CHAPTER THREE

THE BASIC RULES OF RARE COIN INVESTMENT

There are a number of factors to keep in mind when investing in rare coins: the type of coins to buy, grading, prices to pay, the structure of the market, and so forth, as well as different avenues of purchase and sale. If, at first, this all sounds complicated, do not get discouraged. It is not as difficult as it might seem. Once you have become familiar with some basic principals, the path of a rare coin investment is no more difficult to follow than that of any other investment.

Since market emphasis has shifted from the investor to the collector, the methods of acquisition — indeed, the nature and size of collections themselves — have changed dramatically. In the old days — by which we mean prior to 1950 — purchasers built their collections slowly, year after year, through sources as varied as professional numismatists, U.S. Mint sales, hobby shops and mail order houses. Only in the last thirty years have investors played a role in coin prices. In the past five years we have witnessed the largest shift ever from investor to collector domination in the market. That is why this market is larger and has more sustainability than previous ones. Between the mint and all its promotions, the internet, and the grading service registry sets, there have been a tremendous number of collectors who view the investment aspect as secondary to collecting.

Amon Carter Sr., founder and publisher of the Fort Worth Star-Telegram, began collecting in the 1940s. His son, Amon Jr., assumed both his father's publishing and numismatic mantles in 1955, and, by the time of his death in 1982, had built the family coin collection into one of the world's finest. One of the collection's prizes, a 1794 mint state silver dollar, was snapped up by the old man in 1947, in a mail bid sale, for $1,200. When this extreme rarity — a famous and well-known specimen of the Mint's first silver dollar — sold at auction in January of 1984, the price paid was $264,000, a gain in value of some 22,000 percent. Today it is offered for millions of dollars. This is by no means a unique example of rare coin appreciation.

The Bareford Collection, assembled in the 1950s for a total of $16,000, sold at auction in the late seventies for $1.2 million (and that was just for the gold cons). Today just one coin from that collection, an 1804 Silver Dollar is worth as much as the whole collection realized in 1978.

One of the few surviving examples of the privately made Brasher Doubloon, America's most valuable coin, was purchased at auction for $3,000 in 1922 by Virgil M. Brand, the Chicago brewery tycoon, who compiled the biggest coin collection of all time. His Brasher Doubloon was auctioned 57 years later for $430,000 and bought by a Chicago dealer, and it brought $1.6 million.

Even this pales beside the price brought by the Garrett specimen of the Brasher Doubloon. T. Harrison Garrett began collecting in 1860; his sons, Robert and John Work, continued adding specimens through the early 1940s. At the Garrett auction in November 1979, their Uncirculated Brasher Doubloon sold for $725,000 a then all-time record of astonishing proportions. In 2005 an About Uncirculated(55) Brasher of the same type sold at the FUN sale for $2,990,000. As you can plainly see, there is money to be made — if you follow a few simple rules of investment.

The Ten Basic Rules Of Rare Coin Investment

1. Buy the best quality and rarity you can afford.

The truth is, you can overstress rarity. Given a choice between an MS-67 common coin and an MS-63 rarity, there is none. Rarity is far more important. DiGenova has been stressing this very point for more than twenty years: Buy the best quality that makes "price sense" for the coin. For instance. a Chain Cent in XF at $30,000 may be a better investment than an MS-60 at $200,000. In fact, DiGenova is certain of that. An 1893-S Morgan Dollar in AU-58 at $35,000 is better than an MS-65 at $500,000. An 1886-O Dollar is $10,000 is MS-64 and $150,000 in MS-65. I would not recommend this date in the latter grade, but would buy instead a really fantastic MS-64. It will be a better buy and a much better investment. An MS-60 coin is not and will never be a bargain basement version of an MS-65. Buy the best quality available. The best brings the best price at sale. And that, after all, is the point. However, some coins do not survive in the best quality. They just don't exist. Keep in mind that if you can purchase a MS-60 rare coin that is not known in better condition than MS-60, it may be a better buy than a MS-65 coin that thousands are available at that grade or even a higher grade.

2. Diversify.

Not just within your overall portfolio, but among your rare coins as well. This, when you get right down to it, is nothing more than good common sense. Spreading your investment across the numismatic board insures that your coins will support each other when different market areas are strong or weak, and keeps you flexible, with different specimens peaking at different times.

We, and many Financial Planners, recommend that no more than ten to fifteen percent of the average investment portfolio be devoted to numismatics. As has been repeatedly noted, no single option can fulfill all your investment needs; and successful individuals pursue as much diversity as is reasonable and prudent. This percentage affords the liquidity, stability, and diversification and, above all, high returns that all investors seek.

3. Buy coins that you can sell.

This is not as obvious a statement as it sounds. Whatever you have set aside for rare coin investments, some dealers might advise you to spend it all on one coin. While, in some cases, this may make sense, depending on what you buy, such a course may limit your liquidity. Of course, it may improve your profitability.

Stay away from esoterica, that is Colonial coins and paper money, tokens, broken bank notes and so forth. In a market full of available and popular merchandise, why bother with gambles and long shots if you don't understand them? The average serious rare coin investor should restrict purchases to those areas of the market that have proven performance records and solid opportunity for growth.

It is impossible to complete certain series. Rare dates in those ceries will be more difficult to sell than those in a series that can be completed. An 1859-O Eagle in Uncirculated, for example, is a rare and undervalued coin but could potentially be a problem to sell.

These are:

a. gold coins of numismatic (as opposed to bullion) value. For example, the most affordable better date/or rare date and mint St. Gaudens Double Eagles (1907-32);

b. Rare date nineteenth century type coins; such as Barber Dimes, Quarters and Halves, Liberty and Shield Nickels, etc;

c. Silver dollars, better or rare dates of the Morgan, (1878-1921) and Peace (1921-1935) types; and

d. What have come to be known as "20th Century Type" — Better or rare date Buffalo Nickels, Mercury Dimes, Lincoln Cents up to the mid Twentieth Century. Stay away from Modern Commemorative and late date coins without track records.

e. Rare coins. We suggest, as an example of an effective portfolio mix in today's market, the following types of coins, for example, a High Relief Saint Gaudens, early gold before 1838, Proof type before 1840, Mint State Type before 1840, Rare date Gold in condition. Read about this in detail in Chapter Five.

Better date choice and gem quality gold coins remain among the rarest and most desirable of U.S. coins, thereby all but guaranteeing their continued upward growth. Type coins have considerable aesthetic and historical appeal, and are in relatively short supply in Choice Uncirculated condition, while the lower grades are readily found. Silver dollars have remained popular with collectors and in the very forefront of the market since it took off in the early 1990's, and continue to post strong, steady gains. The least expensive group, with the largest base of collectors, modern singles represent a strong, and still developing, market sector, with enormous future potential if you can't afford better.

4. Seek professional help.

Work with a professional numismatist if you are making your first venture into the rare coin market. Just as you would never buy stocks without a broker, do not try to buy coins on your own. And take his advice. Like a doctor, if he tells you to take four pills, either take the four pills or get a new doctor, but never self medicate. Though you may, after some years of dedicated study and consistent hands-on involvement, have enough knowledge to do some of your own trading, reading any book — as thorough and comprehensive as it may be — will not give you all you need to know. Key dates within a very collected series like Morgan silver dollars, or key dates within scarce type can sometimes be purchased for near common date coins of the same type. This is where experience within the field helps in making picks.

5. Make your purchases from a reputable dealer.

This industry, like every other investment industry, has plenty of incompetents. You would not buy stocks from a stranger on the street. Be just as careful picking your numismatist. Friends already active in numismatic investment might be able to help you in this regard. Always get a bill of sale and pay by check.

6. Do not overpay.

This, too, seems obvious. But think about it. How is a novice to gauge real worth? How can someone making an initial foray into numismatics distinguish between a good value and a flagrant rip-off? It can be difficult, and tricky. Most numismatic investment firms mark up their purchases approximately thirty percent over wholesale. However, markups of up to 200 percent are not unheard of, and these, obviously, can wreak havoc upon your potential profits.

The best way to avoid overpaying — apart from dealing with a reputable coin broker — is to familiarize yourself with prices. Comparison shop. Study the bid/ask prices in the Coin Dealer Newsletter, or the weekly newspapers, Coin

World and Numismatic News. Try to get some consensus of where prices are for a coin or a particular group of coins. Once you can reasonably ball-park the merchandise of your choice, you will be able to question dealers with a certain amount of knowledge — and, thus, power. Always beware of prices that are too low — such coins may have been tampered with, or misgraded, or more often, just plain bad deals.

7. Become as knowledgeable as you can about all your investments.

You should know at least enough to avoid suspect deals and apparent hustles. It is best to learn to grade and evaluate a coin yourself. There are classes you can take from reputable organization, such as the American Numismatic Association, who offer such training. It is well worth the cost.

8. Take delivery of your investment.

The whole purpose of owning a hard asset, from historical times to the present, is to hold onto it. Do not let anyone, even your trusted dealer of proven reputation, keep your coins for you if you can avoid it. This way you can also have the coins evaluated by another trusted individual or company to make sure you are getting what you pay for.

9. Carefully store and insure your portfolio.

This is so easy and inexpensive that you might forget, or do it carelessly. But remember: your coins will only be of value, when the time comes to sell, if they are in the same pristine condition as when you bought them. So find a suitable safe deposit box, and tuck them in for the long haul. If possible, find a bank with climate controls, to avoid large temperature swings from summer to winter. Be sure the insurance policy you select contains a provision covering bank theft.

For coin dealers, theft and robbery are ever present possibilities, and elaborate protective measures are necessary. Costly insurance policies — requiring intricate alarms and detection devices, the service of guards, and all but impregnable safes — must be maintained to safeguard inventory not kept in bank vaults. When transporting his stock, perhaps from one coin show to another, the dealer is an ideal target. Portable, easily concealed, highly liquid, rare coins are simple to steal and fence.

Fortunately, the investor is spared these concerns, and may protect his portfolio much more simply. The most important rule to remember, of course, is never store coins at home. Do not be tempted by your investment's attractiveness, or that handsome display holder with which you may have been provided, to set it on the piano beside the family portrait. A common burglar will have less trouble unloading your Barber Dime than your clock radio. Nor is a home safe entirely reliable, especially if you are requested, at gunpoint, to open it. Al Capone, feared Chicago gangster once said that it is easier to do business with a gun and a smile than with just a smile alone. Remember, what a safe deposit box takes from you in aesthetic pleasure it returns in peace of mind.

10. Buy and hold.

We have characterized rare coins as a long-term investment, giving five years as the minimum length of holding time. Do not invest funds that cannot be tied up for this period of time. It is also true that money can be made after 18 months or less. But the fact is, truly legendary profits have been made over the past 30 years, and not by people who were seeking merely to outpace inflation, or even to ride the cycles, which characterize the market. The really big scores were realized by those who, after following the rules of investment delineated above, were willing to sit back for up to a decade or more and let values escalate. Their patience was rewarded with gains, not atypically, on the order of 1,000 percent. Now, it is difficult to let profits of 30, 40, and 50 percent or more go by without itching to sell — especially when the market flattens out and prices begin to drop. It is hard not to lose your nerve. But if you can manage to buy and hold — and hold, and hold — your fortitude will be grandly, financially rewarded.

On the other hand — and there always is another hand, it seems — do not get greedy. Set a target, know when the time has come to sell, and sell.

Taxes

It is also of benefit to the investor to keep abreast of the tax laws pertaining to rare coins. At present, transactions remain anonymous, but this could change. Rare coins were disallowed in self-directed pension plans, such as Individual Retirement Accounts (IRAs) and Keoghs, many years ago for political reasons; again, this situation may well reverse itself. Knowing where you stand at all times will better enable you to make decisions regarding what to buy, what to sell, and when.

For general tax purposes, two sets of rules apply: the first pertains to the collector, for whom coins are a hobby, the second to the investor interested in financial gain. Both may turn a profit, but it is the collector who will be taxed at the higher rate: capital gains reductions are only available to the investor. Further, the investor may deduct related expenses, including those stemming from income production (professional fees, insurance, and the like) and property management (such as a safe deposit box), as well as any financial losses incurred.

The question is: how does the Internal Revenue Service decide whether or not someone is an investor? This has at times proven difficult, and numerous court cases have been devoted to determining whether or not a collection has been accumulated for pleasure or profit. There are some federal guidelines; these include whether or not the activity has been carried out with a degree of expertise, the amount of time consumed, and proof of the expectation of gain. The profit motive is also presumed present if the income from an activity is greater than the accumulated deductions for two out of five years, measured consecutively. Investors must also avoid the hallmarks of coin collecting — display cases, home storage, and so forth; and hobbyist's materials, when purchased, should not be deducted as business expenses. Good records must be kept, including the date, mint, denomination and grade of each coin, dates and prices of purchases and sales and commission fees incurred. And don't forget to pay your taxes. What good are profits if you're in prison?ore about taxes later.

Like-kind Exchanges

I regularly see collectibles dealers offering customers the opportunity to engage in "like-kind" exchanges under Section 1031 of the Internal Revenue Code.That code provision allows taxpayers,under certain limited circumstances, to trade property that has appreciated in in value for items of the same "nature or character' without recognizing income or capital gains on the transaction. For investors interested in shifting from one area to another, this can be a good tax avoidance and estate planning technique.

But the key words to remember are "limited circumstances:' and too often neither the customer nor the dealer entering .into exchange transactions is familiar enough with the intricacies of Section 1031 to understand whether those transactions will quality.The first limitation on like-kind exchanges involves which categories of tax payers can participate in them.

Like-kind exchanges between "related parties" such as relatives or controlled corporations or other entities will not receive Section 1031 treatment except under certain circumstances. In other words, the parties to the exchange must be completely arm's length. In addition, related parties must each hold the property they obtain in an exchange for at least two years. This, of course, is to prevent sham transactions being staged solely for the tax benefits.

Second, both the items being traded and those received must be held purely for investment purposes .In the case of collectibles, the IRS has developed a test for determining whether a tax payer is motivated primarily by a desire to make a profit, rather than simply to collect.

The particulars of this test are somewhat complex, and I recommend that collectors consult an attorney or accountant before taking the position with the IRS that they own collectibles for investment purposes. The IRS rules also mean that collectors who have asserted that they are "dealers" for tax purposes (in order to deduct certain expenses as business expenses and offset their collectibles losses against their ordinary income) will not be able to benefit from a "like-kind" exchange. This is because the IRS will then consider their collections to be "stock in trade,' (inventory), which is ineligible for Section 1031 treatment.

Third, the items must truly be of "like-kind" and the IRS is very specific about this.A computer and a printer are of like kind and may be exchanges under Section 1031, but a copyright on a song and a copyright on a book are not of like kind. IRS regulations set forth categories of "assets" and 'products" that are, and are not, eligible for like-kind exchanges.These regulations do not include any collectibles, and the IRS has been difficult there. For example, a trade of rare U.S. gold coins (such as a 1927 Saint-Gaudens gold $20 double eagle) for gold U.S. bullion coins (such as a 1995 American Eagle 1 ounce gold $50 coin) will not qualify, and individual rulings have differed with respect to attempted like-kind exchanges of rare coins of differing metal content.Finally, like-kind exchanges do not eliminate the tax, but simply defers recognition of income or gain until such time as the newly acquired asset is sold. A taxpayer may exchange a coin that he or she purchased for $1,000 (and which is now worth $5,000) for another coin of the same "nature and character' that is worth $5,000. Assuming that the taxpayer ultimately sells the second coin for $10,000, he or she will he taxed on a $9,000 gain. In other words, the taxpayer's cost basis in the second coin will be $1,000, not $5,000. It's also worth noting that since 1990, the IRS has required taxpayers claiming Section 1031 exchanges to file Form 8824, which calls the IRS's attention to the event and may trigger an audit if the amounts involved are substantial enough.

Where items are clearly not "like-kind" or Section 1031 otherwise doesn't apply, collectors and investors nevertheless attempt to avoid income tax on appreciated property through the use of barter, i.e., trading items for other items without cash changing hands. But bartering collectibles is generally not a good tax avoidance technique.

While taxable gain on art and collectible items is not recognized until the items are sold, a barter is treated by the IRS as a"sale" because the taxpayer is disposing of the item in exchange for value. The celebrated artist Peter Max was indicted in1996 for failing to report income from the barter of nearly $1 million of art works for the purchase of two residences. The issue was not whether the real estate Max purchased was worth more than the paintings he used to pay for them. Rather, the government asserted that Max received compensation for his paintings that was taxable as income, even though the compensation was of a non-cash variety. One last point - like-kind exchanges and barters are not necessarily exempt from sales or use taxes, and if a dealer is involved it is best to check on this before completing the deal. More about taxes later.

Buying

When you go to a contemporary coin dealer to make a purchase, you are not limited, as you once were; to those specimens he or she has in stock. For over twenty years, approximately 500 of the nation's most prominent numismatists have been linked by teletype, and now by various internet systems. Among them are the Certified Coin Exchange and Coinnet, which between them now have over a thousand members receiving up-to-the-minute pricing information, live bids as asks, and a real, comprehensive market comparable to the NASDAQ. The internet enables dealers to immediately communicate with one another, and exchange data relating to, among other things, available merchandise. The sophistication of the system streamlines the process for those seeking to start investing quickly.

Because the extraordinary demand for rare coins has created something of a shortage of top-quality merchandise, some numismatic houses have begun to put together limited and / or general partnerships, enabling investors (usually for a minimum of between $25,000 and $50,000) to get involved with portfolios worth a million dollars or more. Such partnerships simplify the investment process, leaving the purchasing and management to the experts, and eliminating the problems inherent in searching out desirable specimens, as well as substantially diversifying the overall risk.

With or without professional help, there are a variety of ways to buy coins. The most common methods are at a coin show or public auction, over the internet, or through the mail. Many publications directed toward those interested in numismatics feature lists of coins for sale. These publications function as clearing houses for the world's coin collecting community; through them, you may locate interesting coins, or advertise those you wish to sell. Any resulting transactions may then be completed through the post. Mail-order coins may require an advance deposit, but they are always sold on an approval basis; when dealing with a reputable house, the buyer may reject them without fear of monetary loss. This technique is an old and honored one in the trade, dating from the 18th century; and the collector who chooses to act alone will find this method convenient.

The coin show is another important forum for trade, and conventions are held continuously in various places around the country. Each show, organized by an individual or association, occupies a date on a full calendar of shows, and, frequently, will be repeated annually. This provides a steady stream of shows at which to trade — a circumstance which is, of course, of benefit to investors. If, for example, after consulting with a client a coin broker does not have in stock those specimens best suited to the client's investment strategy and budget, the broker may dispatch a staff member to a show to make the purchase, or alert other dealers as to his needs.

Almost as important as the coin show, and often held in conjunction with it, is the coin auction. This is perhaps the most exciting forum for the trading of rare coins, though not for the novice or investor lacking professional advice. The outcome is always uncertain. A particular "lot" may sell for a song, or set a record. It all depends upon the bidders. The auction is in many ways a place of negotiation, one at which interested parties conduct business publicly, signaling interest, opinion — even, perhaps, the start of a trend — with the mere raise of a bid.

Bids may be submitted in two ways: via the mail, to the auction house before-hand; or, conventionally, given verbally at time of auction. Often both methods are used, with the lot going to whoever has, in the end, the highest bid. This is particularly useful for auctions that are also events, as may be the case when large collections or estates reach the block. When the auction is of nationwide interest, mail bids enable those who cannot attend to participate.

When buying at auction, it is a good idea to follow a few basic rules. Do not bid on a specimen you have not thoroughly examined or have had examined by an expert for you. Determine what a coin is worth to you, based on your means, and a realistic estimate of what it will bring at sale. Do not rely solely on the advice of the auction house as regards what you should bid. And never go after a coin simply because a known Numismatist is doing so. It might be his own coin that he is bidding on.

Selling

When it comes to leaving the market, rare coins can be offered with complete liquidity if your timing is right. Very few investors in coins, or any other investment for that matter, actually buy at the bottom and sell at the top. Keep your eyes open for the time to sell, because at some time or another you will want to sell and you will want to sell when the prices are good, not necessarily when you personally want to get out of the market. The industry — comprised of dealers linked together by internet, teletype, and computer inventory terminals, widely circulated coin publications, direct mail catalogues, and weekly national coin shows and auctions — responds rapidly to changing market trends, providing innumerable outlets for the investor ready to sell, whether he is divesting himself of a single coin or an entire portfolio.

The market's backbone is, of course, comprised of investors and collectors, of whom, according to the U.S. Mint, there are some 130 million in the United States alone, nearly one in three Americans. These individuals, who are also tied in to retailers, numismatic organizations, and coin publications, offer a steady, stable market for quality coins. This is particularly reassuring in a world in which the fate of so many investments is determined by uncertain political climates and questionable international financial policies.

If you decide to sell your coins at auction, be sure that you have an exact written determination of the grade prior to making the consignment. Better coins should be sold separately, rather than in a group lot. Comparison shopping, again, can be of use, as certain auction houses will offer better terms, particularly on commissions. The dealer who sold you the coins originally may be of help in arranging the resale. Do not ask too little for your higher-grade coins, or too much for lower-grades—a typical seller error.

We have discussed a variety of ways to purchase and invest in rare coins. Though some of these have not required the services of a professional, the novice rare coin investor would be well advised to seek out, and avail himself of, the talents of an experienced Numismatist. A quality coin broker brings to the job knowledge of history, the market, and the market's future, as well as being able to grade and authenticate accurately. Moreover, most Numismatists will guarantee their expertise — a substantial psychological boon.

If, as previously noted, quality and rarity are indeed everything, then the ability to determine quality — accurately and consistently — is perhaps the most important skill a numismatist may possess. Within the profession, the skill is known as grading; and, in the following chapter, we will examine grading, authenticity, rarity, and the establishment of value in detail.

**CHART 14 PROFESSIONALLY BALANCED PORTFOLIO.
Recommendations from a $25 billion investment company**

SIM ANALYSIS PROFILE

INVESTORS:
Married couple: Man – 46, Woman – 43.

TWO CHILDREN:
18 – entering college, 15 – high school sophomore.

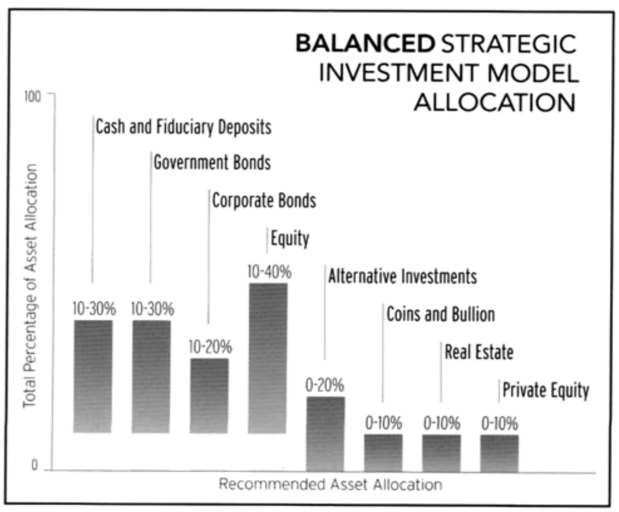
ASSETS:
$1 million investable (not including house, car, etc.).

OBJECTIVES:
Pay for children's college; retire at 60; start a bed-and-breakfast.

RISK TOLERANCE:

- Is a mid- to long-term investor (5+ years) and has a general understanding of market conditions.
- Would like to participate in global equity markets, achieve 8 to 10 percent a year return, and avoid tremendous market swings in principal and return.
- Interested in investments including stocks and bonds, but also guidance into areas of the market with which they are not familiar.
- Would also like the money managed and to be more hands-off with the day-to-day investment decisions.

ANALYSIS:
Recommendation for allocation: Balanced SIM Allocation, targeting a 9 percent per year return, with 50 percent less risk than the overall market. The allocation would include stocks, bonds, cash deposits, alternative investments, precious metals, private placements and real estate in a managed allocation for the specific needs of this client.



Coinage of the States

Before the establishment of the U.S. Mint, the Articles of Confederation granted the individual states the right to issue their own coins. During the period 1785–88, four states produced coins: Vermont, Connecticut and New Jersey issued copper cents; Massachusetts issued both cents and half-cents. As large quantities of the state issues were minted, they are readily available today and can be put together to form an interesting collection of early American coins. Two examples of the coinage are shown below.

1787 CONNECTICUT COPPER

The laureated bust on the obverse gives the Connecticut coppers a late-Roman Empire appearance. The figure of Liberty appears on the reverse. Most of the 1787 and 1788 coppers were crudely struck.

1787 NEW JERSEY COPPER

A horse's head, a plow and the legend, "Nova Caesarea" (New Jersey) appear on the obverse. The reverse features a shield and the legend, "E Pluribus Unum" (One out of many), the legend that appears on many later United States coins.