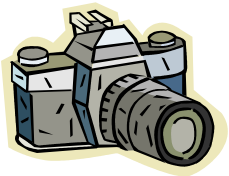


What I did on Spring Break

Follow along in Monica Haven's peripatetic footsteps as she journeys to various financial venues. From the Federal Reserve to the Mint, from the New York Stock Exchange to the Archipelago, from bank to brokerage firm, discover the workings of our economic system across the geographic landscape.

I. History of Money

A. Colonial Times

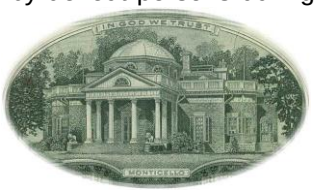
- 5 Types: Native currencies (wampum & furs), Country Money (tobacco and other "cash" crops), foreign coins (including Spanish eight reales or "pieces of eight"), British coinage, paper currency
- 1764: British banned all paper currency in Colonies

B. Post-Revolutionary War

- Revolutionary War funded with an expansionary flood of paper money. Eventually Continentals fell to 1/1000th of their original nominal value
- 1791: Bank Act established the first Bank of the United States as a central bank owned by private citizens (its charter expired 1811)
- 1792: U.S. coinage system established—first coins produced at Philadelphia Mint
- 1797: Dollar was established as national currency, but was soon replaced by Spanish dollar due to gold and silver bullion shortages
- 1836: 1600 state-chartered banks issued paper money (30,000 varieties of color and design)
- 1838: Charlotte Mint began producing coins (operations suspended in 1861)
- 1854: San Francisco Mint began producing coins (closed in 1937)

C. Reconstruction

- Union funded Civil War by levying a tax on states in proportion to their population and a general income tax. Both yielded less than $200 million and were supplemented by the issuance of $500 million war bonds. The Confederacy borrowed $15 million on a cotton crop that could not be exported due to the blockade. Hyperinflation ensued when the southern states simply printed money.
- 1862: Treasury was given the right to issue legal tender ("Greenbacks"). Intended as a temporary currency, their number in circulation was gradually reduced—the last Greenback was issued in 1971.
- 1863: National Currency Act established anti-counterfeiting measures
- 1865: Secret Service established to combat counterfeiting
- 1866: "In God We Trust" placed on coins in response to appeals by devout persons during war times



Excerpt from letter by Rev. M. Watkinson:
Would not the antiquaries of succeeding centuries rightly reason from our past that we were a heathen nation? What I propose is that instead of the goddess of liberty we shall have next inside the 13 stars a ring inscribed with the words PERPETUAL UNION; within the ring the all seeing eye, crowned with a halo; beneath this eye the American flag, bearing in its field stars equal to the number of the States united; in the folds of the bars the words GOD, LIBERTY, LAW. This would relieve us from the ignominy of heathenism.

- 1873: America unofficially converted from silver to gold standard (official conversion in 1900)

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D. 20th Century and Beyond

- 1906: Secret Service assumed responsibility for protection of the President
- 1913: Federal Reserve Act enacted to establish the Federal Reserve System as the nation's central bank [see below]. Issuance of Federal Reserve Notes authorized—now the only currency produced
- 1928: NY Federal Reserve Bank cuts discount rate to help Britain stay on the gold standard. This ease of credit ultimately fuels the economic collapse. The basic design of U.S. currency is selected
- 1929: October 24th Black Thursday. Banks tighten credit and strangle the economy.
- 1933: Roosevelt declares a 10-day bank holiday. The standard design and size of currency is introduced. Federal Deposit Insurance is enacted [see below].
- 1931: More than 1,000 banks fail in last quarter
- 1957: "In God We Trust" is placed on paper currency
- 1971: U.S. abandons gold standard; NO circulating currency in the world is redeemable for gold
- 1990: Security thread and micro-printing are introduced to combat counterfeiting
- 1998-2008: Five state quarters will be introduced each year for 10 years
- 2000: Additional anti-counterfeiting measures, including oversized portraits, watermarks, and security threads that glow when exposed to UV light are introduced
- 2003: Check Clearing for the 21st Century Act (Check 21) became effective on October 28, 2004. The act facilitates check truncation by creating a new negotiable instrument called a substitute check, which will permit banks to process check information electronically, and to deliver substitute checks to banks that want to continue receiving paper checks.

II. Constitutional Premise

Article I, § 8 (excerpted)

The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence [sic] and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States;

To borrow Money on the credit of the United States;

To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;

To coin Money, regulate the Value thereof, and of foreign Coin, and fix the Standard of Weights and Measures;

To raise and support Armies, but no Appropriation of Money to that Use shall be for a longer Term than two Years;

To make all Laws which shall be ***necessary and proper*** *for carrying into Execution the foregoing Powers and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof.*

Case Law: McCulloch v Maryland, 17 U.S. 316 (1819)

Does Congress have the power to charter a federal bank? Yes. Although not specifically enumerated in the Constitution, the court found that Congress indeed had authority under the Necessary and Proper Clause since the legislative branch must be allowed to use reasonable means to exercise its responsibilities.

III. Traveling along the road of high finance…

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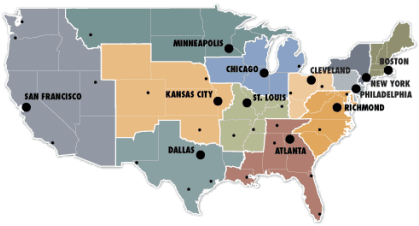
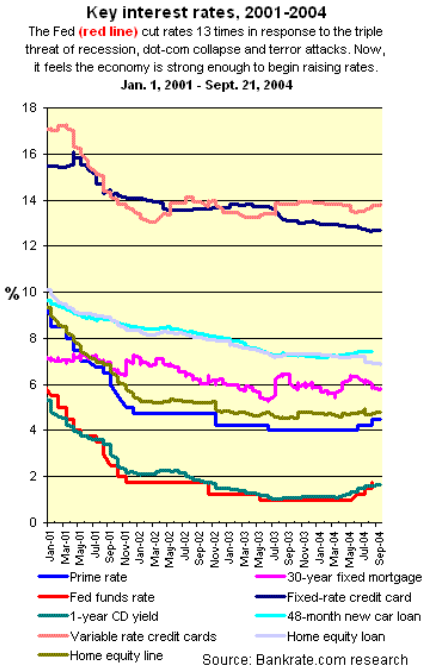
V. Federal Reserve System

A. Organization



- Quasi-public, non-profit, and independently operated system. The reserve bank is a corporation whose non-transferable stock is owned by the 11 member banks.
- The 7-member Board of Governors are appointed by the President and confirmed by the Senate to serve 14-year terms. Members may serve only one full term, but a member who has been appointed to complete an unexpired term may be reappointed to a full term. The President designates, and the Senate confirms, two members of the Board to be Chairman and Vice Chairman, for four-year terms. Alan Greenspan originally took office as Chairman and to fill an unexpired term as a member of the Board on August 11, 1987. He was reappointed to the Board to a full 14-year term, which began February 1, 1992, and ends January 31, 2006. He has been designated Chairman by Presidents Reagan, Bush, Clinton, and Bush.
- Income is earned from interest on government securities, interest on bank loans, and market fees for some financial services. 95% net earnings are turned over to the Treasury.



B. Board Functions: Since 1981, eight regularly scheduled meetings have been held each year at intervals of five to eight weeks.

- Formulate monetary policy. The 7 Board members constitute a majority of the 12-member Federal Open Market Committee (FOMC) which makes the key decisions affecting the cost and availability of money and credit in the economy. The other 5 members of the FOMC are Reserve Bank presidents, one of whom is the president of the Federal Reserve Bank of New York. The other Bank presidents serve one-year terms on a rotating basis. By tradition the Chairman of the Board of Governors acts as the Chairman of the FOMC and the President of the New York Bank as its Vice Chairman.
- Set reserve requirements and discount rate policy.
- Establish margin requirements, which limit the use of credit for purchasing or carrying securities.

V. Department of Treasury

A. Mission: To promote the conditions for prosperity and stability in the US and the rest of the world; create economic and employment opportunities; and influence global financial and economic issues.

B. Organization

The Department of the Treasury is organized into two major components: The departmental offices which are primarily responsible for the formulation of policy and the operating bureaus which carry out the specific operations assigned. The basic functions include:

- Managing Federal finances;
- Collecting taxes, duties and monies paid to and due to the U.S. and paying all bills;
- Producing postage stamps, currency and coinage;
- Supervising national banks and thrift institutions;
- Advising on domestic and international financial, monetary, economic, trade and tax policy;
- Investigating and prosecuting tax evaders, counterfeiters, and forgers.

VI. U.S. Mint

A. Mission: To produce an adequate volume of circulating coinage for the nation to conduct its trade and commerce; ca. 11 billion and 20 billion coins annually. Other responsibilities include:

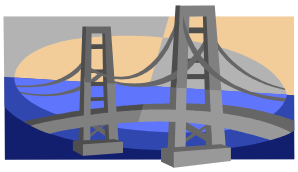
- Distributing U.S. coins to the Federal Reserve banks and branches.
- Maintaining physical custody and protection of $100 billion of U.S. gold and silver.
- Producing proof and uncirculated coins, commemorative coins, and medals for sale.
- Manufacturing and selling platinum, gold, and silver bullion coins.
- Overseeing of production facilities in Denver, Philadelphia, San Francisco, and West Point, as well as the U.S. Bullion Depository at Fort Knox, Kentucky.
- Receiving, redeeming, and processing mutilated coins.

B. Locations

1. United States Mint Headquarters, Washington, D.C.
Policy formulation and central agency administration.

2. Philadelphia Mint, Pennsylvania
Engraving of coins and medals, including commemorative coins.

3. Denver Mint, Colorado:
Production of coins of all denominations for general circulation and storage of gold and silver bullion.



4. San Francisco Mint, California:
Production of regular proof coin sets and selected commemorative coins.

5. West Point Mint, New York
Production of all silver, gold, platinum, and bi-metallic commemorative coins and storage of silver, gold, and platinum bullion.

6.  **United States Bullion Depository, Fort Knox, Kentucky**
Storage of U.S. gold bullion.

C. Money Facts

- Coins produced in 1998 by denomination, was as follows: pennies, 10,257,400,000; nickels, 1,323,672,000; dimes, 2,335,300,000; quarters, 1,867,400,000; half-dollars, 30,710,000.
- 48% of the notes printed by the Bureau of Engraving and Printing are $1 notes.
- A $1 bill lasts 18 months; $5 bill, two years; $10 bill, three years; $20 bill, four years; and $50 and $100 bills, nine years.
- The Bureau of Engraving and Printing produces 38 million notes a day with a face value of approximately $541 million. 95% of the notes printed each year are used to replace notes already in circulation.

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Year	Cash in Circulation	Cash per Capita
1910	$ 3,148,700,000	**$ 34.07**
1920	$ 5,698,214,612	**$ 53.18**
1930	$ 4,521,987,962	**$ 36.74**
1940	$ 7,847,501,324	**$ 59.40**
1950	$ 27,156,290,042	**$ 179.03**
1960	$ 32,064,619,064	**$ 177.47**
1970	$ 54,350,971,661	**265.39**
1980	$ 127,097,192,148	**$ 570.51**
1990	**$ 266,902,367,798**	**$ 1,062.86**

VII. Stock Markets

A. Function: To raise venture capital and provide for investment liquidity.

Three Trading Forums

OTC NASDAQ Floor Exchanges

B. Electronic Markets

In January 1997, the SEC implemented new Order Handling Rules that created the opportunity for Electronic Communications Networks (ECNs), such as the Archipelago, to interact directly with the NASDAQ National Market System. These computer systems can systems that automatically match buy and sell orders at specified prices.

The ARCAX was formed in December 1996 and partnered with the Pacific Exchange in 2000 to create the first totally open, electronic stock market in the US.

E. Securities and Exchange Commission (SEC)

Mission: To protect investors, maintain the integrity of the securities markets, and oversee key participants in the securities world, including stock exchanges, broker-dealers, investment advisors, mutual funds, and public utility holding companies.

Established in 1934, the SEC consists of five presidentially-appointed Commissioners, four Divisions, and 18 Offices. Commissioners' terms last five years and are staggered so that one term ends on June 5th of each year. To ensure that the Commission remains non-partisan, no more than 3 Commissioners may belong to the same political party.

F. National Association of Securities Dealers (NASD)

Mission: To bring integrity to the markets and confidence to investors. The NASD registers member firms, writes rules to govern their behavior, examines them for compliance, and disciplines those that fail to comply. It is a self-regulatory organization that educates industry professionals (including roughly 5,200 brokerage firms, over 96,000 branch offices and more than

664,000 registered securities representatives) and investors, and supports member firms in their self-compliance activities.

VIII. Insurance

A. FDIC

The Federal Deposit Insurance Corporation is an independent agency of the US government which protects against the loss of insured deposits if an FDIC-insured bank or savings association fails. FDIC insurance is backed by the full faith and credit of the US government.

The basic insurance limit is $100,000 per depositor, per insured bank. Deposits in separate branches of an insured bank are not separately insured. Deposits maintained in different categories of legal ownership at the same bank can be separately insured. Therefore, it is possible to have deposits of more than $100,000 at one insured bank and still be fully insured.

History:

1933: Congress creates the FDIC
1934: Deposit insurance coverage initially set at $2,500 then raised midyear to $5,000
1980: Deposit insurance increased to $100,000; FDIC insurance fund is $11 billion
1988: 200 FDIC-insured banks fail; FDIC loses money for the first time
1990: First increase in FDIC insurance premiums from 8.3¢ to 12¢ per $100 of deposits
1993: Banks begin paying premiums based on their risk.

B. SIPC

The Securities Investor Protection Corporation ensures that customers of a failed brokerage firm receive all non-negotiable securities that are already registered in their names or in the process of being registered. All other so-called "street name" securities are distributed on a pro rata basis. At the same time, funds from the SIPC reserve are available to satisfy the remaining claims of each customer up to a maximum of $500,000, including $100,000 of cash. Recovered funds are used to pay investors whose claims exceed SIPC's protection limit of $500,000. SIPC often draws down its reserve to aid investors. Although not every investor is protected by SIPC, SIPC estimates that no fewer than 99 percent of persons who are eligible have been made whole in the failed brokerage firm cases that it has handled to date.

IX. International Monetary Organizations

A. World Bank: Established to fight poverty and improve the living standards of people in the developing world by providing loans, policy advice, technical assistance to reduce poverty.

B. International Monetary Fund (IMF): An organization of 184 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty.

C. European Union: Member States have set up common institutions to which they delegate some of their sovereignty so that decisions on specific matters of joint interest can be made democratically at European level. This pooling of sovereignty is also called "European integration." Its membership has grown from six to 15 nations, with 10 more in May 2004 and 2 in 2007. The enlarged EU of 27 countries will have a population of nearly half a billion.

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