Questions for the Record
From The Honorable David Schweikert
To Lorelei St. James, Director, Physical Infrastructure,
Government Accountability Office

November 29, 2012, Hearing on
The Future of Money: Dollars and Sense

1. What are the net benefits to the government of replacing the $1 note with a $1 coin using a 1-year and a 2-year transition period?

Based on information from the U.S. Mint, neither a 1-year nor a 2-year transition period is feasible to produce the approximately 9 billion $1 coins necessary to replace the $1 note. According to U.S. Mint officials, production would be limited to 500 million $1 coins in the first year and 1.5 billion in the second year. Depending on the actions taken during these 2 years, production during the third year could be as high as 9 billion. If production in the third year were at 9 billion, then we estimate the net benefit to the government would be about $4.5 billion over 30 years (or about $150 million per year on average).[1]

According to U.S. Mint officials, it could possibly transition in 2.5 years, but it would cost approximately $12 million. When we reported in 2011, the U.S. Mint had sufficient capacity to produce $1 coins, in large part, because the recession had decreased demand for other coins. Since that time, the U.S. Mint has stopped producing $1 coins for circulation, reduced its workforce by moving from three shifts per day to two shifts, and moved the stamping presses formerly used to make $1 coins into penny production. In addition, orders for other coins have increased as the economy has improved. As a result, less capacity is available for immediate $1-coin production. According to U.S. Mint officials, in order to ramp up production of $1 coins, the agency would need to hire approximately 120 new employees and upgrade equipment. Specifically, it would need to purchase and install up to 9 burnishing machines and 12 edge-lettering machines. The estimated time to hire new employees and purchase and install this new equipment is up to 2 years, according to U.S. Mint officials.

Furthermore, the effect of the length of the transition period has less impact on the total costs and benefits than the total number of $1 coins produced over 30 years. A faster transition has very little effect on the total number of coins produced and the transition costs incurred by the U.S. Mint, which are small relative to the total net benefits over 30 years.

2. What is the net benefit to the government if a replacement ratio greater than 1.5 coins to 1 note is used?

[1]For comparison, my testimony reports a net benefit of $4.4 billion over 30 years, or an average of about $146 million per year. Adjusting the coin production levels during the transition to account for the new limitations at the U.S. Mint would lower this estimate to about $4.3 billion over 30 years, or an average of about $142 million per year. We used this adjusted production timeline while answering questions 2 and 3 below.

We estimate that a replacement ratio of two $1 coins for each $1 note would result in a net benefit of approximately $7.3 billion over 30 years (or about $242 million per year on average).[2] Given the U.S. Mint's available production explained above, the transition in this scenario would last 5 years and would require continued production of $1 notes during that time to avoid a shortage of $1-denominated currency. However, as we explained in our 2011 report, we consider a ratio of 1.5 coins for each note to be more realistic for the needs of the economy.[3] If fewer coins than 2 are needed for each note, excess coins would not be demanded into circulation and the benefits of the transition to a $1 coin would not be as high as we calculated under this scenario. Moreover, the excess coins would be held in storage, contributing to the large stockpiled inventory of $1 coins.[4]

3. What is the net benefit to the government if the lifespan of the $1 note were 24 months as stated on the FRB's own regional bank websites?

If the lifespan of the $1 note were 24 months, the estimated net benefit to the government of replacing the $1 note with a $1 coin would be approximately $6.2 billion over 30 years (or about $205 million per year on average). Similar to the result above, a shorter note lifespan means that the transition period would be extended to 5 years and the production of some $1 notes would need to continue during this period.

However, available evidence indicates that the lifespan of a $1 note is now over 50 months. According to the Federal Reserve, information on any regional bank's website citing a lifespan of 24 months is dated and incorrect. According to a Federal Reserve official, the lifespan of the $1 note has increased in recent years because of enhanced technology that the agency uses to evaluate the fitness of notes. When notes are circulated through the Federal Reserve System, they are evaluated for fitness: notes that are deemed to be too worn are destroyed and notes that are deemed to be in good condition are returned to circulation. In the past, many notes were destroyed not because they were too worn but because they were not faced correctly when they passed through the processing equipment. Over the past few years, the Federal Reserve has made technical improvements to its equipment to prevent this problem. This has resulted in a lower "shred rate" and, subsequently, a longer average life for $1 notes.

[2]We used the same 2-to-1 replacement ratio that we used in our 2000 analysis of the net benefits of $1 note replacement. We arrived at the 2-to-1 ratio based on the experiences of other countries at that time. See GAO, *Financial Impact of Issuing the New $1 Coin*, GAO/GGD-00-111R (Washington, D.C.: Apr. 7, 2000).

[3]GAO, *U.S. Coins: Replacing the $1 Note with a $1 Coin Would Provide a Financial Benefit to the Government,* GAO-11-281 (Washington, D.C.: Mar. 4, 2011).

[4]In my testimony, I noted that approximately 1.4 billion $1 coins were stored with the Federal Reserve as of September 30, 2011.