Statement by Philip N. Diehl

Mister Chairman, Members of this Committee, it was my honor to serve as the Director of the United States Mint from 1994 to 2000. Thank you for your invitation to appear before you.

The U.S. Government Accountability Office (GAO) has, for the seventh time, gotten it right: replacing the dollar note with a dollar coin will save the United States Government and American taxpayers billions of dollars, and Congress should accept GAO's recommendation to enact this change.

GAO stands for accountability, reliability, and independence. Since 1990, GAO has issued seven reports, all reaching the same conclusion: billions will be saved. The estimated savings over 30 years have ranged from $4.4 billion to $15.7 billion. It didn't matter whether a Republican or Democrat asked the question, the answer always came back the same.

I've been gone from the U.S. Mint for 13 years, and I have no financial interest in this matter. I'm here because I think this is sound public policy. In a time when Congress is considering painful cuts in government spending affecting virtually every American, why would we not take this small and painless measure. Virtually every Western economy has replaced its lowest denomination note with a coin of the same denomination, and I'll wager that no elected representative lost their job as a result. Congress has twice avoided the tough choice in passing dollar coin legislation hoping a coin could circulate alongside the dollar note despite overwhelming evidence that this will not happen.

That said, based on my own experience, I can say opponents' claims that the public will never accept a dollar coin are false. When the Sacagawea dollar coin was launched in 2000, public demand was so strong that the Mint shipped more coins in its first year, 1.3 billion, than it did in the entire 20-year history of the Susan B. Anthony dollar. Although the public greeted the Sacagawea dollar enthusiastically, the new dollar coin could not overcome the continued presence of the dollar note.

Opponents of this measure will cite survey research they claim demonstrates the public opposes substituting a dollar coin for a dollar note. But if survey respondents are informed this change will mean billions in savings, two-thirds support it.

This isn't rocket science, and no new coin is required. We did that 13 years ago. Opponents may claim the logistics are difficult or they might raise doubts about how long it will take to manufacture the 9 billion or so new coins GAO estimates will be needed to add to those already in circulation. I have doubts about these objections. During my last year as Director of the Mint we produced 28 billion coins and had capacity to produce another 2 billion that year. I understand the Mint will produce around 9 billion coins this year. Unless there has been a radical reduction in the capacity of the U.S. Mint plants in Philadelphia and Denver, and to my knowledge there has not been, the Mint is capable of meeting these requirements.

The Mint has told GAO it will need about $8 million in additional equipment, a figure that strikes me as reasonable. According to the Mint's financial reports, each dollar coin makes 82 cents in bottom-line profit for the Treasury. Spending $8 million to make $7.4 billion in net dollar coin profit sounds like a pretty good deal to me.

You have already heard all the reasons why this can't or shouldn't be done. Let me explain why I think it can, and dispel a number of the myths created to block this change.

Success Throughout the World

Considering the broad, bi-partisan support for reducing federal deficits, you would think that saving American taxpayers billions of dollars with no pain and minimal inconvenience would be welcomed. These savings aren't hypothetical – most major economies of the world, including the G-8 nations, long ago realized substantial savings from eliminating their small denomination paper currency. Canada, which made the change in 1987, reaped savings that were ten times what had been forecast. Instead of saving $175 million over 20 years, as estimated, Canadian officials later determined that they actually saved $450 million in the first five years. The change was so successful, the Canadians went for a second round, eliminating their $2 note and introducing a $2 coin in 1996.

As GAO has repeatedly stated, "Over the last 47 years, Australia, Canada, France, Japan, the Netherlands, New Zealand, Norway, Russia, Spain, and the UK, among others, have replaced lower-denomination notes with coins. Most of these replacements occurred in the 1980s."

Dollar Coins Work

When I was Director of the Mint, I worked with Republicans and Democrats alike to enact the Dollar Coin Act, launching a beautiful, easily recognizable, new Sacagawea dollar coin. Today's conventional wisdom is that the dollar coin was a failure, but it certainly wasn't at the time. As I said previously, demand was much stronger than we anticipated, and we had to quickly ramp up production. In fact, demand from banks was so strong we developed a direct shipment program to reduce delivery delays through the Federal Reserve Bank (FRB).

Given some of the press reports, you might think many of those Sacagawea dollars gathered dust in (FRB) vaults. Not so. By December 2002 nearly 1.5 billion Sacagawea dollars had been issued by the Mint while only 183 million remained in FRB vaults. But demand for the new dollar coin ultimately flagged due to the loss of a champion of the coin and resistance within the government and the banking sector. Frankly, you will never overcome this resistance without removing the dollar note.

The FRB has repeatedly testified before this Committee that its vaults were bulging with unwanted dollar coins, "almost $1 billion as of May 31, 2010." What you wouldn't have known without reading the fine print is that as of that same date, the FRB also held inventories of other denominations amounting to six billion coins, including 3.3 billion quarters and 1.5 billion pennies, or that coin inventory is distributed throughout a network of approximately 110 coin depots across the United States to ensure immediate availability and prevent localized shortages.

What is also noteworthy about the FRB's inventory numbers in 2010 is that new coin demand had fallen dramatically in 2009 and 2010, to an average of about 5 billion coins per year. This pattern is as regular as the night following the day. Coin demand plummets during recessions and surges with strong economic growth.

Contrast the FRB's 2009-2010 inventory with the prior four years when new coin demand averaged nearly 14 billion per year. Even with coin demand cut by 65%, the FRB still required 7 billion circulating coins in its inventory, with only one-seventh of those dollar coins.

Before the Susan B. Anthony was issued in 1979, Treasury and the Federal Reserve knew a new dollar coin could not succeed unless the dollar note was eliminated at the same time. I know because I saw the research. This knowledge was ignored. It was ignored again in 2000. I know because I was there. We need to face the simple truth: dollar coins do not circulate because we refuse to remove the dollar note.

Barriers

For many years, the dollar coin has faced another significant obstacle: the FRB's preference for the dollar note. I discovered this for myself when the Mint launched the Sacagawea dollar in 2000. The FRB is the sole channel through which the Mint distributes coins to banks and ultimately to businesses and consumers. If the FRB doesn't order a coin, it doesn't get into the hands of the public.

When we were planning the Sacagawea launch in 2000, we did an extensive survey of banks and the FRB to coordinate the logistics of distributing the new coin. They confronted us with a dilemma saying they would not order the Sacagawea dollar unless we first demonstrated there was demand for it. And they said survey research wasn't sufficient. This presented us with a Catch 22 situation since we couldn't prove there was public demand unless we could get the coin into the marketplace.

We solved this challenge by bypassing the FRB and the banks, shipping the coins directly to Wal-Mart stores nationwide. In just a few weeks, Wal-Mart distributed 100 million Sacagawea dollars as change in routine retail transactions, demonstrating that Americans welcomed the new coin. In fact, Wal-Mart wanted another 100 million coins, but when the banks started receiving calls from customers asking for the coin, they realized we had just proven public demand and they wanted shipments immediately.

This debunked another piece of conventional wisdom that Americans are opposed to eliminating the dollar note. When readily available to the public, coins are accepted. And as I said earlier, opinion polls consistently show that, when informed of the savings of substituting a dollar coin for the dollar note, two-thirds of Americans support making the switch.

Dollar coins faced other artificial barriers after the release of the Presidential Dollar coins in 2007. The FRB restricted delivery of bank orders for each new coin design to only two weeks, four times a year. What business is going to make use of a coin it isn't certain will be consistently available from its bank? This rule means businesses are unable to integrate the dollar coin into their operations so banks don't order the coin. FRB inventories then accumulate, and once again, the dollar coin is declared a failure.

Seigniorage

As GAO has reported, both notes and coins are products that make a "profit", termed "seigniorage", but they are accounted for differently. Seigniorage is the difference between the face value of a note or coin, and its cost. The FRB buys coins from the Mint *at full face value*. The Mint then records all coin seigniorage, or profit, on its books, and ultimately deposits profits into Treasury's general fund. In contrast, the FRB buys notes from the Bureau of Engraving and Printing *at cost,* with the FRB recording all note profit, or seigniorage, on its books. In 2011 the FRB's note seigniorage was estimated at nearly $200 billion, and the FRB returned $77 billion to Treasury. I am not an expert on the Federal Reserve's finances, but the math here is pretty simple: eliminating the dollar note denies the FRB a significant source of its profits.

GAO Savings Estimate Likely Understated

I was surprised, as some of the Committee members may have been, by the dramatic reduction in GAO's annual savings estimate from $522 million, issued in 2000, to $184 million in its updated 2011 Report. A significant part of this reduction can be attributed to the FRB's reported increase in the lifespan of the dollar note. For the past 20 years or so, the FRB had cited a lifespan of 13 to 18 months for the note. This was the case when I was Director. In 2011, the FRB more than doubled the lifespan to an average of 32 to 40 months.

Then, in preparation for the 2012 Report, the FRB provided GAO with an eye-popping lifespan estimate of 56 months, again nearly doubling the estimate from the year before. Mr. Chairman, it's hard for me to imagine what accounts for the $1 note's sudden immunity to the wear and tear of circulation. Maybe we all treat the dollar bill more gently, or maybe they've developed some kind of Kevlar technology to ruggedize it. In any case, I note this change as worthy of attention.

In addition, GAO has calculated that the Mint will need four years to manufacture the quantity of dollar coins required to replace the dollar notes now in circulation and as a result the Mint will be forced to absorb dollar coin production costs without reimbursement for several years, creating a net loss during those years. As I've said, Mr. Chairman, I've been gone from the Mint for 13 years, but based on what I know of the Mint's capacity, both human and technological, I'd be very surprised if it took four years to build a sufficient inventory to replace the dollar note. My judgment is that if your legislation mandates the removal of the dollar note and gives the Mint enough time to plan for an increase in production, the Mint could produce the require inventory of coins in a year or two, with the current FRB inventory of dollar coins providing a head start. Therefore, I suggest you consider shortening the transition time, currently set at four years, so the Treasury can begin to realize these savings sooner rather than later.

Also of note, after the release of GAO's 2011 Report and their estimated savings projection of $5.5 billion over 30 years, the junior Senator from Massachusetts, where the cotton-linen for the dollar note is produced, asked GAO to change its assumptions and rerun its analysis. Even with assumptions far more favorable to the dollar note, GAO still estimated savings of $4.4 billion over 30 years. Remarkably, this is the GAO analysis that opponents of this bill are criticizing, one using their chosen methodology. So if the 2012 estimate was reached through "gimmick accounting", as one opponent has said, I could venture a guess where the gimmick originated. My own opinion is that GAO's 2011 estimate, without the "gimmick accounting" and changed assumptions in the 2012 estimate, is probably more sound.

Conclusion

Thank you, Mr. Chairman. That concludes my testimony.