of counterfeiting operations requires a close partnership between our domestic and international field offices and their law enforcement counterparts, as well as an immediate response by the law enforcement community.

The Secret Service's permanent presence overseas has been pivotal in establishing the partnerships necessary to successfully suppress foreign-based counterfeiting operations. For example, Project Colombia is a continuation of the Secret Service's efforts to establish and support Vetted Anti-Counterfeiting Forces (VACF). Since its inception in 2001, Project Colombia partners have seized approximately $239 million in counterfeit U.S. currency, arrested more than 600 suspects, suppressed nearly 100 counterfeit printing plants, and reduced the amount of Colombia-originated counterfeit passed within the United States by more than 80 percent.

In one instance in early 2009, agents from the Bogota Resident Office and officials with the Colombian National Police and the VACF contacted our Madrid Resident Office regarding a counterfeit suspect. Through extensive collaboration between the Secret Service, the VACF, and

the Spanish National Police (SNP), the SNP intercepted a package originating from Colombia, which contained negatives bearing images of counterfeit FRNs. Then, in January 2010, the SNP conducted a search warrant at one suspect's residence and seized $1.3 million in counterfeit U.S. currency, an offset printing press, two computers, photo negatives bearing the image of FRNs, and other items consistent with producing counterfeit currency. Ultimately, five Spanish suspects were charged by the Spanish National Police with violations of fraud and negotiating counterfeit instruments.

Our investigative successes in Colombia have forced these criminal elements to relocate to other parts of South America. For example, from FY 2008 to FY 2009, the Secret Service noted a 156 percent increase in worldwide passing activity of counterfeit U.S. currency emanating from Peru. These counterfeit notes, referred to as the Peruvian Note Family, have emerged as one of the leading domestically passed notes in the last 18 months. In response to the increase in passing activity of the Peruvian Note Family, which was second only to the domestic passing of digital counterfeit in FY 2008, the Secret Service formed a temporary Peruvian Counterfeit Task Force (PCTF) in collaboration and partnership with Peruvian law enforcement officials. Since opening in Lima, Peru on March 15, 2009, the PCTF has yielded 38 arrests, 17 counterfeit plant suppressions, and the seizure of more than $20.6 million in counterfeit U.S. currency. Due to the overwhelming success of the PCTF, the Secret Service and Peruvian law enforcement officials have agreed to extend operations for an additional six-month period in FY 2010.

To highlight one of the PCTF successes, during the spring of 2009, PCTF agents and members of the Peruvian National Police (PNP) developed critical investigative leads through the use of confidential informants to obtain information on counterfeit operations in Lima, Peru. PCTF agents and PNP officers executed four search warrants on target locations where counterfeit U.S. FRNs were suspected of being manufactured. The four search warrants resulted in the arrest of ten suspects and the seizure of $9.84 million in counterfeit FRNs, 11 lithographic presses, photo equipment, 15 lithographic plates, and numerous sets of negatives for the Peruvian note.

As new technologies continue to yield sophisticated criminal methods, the challenges facing law enforcement are significant given that large quantities of counterfeit currency and other obligations can be reproduced quickly and efficiently. The collaboration with international law enforcement agencies in Latin America and around the world is critical for the Secret Service to successfully combat distribution and foreign counterfeit production.

Partnerships

In addition to the increasing complexity of financial and electronic crimes, the Secret Service must contend with the fact that these types of crimes transcend national borders more fluidly than ever before. As a result, our counterfeit and cyber crime investigations require seamless coordination between Secret Service domestic and international field offices, headquarters, and our law enforcement partners throughout the world.

Currently, the Secret Service operates a network of 142 domestic and 22 international investigative field offices across 18 countries, to carry out its investigative and protective responsibilities. By working closely with other federal, state, and local law enforcement

representatives, as well as with international law enforcement officials, the Secret Service is able to establish comprehensive networks of information and resource sharing. The technical expertise and the comprehensive networks of information and resource sharing bridge jurisdictional boundaries. This partnership approach to law enforcement is vital in order for the Secret Service to fulfill its dual mission of protection and investigations. Such communication and cooperation is the blueprint we have successfully developed over the course of many decades of experience.

Electronic Crime and Cyber Investigations

Through our work in the area of financial crime, the Secret Service has developed a particular expertise in the investigation of cases involving network intrusions of businesses that result in the compromise of credit and debit card numbers and all related personal information. A considerable portion of this type of electronic theft appears to be attributed to organized cyber-groups, many of them based abroad, which pursue both the network intrusions and the subsequent exploitation of the stolen data. Stolen credit card information is often trafficked in units that include more than just the card number and expiration date. These "full-info cards" include information such as the card holder's full name and address, mother's maiden name, date of birth, Social Security number, a PIN, and other personal information that allows additional criminal exploitation of the affected individual.

The increasing level of collaboration among cyber-criminals makes these cases more difficult to investigate and also increases the potential harm to companies and individuals alike. Illicit Internet carding portals allow criminals to traffic stolen information in bulk quantities globally. These portals, or "carding websites," operate like online marketplaces where criminals converge to trade in personal financial data and cyber-tools of the trade. The websites vary in size, from a few dozen members to some of the more popular sites boasting memberships of approximately 8,000 users. Within these portals, there are separate forums, moderated by notorious members of the carding community, where members meet online and discuss specific topics of interest. International cyber-criminals buy, sell, and trade malicious software, spamming services, credit, debit, and ATM card data, personal identification data, bank account information, hacking services, and other contraband.

One of the Secret Service's major investigations into a network intrusion was initiated in January 2009. The intruders breached Heartland Payment Systems corporate environment via Structured Query Language (SQL) injection and navigated to the credit card processing environment where a custom packet "sniffer," modified to capture payment transaction data, was recovered.

The Secret Service investigation revealed that over 130 million credit card accounts were at risk of being compromised and that data was ex-filtrated to a command and control server operated by an international group related to other ongoing Secret Service investigations. During the course of the investigation, the Secret Service investigation revealed that this same international group committed other intrusions into multiple corporate networks, stealing credit card and debit card data.

Various investigative methods, including search warrants, Mutual Legal Assistance Treaties, pen traps, and subpoenas, were used to identify three main suspects of this international group. On March 26, 2010, one of the suspects, Albert Gonzalez, was sentenced to 20 years in prison for his role in the Heartland, Hannaford's, and 7-11 intrusions and two unnamed co-conspirators were indicted for their role in this investigation. Efforts to locate them are ongoing.

Collaboration and Training

To illustrate the innovative approach to meeting increased investigative demands and collaborate with our law enforcement partners, the Secret Service, in partnership with others in the Department of Homeland Security, developed the National Computer Forensics Institute (NCFI) in Hoover, Alabama. NCFI is a cyber crimes training facility designed to provide state and local law enforcement officers with critical expertise in computer forensics and digital evidence analysis. By the end of 2010, the Secret Service will have provided critical training to 932 state and local law enforcement officials representing 300 agencies from 50 states and two U.S. territories. These individuals will now be available to serve as a force multiplier and assist the Secret Service with investigations as necessary.

The Secret Service also maintains an ongoing, robust relationship with the International Law Enforcement Academy (ILEA), which has locations in Budapest, Hungary; Bangkok, Thailand; San Salvador, El Salvador and Gabarone, Botswana. The Secret Service's work with ILEA provides a critical opportunity to forge new relationships with international law enforcement partners and share its expertise in combating counterfeiting, financial crimes and cyber crimes. Providing this training to foreign law enforcement partners has allowed the Secret Service to expand its investigative footprint in countries where these types of crimes are proliferating at an alarming rate. In FY2009, the Secret Service, in conjunction with ILEA, trained more than 900 foreign police officers from more than 70 countries.

Additionally, the Secret Service continues our public education and training in an effort to prevent and suppress the manufacturing, distribution and sale of counterfeit U.S. currency domestically and abroad. Secret Service personnel continuously conduct training seminars on topics such as financial crimes and computer forensics in an effort to augment the Secret Service's mission.

Conclusion

In closing, I would like to express my appreciation for the support that Congress has shown the Secret Service over the years. What began 145 years ago as a small group of agents responsible for combating the crime of counterfeiting currency has grown into a diverse, internationally respected, federal law enforcement agency charged with a unique, dual mission of protecting the nation's critical financial infrastructure and protecting the nation's highest leaders, visiting heads of state and government, and designated National Special Security Events.

The Secret Service, in concert with its partners – public and private, domestic and international, law enforcement and civilian – will continue to play a critical role in preventing, detecting,

investigating and mitigating the effects of increasingly complex financial and electronic crimes and will continue to rely on its most valuable asset – its specially-trained, dedicated personnel in the field – to investigate these crimes, develop strong cases for prosecution, and bring offenders to justice.

Chairman Watt, Ranking Member Paul and distinguished members of the Subcommittee, this concludes my prepared remarks. I would be pleased to answer any questions that you may have.

Statement from Gary Marks, Chairman,
Citizens Coinage Advisory Committee to the
House Committee on Financial Services
Subcommittee on Domestic Monetary Policy and Technology
July 20, 2010

Mr. Chairman and members of the Committee,

Thank you for the opportunity to address the matter of design quality for the coins and medals produced by the United States Mint.

I am the Chairman of the Citizens Coinage Advisory Committee (CCAC). In 2003, Congress created the CCAC to "advise the Secretary of the Treasury on any theme or design proposals relating to circulating coinage, bullion coinage, congressional gold medals and national and other medals produced by the Secretary of the Treasury in accordance with section 5111 of title 31, United States Code."

As a committee designed specifically to advise the Secretary of the Treasury, the CCAC serves in an independent capacity from the United States Mint.

Over the past three years, members of the CCAC have expressed concerns to Mint officials that design proposals for various medals and for circulating and commemorative coinage programs have lacked the quality appropriate for the United States of America. Specifically, the lack of design quality has been evidenced in designs that are cluttered and lack focus (see Exhibit A, attached, for example), the use of design devices that are so small they cannot be readily discerned by the naked eye, and the use of what I call "storyboard" depictions that attempt to illustrate design themes in literal terms rather than through the use of allegorical or symbolic devices. Historically, some of this nation's most acclaimed coin designs have been achieved through the effective use of allegory and symbolism.

In other instances, the CCAC has been provided a single design proposal for a medal and asked to make a recommendation. If the CCAC finds the design unacceptable or lacking, production timelines are often so tight that the Mint is unable to provide alternate designs for review. In a similar vein, the CCAC was recently provided a set of three proposed designs for the obverse of the silver dollar for the 2011 Medal of Honor Commemorative Coin Program. All three designs were virtually the same except for a few small variations (see Exhibit B attached). When the choices we are asked to make become nearly meaningless for the lack of variation or because only one design is proposed, the ability of the CCAC to effectively administer its advisory role is severely diminished.

In a recent review of the 2011 United States Army Commemorative Coin Program, the CCAC was presented with a design showing a United States

soldier pointing a rifle in the direction of a United States Army helicopter; giving the unintended appearance of trying to shot it down (see Exhibit C attached). In another example, the Army emblem was rendered with inscriptions reversed from their official position (see Exhibit D1 – actual emblem – attached, and Exhibit D2 – Mint design – attached).

Despite these examples, members of the CCAC have been hopeful that necessary changes would be made and that, in fact, a renaissance in United States coinage design would occur. This hope has been founded in a vision articulated by Mint Director Edmund C. Moy in 2007.

During the Art Medal World Congress held in Colorado Springs in September of 2007, Director Moy issued a stirring call "....to spark a neo-renaissance for coin design and achieve a new level of design excellence..."

I count myself as a strong supporter of the vision to bring about the neo-renaissance the Director has called for. I know that many of my fellow members on the CCAC share the same or similar convictions and desire to see a true modern revival of excellence for the designs of our nation's coinage.

Yet, nearly three years after the Director's call for design excellence, members of the CCAC continue to express dissatisfaction with the Mint's design proposals.

Let me be very clear. It is not my intent to find blame or to point fingers, but rather to identify what must happen going forward to bring about the positive change we desire. Let me also be very clear that the Mint's art staff is highly skilled and very capable of producing high quality designs. I have seen moments of genius from these artists and I believe the answer will be found when we discover what changes need to be made to liberate them to perform at their full potential.

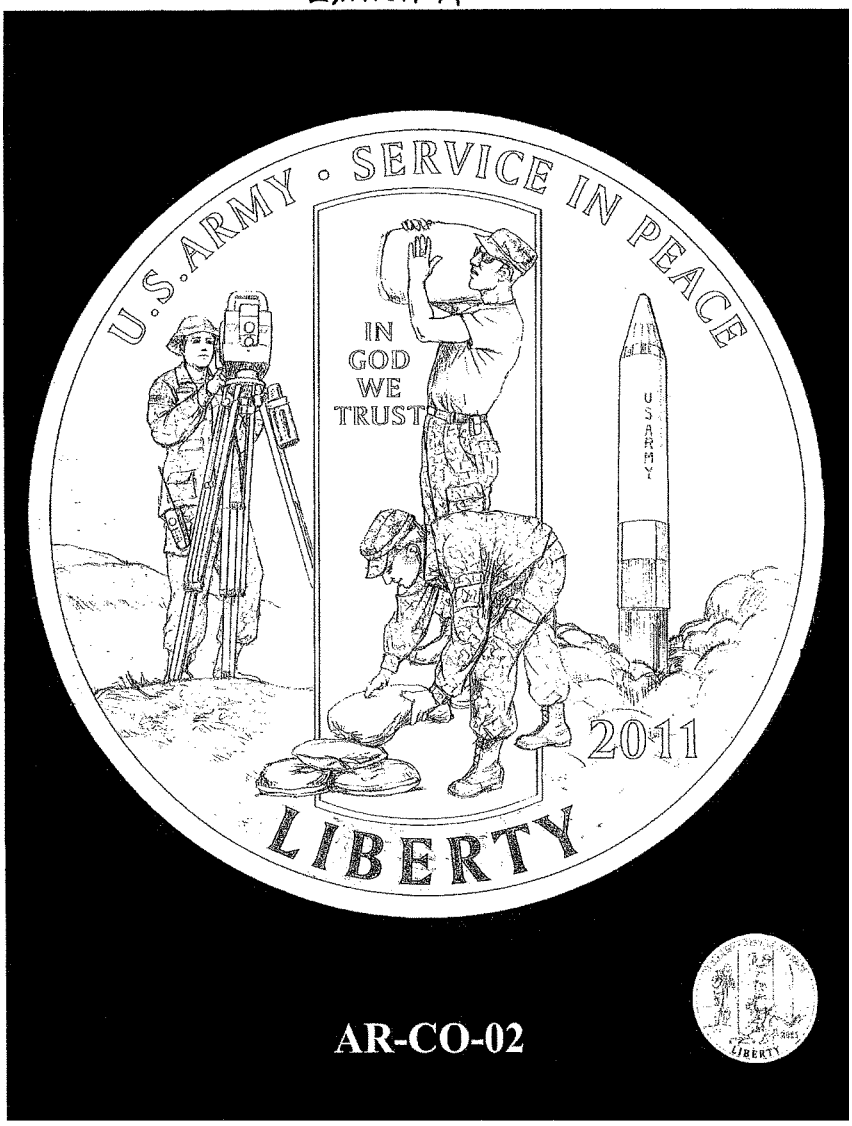
Therefore, acting in my statutory role of the CCAC's Chairman, I recently appointed a Subcommittee on Coin Design Excellence comprised of five CCAC members. I have given the subcommittee the task of investigating the Mint's design processes, identifying changes that would lead to improved designs and subsequently developing recommendations designed to further the needed changes. It is my intent that such recommendations would be issued by the CCAC to the Secretary of the Treasury within the next several months.

Once the CCAC has issued its design quality recommendations, I would be pleased to provide copies to this committee or to any Members who might be interested.

The CCAC's FY2009 Annual Report has just been released and is available to all interested parties here in the meeting room.

Thank you for the opportunity to report to you on the design quality issue and the CCAC's recent efforts to develop recommendations for improvement. I would be pleased to answer any questions that you might have.

Exhibit A



AR-CO-02

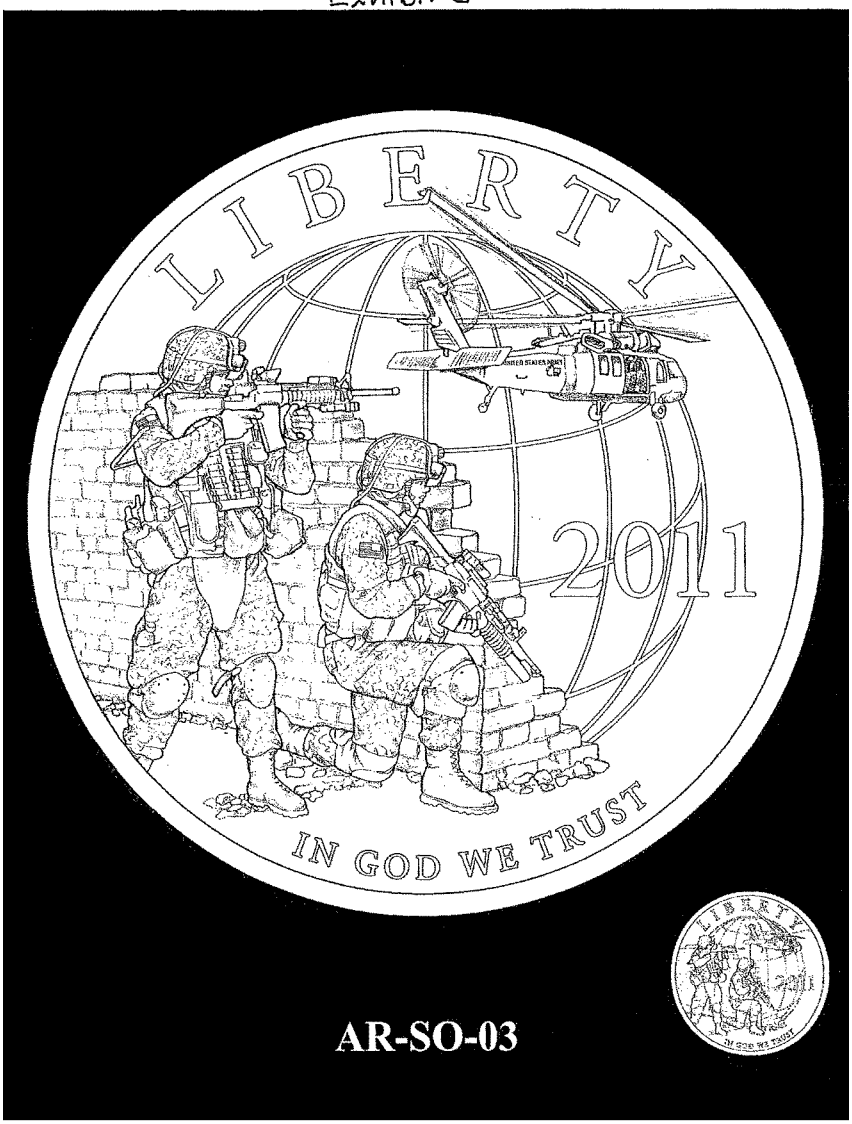
Exhibit B

MOH SO-01

MOH SO-02

MOH SO-03

Exhibit C

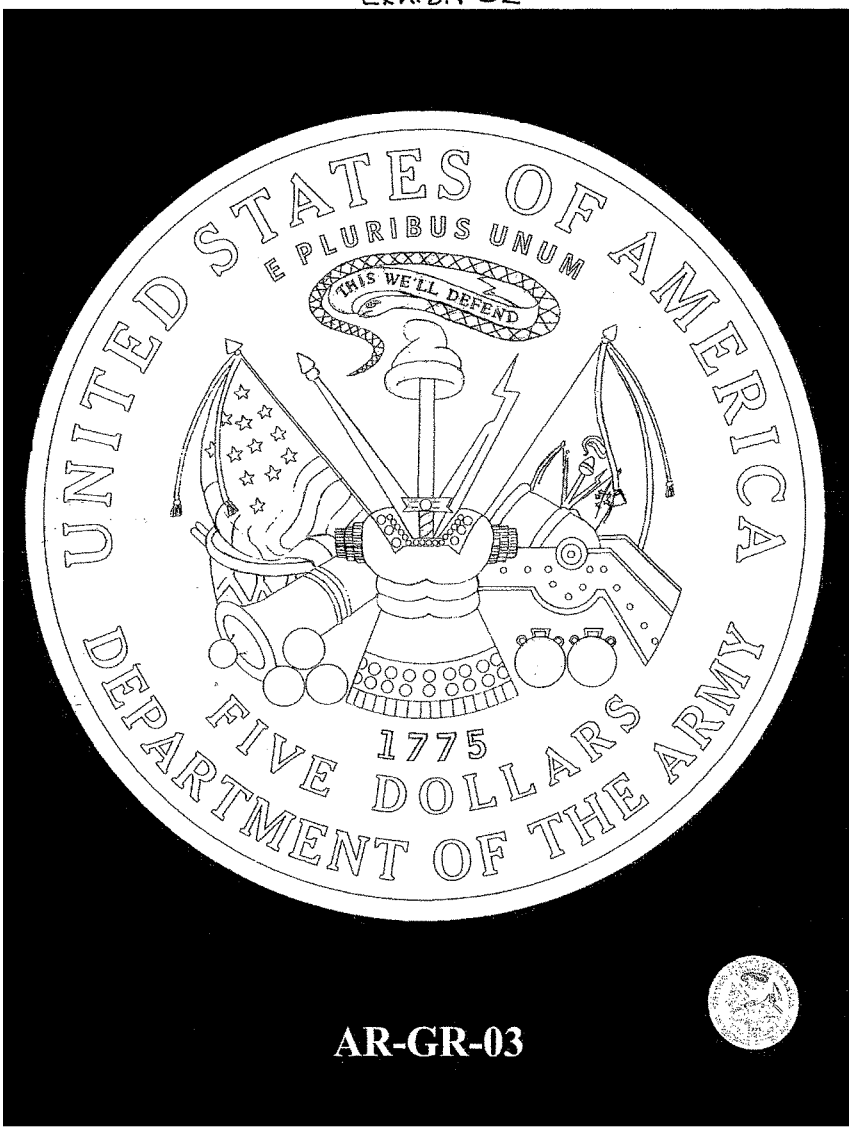


AR-SO-03

Exhibit D1

DEPARTMENT OF THE ARMY
UNITED STATES OF AMERICA
THIS WE'LL DEFEND
1775

Exhibit D2



AR-GR-03

TESTIMONY OF

EDMUND C. MOY

DIRECTOR, UNITED STATES MINT

BEFORE

THE SUBCOMMITTEE ON DOMESTIC MONETARY POLICY AND TECHNOLOGY

UNITED STATES HOUSE OF REPRESENTATIVES

JULY 20, 2010

Chairman Watt, Ranking Member Paul, Members of the Subcommittee, thank you for inviting me here today. I welcome the opportunity to appear before this subcommittee to provide you with this report on the operations and programs of the United States Mint. I will also provide you information today that will clearly demonstrate the need for immediate passage of the "Coinage Materials Modernization Act," the Administration's legislative proposal that has the potential of saving over a billion dollars in the next ten years by adopting suitable and acceptable lower-cost materials for the Nation's circulating coinage.

OPERATIONS AND PROGRAMS OF THE UNITED STATES MINT

At the conclusion of Fiscal Year 2009, I reported that the United States Mint:

- transferred $440 million in seigniorage to the Treasury General Fund through the sales of circulating coinage to the Federal Reserve Banks (the lowest seigniorage over the most recent five years because of low circulating coin demand and higher costs of metal);
- transferred $35 million in numismatic net revenues to the Treasury General Fund (this amount is the FY 2008 net revenues, less protection expenses returned);
- minted and issued 5.2 billion circulating coins to fill orders from the Federal Reserve Banks (during an average year, the Federal Reserve would order, and the United States Mint would mint and issue, 15 billion circulating coins);
- reported $440 million in numismatic revenues (lower than the average of the last three fiscal years by 19 percent);

- minted and issued 27.6 million ounces of gold, silver and platinum bullion coins (triple the amount of recent years).

I will now discuss more fully the major forces behind these results and the programmatic consequences resulting from them.

Circulating Coinage

The primary mission of the United States Mint is to mint and issue circulating coinage to meet the needs of the United States. Circulating coin production was at a 45-year low in 2009 because of low coinage demand and high inventories of coins in the Federal Reserve Banks. Total circulating coins shipped to Federal Reserve Banks decreased 47.8 percent – to only 5.2 billion coins in 2009 – and continued the decline in orders that began in 2008 when 10 billion circulating coins were ordered. Our most recent orders from the Federal Reserve Banks show increased demand for the next 12 calendar months at 7 billion.

As the Subcommittee knows, the United States Mint does not use appropriated funds for its operations and programs, but instead retains receipts from the sale of circulating coins to the Federal Reserve Banks to fund the bureau's circulating coinage costs. The United States Mint is committed to the goal of keeping the unit cost of production of each coin as low as practicable. However, the cost of the metals and alloys that Federal law requires us to use for our circulating coinage has become significant, affecting the circulating financial results. In fiscal year 2009, the United States Mint transferred to Treasury $427.8 million in seigniorage from circulating coins. The $1 coin

accounted for 74.5 percent, the quarter-dollar coin for 30.9 percent, the dime coin for 3.6 percent, the 5-cent coin for -0.5 percent, and the one-cent coin for -4.6 percent of total Fiscal Year 2009 seigniorage.

Implementing 2010 Circulating Coin Programs

Since inception of the various $1 coin programs, the United States Mint has issued 3.9 billion $1 coins, of which the Federal Reserve Banks hold 1.1 billion $1 coins in their inventories. These include the Susan B. Anthony Dollar, the Golden Dollar featuring Sacagawea, the Presidential $1 Coin and the Native American $1 Coin.

Of the 3.9 billion, the United States Mint has distributed 1.7 billion Presidential and Native American $1 Coins since 2007. We have continued to encourage the awareness and use of these coins, spending about $30 million on these efforts since the Presidential $1 Coin Act of 2005. These efforts have resulted in some successes, which include use by transit systems in New York and Washington, D.C. and general acceptance of the $1 coin; however, most Americans are not using $1 coins often in their daily transactions.

We have fulfilled our statutory requirement to aggressively and cost effectively promote the use of the $1 coin. This has included identifying, analyzing and removing obstacles to the robust circulation of the coin. However, despite these efforts, the Federal Reserve Banks have an inventory of approximately 1.1 billion $1 coins. This inventory level is of great concern to us. Generating robust $1 coin circulation and drawing down

existing coin inventories depend on far greater utilization where most consumer cash transactions occur—at the cash register. While we continue to explore innovative, yet cost-effective ways to encourage sustained use of the $1 coin at the retail level, we are unsure as to whether we can cost effectively achieve significant and sustainable increases in $1 Coin circulation.

In 2010, the United States Mint began a new 12-year circulating commemorative coin program authorized by Congress and approved by the President in December 2008, known as the America the Beautiful Quarters™ Program. These coins will commemorate a national park or other national site in each state, the District of Columbia and five U.S. territories. Under this program, the United States Mint will issue quarters at the rate of five new reverse designs per year in the order in which the featured site was first placed under Federal conservancy as a national park or site. We seek to ensure that this new program will generate the same financial success, interest from the public, and benefits to children and educators that we experienced with the 50 State Quarters Program.

Thus far, production levels are a fraction of those for the 50 State Quarters Program—in part attributable to low demand from both the economic conditions and the Federal Reserve Banks' existing inventories of previously issued quarter-dollar coins. As of June 22, we have sold 97 bulk bags of the Hot Springs National Park and Yellowstone National Park Quarters, totaling 19.4 million quarters, through this bulk purchase program. Later this year, we also will make available for sale to Authorized Purchasers

the three-inch five-troy ounce .999 fine silver bullion quarter-dollar coins bearing the designs that duplicate each of the America the Beautiful Quarters Program coins.

Gold, Silver and Platinum Bullion Coin Programs

Uncertainty surrounding traditional investments and concerns about inflation drove investor demand for bullion precious metals in all forms to exceptional highs in 2009. Demand seemed to be subsiding in early 2010 but in May 2010, we again saw an increase in orders for silver bullion coins to over 3.6 million—near a historic high for a month. In Fiscal Year 2009, bullion coin sales approached $1.7 billion—an all-time high and nearly 80 percent above the previous year's sales. The United States Mint increased both planchet acquisition and production to meet rising demand. We sold 27.6 million ounces of gold, silver and platinum bullion coins, up 9.2 million ounces from Fiscal Year 2008 and a 132 percent increase over average annual bullion coin sales since Fiscal Year 2005. We had no difficulty in obtaining gold, silver and platinum in raw material form, but we experienced considerable difficulty in getting this raw material fabricated into planchets by our vendors in sufficient quantities to meet public demand.

There were three significant consequences for the United States Mint from this increased worldwide demand for bullion. First, orders for gold and silver bullion coins from Authorized Purchasers exceeded supply for all of Fiscal Year 2009. As a result, we established an allocation system under which each Authorized Purchaser received partial fulfillment based on its order history.

Second, sales of discretionary gold and silver proof and uncirculated coins, which use the same planchets as their mandatory bullion coin counterparts, were hurt because we had to divert all incoming planchets in our effort to fulfill our statutory obligation to meet public demand for bullion coins. As a consequence, we did not mint and issue the very popular American Eagle One-Ounce Proof Gold and One-Ounce Proof Silver Coins in 2009.

Third, because we could not produce these popular coin products, those who had become accustomed to purchasing them on an annual basis were very disappointed. As Director of the United States Mint, I appreciate the disappointment of these collectors, but I am encouraged to know that the Subcommittee is exploring the possibility of an amendment to the law that would afford the Secretary the authority to approve the minting and issuance of American Eagle Silver Proof and Uncirculated Coins even when we are unable to meet the public's demand for the bullion versions of these coins. American Eagle coin collectors and our many other customers who purchase these products as gifts would likely welcome such a change. Indeed, such a change would be one of the most positive customer satisfaction measures that could be taken to benefit your coin collecting constituents without having an effect on American's ability to acquire investment-grade silver bullion. We have already provided you technical drafting assistance that your staff have requested to accomplish this change; however, such a change needs to be enacted soon. We can mint 200,000 per month, and if we can begin by September, we will be able to produce about 830,000 one-ounce

silver American Eagle coins to meet collector demand for this product in the remaining months of 2010.

Numismatic Products

Our numismatic programs experienced some rough retail conditions in Fiscal Year 2009 as the economic conditions weakened retail sales across the country, and because we were unable to make the American Eagle numismatic coin products available for sale. Net revenue stood at $41 million for the year; based on gross revenues of $440 million, this means we successfully met our mandate that the numismatic program be self-sustaining while keeping our product prices as low as practicable.

The 2009 Ultra High Relief Double Eagle Gold Coin demonstrated the production excellence that can be accomplished using present-day technology to achieve the intent of classic American coinage. In addition, two 2009 commemorative coin programs were executed as authorized by law: the Abraham Lincoln Commemorative Coin Program and the Louis Braille Bicentennial-Braille Literacy Commemorative Coin Program. These commemorative coin programs are authorized, in part, to provide funding, through qualifying surcharges, to their designated recipient organizations. Total sales of the Lincoln Commemorative Coin were $19.2 million with $5 million being available to the Abraham Lincoln Bicentennial Commission to further its work. Total sales of the Braille Commemorative Coin were $8.3 million with $2.2 million available to the National Federation of the Blind to further its programs to promote Braille literacy.

This year we are carrying out the American Veterans Disabled for Life Commemorative Coin Program and the Boy Scouts of America Centennial Commemorative Coin Program.

2010, 2011, 2012 Coin and Medal Design, Approval and Production

The United States Mint is currently working on approximately 100 distinct coin and medal designs for programs from 2011 through 2013, including five Congressional Gold Medals or other medal programs, and more are expected. This is a large and challenging workload for our staff, artists, sculptor-engravers, die-makers and others who produce multiple designs for consideration by the parties that review this work, including the Citizens Coinage Advisory Committee, the U.S. Commission of Fine Arts, affinity organizations, and medal recipients or their designees. There is an enormous amount of behind-the-scenes planning and creative work by hundreds of individuals to meet the standards of excellence in design, manufacturing, and marketing to make these products successful. I am very grateful for the highly dedicated workers throughout all our facilities nationwide who make our work for the American public and for Congress possible.

COINAGE MATERIALS MODERNIZATION

Since 1982 alone, the taxpayers of this Nation have saved well over $71 billion through the foresight of our predecessors who, in 1965, had the courage to change the composition of our coins from silver to their current clad composition. Unfortunately, we do not have accurate data (i.e., prevailing market silver prices, clad (cupro-nickel alloy)

prices and mintage volumes from 1965 to 1981). Seventeen years of additional savings are thus unaccounted for. Now, in 2010 we stand at the cusp of an opportunity to achieve additional savings by passing the Coinage Materials Modernization Act.

Fiscal Year 2009 operational results show that all circulating coin denomination per-unit costs—with the exception of the 5-cent coin—have increased from the previous year. The per-unit costs for the one-cent and 5-cent coins continued to exceed their face values in Fiscal Year 2009, as they have since 2006. The chart below depicts the production costs of each circulating coin:

COST OF PRODUCING CIRCULATING COINS – FY 09				
One-Cent	Five-Cent	Dime	Quarter	$1
$0.0162	$0.0603	$0.0565	$0.1131	$0.340

As my staff and I have met with Members of Congress to discuss the spiraling costs of our Nation's coinage, we have heard only support and encouragement to come forward with a solution to address this problem. I am pleased that the Administration has taken an active interest in this matter and included a proposal in the Fiscal Year 2011 Budget ("Other Savings: Coinage Materials" attached).

The Administration proposal expands the Secretary of the Treasury's authority to determine the weight and composition of the $1 coin to all circulating coinage—the one-

cent, 5-cent, dime, quarter-dollar, and half-dollar coins. This approach will fairly and efficiently manage the highly technical evaluations of alternative materials using a transparent, open, deliberative, and market-driven process that will ensure the interests of all those parties that may be affected—be they vending machine operators, coin handling equipment manufacturers, banks, armored carriers, transit officials, or members of the general public—will be considered and appropriately served. Moreover, the proposal is a durable solution that would ultimately result in significant taxpayer savings by providing to the Secretary of the Treasury the flexibility to respond quickly to changing market conditions.

Saving Money

The current situation is unprecedented. Compared to their face values, never before in our Nation's history has the Government spent as much money to mint and issue coins and, with regard to the one-cent and 5-cent coins, never before has the Nation spent more to mint and issue a circulating coin than its legal tender value. This problem is needlessly wasting hundreds of millions of dollars.

However, the Department of the Treasury has decades of proven success in determining the materials for our highest and lowest coin denominations, and now we are proposing to save millions of dollars per year— over one billion dollars in the next 10 years—by determining the materials for the other coin denominations. This measure would affect the seigniorage earned by the United States Mint, revenue which is not included in the Federal Budget. As a practical effect, the savings realized from adopting

new materials for circulating coinage would not provide discretionary or mandatory offsets in the Federal Budget. Instead, the savings would reduce the U.S. government's need to borrow, providing a potential source of deficit reduction.

Congressional Precedent Exists for Delegating the Authority to Select Coinage Materials to the Secretary of the Treasury.

I want to stress that delegating the authority to test and select alternative materials to the Secretary of the Treasury is a sound, legal, and proven approach to determining the composition of our Nation's coinage.

Twice in the last 50 years, the Government took action to protect our taxpayers from needlessly bearing the increased costs of coinage materials. In 1965, as the value of silver climbed because of industrial demand, Congress approved a change in the composition of the dime, quarter-dollar, and half-dollar coins from silver to cupro-nickel clad. Similarly, in 1974, Congress granted to the Secretary of the Treasury the authority to vary the copper-zinc alloy of the one-cent coin. After several years of rising copper prices, again because of industrial demand, the Secretary exercised this authority in 1982, changing the alloys in the one-cent coin to its present composition of copper-plated zinc. So history and economic reality tell us why we are in the current situation, and also tell us that it will recur in the future if we fail to act. That is why the Administration seeks a durable solution that will substantially reduce the cost our citizens must pay for the Nation's coinage now and in the future.

By delegating the authority to the Secretary of the Treasury to select circulating coinage compositions, Congress can be assured such changes will be made effectively. The United States Mint would accomplish these changes by employing an open, public process to determine new coinage materials. Specifically, we will seek public and industry comment to ensure consideration of all factors relevant to the acceptability of new coinage materials, including physical, chemical, metallurgical and technical characteristics; material, fabrication, minting, and distribution costs; material availability, sources of raw materials, and environmental impact; coinability; durability; effects on sorting, handling, packaging and vending machines; appearance; resistance to counterfeiting; and commercial and public acceptance. Once the agency has a comprehensive inventory of these factors and their relative significance, the United States Mint would then employ an objective, competitive, and public process to solicit and evaluate proposals for new coinage materials.

CONCLUSION

Congress has already delegated the authority to select the composition of some coins to the Secretary of the Treasury, and the United States Mint, has capably coined money under laws passed by Congress since 1792. Thirteen years ago, Congress passed the United States $1 Coin Act of 1997, which granted to the Secretary of the Treasury the sole discretion to select the materials for the $1 coin. The Administration's current proposal builds on these precedents established by Congress. Indeed, it does no more and no less than the United States $1 Coin Act of 1997 did for the $1 coin.

Thank you, Mr. Chairman and Members of the Subcommittee. I am here to answer any questions you may have.

For release on delivery
2:30 p.m. EDT
July 20, 2010

Statement of

Louise L. Roseman

Director

Division of Reserve Bank Operations and Payment Systems

Board of Governors of the Federal Reserve System

before the

Subcommittee on Domestic Monetary Policy and Technology

of the

Committee on Financial Services

U.S. House of Representatives

July 20, 2010

Chairman Watt, Ranking Member Paul, and members of the Subcommittee, I am pleased to appear before you on behalf of the Board of Governors of the Federal Reserve System to discuss Federal Reserve activities related to currency and coin. I plan to touch on currency developments and management of coin distribution.

Roles in Currency and Coin Distribution

First, it may be helpful to describe briefly the Federal Reserve's role in currency and coin distribution. The Board issues the nation's currency in the form of Federal Reserve notes. The Federal Reserve Banks distribute currency and coin for general circulation through depository institutions. The Reserve Banks also receive deposits of currency and coin from these institutions. Currently, thirty Reserve Bank cash offices provide cash services to approximately 9,200 banks, savings and loans, and credit unions in the United States. The remaining depository institutions obtain currency and coin from correspondent banks rather than directly from the Federal Reserve.

Each year, the Board projects the need for new currency, which it acquires from the Department of the Treasury's Bureau of Engraving and Printing (BEP) at approximately the cost of production. Our new-currency budget for 2010 is $703 million. The Federal Reserve issues notes at face value, which are recorded as liabilities on the Reserve Banks' balance sheets. The Reserve Banks, as required by law, pledge collateral (principally U.S. Treasury, federal agency, and government-sponsored enterprise securities) equal to the value of currency in circulation. This collateral produces a substantial portion of the earnings that Reserve Banks distribute to the Treasury each year. In the years preceding the recent increases to the Reserve Bank balance sheets, when currency represented the large majority of Reserve Bank liabilities, the annual distributions to the Treasury generally ranged from $20 to $30 billion. In 2009, the Reserve Banks distributed $47.4 billion to the Treasury.

The Federal Reserve monitors trends in and publishes statistics on noncash transactions such as checks, credit and debit cards, and other electronic payments, but it does not publish statistics on individuals' use of cash.[1] Obtaining reliable data on cash transactions is more difficult because, unlike noncash payment methods, cash transactions do not flow through centralized systems at institutions that specialize in payments processing such as depository institutions and payment networks. Data on cash transactions would have to come from alternative sources, such as consumers or businesses, from whom representative data may be difficult to collect. Despite the difficulty of direct measurement of cash transactions, the Federal Reserve does monitor and study cash use in the United States through the information it collects in its role as currency processor, and from consumers and businesses. Although there is no direct information on trends in cash use, statistics on the growth in the use of noncash payment methods suggest some substitution away from cash in recent years. In addition, discussions Federal Reserve officials have had with select retailers suggest that cash transactions continue to grow although at a much slower rate than electronic forms of payment.

The Federal Reserve's role in coin operations is more limited than its role in currency operations. The United States Mint issues circulating coins that the Reserve Banks purchase at face value and record as assets on their balance sheets.[2] The Reserve Banks distribute new and circulated coin to depository institutions to meet the public's demand and take as deposits coin that exceeds the public's needs. The United States Mint determines annual coin production; however, the Reserve Banks influence the process by providing the Mint with monthly coin orders and a 12-month, rolling coin-order forecast. The Mint transports the coin from its production facilities for circulating coin in Philadelphia and Denver to the Reserve Banks'

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[1] The Federal Reserve publishes currency in circulation data in its weekly H.4.1 report. In addition, the Federal Reserve also reports Reserve Banks' payments and receipts of currency and coin into and from circulation.
[2] Coins held by the Reserve Banks are non-interest-earning assets on their books.

offices and offsite locations. While the Reserve Banks store some coin in their vaults, they also contract with coin terminals to store, process, and distribute coin on their behalf.[3] Armored carrier companies generally operate the coin terminals, which have improved the efficiency of the coin-distribution system. Today, 174 coin terminals store about 37 percent of the Federal Reserve's coin inventory volume, but account for about 88 percent of Reserve Bank daily distributional activity.[4] The value of U.S. coins in circulation as of May 31, 2010, was approximately $40.4 billion, or about 4.3 percent of total currency and coin in circulation.

Currency Developments

Trends in Currency Demand

The Federal Reserve measures demand for U.S. currency by the amount of currency in circulation. From 1980 to 2009, currency in circulation increased an average of 7.0 percent per year from $124.8 billion to $888.3 billion, as shown in chart 1.[5] Domestic demand for currency is largely based on the use of currency for transactions and is influenced primarily by income levels, prices of goods and services, the availability of alternative payment methods, and the opportunity cost of holding currency in lieu of an interest-bearing asset. In the United States, demand (in terms of number of notes) for smaller denominations ($1s through $20s) exceeds demand for larger denominations ($50s and $100s). Consumers frequently use smaller-denomination notes for small transactions and alternative payment methods (for example, debit and credit cards) for larger purchases. In contrast, foreign demand is influenced primarily by the

[3] These armored carrier companies do not charge the Reserve Banks a fee for these services. In the 1990s, the Federal Reserve and the armored carrier companies reached a mutually beneficial agreement that the armored carriers would provide coin services on behalf of the Federal Reserve at no cost in exchange for access at the armored carrier terminals to Reserve Bank coin inventories, which significantly reduced the transportation expenses incurred by the armored carriers in obtaining the coin from Reserve Bank locations.

[4] The armored carrier companies are most interested in storing coin that is routinely used in cash transactions (primarily pennies, nickels, dimes, and quarters) because they can charge fees to the depository institutions for providing coin services in preparing the coin for sale to their customers.

[5] The value of currency in circulation was $242.3 billion at year-end 1989; $601.2 billion at year-end 1999; and $888.3 billion at year-end 2009.

political and economic uncertainties associated with certain foreign currencies, which contrast with the U.S. dollar's historically relatively high degree of stability. Because U.S. currency is held abroad primarily as savings, foreigners tend to hold high-denomination notes. The Federal Reserve estimates that as much as two-thirds of currency in circulation is held abroad.[6]

The foreign component of currency in circulation is estimated to have increased significantly beginning in the late 1980s and continues to grow today. In the 1990s, currency in circulation grew at an average annual growth rate of approximately 7.7 percent, resulting primarily from increases in foreign demand and a surge in demand at the end of the decade.[7] As shown in chart 2, during the decade beginning in 2000, the average annual growth rate of currency in circulation moderated to about 5.3 percent (which is a rate consistent with growth during the 1960s). As reflected in chart 3, however, annual growth rates began to decline in 2001 and significantly declined to below one percent in 2008 (through August). Demand slowed over this period partly because the value of the dollar decreased against many other major currencies; international markets gained trust in their own economies and national currencies; electronic payments displaced some cash usage; and the effect of the recent recession. This decline was reversed, however, beginning in September 2008, as currency demand increased significantly as a result of the financial crisis. Currency growth increased substantially, from 0.8 percent year-to-date through August 2008 to 7.7 percent for full-year 2008. As the effects of the financial crisis persisted, strong growth continued in 2009; currency in circulation increased from $775 billion at the end of 2007 to almost $900 billion by year-end 2009. As of May 31,

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[6] In addition to being used as a store of value, U.S. currency is also used broadly for transactional purposes in officially dollarized countries, such as Panama, Ecuador, El Salvador, and East Timor, and in other countries where the U.S. dollar co-circulates with local currencies.

[7] In preparation for the century date change, currency in circulation increased 22.1 percent from its December 1998 level. Uncertainty associated with the century date change increased the public's precautionary demand for cash, but as the event passed without incident, the public returned much of the currency it had amassed to depository institutions.

2010, the value of currency in circulation was $902.2 billion, or about 95.7 percent of total currency and coin in circulation.

The effects of the financial crisis on currency in circulation domestically were less significant than on currency in circulation internationally. Although domestic demand appears to have increased briefly in the fall of 2008, the increase of the FDIC deposit insurance limit and other government actions to address the crisis allayed domestic concerns and demand seems to have returned quickly to normal levels. The majority of the growth rate increase was driven by demand for $100 notes internationally. The Federal Reserve requested that the BEP accelerate the Board's print order for $100 notes during this period so that the Reserve Banks could continue meeting international demand.[8] Although payments of $100 notes abroad have returned to normal levels, most of the currency the Reserve Banks paid into circulation during the financial crisis remains in circulation as Reserve Bank receipts from circulation remain historically weak.

Evolving Currency Designs of Federal Reserve Notes

The U.S. government redesigns U.S. currency to improve its security and protect the public from counterfeiters. Through an interagency cooperative agreement of the Treasury Department and its Bureau of Engraving and Printing, the Federal Reserve System, and the United States Secret Service, the Board participates on the Advanced Counterfeit Deterrence Steering Committee (ACD) and recommends U.S. currency design changes to the Secretary of the Treasury, who has sole statutory authority to approve new currency designs. Decisions about the redesign of each denomination are guided by the ACD's evaluation of the range of ongoing

[8] Chart 4 shows the Federal Reserve's annual currency print orders from the BEP from 1990 through 2010.

counterfeit threats from digital technology and traditional printing processes, and advancements in banknote security features.[9]

Through this cooperative effort, in 1996, the United States produced the first significant redesign of U.S. currency in 65 years (the Series-1996 design family). This redesign began with the $100 note in March 1996 and concluded with the $5 and $10 notes issued together in May 2000. The 1996-design family incorporated portrait watermarks, embedded security threads, and color-shifting ink to combat the predominant threat of the traditional counterfeiter. To address a phenomenon known as "opportunistic counterfeiting," which is the use of digital technology available in the home by non-professional or casual counterfeiters, the ACD recommended another redesign of the currency, which began with the $20 note in October 2003, followed by the $50 note in 2004, the $10 note in 2006, and the $5 note in 2008.

The final denomination in the 2004-design family, the $100 note, was unveiled on April 21. The unveiling of the $100 note was the first step in a multi-agency program to educate consumers, businesses, banks, and governmental entities around the world about the new $100 note before it begins circulating. Under the auspices of the ACD, we conducted extensive qualitative and quantitative research to understand better how domestic and international users verify the authenticity of the $100 note. Through this research, three major points emerged: (1) those who use U.S. currency do not want drastic changes when we introduce new designs and prefer only a few security features that are easy to use; (2) the security features in the current-design $100 note are considered effective; and (3) it was important to some users that any new

[9] The ACD has set as general policy guidance that currency will be redesigned every 7 to 10 years depending on specific counterfeiting threats and experience related to a particular denomination. The first Series-2004 design family of notes was issued about seven years after the first Series-1996 note was issued.

security features can be used discreetly.[10] Building on the currency-design efforts that began in 2003, this note reflects what we learned from the research and includes new, state-of-the-art security features such as the 3-D security ribbon and the color-shifting bell in the ink well. The Federal Reserve will begin distributing the new $100 note on February 10, 2011.

Management of Coin Distribution

The Federal Reserve has been working for some time to improve the efficiency of the Reserve Banks' coin activities by implementing a program to manage coin distribution from a national perspective. Before the Federal Reserve moved to centralized management of coin distribution, each Reserve Bank made independent ordering and distributional decisions. Today, the Reserve Banks' national Cash Product Office (CPO) manages coin nationally for the Federal Reserve System, taking into account the Reserve Banks' input regarding local estimates of coin demand. The CPO produces a consolidated monthly coin order on behalf of the Reserve Banks for the United States Mint. Along with the order, the CPO provides the Mint with a rolling, 12-month order forecast for planning purposes. The key element of the CPO's forecast is predicting net payments to circulation--the difference between payments to and receipts from circulation. The order and forecast are based on expected net payments relative to Reserve Banks' inventory levels. The Reserve Banks ensure sufficient inventories are positioned at each office and coin terminal to meet the forecasted demand.

As a result of improved inventory management, over the past five years, the Reserve Banks have increasingly used previously circulated pennies, nickels, and dimes to fill orders from depository institutions while decreasing their orders for these coins from the United States Mint by almost 31 percent, compared with the average orders over the previous five years, as

[10] The two primary security features (portrait watermark and embedded security thread) in the current-design $100 note require the user to hold the note up to light to check for authenticity. Although these features will remain in the new-design $100 note, new security features have been added that will require only slight movements of the note to authenticate.

shown in chart 5. This has reduced Reserve Bank inventories of pennies, nickels, and dimes as of May 31, 2010, to their lowest levels since early 2000, although they are still sufficient to meet demand.[11] The Reserve Banks have not experienced surpluses or shortages of pennies, nickels, or dimes since 1999 when they experienced a temporary shortage of pennies.

Commemorative Circulating Coins

Demand for coin for transactional purposes can be met by any design of a denomination. For example, a retailer that orders quarters from its bank typically does not care what design(s) it receives. Demand for a commemorative circulating coin by collectors, however, is design-specific. In the early years of the 50 State Quarters program, the Reserve Banks ordered more new quarters than were necessary to meet demand in order to fill many depository institution orders with new coins rather than with available inventories of circulated quarters. The residual coins from each release, plus the excess quarters redeposited by depository institutions, created excessive inventories at the Reserve Banks. The Reserve Banks were able to reduce those inventories because of regular demand for quarters.[12] Because of low transactional demand for $1 coins, however, the Federal Reserve's experience with commemorative circulating $1 coin programs has differed significantly. For previous $1 coin programs, the Reserve Banks have encountered large excess inventories for much longer periods, and our experience with the Presidential $1 Coin Program is consistent with those programs.[13]

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[11] As of May 31, 2010, the Reserve Banks held about 1.5 billion pennies, 343 million nickels, and 546 million dimes.

[12] The Reserve Banks' quarter inventories reached a peak of 3.0 billion pieces in January 2003 and declined to 2.1 billion by year-end 2007. Inventories increased significantly in 2008 and 2009, however, because of considerably lower payments to circulation during the recession. The Reserve Banks expect to reduce those inventories once again, as demand improves. During 2010 through May, improved demand enabled the Reserve Banks to reduce inventories by almost 500 million pieces, or a 13 percent reduction since year-end 2009. As of May 31, 2010, the Reserve Banks held 3.3 billion quarters.

[13] Because there is almost no transactional demand, Reserve Bank inventories of half-dollar coins also increase each year. Since 2001, Reserve Banks' inventories have increased by 110 million pieces even though the Reserve Banks have only ordered 24 million pieces over that time period.

Presidential $1 Coin Program

Before the Presidential $1 Coin Program began in 2007, demand for $1 coins, measured in Reserve Banks' net payments to circulation, was about $60 million per year (for comparison, net payments of $1 notes to circulation in 2006 were $289 million). Reserve Banks' payments to circulation increased significantly in the first year of the Presidential $1 Coin Program but have consistently declined since that time, while receipts from circulation have significantly increased.[14] With Reserve Bank payments to circulation decreasing and receipts increasing each year of the program, Reserve Banks' inventories of $1 coins are growing substantially. As shown in chart 7, previous $1 coin supplies, plus the excess $1 coins returned by depository institutions, have elevated total Reserve Banks' inventories of all $1 coins to almost $1 billion as of May 31, 2010, compared with $67 million before the start of the program. At the current rate of inventory growth, the Federal Reserve estimates that it could hold as many as $2 billion by the time the program is expected to end.[15] This inventory growth, in large part, is because a requirement in the Presidential $1 Coin Act requires the Federal Reserve to make each new design available to the public in unmixed quantities for an introductory period. Therefore, the Reserve Banks must order each new design from the Mint even though the Reserve Banks have ample inventories of $1 coins.

Banking industry and armored carrier representatives have indicated that transactional demand for $1 coins has not increased materially since the start of the Presidential $1 Coin Program and that overall demand continues to come primarily from collectors. They have also indicated, however, that the program is working very well from their perspectives, that the coins

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[14] As chart 6 indicates, depository institution demand has decreased for each successive Presidential $1 coin design. About 70 percent of $1 coin payments to circulation occur during the special ordering periods for each new release.
[15] Because of the reluctance of most armored carrier companies to hold excess inventories of $1 coins that have low transactional demand and Reserve Banks' vault storage contraints, the Federal Reserve is investigating additional options to store these coins. The Reserve Banks have currently identified additional storage options at estimated one-time costs of about $6 million.

are easy to order, and that our communication about program details is effective.[16] Most representatives did not believe that demand would increase significantly for future coin releases, with the possible exception of the coins commemorating the most popular former Presidents.

Native American $1 Coin Program

The Native American $1 Coin Act requires that at least 20 percent of all $1 coins minted and issued in any year be Native American $1 coins. Because the Reserve Banks already have excessive inventories of $1 coins, the Reserve Banks do not plan to purchase Native American $1 coins unless needed to meet demand.[17] As a result of the legislative requirement to issue these coins, the Mint began paying Native American $1 coins (and some Presidential $1 coins) directly to circulation through its Direct Ship program, which allows the public to order boxes of $1 coins in $250 increments. The Mint indicates that it paid to circulation $12 million $1 coins in 2008 and $121 million in 2009.[18]

Total Demand for $1 Coins

Taking into consideration the Reserve Banks' net payments to circulation and the Mint's direct payments to circulation, total demand for $1 coins in 2009 was nearly triple that of 2006, before the start of the Presidential $1 Coin Program. This increase, however, was from a very low base of only $60 million per year. Demand has declined by two-thirds since the initial year of the Presidential $1 Coin Program.[19] It is unclear what portion of $1 coin demand is for transactional versus collector purposes, or where demand for $1 coins will ultimately stabilize. What is clear, however, is that the legislative requirements associated with these programs are

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[16] The Federal Reserve meets at least annually with representatives of depository institutions with the largest cash volumes, community bankers, and armored carriers to gather feedback about demand and potential obstacles to the circulation of $1 coins.

[17] See 2007 Annual Report to the Congress on the Presidential $1 Coin Program, page 24. http://www.federalreserve.gov/boarddocs/RptCongress/dollarcoin/dollarcoin.htm.

[18] The Mint is not currently charging shipping and handling fees for this program.

[19] Considering both the Reserve Banks' net payments and the Mint's direct payments, total $1 coin demand was $513 million in 2007, $235 million in 2008, and $171 million in 2009.

resulting in steadily rising Reserve Bank inventories and the attendant costs of dealing with those inventories.

Metal Content of Coins

As the issuing authority for currency, the Federal Reserve appreciates the importance of identifying and incorporating cost-effective materials into the production of our nation's money. We commend the United States Mint for seeking solutions to the problem of higher raw material costs. Changing the metal content of pennies and nickels, even if doing so changes the weight and electronic signature, would not have a material adverse effect on the operations of the Reserve Banks. The Reserve Banks stopped routinely weighing penny and nickel deposits in 2003 after determining that the costs exceeded the benefits of doing so. Instead, the Reserve Banks give depository institutions credit on deposits of coin on a "said to contain" basis. As a result, we do not anticipate significant internal operational challenges associated with any such changes. Changing the metal content of dimes, quarters, half-dollars, and $1 coins, if it affects the respective weights, could affect Reserve Bank coin terminal operations. Coin terminal operators weigh incoming deposits of these denominations.

If a change in metal content changes a coin's weight or electronic signature, it could materially affect businesses that use coin-accepting machines, such as the vending industry, or other businesses that rely on these characteristics. While such a change probably would not be a material issue with respect to pennies, which are generally not accepted in vending equipment, it may be for larger-denomination coins. Those businesses are better placed to comment on the extent to which they would be required to make changes to their equipment to recognize coins of the same denomination that have different weights and electronic signatures.

Conclusion

The Federal Reserve will continue to work to meet demand for currency and coin efficiently and effectively. I appreciate the opportunity to discuss these issues with you and would be happy to answer your questions.

Chart 1

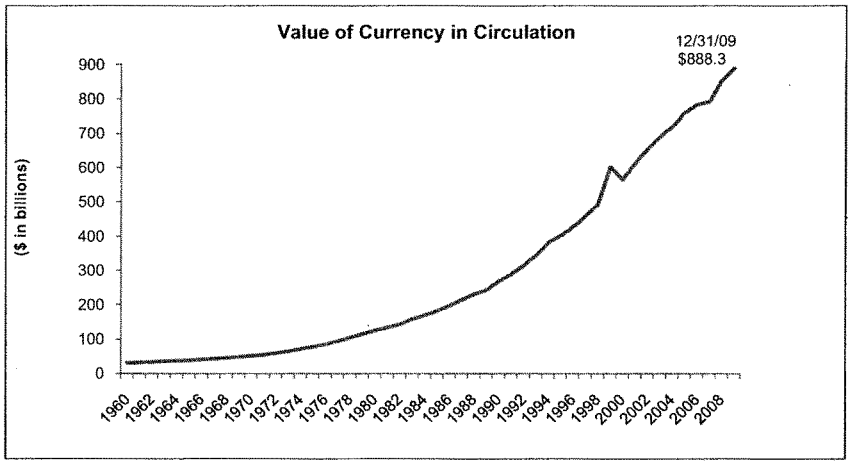


Chart 2

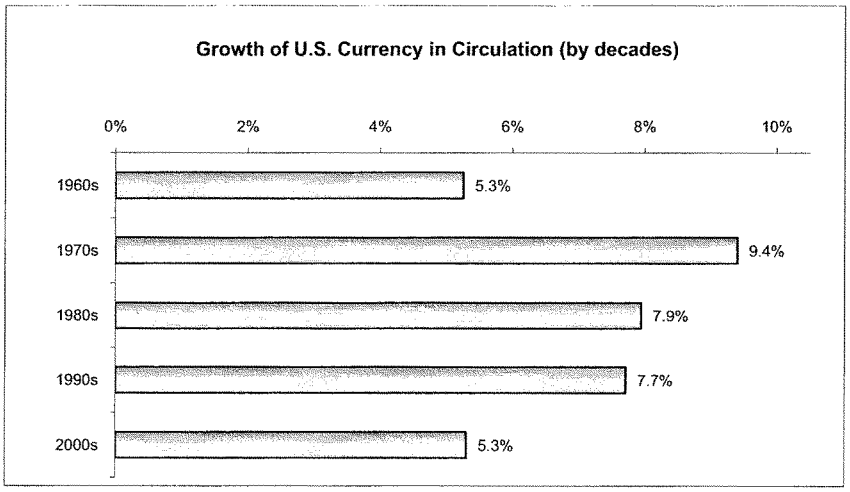


Chart 3

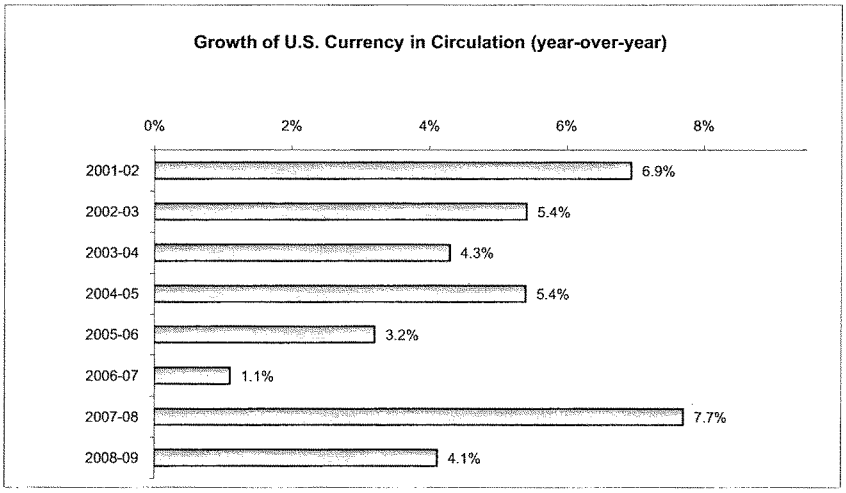


Chart 4

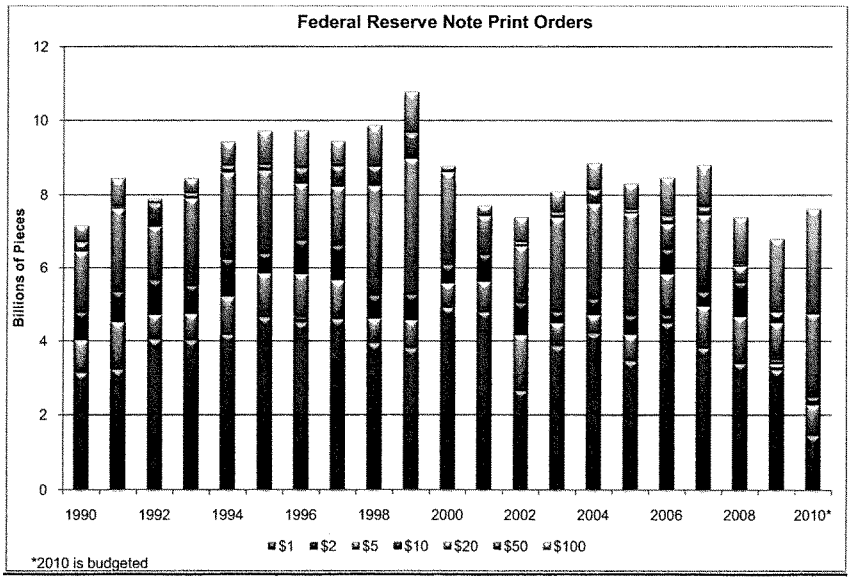
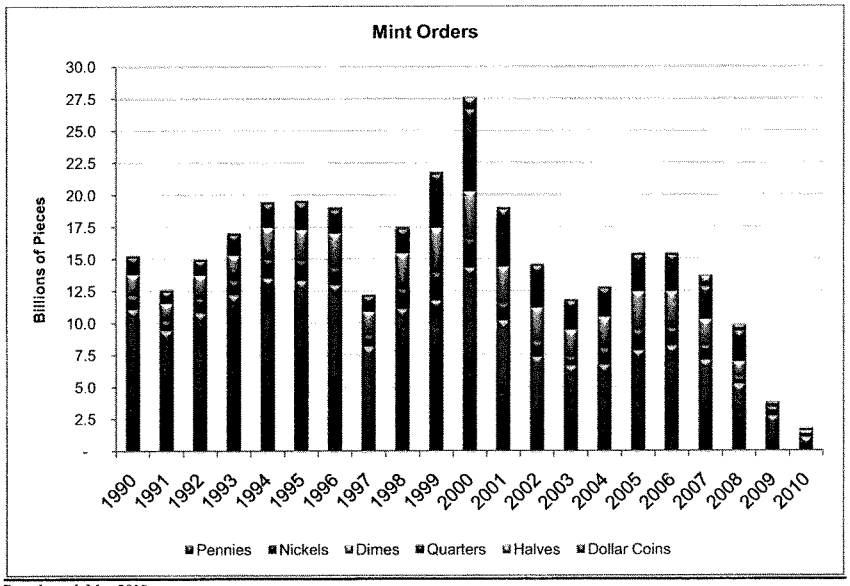
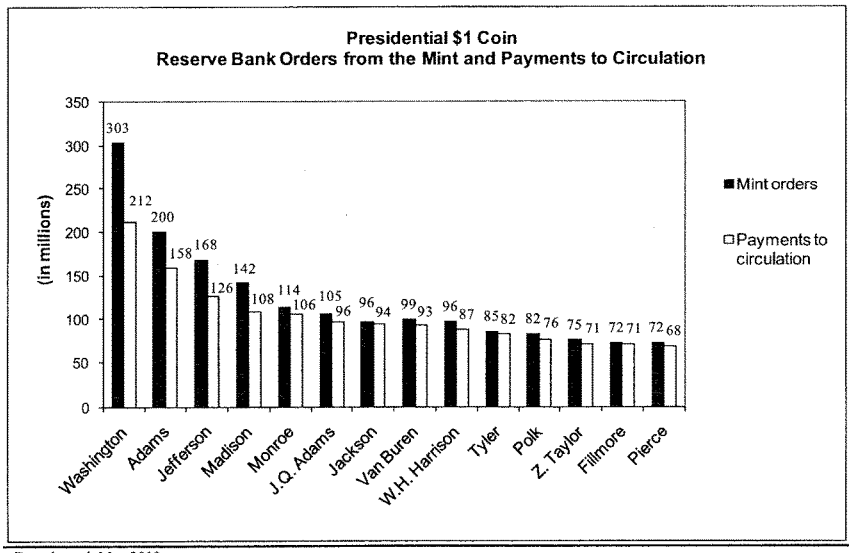


Chart 5



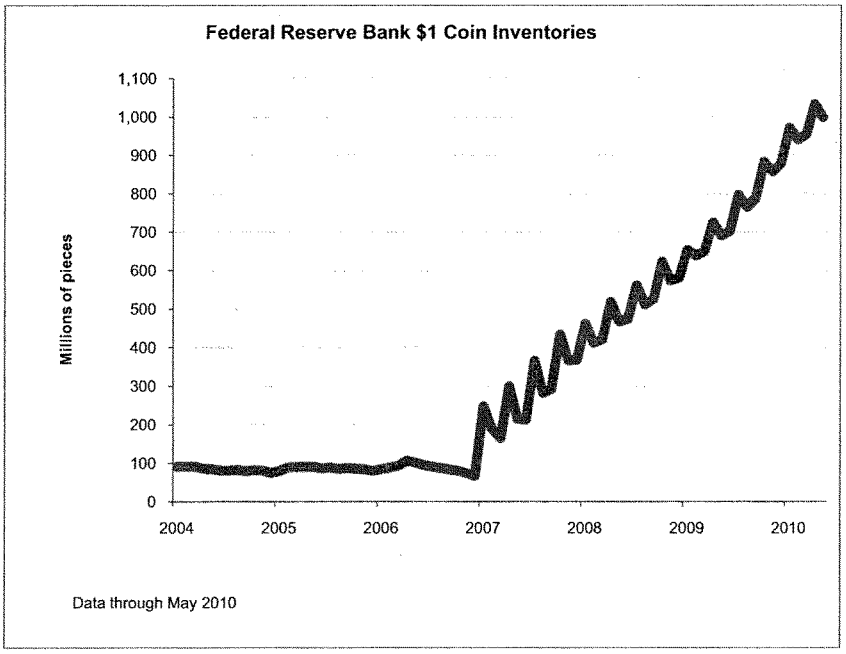
Data through May 2010

Chart 6

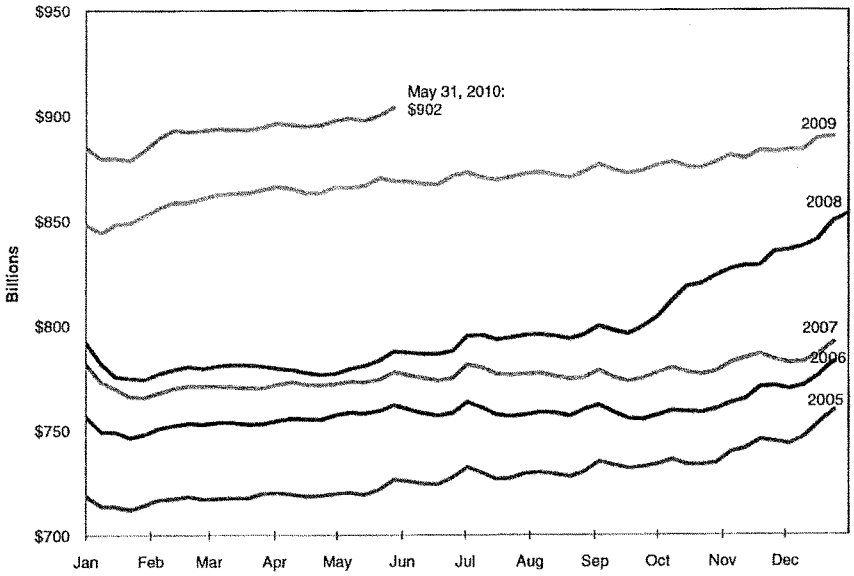


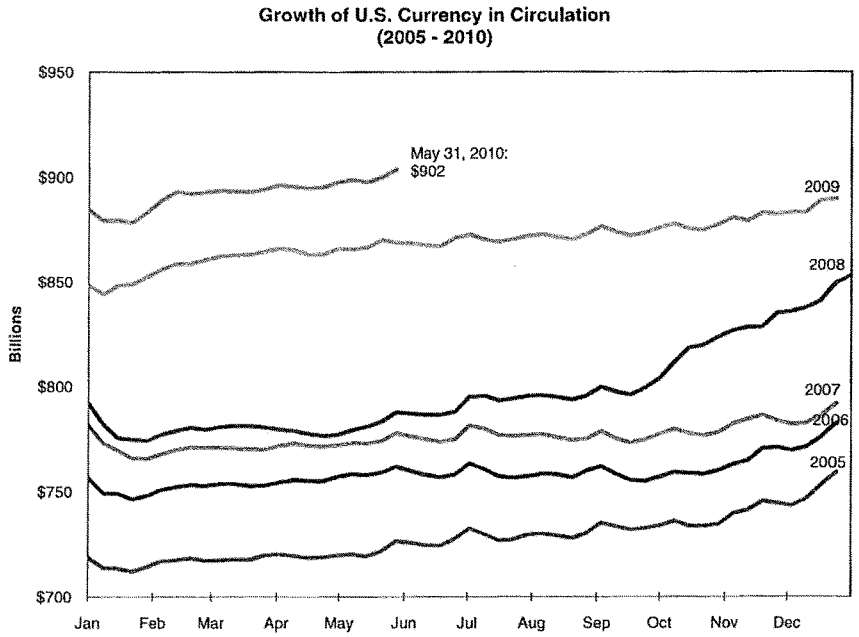
Data through May 2010

Chart 7


Federal Reserve Bank $1 Coin Inventories
Millions of pieces
1,100
1,000
900
800
700
600
500
400
300
200
100
0
2004
2005
2006
2007
2008
2009
2010
Data through May 2010

Growth of U.S. Currency in Circulation
(2005 - 2010)




Growth of U.S. Currency in Circulation
(2005 - 2010)
$950
$900
$850
$800
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Billions
May 31, 2010:
$902
2009
2008
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2006
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Jul
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Sep
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Nov
Dec

Serving the Vending, Coffee Service and Foodservice Management Industries

August 26, 2010

Mr. Thomas G. Duncan
General Counsel
The U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Dear Mr. Duncan

Thank you for the opportunity to respond to Chairman Watt's questions regarding the impact of the Dodd-Frank Act.

1. Has NAMA studied the projected impact of the Dodd-Frank Act's interchange fee provisions on the vending industry? Please discuss.
   NAMA has reviewed the legislation. While we did not advocate or engage in legislative activity on this issue we did monitor the legislation. At this time, the majority of vending machines do not accept debit card transactions, so we do not anticipate a major impact. Media coverage of the legislation indicates that once the Federal Reserve completes their study that interchange fees for debit cards will be reduced, which may save operators money. Many vending operators would like to accept debit card and other forms of cashless payments. However the costs of "micro-transactions" and equipment costs are proving a barrier to many of our small businesses. So if costs come down, it may provide additional incentives for vending operators to begin offering a debit payment solution.

a. How will interchange fees be absorbed or passed onto consumers. Please discuss.
   The sales of vended items are extremely sensitive to price increases. In this economy it is likely that a reduction in interchange fees will be passed along to consumers in the form of reduced prices. However, with a large number of state and local sales tax increases, it is also possible that any reduction in interchange fees will be used to offset these sales tax increases.

b. Will the processing of interchange fees be uniform or differ by industry sector or individual vendor?
   With the large number of vending machine operators in the nation, it is very hard to determine how individual vending operators will process these transactions. We assume that they will differ based on individual business models.

Thank you again for this opportunity, and I look forward to answering any additional questions from the committee.

Sincerely,

Craig A. Hesch
Chairman

The National Automatic Merchandising Association • www.vending.org

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QUESTIONS FOR THE RECORD – HOUSE FINANCIAL SERVICES SUBCOMMITTEE ON DOMESTIC MONETARY POLICY AND TECHNOLOGY (Hearing: 7/20/2010)

Please describe the formal and informal working relationship between the U.S. Mint (Mint), Bureau of Engraving and Printing (BEP), Federal Reserve Board (FRB) and U.S. Secret Service (USSS) regarding U.S. coins and currency.

U.S. Mint

The U.S. Secret Service's Criminal Investigative Division and the U.S. Mint's Office of Protection communicate approximately once per week to discuss emerging threats and assist each other with criminal investigations. When either agency encounters a threat to circulating coinage, they acquire samples and analyze it in their labs. The two agencies then meet at Mint Headquarters to discuss their findings, compare the samples against genuine Mint specimen coins, and coordinate a law enforcement response.

Bureau of Engraving and Printing and Federal Reserve Board

The Secret Service, BEP and FRB are all members of the Inter-agency Currency Design Taskforce (ICD) and the Advanced Counterfeit Deterrence Steering Committee (ACD). At least once per quarter, both of these formal committees meet to discuss ongoing initiatives to design safe and effective banknotes and to discuss interagency opportunities to deter counterfeiters.

The ICD provides an interagency forum to discuss ongoing technical enhancements to U.S. currency design. With almost thirty billion U.S. banknotes circulating around the world, changes to the design of Federal Reserve Notes can have a significant impact on the production, issuance and protection roles played by the three agencies. The ICD weighs these impacts on an ongoing basis in an effort to produce the most effective redesigns possible.

The ACD acts to address counterfeit deterrence issues and make decisions on both the final currency designs and their counterfeit deterrent features.

Collectively, numerous members of the Secret Service Office of Investigations and its Criminal Investigative Division correspond informally with their counterparts from the BEP and FRB on a daily basis.

How do these agencies collectively report to Congress?

At this time, the Secret Service does not collectively report with other agencies to Congress.

Are changes needed in the formal reporting structure to ensure that Congress is properly informed about any issues arising regarding U.S. coins and currency?

In an attempt to ensure that Congress is properly informed about issues arising regarding our investigative efforts, the Secret Service proposes that we submit to the House Committee on Financial Services, Subcommittee on Monetary Policy and Technology, our annual report. The report will provide Members with an annual summary of the significant counterfeiting investigations conducted by the Secret Service. It will also provide Members with fiscal year statistical data summarizing the amounts of counterfeit currency that were fraudulently passed in exchange for goods and services or seized by the Secret Service and its foreign law enforcement partners.

Testimony of James Mulroney
Coin Director – Brink's Inc.

Before

House Committee on Financial Services Subcommittee on Domestic Monetary Policy and Technology

"The State of US Coins and Currency"

***Written Response* – Date: July 21, 2010**

Chairman Watt, Ranking Member Paul, Members of the Subcommittee, thank you for inviting me a attend your meeting.

I am sorry my schedule did not permit me to join your committee meeting on July 20, 2010. I am however, please to share information from the private sector that the committee may find helpful concerning the "state of coin and currency" in the US.

I appreciate the opportunity to share some of the industries challenges and struggles and offer a few possible solutions or suggestions to improve the system that may help reduce cost and inefficiencies. I will respond to questions asked in the correspondence received from *Mr. Melvin L. Watt (Chairman)*, in addition to making other comments that may be considered helpful to the Financial Services Subcommittee members.

A little background on myself:

I have been in the ***coin business*** for 29 years in the private sector as Director of Coin Services for Brink's Inc. Over the years, I have worked directly with the Federal Reserve, Financial Institutions (FIs), US Mint, Canadian Mint and hundreds of coin venders, recyclers and users in the US and around the world. In the past several years I headed up an initiative to help reduce inventory levels for Brink's with the FIs and Federal Reserve.

Brink's Inc. was established in 1859 and is the largest Armored Car carrier in the US. Brink's provides the industry with armored car services, currency processing, coin services and ATM services. I will speak specifically about "coin" concerns in my testimony.

Over the past 25 years, Brink's has become the largest provider of Coin Services in the US. Our Coin Services include taking "loose coin" from depositing customers and putting them through high-speed machines, which are wrapped in a roll, on behalf of the FIs and their customers. In addition, we also provide "coin counting/sorting" services for Financial Institutions, transit/toll roads, vending companies and large coin recyclers such as Coinstar. We count and sort more than $3 billion dollars in coin a year for our customers. We receive direct coin shipments from the US Mint on behalf of the Federal

Reserve. We handle billions of dollars of coin each year for our customer, which includes about 35% for the Federal Reserve.

Brink's is one of the few entities that sits in the middle of all functions in the "coin handling and distribution system" in the US. Therefore, we have the opportunity to see how each player (Fed, US Mint, FIs, Armored Carriers, Coin Venders, etc.) participate, interface, and how well the system actually works or doesn't.

Brink's produces approximately 1.1 billion wraps of coin per year and operates over 50 Coin Processing Centers in the US. In about 30 of these Coin Processing Centers, we provide Coin Terminal services for the Federal Reserve.

The Federal Reserve developed Coin Terminal concept with the armored car companies some 20 years ago. It was designed to reduce the amount of inventory needed in the system (markets) and help limit the frequency of coin deposits and withdrawals at the Federal Reserve Banks. From the Armored Carrier's prospective, the Coin Terminal program was not intended to become a warehouse for excess coin storage for the Federal Reserve. Generally, there are no fees paid by the Federal Reserve or FIs for this service and convenience. Prior to the Fed Coin Terminal concept, the Federal Reserve held the majority of the inventories in the system, which gave them more over-site of the inventory levels, which resulted in "no" excess coin issues. Something to think about as you explore some of these coin inventory issues.

In June 2010, inventories held at Brink's for the FIs and Federal Reserve were slightly over $300 million in coin. In June 2009, inventory levels actually exceeded the $400 million mark. However, the Federal Reserve has helped to reduce inventories held at Brink's to the current $300 million level, which we appreciate.

However, to meet our customer needs and demands, Brink's uses approximately $167 million in coin out of the $300 million in our inventories. This difference of $133 million in coin is considered "excess", which not only takes up considerable floor space in our facilities, but also is very costly to Brink's and the system.

To put this into prospective, very few people ever actually see what $133 million dollars in coin really looks like; picture it this way, it sits on about 4500 metal skids, and weighs approximately 11 million pounds, it would take a 40,000 sq. ft. warehouse to store this and if you were to move 16 skids of coin at a time on a tractor-trailer truck, it would require 280 trucks to move.

Keep in mind, Brink's is only about 25% of this "coin distribution system", the Federal Reserve holds a much higher percentage and all the other carriers (Loomis/Dunbar, etc.) combined hold about the same as Brink's.

Questions that should be asked and Comments:

The current coin distribution system was developed over 20 years ago and although the Federal Reserve has made improvements over the past few years, (yet we find the system in an excess coin position) the real focus should be "is it the most efficient and cost effective system to meet the industries requirements in 2010 and moving forward"?

> Is there a "common sense approach" in managing and distributing coin that could save the taxpayers, US Mint, Federal Reserve and Armored Carriers time and money? *Possibly a system similar or closer to the Canadian model, in which the Canadian Mint manages inventory levels and rarely find themselves in excess coin levels. In the US, someone needs to "own" the entire process, which includes providing all required materials, warehouse facilities and processes to truly manage the "coin pool" efficiently. If it is not the Federal Reserve or US Mint, then consider out-sourcing that duty to the private sector.*
>
> Are the policies for handling, storage and containerizing coin (bulk bags vs. small bags) up-to-date to meet industries needs today? *Definitely "no". The Federal Reserve only accepts small bags of coin for deposits vs. "bulk bags".*
>
> Are manufacturing, storing and handling of excess coin cost-effective for all parties in the industry? (Taxpayers, US Mint, Federal Reserve, Financial Institutions, and Armored Car Companies). *Again, I would suggest we could do much better as a group if we had a common goal.*
>
> Are "coin deposit policies" consistent and standardized to benefit all parties (Fed, FIs, Armored Carriers) participating in the system? *I would suggest 'no".*

Recommendations and Suggestions:

Managing Inventories (Ownership)

The industry should look at developing a better *distribution model* to help manage and distribute the inventory needs for the system. We should start by agreeing to "meet" the industries needs first, not only one or two of the players in the system. As you know, the Mint produces the coin, the Federal Reserve orders this coin into the system, the FIs and consumers use a portion of the entire inventory and the *system players* ....Armored Carriers, are left trying to manage the excessive inventories, normally at their own cost.

As an example: history and data shows (see attached US Mint Coin Production sheets) that producing a high of 14.2 billion pennies in 2000, to a low of 2.3 billion pennies in 2009, is hardly managing the system. Keep in mind, the US Mint was only filling the Federal Reserve's orders. Living through this, it is hard to determine logical reasons for these types of fluctuations. Some declare this as just "meeting demand", or was it more of a "distribution problem?" *YES, to a distribution problem!*

Most times it comes down to someone unwilling to pay to move or transport coin between Armored Carriers or Federal Reserve vs. the Federal Reserve opting to order more coin from the US Mint, in which the Mint pays for the transportation. This behavior added millions of coin into a market that did not need them. This is why someone should "own the entire distribution process" and have the authority to eliminate out-dated policies, which would improve the majority of the distribution issues.

The very large swings in Mint production, "to meet a perceived demand", should send up a red flag that the system is not working well and should be improved. Fluctuations like this puts the US Mint in a very difficult position trying to manage and/or forecast production month-to-month and year after year. But, more importantly, it puts even a bigger burden on the "system" to cope with large amounts of excess coin that now has to be stored outside the Federal Reserve facilities due to space constraints.

And finally, through the Mint's publications, starting in 2006, it cost the US Mint more than a penny to produce a penny (same applies to nickels). As we know, when the Mint could produce a penny for less than a penny, it may have added some revenues to the US Treasury, but it was and is very costly to the taxpayers to produce no value and un-needed penny coins. *I am in favor of the Congress mandating the change in metal content in pennies and nickels, to reduce the cost to the taxpayers and US Mint. As we all know, the vending industry does very few transactions with pennies and nickels, due to the buying power of the penny and nickel today. To make my point, when was the last time you used a bubble-gum machine with your kids or grandkids? The majority of these vending machines today will not take pennies or nickels anymore, but use a "quarter" to purchase gum.*

The Congress should consider removing the penny altogether or at a minimum at least change the metal content. At this time, I would not recommend changing the metal content for higher denominations (dimes and up), because this may cause additional expense for the vending industry changing or adjusting coin detection technology and equipment, although, the Canadian's have already accomplish several years ago. This should be investigated before the door is closed on this!

Standardize Container for all Coin Deposits – Examples; The US Mint ships coin to the Federal Reserve in "bulk bags", i.e., ($4000 in pennies, weighing about 2500lbs.). However, the Fed will not accept coin deposits from FIs (industry) in "bulk bags". All coin must be packaged into 50 smaller bags, which is of equal value to the "bulk bag" amount. This out-dated policy is very costly to the system and should be changed to meet industries needs.

Skid Availability – Committee members may not know that a metal skid is required to stack and store every 50 bags of coin in both the Federal Reserve and for Armored Carriers. The Federal Reserve is the only entity that orders new-minted coin into the system from the Mint. Being the Mint owns these skids, they request these metal skids be returned within 60 days. This sounds practical from the Mint's prospective, however, when the amount of coin coming into the system goes into "excess mode", and the

Federal Reserve returns empty metal skids to the Mint, the industry is left to deal with the shortage of skids to store and handle the Federal Reserve's and FI's inventories. This policy adds enormous labor and handling cost to the industry and many times restricts the FIs ability to make timely deposits into the Federal Reserve Bank due to not having metal skids available. *Solution, if the coin is brought into the system, then the Fed/Mint should provide a metal skid to store this coin on. It should not be required that the industry provide metal skids when they have no control ordering coin into the system in the first place. Again, the system needs an "owner" of the entire process.*

Comments:

The Congress should require a "common sense approach" to help improve the coin distribution system in the US, with the only objective of making it work efficiently and more cost effective. Eliminating outdated policies and practices will help reduce overall cost to US Mint, Federal Reserve and the industry, this could be a win-win for all. This subject does not need to be studied for the next several years, at a cost to the taxpayers, but a small group of government and industry players (Fed, Mint, FIs and Armored Carriers) starting with a clean sheet of paper, along with the willingness to break down old barriers and policies, and given the proper over-site and authority the proper distribution system that benefits all could be developed with in the next year.

In 2009, the US Mint reported that the 2.3 billion pennies and 86 million nickels produced at a loss of $22 million dollars to the taxpayers. In 2008, the Mint also reported a loss of close to $100m producing pennies and nickels. Reportedly, due to the higher cost of copper, zinc and nickel. US Mint reports a penny cost $.0162 and a nickel cost $.063 to produce.

Please see attached documentation (1 year Copper/ Nickel Spot). Keep in mind, in Feb 2009, copper spot prices where at $1.50 per pound and rose gradually to a little over $3.00 per pound by the end of that year. In 2010, copper prices reached the $3.50 per pound level, so the Mint's cost to produce more pennies, and nickels looks like it will only continue to lose money. ***Why*** is this allowed to continue in these current financial times? Does it any longer make sense for the US Mint and Taxpayers to continue to lose money producing any coin, particularly the penny?

The Congress should consider either eliminating the penny and allow the market to remove pennies at no cost to the Federal Government or taxpayers, and/or provide the US Mint with a mandate to change the metal content of the penny and nickel within the next year.

If we think logically, no R&D study by the Mint should be required, being it has already been developed by our Canadian friends to the north, which have had steel plated coins for several years now; therefore, the technology and suppliers already have been developed. The metals industry is capable of providing materials within a very short period of time to address this change in penny and nickel metal content. And it is also good for American jobs!

Incidentally, it would also make sense for both Countries (US & Canada) to share the same "metal content" for its coins, like the Euro has. This would certainly help the vending and processing companies manage their technology when identifying coins during the counting and sorting process.

By the way, if Congress eliminated the penny, the system would see a reduction in overall floor space required for just the penny inventories by almost 50%. This would relieve our excess coin handling and storage issues within the next year.

Lastly, concerning the $1 coin, and the $1 billion plus coins in the Federal Reserve, along with the amount of taxpayer's money spent studying why this coin is not accepted. We all understand how the special interest group's prevented this needed change when the dollar coin was re-introduced in 2000. Why we spend $500 million each year manufacturing *paper money* is beyond understanding. We need to eliminate the DOLLAR BILL and let the dollar coin help reduce our printing and handling cost. The American people and industry will adjust to this change, like every other country has. The US is not leading the world in the use of sensible "coins" anymore, not only metal content but also using the proper denominations to meet societies needs. The half dollar coin should be eliminated, being society does not use these and they were created well before the invention of the SBA dollar coin in 1979. Removing the penny and half dollar coins are low hanging fruit and would make an impact on some of the nation's coin issues.

I hope you find this information helpful and thank you for allowing me to express my thoughts and concerns. I am available for further questions you may have by phone or email.

James Mulroney
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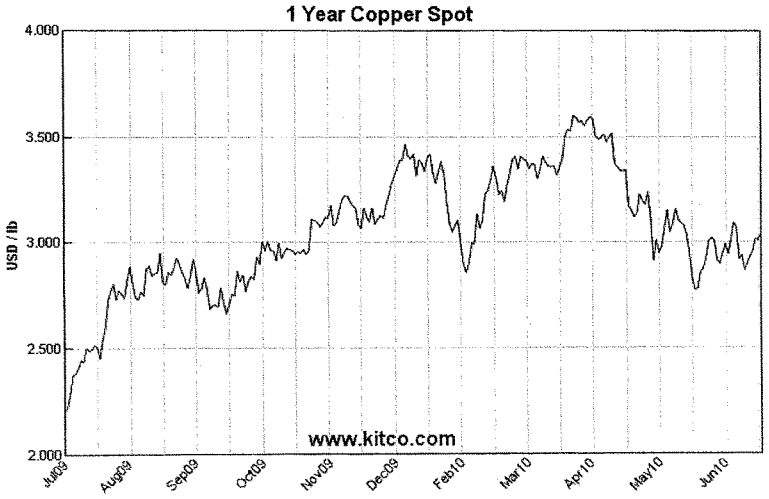
Marietta, GA. 30062
678-290-9184
James.Mulroney@brinksinc.com

United States Mint Coin Production

Year	1¢	5¢	10¢	25¢	50¢	$1	Total coins	Change
2000	14,277,420,000	2,355,760,000	3,661,200,000	6,477,470,000	42,066,000	1,286,056,000	**28,093,434,000**	
2001	10,334,590,000	1,303,384,000	2,782,390,000	4,806,984,000	40,704,000	133,407,500	**19,401,459,500**	-30.9%
2002	7,288,855,000	1,230,480,000	2,567,000,000	3,313,704,000	5,600,000	7,597,610	**14,413,236,610**	-25.7%
2003	6,848,000,000	824,880,000	2,072,000,000	2,280,400,000	5,000,000	6,160,000	**12,036,440,000**	-16.5%
2004	6,836,000,000	1,445,040,000	2,487,500,000	2,401,600,000	5,800,000	5,320,000	**13,181,260,000**	9.5%
2005	7,700,050,500	1,741,200,000	2,835,500,000	3,013,600,000	7,300,000	5,040,000	**15,302,690,500**	16.1%
2006	8,234,000,000	1,502,400,000	2,828,000,000	2,941,000,000	4,400,000	7,700,000	**15,517,500,000**	1.4%
2007	7,401,200,000	1,197,840,000	2,089,500,000	2,796,640,000	4,800,000	950,670,000	**14,440,650,000**	-6.9%
2008	5,419,200,000	640,560,000	1,050,500,000	2,538,800,000	3,400,000	489,120,000	**10,141,580,000**	-29.8%
2009	2,354,000,000	86,640,000	146,000,000	533,920,000	3,800,000	423,640,000	**3,548,000,000**	-65.0%
YTD June 2010	1,851,230,000	112,320,000	406,000,000	177,200,000	3,500,000	275,100,000	**2,825,350,000**	


1 Year Copper Spot
4.000
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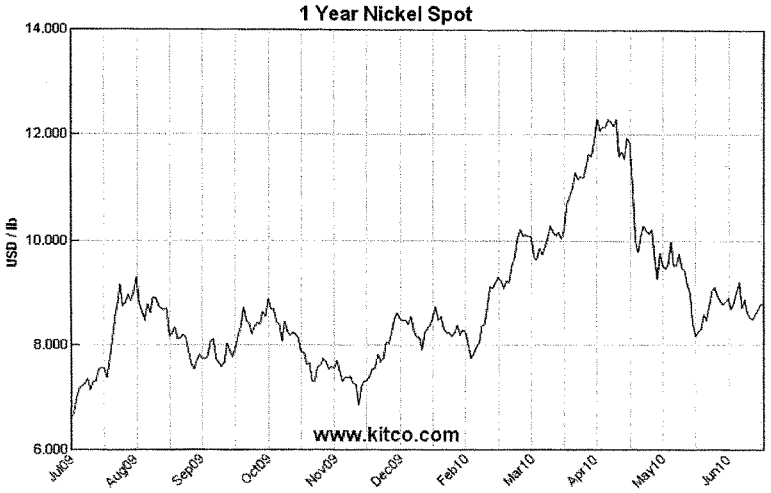
1 Year Nickel Spot
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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

LOUISE L. ROSEMAN
DIRECTOR
DIVISION OF
RESERVE BANK OPERATIONS
AND PAYMENT SYSTEMS

September 15, 2010

The Honorable Melvin L. Watt
Chairman
Subcommittee on Domestic Monetary Policy
and Technology
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Enclosed are my responses to the written questions you submitted following the July 20, 2010, hearing before the Subcommittee on Domestic Monetary Policy and Technology for inclusion in the hearing record. Also, I have provided recommendations for changes to the Presidential $1 Coin Act, as you requested during the hearing.

Please let me know if I can be of further assistance.

Sincerely,

Enclosure

Email: Louise.Roseman@frb.gov
Phone: (202) 452-2789 • Fax: (202) 452-2746

Questions for The Honorable Louise Roseman, Director, Division of Reserve Bank Operations and Payment Systems, Board of Governors of the Federal Reserve System, from Chairman Melvin L. Watt:

1 (a) Please describe the formal and informal working relationship between the U.S. Mint, Bureau of Engraving and Printing, Federal Reserve, and the United States Secret Service regarding U.S. coins and currency.

Maintaining confidence in and the integrity of U.S. currency are shared responsibilities of the Federal Reserve, the Treasury Department and its Bureau of Engraving and Printing (BEP), and the United States Secret Service (USSS). The Board of Governors of the Federal Reserve System (the Board) is the issuing authority for U.S. currency. The Secretary of the Treasury has sole authority for the design of U.S. currency, and the BEP is the government's printer of security documents (primarily Federal Reserve notes). The United States Secret Service, formerly an agency of the Department of the Treasury, has responsibility for investigating counterfeit activity.

Almost 30 years ago, the Secretary of the Treasury and the Chairman of the Board chartered the Advanced Counterfeit Deterrence (ACD) Steering Committee, consisting of senior representatives of the Treasury, the BEP, the Federal Reserve, and the USSS to establish policy for the U.S. currency program and for making design recommendations to the Secretary of the Treasury. The ACD Steering Committee meets regularly to discuss trends in currency usage and counterfeit activity, as well as topics of mutual interest, such as threats to U.S. currency, developments in new security features and new currency designs, and the public education program for new currency designs.

The ACD Steering Committee is supported by policy and technical specialists within the Federal Reserve, the BEP, and the USSS through the Interagency Currency Design Committee and its Technical Working Group. These groups generally meet at least monthly.

In addition, the Board is a member of a consortium of central banks known as the Central Bank Counterfeit Deterrence Group (CBCDG), which seeks international solutions to common counterfeiting threats such as opportunistic counterfeiting. The BEP and the USSS provide technical staff to support the work of the CBCDG.

The Federal Reserve, the BEP, and the USSS also work together on the Reprographic Research Center (RRC) and the Central Bank Cash Machine Group (CBCMG). The RRC is a central bank center for the member countries to conduct adversarial analysis on new currency designs and to determine the robustness of proposed security features. In addition to the Board, the BEP and USSS also participate in counterfeit deterrence activities at the center.

The CBCMG provides a forum for technical experts and program managers from the Board, the Reserve Banks' Currency Technology Office, the BEP, and the USSS, together with their counterparts in other countries, to form cooperative relationships with the manufacturers of equipment that accepts and dispenses currency. The CBCMG enables us to better understand how these manufacturers use characteristics of banknotes to authenticate U.S. currency. The work of the CBCMG will also help ensure that currency functions smoothly for all types of transactions, including person-to-machine transactions, as we change currency designs.

Informally, the Board regularly collaborates with the Treasury Department, the BEP, and the USSS on a broad range of currency-related topics that are of common concern to the three agencies.

The Federal Reserve also collaborates with the United States Mint; however, our role is different in that the Mint is the issuing authority for coin. The Reserve Banks' national Cash Product Office (CPO) works closely with the United States Mint to discuss, for example, monthly coin orders, annual projections, and planning for new coin releases. In addition, the CPO, Mint, and Board staffs participate on a working group that meets monthly to discuss issues that are relevant to each entity. Senior staff from the Board and the U.S. Mint meet quarterly to discuss topical issues and to reach mutual understanding of factors that affect the coin business.

1 (b) How do the agencies collectively report to Congress?

The Federal Reserve Board provides coin and currency information to the Congress in its *Annual Report* and its *Annual Report: Budget Review,* and provides more-detailed information regarding the Presidential $1 Coin Program in a separate annual report, as required by the Presidential $1 Coin Act of 2005.[1] The agencies, however, do not collectively report to Congress.

In the past, the agencies have reported collectively in special cases about specific topics that the Congress has asked about. For example, the Treasury Department provided a triennial report to the Congress on work conducted by all three agencies as part of the International Currency Awareness Program (ICAP), pursuant to the Antiterrorism and Effective Death Penalty Act of 1996 (PL 104-132).[2] The final report was delivered to Congress in 2006. At the time the Congress imposed this requirement, there were few formal channels from which the U.S. government could obtain reliable data about the use and counterfeiting of U.S. currency abroad. In more recent years, however, we have developed much more robust information channels. These channels include the global wholesale banknote dealers (commercial banks) in Europe and Asia that distribute new banknotes to and repatriate old-design and unfit banknotes from customers around the world, under contract with the Federal Reserve. These dealers provide market intelligence on the use of U.S. currency and assist law enforcement with its investigations of counterfeit activity. In addition, we understand that law enforcement has developed effective relationships and ongoing communications with law enforcement entities around the world, largely through the contacts made during the earlier ICAP visits. In addition, through its

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[1] See *2009 Annual Report* of the Board of Governors of the Federal Reserve System, pages 176-177, http://www.federalreserve.gov/boarddocs/rptcongress/annual09/pdf/AR09.pdf;
Annual Report: Budget Review, pages 23-25,
http://www.federalreserve.gov/boarddocs/rptcongress/budgetrev10/ar_br10.pdf;
Annual Report to the Congress on the Presidential $1 Coin Program,
http://www.federalreserve.gov/BoardDocs/RptCongress/dollarcoin/2010/dollarcoin2010.pdf.

[2] *The Use and Counterfeiting of United States Currency Abroad,* January 2000, March 2003, September 2006;
http://www.ustreas.gov/press/releases/reports/counterfhp154.pdf;
http://www.ustreas.gov/press/releases/reports/2003.pdf;
http://www.ustreas.gov/press/releases/reports/the%20use%20and%20counterfeiting%20of%20u.s.%20currency%20abroad%20%20part%203%20september2006.pdf

USDollars website, the USSS collects real-time information on suspect counterfeit activity around the world.[3]

1 (c) Are there changes needed in the formal reporting structure to ensure that Congress is properly informed about any issues arising regarding U.S. coins and currency?

No. The Board will continue to inform Congress about issues regarding U.S. coins and currency through its normal reporting channels (identified in question 1(b)).

Issues Relating to the Presidential $1 Coin Program

You had asked at the July 20th hearing for recommendations for how Congress could save taxpayer funds, particularly with respect to requirements related to coins.

We believe that both the Federal Reserve and the United States Mint have taken appropriate and reasonable steps to remove barriers to the improved circulation of $1 coins. Along with the Mint, we have conducted regular outreach with the banking industry, armored carriers, retailers, and federal entities to educate them about the Presidential $1 Coin Program and to gather feedback about obstacles to $1 coin circulation. We have used the information we learned from that outreach to make changes to some of our distribution practices. For example, we distributed each new design in advance of the release date so that the coins were available throughout the distribution network on the public release date, we distributed the new coins in rolls as well as bags, and we ensured that the new coins were distributed in unmixed quantities to avoid commingling of $1 coin designs. We also informed all federal entities of the Presidential $1 Coin Act requirement that they accept and dispense $1 coins. Despite these efforts, the public has not embraced the use of $1 coins for routine transactions. We, therefore, offer the following recommendations for legislative action:

- **Remove the requirement that the Federal Reserve make unmixed supplies of each new Presidential $1 coin design available for an introductory period.** The Reserve Banks now hold more than one billion $1 coins, and we project that they could hold more than $2 billion in $1 coins by the time the Presidential $1 Coin Program is expected to end. This inventory growth is due, in large part, to the legislative requirement that the Reserve Banks make each new presidential design available to their customers for an introductory period. We have no such requirement for any other coin. Therefore, absent a legislative change, the Federal Reserve must continue to order each new presidential design from the Mint even though it already has more-than-ample inventories to meet demand.

- **Eliminate the requirement that the Mint and the Board submit annual reports to the Congress on the Presidential $1 Coin Program.** The primary circulation obstacle for $1 coins is the same as it was before the Presidential $1 Coin Program: The public generally prefers to use $1 notes. We would recommend that the report be eliminated.

[3] USDollars URL address is: https://www1.usdollars.usss.gov/usd/dollarbills.nsf/Home?opennavigator.

STATEMENT OF

MARK WELLER

EXECUTIVE DIRECTOR
AMERICANS FOR COMMON CENTS

ON THE

"THE STATE OF U.S. COINS AND CURRENCY"

BEFORE THE

HOUSE FINANCIAL SERVICES SUBCOMMITTEE
ON DOMESTIC MONETARY POLICY AND TECHNOLOGY

UNITED STATES HOUSE OF REPRESENTATIVES

JULY 20, 2010

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Mr. Chairman and Members of the Committee, my name is Mark W. Weller and I am Executive Director of Americans for Common Cents. I am pleased to submit testimony today concerning the one-cent coin, its cost, and its importance to the American economy and culture.

By way of background, Americans for Common Cents was established in 1990 to conduct research and educate Congress on the need to retain the penny. Our organization is broad-based and comprised of, and endorsed by, many of the nation's leading coin and numismatic organizations, charitable organizations that benefit from penny donations, and companies involved in the manufacturing and transport of the penny.

My message this afternoon is a simple one. Consumers and charities benefit with a low denomination coin. It is prudent to look at ways to make our coins less expensively, but we need to ensure that Congressional and Mint discussions about alternative metals not lead to quick or uninformed decisions. The penny is important to the economy and without it working families and America's many charitable organizations will be harmed. Our current involvement with the penny has led us to four conclusions which I want to share with you.

1. Historically, penny production has generated millions in revenue for the Treasury. Net government revenue generated by penny production has exceeded $900 million since 1982, even accounting for recent increased costs.

2. The American public overwhelmingly supports keeping the penny. Polling over the past 20 years shows that between two-thirds and three-quarters of American's want to keep the penny.

3. The economy benefits with a low denomination coin. The alternative to the penny - rounding to the nickel - harms consumers and the economy. Rounding simply can't be done fairly and will negatively impact working families every time they buy a gallon of gas or a gallon of milk. Also, the one-cent coin is our nation's first line of defense against inflation. Without it, we would see a jump in prices that would add billions to government outlays.

4. The penny fuels millions of dollars annually in charitable contributions. America's many wonderful charities raise millions of dollars annually from the penny and other coinage. While some may question the value of the penny, collectively the penny is very powerful and helps fund many charitable causes that make a difference in communities every day.

Taken together, the findings outlined above, and discussed in more detail below, suggest that the adverse public policy and economic effects associated with elimination of the penny are considerable. It makes sense to look for ways to make our coins less expensively, but these discussions should not lead to policies that will cause harm. Additionally, we believe any attempt to alter our coinage system by removing the penny will meet strong public resistance and fail.

COINAGE COSTS AND TAXPAYER SAVINGS

Today, countries around the world are concerned about the cost of producing quality circulation coins, especially when the cost to produce their coins approaches the face value of the coin. The United States is not alone as countries look at alternative metals and ways to make their coins less expensively. As the Mint and Congress explore options to make coins more cost effectively, several factors should be paramount.

1. Historically, penny production has generated millions in "revenue" for the Treasury, which reduces government borrowing costs. (Revenue is a result of seigniorage - the difference between the face value of the coin and the costs of its mintage.) Between 1982 and 2006, seigniorage from the penny earned the Treasury almost $1 billion. During this time, the Government Accountability Office said that eliminating the penny would increase government borrowing to finance the deficit and increase the deficit by almost $18 million a year; there would not be budget savings.

Beginning in late 2006, there was a super surge in world wide metals prices caused by market speculation, increased global demand, and supply disruptions that increased penny production costs. Since that time, the price of the primary penny metal, zinc, has dropped by 60 percent. From 2007 to 2009, total coin volume through the Mint dropped 63%. Although metal prices have decreased, and penny production and transport costs have remained relatively constant, the low coin demand has negatively impacted the penny's cost.

2. The cost of penny metal and fabrication costs have remained relatively constant recently. Mint coin production reports show that the total coins produced dropped from 10.1 billion coins in 2008 to 3.5 billion coins in 2009. While production numbers for the first half of calendar 2010 show an uptick in total coins produced, the anticipated coin production for calendar 2010 is down 50 percent from just two years ago. Consequently, there is a fixed amount of Mint overhead that is being allocated to a smaller number of coins. Historically, the penny has accounted for 60 to 70 percent of Mint coin production. As Congress and the public review reports on the cost of coins, it is important to identify the various segments that comprise those costs.

On July 16, 1996, the GAO testified before the Domestic and International Monetary Policy Subcommittee regarding the penny's cost. In a three page letter to the GAO, then-Mint Director Diehl strongly objected to a GAO accounting "scenario" that spread Mint costs based on the number of coins produced rather than labor cost, calling the GAO methodology "faulty" and incorrect. Director Diehl was particularly concerned that the GAO incorrectly added almost $10 million to Mint overhead thereby inflating the cost of the penny. The Mint noted that the GAO's proposed reallocation of cost (based on the number of coins produced rather than labor cost) double charged portions of the penny fabrication process. That is, the GAO assigned penny contractor costs to make the coins for the Mint and then also added significant parts of Mint non-penny costs. It is important to realize that the Mint receives the penny in a form ready to be struck directly into legal tender. For the other denominations, the Mint begins with raw metal strip. It is unfair to apply all the Mint's overhead based on volume when only a small fraction of the operations on the penny are performed by the Mint.

3. Nickel produced at a loss as well. Suggesting that eliminating the penny saves money is a short-sighted view. The nickel cost more to make than the penny in FY 2008, so it's hard to see how the government saves money by making more nickels. The Mint's cost estimates to produce the nickel (75% copper and 25% nickel) were 6.4 cents in FY 2008, down from 9.2 cents - almost a dime - in FY 2007. The economic dislocations from 2009 and 2010 make future predictions difficult, especially in light of the Mint halting nickel and dime production in 2009. But one point is clear, the impact of increased metals costs and Mint overhead cost allocations would become measurably greater if the penny were eliminated and the nickel became the lowest denomination, and most widely produced, coin.

In response to a question by Congresswoman Maloney in July 2006, the Mint stated that at early 2006 prices for nickel and copper, it would lose approximately $100 million annually to make 3 billion nickels if the penny was eliminated. In addition, the Mint noted that fixed costs associated with production of the penny would have to be absorbed by the remaining denominations of circulating coins, adding several million more in losses.

Americans need to understand that they won't save government revenue if the penny is eliminated. The Mint is losing money making nickels as well, which should lead to a thorough examination of alternative metal compositions for our coins. We support calls in Congress and the Mint for a review of alternative metals for producing our coins.

AMERICANS WANT TO KEEP THE PENNY

National polling over the past two decades has consistently shown that between two-thirds and three-fourths of Americans support keeping the cent in circulation.

A Gallup Organization poll in 1990 and Opinion Research Corporation surveys conducted in 1995, 1996, and 2001 show Americans are persuaded by several factors, such as antipathy toward price rounding. And a 1992 CNN/Time survey conducted by Yankelovich found 74 percent of Americans support keeping the penny in circulation. More recently, a 2006 Coinstar National Currency Poll found that two-thirds of Americans want to keep the penny as legal tender, virtually the same percentage (65 percent) as in 2001.

Thus, polls conducted by Americans for Common Cents and independent polls such as those by Coinstar, USA Today, and CNN/Time never have shown the level of public support for the penny below 60 percent.

CONSUMERS AND THE ECONOMY LOSE WITHOUT THE PENNY

Faith in the strength of the economy and the nation is tied to perceptions about the currency system, and public acceptance is an important criterion for evaluating currency and coinage changes. The penny has become embroidered into the social and commercial fabric of our society. Any benefits associated with possible cost savings with elimination are outweighed by the public policy and economic costs.

1. The penny serves as a hedge against inflation. Eliminating the penny will have an impact on inflation, both real and perceived. Even a small increase in inflation mounts to considerable sums

since virtually all government outlays (e.g. Social Security, welfare programs, interest on the public debt) and many private sector costs (e.g. wages) are tied either formally or informally to the Consumer Price Index. A conservative estimate of rounding translates into government outlays being close to $2 billion over 5 years. By contrast, annual costs for the penny for FY 2009 exceed revenue by about $20 million.

In 2006 the *Wall Street Journal* editorialized that eliminating the penny would "wave a symbolic white flag before the forces of inflation." They likened taking the penny out of circulation to actions one usually associates with nations like Argentina, Bolivia, and Mexico that periodically degrade their peso currencies and create hyper inflation.

Under the current fragile economic climate, the last thing Congress should do is increase inflationary pressure.

2. Rounding doesn't work. If there is one principal that economists generally agree on it is that the behavior of firms (employment, production, advertising, pricing decisions) is guided by a straight forward objective -- the desire to maximize profits. There is no obvious incentive for firms to price in a way that will lead to rounding down. In fact, Raymond Lombra, Ph.D., Professor of Economics at Penn State University, told this Committee in 1990 that we can be certain pricing schemes will be designed to take advantage of single item and small number cash purchases in a way that leads to net rounding up. Such considerations suggest that there will be no tendency for the rounding "tax" to disappear over time.

Over three-quarters of Americans (77 percent) are concerned merchants would raise prices without the penny. And they're probably right. The claim that rounding will have no noticeable effect on the typical consumer is predicated on the notion that there is an equal 10 percent probability of purchase prices ending in any particular digit. In fact, what little evidence there is suggests the equal probability assumption is false. Some retail food pricing studies and restaurant studies demonstrate that prices ending in odd digits are much more common than those ending in even digits, and that prices ending in "9" are most often observed.

3. Rounding will disproportionately affect those who least can afford it. Federal Reserve studies show that people with relatively low incomes (particularly the young, elderly, and minorities) use cash more frequently than individuals with higher incomes. More than 10 million "unbanked" Americans lack accounts at mainstream financial institutions and must rely on cash and coins for purchases.

Since only cash transactions will be subject to rounding, it follows that cessation of penny production would be regressive in that the poor will bear a larger share of the aggregate burden than will other segments of society. As a result, those with the least ability to afford the "rounding tax" will experience the greatest burden in paying for it.

CHARITIES THRIVE ON PENNY DONATIONS

Many local fundraising drives are fueled by pennies. So too are canister collections by charitable organizations such as the Ronald McDonald House, Muscular Dystrophy Association, the Taco Bell Foundation and Salvation Army, among others, who rely heavily on donations from the collection of pennies. This collections prove the penny's value as money.

America's charities are the foundation of our nation's social safety net and help to ensure that people in need get the help they deserve. As our economy declined in the last two years, contributions to charities have dramatically decreased. Knowing this, can there be any doubt that penny drives and other innovative ideas are critical to all charities.

One example from last February is particularly telling. On the 200th anniversary of Abraham Lincoln's birth, the Leukemia & Lymphoma Society celebrated in New York the 1.5 billionth ($150 million) penny collected by school students across the country for the "Pennies for Patients" program. The Leukemia & Lymphoma Society certainly recognizes that every penny literally counts. Indeed, the $150 million collected in their Pennies for Patients program proves that pennies do add up to significant sums. With every life saved from blood cancer, their annual penny drives debunk the nay-sayers proving the penny's value.

CONCLUSION

Today, countries around the world are concerned about the cost of producing quality circulation coins, especially when the cost to produce their coins approaches or exceeds the face value of the coin. We look forward to working with Congress and the US Mint during these important discussions to ensure that the one-cent coin is retained.

The alternative to the penny, rounding transactions to the 5-cent coin, is bad for consumers and our economy. Under the current economic climate, elimination of the penny would automatically increase inflationary impacts during a period of recessionary pressure.

In addition, Americans overwhelmingly want to keep the penny; 70 percent of Americans support keeping the coin. And finally, no one has explained how we would replace millions of dollars raised by penny charitable drives every year if we didn't have the penny. Notable charities like Ronald McDonald House Charities and the Leukemia & Lymphoma Society rely significantly on small, yet critical, penny contributions.

Government resources and creditability should be devoted to making our coins more cost effectively, not pursuing initiatives that will cause considerable adverse effects.

In these uncertain economic times, the last thing consumers need is price rounding, inflation or reduced charitable assistance. And for those merchants or Americans who don't want their pennies, send them our way. They will be put to good use supporting charities conducting blood cancer research, local food banks, reading programs, and services that have contributed to groundbreaking community programs. The penny is wanted, needed, and appreciated by thousands of organizations and millions of people around the nation.