As stated in our response to GAO dated November 29, 2011, we acknowledged that difficult questions of measurement are still under discussion. However, ORACW generally concurs with these recommendations, and remains committed to incorporating them as an ongoing part of our operations.

We appreciate the opportunity to provide these comments. Please contact me if you have any questions about this response, or the Office of Recovery for Auto Communities and Workers.

Sincerely,

Jay Williams

Note: This letter includes comments on Area 42: U.S. Currency.

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January 30, 2012

Ms. Lorelei St. James
Director
Physical Infrastructure Issues
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Ms. St. James:

Thank you for the opportunity to comment on the GAO's draft discussion of replacing the $1 note with the $1 coin in its 2012 Duplication and Cost Savings report. The GAO has projected a financial benefit to the government of about $4.4 billion over 30 years. We believe this projection overstates the net financial benefit to the government, perhaps substantially.

The report states that the cost of producing sufficient coins to replace all $1 notes is never fully recovered during the 30-year analysis; all savings are attributable to increased seigniorage income.[1] In fact, there is no year in the study in which estimated non-seigniorage benefits exceed costs. Moreover, the analysis does not adequately address the costs to the Federal Reserve of such a replacement and does not address at all the broader societal costs to consumers, retailers and other businesses, and state and local governments.[2]

In addition, replacing the $1 note with the $1 coin may increase the risk of counterfeiting. The current low rate of counterfeiting helps maintain global confidence in U.S. currency. Unlike the $1 note, the $1 coin does not have any effective machine-readable or publicly-usable counterfeit deterrent features. Several countries that have converted low denomination notes to coins have reported higher levels of counterfeiting for low-denomination coins than previously observed for low-denomination notes, and the U.S. Sacagawea $1 coin was counterfeited in some Latin American countries soon after the U.S. Mint issued it.

Finally, the GAO did not provide a sensitivity analysis that reflects differing assumptions, such as possible changes in the public's means of making payments over the next several decades. Although the value of Federal Reserve notes in circulation continues to increase more than 7 percent annually over the past several years, the growth rate for $1 notes has been on

[1] The Congressional Budget Office does not score seigniorage in its budget calculations.
[2] With respect to Federal Reserve costs, the Federal Reserve cancelled plans to build additional storage space for $1 coins following the Treasury's announcement to suspend minting of Presidential $1 coins for circulation. If $1 coins were to replace $1 notes, however, the Reserve Banks would need to build or expand vaults around the country with reinforced floors to accommodate the heavier weight of coins in order to manage coin inventories.

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

average only 2 percent per year. It is possible that the elimination of the $1 note could accelerate the shift of consumer payments to debit cards and other electronic payment alternatives. In addition to potential shifts in consumer payment methods, the analysis did not consider potential increases in raw material costs for coins, or changes in discount rates. Given the certainty of the near-term expenses associated with the transition and uncertainty of the long-term forecasted benefits, it is possible that no savings will ever be realized from the replacement of $1 notes with $1 coins. Sensitivity analysis for these factors would provide a confidence level around the GAO's long-term savings projections. In fact, changes in assumptions have reduced the GAO's average annual discounted net benefit projections from $550 million in its 2000 study, to $186 million in its 2011 study, to $146 million in this report.

Proponents of replacing $1 notes with $1 coins often cite similar steps that have been taken in other economies in recent decades as an indication that such a change has strong financial benefits. In general, the low-denomination note that was replaced by a coin had a far shorter useful life (typically three to six months) than is the case with the $1 note, which currently has a useful life of about 56 months. Further, these decisions were typically made when electronic payment substitutes to cash were less mature than in the current U.S. environment. Therefore, the decisions of other economies have been based on very different circumstances than exist in the United States.

We believe that a fuller societal cost-benefit analysis and a sensitivity analysis that varies key assumptions that are subject to material uncertainty would provide policy-makers with a more complete basis for considering the future of the $1 note and $1 coin.

Sincerely,

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