United States Government Accountability Office

Report to the Secretary of the Treasury

November 2014

FINANCIAL AUDIT

Bureau of the Fiscal Service's Fiscal Years 2014 and 2013 Schedules of Federal Debt

GAO-15-157

November 2014

FINANCIAL AUDIT

Bureau of the Fiscal Service's Fiscal Years 2014 and 2013 Schedules of Federal Debt

GAO Highlights

Highlights of GAO-15-157, a report to the Secretary of the Treasury

Why GAO Did This Study

GAO is required to audit the consolidated financial statements of the U.S. government. Because of the significance of the federal debt held by the public to the government-wide financial statements, GAO audits Fiscal Service's Schedules of Federal Debt annually to determine whether, in all material respects, (1) the schedules are reliable and (2) Fiscal Service management maintained effective internal control over financial reporting relevant to the Schedule of Federal Debt. Further, GAO tests compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt.

Federal debt managed by Fiscal Service consists of Treasury securities held by the public and by certain federal government accounts, referred to as intragovernmental debt holdings. Debt held by the public essentially represents the amount the federal government has borrowed to finance cumulative cash deficits. Intragovernmental debt holdings represent balances of Treasury securities held by federal government accounts—primarily federal trust funds such as Social Security and Medicare—that typically have an obligation to invest their excess annual receipts (including interest earnings) over disbursements in federal securities.

In commenting on a draft of this report, Fiscal Service concurred with GAO's conclusions.

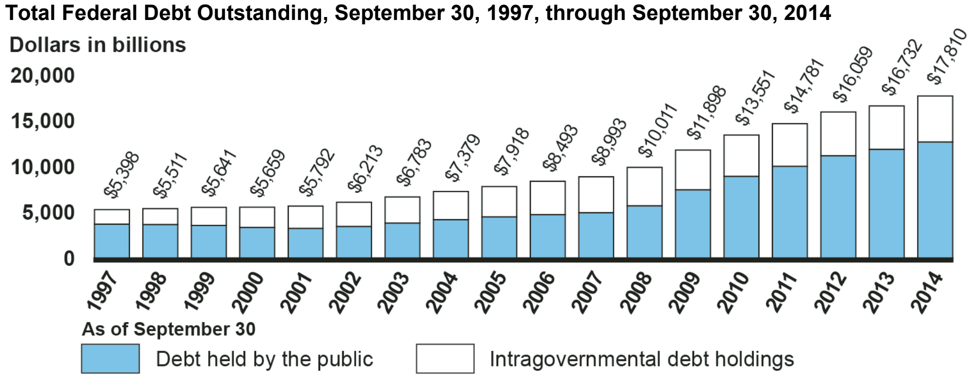
View GAO-15-157. For more information, contact Gary T. Engel at (202) 512-3406 or engelg@gao.gov.

What GAO Found

In GAO's opinion, the Bureau of the Fiscal Service's (Fiscal Service) Schedules of Federal Debt for fiscal years 2014 and 2013 were fairly presented in all material respects, and Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2014. GAO's tests disclosed no instances of reportable noncompliance for fiscal year 2014 with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt.

From fiscal year 1997, the first year of audit, through September 30, 2014, total federal debt managed by Fiscal Service has increased by 230 percent and the debt limit has been raised 15 times, from $5,950 billion to $17,212 billion. During fiscal year 2014, delays in raising the debt limit occurred for a total of 16 business days. Also, the debt limit was suspended for the period October 17, 2013, through February 7, 2014, and again from February 15, 2014, through March 15, 2015.

Total Federal Debt Outstanding, September 30, 1997, through September 30, 2014



Note: A small amount of total federal debt is not subject to the debt limit.
Source: GAO analysis of Fiscal Service information. | GAO-15-157

During the delays, Treasury deviated from its normal debt management operations and took a number of extraordinary actions—consistent with relevant laws and regulations—to avoid exceeding the debt limit. As GAO has previously reported, the debt limit does not restrict the Congress's ability to enact spending and revenue legislation that affects the level of federal debt or otherwise constrains fiscal policy; it restricts Treasury's authority to borrow to finance the decisions already enacted by the Congress and the President. The United States benefits from the confidence investors have that debt backed by the full faith and credit of the United States will be honored. As GAO has also previously reported, delays in raising the debt limit can create uncertainty in the Treasury market and lead to higher Treasury borrowing costs. To avoid such uncertainty and related borrowing costs, GAO noted in its February 2011 and July 2012 reports related to the debt limit that the Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue at the time those decisions are made to avoid potential disruptions to the Treasury market and to help inform the fiscal policy debate in a timely way.

Contents

Abbreviations

Fiscal Service	Bureau of the Fiscal Service
FMFIA	Federal Managers' Financial Integrity Act
GDP	gross domestic product
Treasury	Department of the Treasury

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

November 10, 2014

The Honorable Jacob J. Lew
Secretary of the Treasury

Dear Mr. Secretary:

The accompanying independent auditor's report presents the results of our audits of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Schedule of Federal Debt) for the fiscal years ended September 30, 2014, and 2013. The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and Discounts managed by the Department of the Treasury's (Treasury) Bureau of the Fiscal Service (Fiscal Service), and include accompanying notes.

The independent auditor's report contains (1) our opinion that the Schedules of Federal Debt for the fiscal years ended September 30, 2014, and 2013, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles; (2) our opinion that Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2014; and (3) the results of our tests of Fiscal Service's compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt, which identified no instances of reportable noncompliance.

As of September 30, 2014, and 2013, federal debt managed by Fiscal Service totaled $17,810 billion and $16,732 billion, respectively, primarily for borrowings to fund the federal government's operations. As shown on the Schedules of Federal Debt, these balances consisted of approximately (1) $12,785 billion as of September 30, 2014, and $11,976 billion as of September 30, 2013, of debt held by the public and (2) $5,025 billion as of September 30, 2014, and $4,756 billion as of September 30, 2013, of intragovernmental debt holdings.

Debt held by the public essentially represents the amount the federal government has borrowed from the public to finance cumulative cash deficits. When a cash surplus occurs, the annual excess funds can be used to reduce debt held by the public. In other words, annual cash deficits or surpluses generally approximate the annual net change in the amount of federal government borrowing from the public. Debt held by the public represents federal debt issued by Treasury and held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments. The majority of debt held by the public consists of marketable Treasury securities, such as bills, notes, bonds, floating rate notes, and Treasury Inflation-Protected Securities that are sold through auctions and can be resold by whoever owns them. Treasury also issues a smaller amount of nonmarketable securities, such as savings securities and State and Local Government Series securities.

As we have noted in previous years, Treasury reporting shows that foreign ownership of Treasury securities represents a significant portion of debt held by the public.[1] As of June 30, 2014, the reported amount of Treasury securities held by foreign and international investors represented an estimated 48 percent of debt held by the public. This percentage is slightly higher than the 47 percent as of June 30, 2013, and considerably higher than the estimated 30 percent of debt held by the public as of June 30, 2001. Treasury estimates that the amount of Treasury securities held by foreign and international investors has increased from $983 billion as of June 30, 2001, to $6,013 billion as of June 30, 2014—an increase of $5,030 billion.[2] Estimates of foreign ownership of Treasury securities are derived from information reported under the Treasury International Capital reporting system, not from the financial system used to prepare the Schedule of Federal Debt.[3] These estimates are not reported on the Schedules of Federal Debt, and as such, we do not audit these amounts.

Intragovernmental debt holdings represent federal debt owed by Treasury to federal government accounts—primarily federal trust funds such as

[1]GAO, *Financial Audit: Bureau of the Fiscal Service's Fiscal Years 2013 and 2012 Schedules of Federal Debt*, GAO-14-173 (Washington, D.C.: Dec. 12, 2013).

[2]Department of the Treasury, *Major Foreign Holders of Treasury Securities*, accessed November 3, 2014, http://www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt.

[3]The data reported under the Treasury International Capital reporting system are collected primarily from U.S.-based custodians. According to Treasury, since U.S. securities held in overseas custody accounts may not be attributed to the actual owners, the data may not provide a precise accounting of individual country ownership of Treasury securities.

Social Security and Medicare—that typically have an obligation to invest in federal securities their excess annual receipts (including interest earnings) over disbursements. Most federal government accounts invest in special nonmarketable Treasury securities that represent legal obligations of the Treasury and are guaranteed for principal and interest by the full faith and credit of the U.S. government. The federal government uses the federal government accounts' invested cash surpluses to assist in funding other federal government operations. Unlike debt held by the public, intragovernmental debt holdings are not shown as balances on the federal government's consolidated financial statements because they represent loans from one part of the federal government to another. Under U.S. generally accepted accounting principles, when the federal government's financial statements are consolidated, those offsetting balances are eliminated.

Debt held by the public and intragovernmental debt holdings are very different. Debt held by the public represents a claim on today's taxpayers and absorbs resources from today's economy. In addition, the interest paid on this debt may reduce budget flexibility because, unlike most of the budget, it cannot be controlled directly. In contrast, intragovernmental debt holdings reflect a claim on taxpayers and the economy in the future. Specifically, when federal government accounts redeem Treasury securities to obtain cash to fund expenditures, Treasury usually borrows from the public to finance these redemptions.[4]

We have audited the Schedule of Federal Debt since fiscal year 1997. Over this period, total federal debt has increased by 230 percent. Also during this period, the statutory debt limit was raised 15 times, from $5,950 billion to $17,212 billion.[5] As discussed in the accompanying Overview on Federal Debt Managed by the Bureau of the Fiscal Service, during the last 4 fiscal years, total federal debt has increased by $4,259 billion, or 31 percent, from $13,551 billion as of September 30, 2010, to $17,810 billion as of September 30, 2014. Of the total increase, $3,762 billion was from the increase in debt held by the public and

[4]For more information regarding the federal debt, see GAO, *Fiscal Outlook: Understanding The Federal Debt*, accessed November 3, 2014, http://www.gao.gov/fiscal_outlook/understanding_federal_debt/overview#t=0.

[5]A small amount of total federal debt reported on the Schedule of Federal Debt is not subject to the debt limit. This amount is primarily composed of unamortized discounts on Treasury bills and Zero Coupon Treasury bonds.

$497 billion was from the increase in intragovernmental debt holdings. The last economic recession and the federal government's actions to stabilize financial markets and promote economic recovery contributed to such increases in debt held by the public, especially during fiscal years 2011 and 2012. During fiscal years 2013 and 2014, debt held by the public increased by $706 billion and $809 billion, respectively.

The statutory debt limit was raised on five different occasions during the last 4 fiscal years, increasing by about 20 percent, from $14,294 billion to $17,212 billion. Notably, delays in raising the debt limit occurred in all 4 of these years. For fiscal year 2014, delays in raising the debt limit occurred for a total of 16 business days. Delays result in Treasury deviating from its normal debt management operations and taking a number of extraordinary actions within its legal authorities to avoid exceeding the debt limit.[6]

A delay in raising the debt limit that began in fiscal year 2013 continued through October 16, 2013. During this period, Treasury took extraordinary actions consistent with relevant laws and regulations to avoid exceeding the debt limit. These actions included suspending investments to certain federal government accounts. On October 17, 2013, the Continuing Appropriations Act, 2014 was enacted, which suspended the statutory debt limit through February 7, 2014.[7] Subsequent to the start of the temporary debt limit suspension period, Treasury restored principal and interest to the affected federal government accounts in accordance with relevant laws. The amounts restored included uninvested principal and interest that existed as of the end of fiscal year 2013, which were appropriately not reported on the fiscal year 2013 Schedule of Federal Debt since securities had not been issued at that time to the affected federal government accounts. The fiscal year 2014 increase in debt held by the public of $809 billion was greater than the reported fiscal year 2014 federal deficit of $483 billion primarily due to the above-noted restoration of principal and interest, as well as increases in the government's cash balance and federal direct student loans.

[6] Actions that are not part of Treasury's normal cash and debt management operations are considered "extraordinary actions" by Treasury.

[7] Pub. L. No. 113-46, § 1002, 127 Stat. 558, 566-67 (Oct. 17, 2013).

An increase in the debt limit was not enacted before the suspension period ended and therefore, consistent with the Continuing Appropriations Act, 2014, the debt limit was raised on February 8, 2014, to the amount of qualifying federal debt securities outstanding at that date, or $17,212 billion. As such, on Monday, February 10, 2014, Treasury began taking certain extraordinary actions consistent with relevant laws and regulations to avoid exceeding the limit. These actions continued through February 14, 2014. On February 15, 2014, the Temporary Debt Limit Extension Act was enacted, which suspended the statutory debt limit through March 15, 2015.[8] Subsequent to the start of this temporary debt limit suspension period, Treasury restored principal and interest to the affected federal government accounts in accordance with relevant laws. If an increase in the debt limit is not enacted before the end of this suspension period, consistent with the Temporary Debt Limit Extension Act, the debt limit will be increased by the change in qualifying federal debt securities outstanding on February 15, 2014, compared to those outstanding on March 16, 2015.

As we have previously reported, the debt limit does not restrict the Congress's ability to enact spending and revenue legislation that affects the level of federal debt or otherwise constrains fiscal policy; however, it restricts Treasury's authority to borrow to finance the decisions already enacted by the Congress and the President.[9] The United States benefits from the confidence investors have that debt backed by the full faith and credit of the United States will be honored. As we have also previously reported, delays in raising the debt limit can create uncertainty in the Treasury market and lead to higher Treasury borrowing costs. To avoid such uncertainty and related borrowing costs, we noted, in our February 2011 and July 2012 reports related to the debt limit, that the Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue at the time those decisions are made to avoid potential disruptions to the Treasury market and to help inform the fiscal policy debate in a timely way.

[8]Pub. L. No. 113-83, § 2, 128 Stat. 1011 (Feb. 15, 2014).

[9]GAO, *Debt Limit: Analysis of 2011-2012 Actions Taken and Effect of Delayed Increase on Borrowing Costs*, GAO-12-701 (Washington, D.C.: July 23, 2012), and *Debt Limit: Delays Create Debt Management Challenges and Increase Uncertainty in the Treasury Market*, GAO-11-203 (Washington, D.C.: Feb. 22, 2011).

In fiscal year 2014, the federal deficit shrank for the second year in a row, but this deficit and the need to refinance maturing debt meant that federal financing needs continued to grow. The reported federal deficit for fiscal year 2014 of $483 billion was down from the fiscal year 2013 reported federal deficit of $680 billion. Debt held by the public increased slightly as a percentage of gross domestic product (GDP), from roughly 72 percent of GDP at the end of fiscal year 2013 to roughly 74 percent at the end of fiscal year 2014. Federal deficits contributed less to the growth in debt held by the public in fiscal year 2014 than in prior fiscal years. While today's relatively lower interest rates have kept interest costs lower than they otherwise could have been, despite the recent increases in debt held by the public, interest rates are expected to increase as the economy continues to recover, resulting in increasing pressure on the budget. Over the longer term, debt held by the public as a share of GDP is expected to grow as a result of the structural imbalance between revenue and spending driven on the spending side by rising health care costs and demographics. Increasing numbers of baby-boom generation members are becoming eligible for Social Security retirement benefits and for Medicare. In addition, health care spending has been growing faster than the overall economy over the past several decades and is expected to continue to grow at an increased rate as more members of the baby-boom generation retire and become eligible for federal health programs. The aging of the population and rising health care costs will continue to put upward pressure on spending and, absent action to address the growing imbalance between spending and revenue, the federal government faces an unsustainable growth in debt.

We are sending copies of this report to interested congressional committees, the Fiscal Assistant Secretary of the Treasury, the Commissioner of the Bureau of the Fiscal Service, the Inspector General of the Department of the Treasury, the Director of the Office of Management and Budget, and other agency officials. In addition, this report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions concerning this report, please contact me at (202) 512-3406 or engelg@gao.gov. Contact points for our

Offices of Congressional Relations and Public Affairs may be found on the last page of this report.

Sincerely yours,

Gary T. Engel
Director
Financial Management
and Assurance

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

Independent Auditor's Report

To the Commissioner of the Bureau of the Fiscal Service

In our audits of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Schedule of Federal Debt) for the fiscal years ended September 30, 2014, and 2013, we found

- the Schedules of Federal Debt for the fiscal years ended September 30, 2014, and 2013, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;
- the Bureau of the Fiscal Service (Fiscal Service) maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2014; and
- no reportable noncompliance for fiscal year 2014 with provisions of applicable laws, regulations, contracts, and grant agreements we tested related to the Schedule of Federal Debt.

The following sections discuss in more detail (1) our report on the Schedules of Federal Debt and on internal control over financial reporting, which includes other information[1] included with the Schedules of Federal Debt; (2) our report on compliance with laws, regulations, contracts, and grant agreements; and (3) agency comments.

[1]Other information consists of the Overview on the Schedule of Federal Debt Managed by the Bureau of the Fiscal Service.

Report on the Schedules of Federal Debt and on Internal Control over Financial Reporting

In connection with fulfilling our requirement to audit the consolidated financial statements of the U.S. government, we have audited the Schedules of Federal Debt because of the significance of the federal debt to the federal government's consolidated financial statements.[2] The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and Discounts managed by the Department of the Treasury's (Treasury) Fiscal Service, and include accompanying notes.[3] We also have audited Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2014, based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

We conducted our audits in accordance with U.S. generally accepted government auditing standards. We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our audit opinions.

Management's Responsibility

Fiscal Service management is responsible for (1) the preparation and fair presentation of the Schedules of Federal Debt in accordance with U.S. generally accepted accounting principles; (2) preparing and presenting other information included in documents containing the audited Schedules of Federal Debt and auditor's report, and ensuring the consistency of that information with the audited Schedules of Federal Debt; (3) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of Schedules of Federal Debt that are free from material misstatement, whether due to fraud or

[2] 31 U.S.C. § 331(e)(2). Because Fiscal Service is a bureau within the Department of the Treasury, federal debt and related activity and balances managed by it are also significant to the consolidated financial statements of the Department of the Treasury (see 31 U.S.C. § 3515(b)).

[3] Debt held by the public represents federal debt issued by Treasury and held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments. Intragovernmental debt holdings represent federal debt owed by Treasury to federal government accounts, primarily federal trust funds such as Social Security and Medicare.

error; (4) evaluating the effectiveness of internal control over financial reporting based on the criteria established under FMFIA; and (5) providing its assertion about the effectiveness of internal control over financial reporting as of September 30, 2014, based on its evaluation, included in the accompanying Management's Report on Internal Control over Financial Reporting Relevant to the Schedule of Federal Debt in appendix I.

Auditor's Responsibility

Our responsibility is to express an opinion on the Schedules of Federal Debt and an opinion on Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt based on our audits. U.S. generally accepted government auditing standards require that we plan and perform the audits to obtain reasonable assurance about whether the Schedules of Federal Debt are free from material misstatement, and whether effective internal control over financial reporting was maintained in all material respects. We are also responsible for applying certain limited procedures to the other information included with the Schedules of Federal Debt.

An audit of the Schedules of Federal Debt involves performing procedures to obtain audit evidence about the amounts and disclosures in the Schedules of Federal Debt. The procedures selected depend on the auditor's judgment, including the auditor's assessment of the risks of material misstatement of the Schedules of Federal Debt, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Schedules of Federal Debt in order to design audit procedures that are appropriate in the circumstances. An audit of the Schedules of Federal Debt also involves evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the Schedules of Federal Debt. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, evaluating the design and operating effectiveness of internal control over financial reporting based on the assessed risk, and testing relevant internal control over financial reporting. Our audit of internal control also considered Fiscal Service's process for evaluating and reporting on internal control over financial reporting relevant to the Schedule of Federal Debt based on criteria established under FMFIA. Our audits also included performing such other procedures as we considered necessary in the circumstances.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations. We limited our internal control testing to testing controls over financial reporting. Our internal control testing was for the purpose of expressing an opinion on whether effective internal control over financial reporting relevant to the Schedule of Federal Debt was maintained, in all material respects. Consequently, our audit may not identify all deficiencies in internal control over financial reporting relevant to the Schedule of Federal Debt that are less severe than a material weakness.[4]

Definitions and Inherent Limitations of Internal Control over Financial Reporting

Internal control over financial reporting relevant to the Schedule of Federal Debt is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of the Schedule of Federal Debt in accordance with U.S. generally accepted accounting principles and (2) transactions related to the Schedule of Federal Debt are executed in accordance with laws governing the use of budget authority and with other applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on the Schedule of Federal Debt.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error. We also caution that projecting any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

[4]A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

Opinion on the Schedules of Federal Debt

In our opinion, the Schedules of Federal Debt present fairly, in all material respects, Federal Debt Managed by Fiscal Service and the related Accrued Interest Payables and Net Unamortized Premiums and Discounts as of September 30, 2014, and 2013, and the related increases and decreases for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

Opinion on Internal Control over Financial Reporting

In our opinion, Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2014, based on criteria established under FMFIA.

During fiscal year 2014, Fiscal Service made significant efforts and sufficiently addressed most of the internal control issues related to a significant deficiency in internal control[5] that we reported for fiscal year 2013 concerning information systems controls.[6] While we identified some continuing and new control deficiencies relating to information systems and in other areas, we do not consider them individually or collectively to be material weaknesses or significant deficiencies. We have communicated these matters to management and, where appropriate, will report on them separately to Fiscal Service management, along with recommendations for corrective actions.

Fiscal Service relies on a number of information systems to manage the federal debt. In late fiscal year 2011, Treasury began consolidating the data centers and related operations of Treasury's Bureau of the Public Debt and Financial Management Service into what is now Fiscal Service. In addition, in fiscal year 2013, Fiscal Service began testing a new general ledger system and implemented the new system in fiscal year 2014. These changes may have contributed to some of the above noted control deficiencies that we identified. Fiscal Service's continuing consolidation efforts can introduce risks that require corresponding changes to controls and can hinder the effective operation of controls. As such, it will be important that management sustain focus on assessing

[5]A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

[6]GAO-14-173.

associated risks, monitoring the effectiveness of the operation of controls, and designing and implementing effective internal controls.

Other Matter

Other Information

Fiscal Service's other information contains a wide range of information, some of which is not directly related to the Schedules of Federal Debt. This information is presented for purposes of additional analysis and is not a required part of the Schedules of Federal Debt. We read the other information included with the Schedules of Federal Debt in order to identify material inconsistencies, if any, with the audited Schedules of Federal Debt. Our audit was conducted for the purpose of forming an opinion on the Schedules of Federal Debt. We did not audit and do not express an opinion or provide any assurance on the other information.

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

In connection with our audits of the Schedules of Federal Debt, we tested compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements consistent with our auditor's responsibility discussed below. We caution that noncompliance may occur and not be detected by these tests. We performed our tests of compliance in accordance with U.S. generally accepted government auditing standards.

Management's Responsibility

Fiscal Service management is responsible for complying with laws, regulations, contracts, and grant agreements applicable to Fiscal Service.

Auditor's Responsibility

Our responsibility is to test compliance with selected provisions of laws, regulations, contracts, and grant agreements applicable to Fiscal Service that have a direct effect on the determination of material amounts and disclosures in the Schedules of Federal Debt, and perform certain other limited procedures. Accordingly, we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to Fiscal Service.

Results of Our Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

Our tests for compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements disclosed no instances of noncompliance for fiscal year 2014 that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our tests was not to provide an opinion on compliance with laws, regulations, contracts, and grant agreements applicable to Fiscal Service. Accordingly, we do not express such an opinion.

Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements, and the results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

Agency Comments

In commenting on a draft of this report, Fiscal Service concurred with our conclusions. The complete text of Fiscal Service's response is reprinted in appendix II.

Gary T. Engel

Gary T. Engel
Director
Financial Management
and Assurance

November 3, 2014

Overview, Schedules, and Notes

Overview on Federal Debt Managed by the Bureau of the Fiscal Service

Overview on Federal Debt Managed by the Bureau of the Fiscal Service

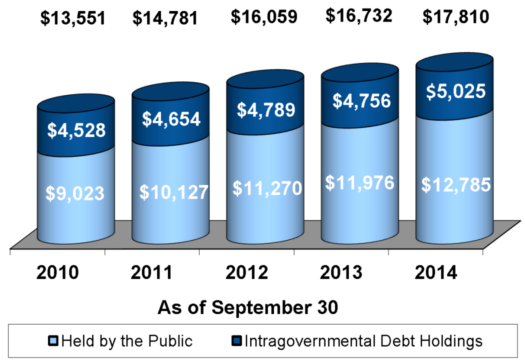
Gross Federal Debt Outstanding

Federal debt managed by the Bureau of the Fiscal Service (Fiscal Service) comprises debt held by the public and debt held by certain federal government accounts (issued under 31 U.S.C. §§ 3101-3113), the latter of which is referred to as intragovernmental debt holdings. As of September 30, 2014 and September 30, 2013, outstanding gross federal debt managed by Fiscal Service totaled $17,810 billion and $16,732 billion, respectively.[1] The increase in gross federal debt of $1,078 billion during fiscal year 2014 was due to an increase in gross intragovernmental debt holdings of $269 billion and an increase in gross debt held by the public of $809 billion. As Figure 1 illustrates, overall intragovernmental debt holdings and debt held by the public increased by $497 billion and $3,762 billion, respectively, from September 30, 2010 to September 30, 2014. The primary reason for the increases in intragovernmental debt holdings is the excess annual receipts (including interest earnings) over disbursements in the Federal Old-Age and Survivors Insurance Trust Fund, Civil Service Retirement and Disability Fund (CSRDF), Military Retirement Fund, and DOD Medicare-Eligible Retiree Health Care Fund. The increases in debt held by the public are due primarily to total federal spending exceeding total federal revenues. From September 30, 2012 to September 30, 2013, intragovernmental debt holdings decreased by $33 billion while debt held by the public increased by $706 billion. Because of a delay in raising the debt limit in fiscal year 2013, the Department of the Treasury (Treasury) had to take extraordinary actions to meet the government's obligations as they came due without exceeding the debt limit, which included suspension of investments to the CSRDF and Postal Service Retiree Health Benefits Fund (Postal Benefits Fund). As of September 30, 2013, the delay still existed and suspension of investments for these funds continued, which contributed to the decrease in the intragovernmental debt holdings.

On October 17, 2013, the Continuing Appropriations Act, 2014 (Public Law No 113-46) was enacted suspending the debt limit through February 7, 2014. On October 17, 2013, the suspended investments were reinvested in the CSRDF and the Postal Benefits Fund. On February 8, 2014 the statutory debt limit was increased to $17,212 billion as a result of Section 1002 "Default Prevention Act of 2013," of the Continuing Appropriations Act, 2014. The debt limit increase was based on the change in qualifying federal debt securities outstanding on October 17, 2013, compared to those outstanding on February 8, 2014. As such, on Monday, February 10, 2014, Treasury departed from its normal debt management procedures and began taking extraordinary actions to avoid exceeding the statutory debt limit. On February 15, 2014, the Temporary Debt Limit Extension Act (Public Law No. 113-83) was enacted suspending the statutory debt limit through March 15, 2015. As of September 30, 2014, outstanding debt obligations subject to the statutory debt limit had increased to $17,781 billion. As of September 30, 2014, gross debt held by the public totaled $12,785 billion and gross intragovernmental debt holdings totaled $5,025 billion.

[1] Federal debt outstanding reported here differs from the amount reported in the Financial Report of the United States Government because of the securities not maintained or reported by Fiscal Service which are issued by the Federal Financing Bank and other specific securities issued outside of the authority of 31 U.S.C. §§ 3101-3113.

Figure 1 **Total Gross Federal Debt Outstanding**
(in billions)

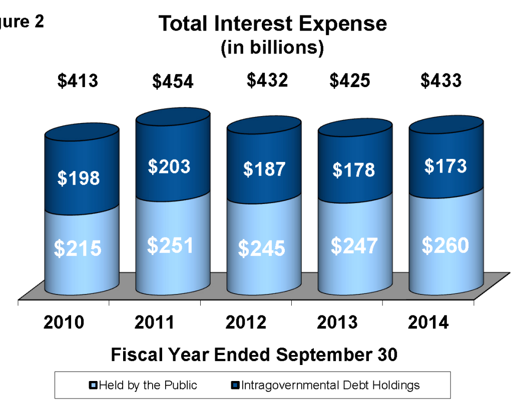


Interest Expense

Interest expense incurred during fiscal year 2014 consists of (1) interest accrued and paid on debt held by the public or credited to accounts holding intragovernmental debt during the fiscal year, (2) interest accrued during the fiscal year, but not yet paid on debt held by the public or credited to accounts holding intragovernmental debt, and (3) net amortization of premiums and discounts. The primary components of interest expense are interest paid on the debt held by the public and interest credited to federal government trust funds and other federal government accounts that hold Treasury securities. The interest paid on the debt held by the public affects the current spending of the federal government and represents the burden of servicing its debt (i.e., payments to outside creditors). Interest credited to federal government trust funds and other federal government accounts, on the other hand, does not result in an immediate outlay of the Federal Government because one part of the government pays the interest and another part receives it. However, this interest represents a claim on future budgetary resources and hence an obligation on future taxpayers. This interest, when reinvested by the trust funds and other federal government accounts, is included in the programs' excess funds not currently needed in operations, which are invested in federal securities. For fiscal year 2014, interest expense incurred totaled $433 billion; this consisted of interest expense on debt held by the public of $260 billion, and $173 billion in interest incurred for intragovernmental debt holdings.

As Figure 2 illustrates, interest expense increased from fiscal year 2010 through 2011 due primarily to an increase in Treasury notes and bonds outstanding, which had higher average interest rates than Treasury bills. Interest expense decreased for fiscal year 2012 due primarily to a decrease in the average interest rates for Treasury notes, bonds and Treasury Inflation-Protected Securities (TIPS). From fiscal year 2012 to 2014, total interest expense increased from $432 billion to $433 billion. This increase results from an increase of $15 billion in interest expense on debt held by the public offset by a $14 billion decrease in interest expense on intragovernmental debt holdings. The $15 billion increase in interest expense on debt held by the public results from the overall increase in the outstanding debt held by the public being almost fully offset by a decrease in the average interest rates for Treasury notes, bonds, and TIPS. The $14 billion decrease in interest expense on intragovernmental debt holdings results primarily from the decrease in the average interest rates on intragovernmental debt holdings. Average interest rates on principal balances outstanding as of September 30, 2014 and 2013, are disclosed in the Notes to the Schedules of Federal Debt.

Figure 2

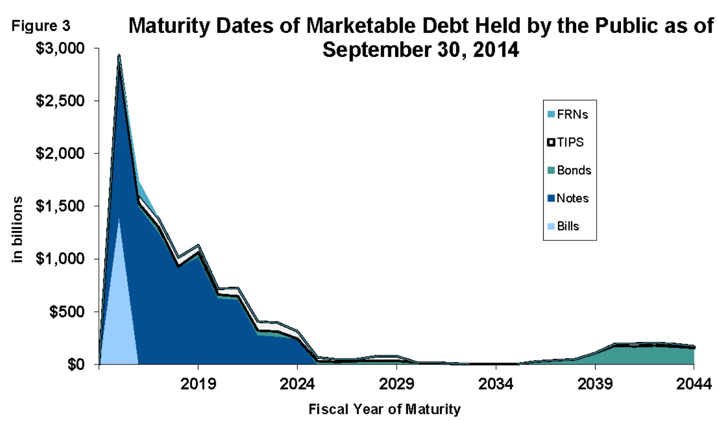

Total Interest Expense
(in billions)
$413
$454
$432
$425
$433
$198
$203
$187
$178
$173
$215
$251
$245
$247
$260
2010
2011
2012
2013
2014
Fiscal Year Ended September 30
Held by the Public
Intragovernmental Debt Holdings

Debt Held by the Public

Debt held by the public primarily represents the amount the Federal Government has borrowed to finance cumulative cash deficits. During fiscal year 2014, Treasury primarily used the existing suite of securities to meet the borrowing needs of the Federal Government while increasing its offerings of longer term securities to extend the average length of maturity. These actions contributed to a decrease in Treasury bills; whereas, Treasury notes, bonds and TIPS increased by $410 billion, $171 billion and $109 billion respectively, in fiscal year 2014. In addition to the existing suite of securities, Treasury began issuing Floating Rate Notes (FRNs), with a term of 2 years, in fiscal year 2014, which increased the offerings of longer term securities. As of September 30, 2014 and 2013, gross debt held by the public totaled $12,785 billion and $11,976 billion, respectively (see Figure 1), an increase of $809 billion. Due primarily to a decrease in short term debt issuances, as compared to the prior year, the total dollar amount of activity for both borrowings and repayments of debt held by the public decreased for fiscal year 2014.

As of September 30, 2014, $12,272 billion, or 96 percent, of the securities that constitute debt held by the public were marketable, meaning that once the Federal Government issues them, they can be resold by whoever owns them. Marketable debt is made up of Treasury bills, Treasury notes, Treasury bonds, TIPS and FRNs with maturity dates ranging from less than 1 year out to 30 years. Of the marketable securities currently held by the public as of September 30, 2014, $7,063 billion, or 58 percent, will mature within the next 4 years (see Figure 3). As of September 30, 2014 and 2013, total marketable debt held by the public maturing within the next 10 years totaled $10,744 billion and $10,250 billion, respectively, an increase of $494 billion.

Figure 3



Debt Held by the Public, cont.

The Federal Government also issues to the public nonmarketable securities, which cannot be resold, and have maturity dates ranging from on demand out to 40 years. As of September 30, 2014, nonmarketable securities totaled $513 billion, or 4 percent of debt held by the public. As of that date, nonmarketable securities primarily consisted of Government Account Series totaling $197 billion, savings securities totaling $177 billion, and State and Local Government Series (SLGS) securities totaling $106 billion. From fiscal year end 2013 to 2014, total nonmarketable securities increased from $399 billion to $513 billion. This increase is primarily the result of the suspension of investments to the Government Securities Investment Fund (G-Fund) as of September 30, 2013 related to the extraordinary actions taken due to the delay in raising the debt limit that continued to exist as of September 30, 2013. On October 17, 2013, the Continuing Appropriations Act, 2014 (Public Law No 113-46) was enacted suspending the debt limit through February 7, 2014. On October 17, 2013, $174 billion was reinvested into the G-Fund, which included amounts uninvested as of September 30, 2013.

The Federal Reserve Banks (FRBs) act as fiscal agents for Treasury, as permitted by the Federal Reserve Act. As fiscal agents for Treasury, the FRBs play a significant role in the processing of marketable book-entry securities and paper U.S. savings bonds. For marketable book-entry securities, selected FRBs receive bids, issue book-entry securities to awarded bidders, and collect payments on behalf of Treasury; and make interest and redemption payments from Treasury's account to the accounts of security holders. For paper U.S. savings bonds, selected FRBs print and deliver savings bonds purchased with federal income tax refunds; and redeem savings bonds, including handling the related transfers of cash.

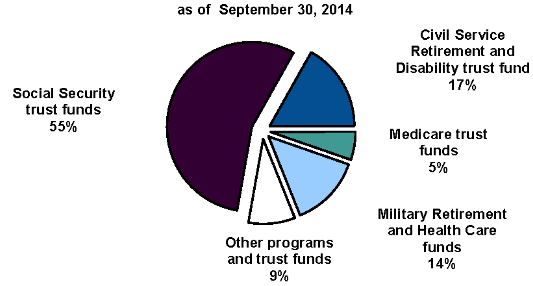
Intragovernmental Debt Holdings

Intragovernmental debt holdings represent balances of Treasury securities held by over 240 individual federal government accounts with either the authority or the requirement to invest excess receipts in special U.S. Treasury securities that are guaranteed for principal and interest by the full faith and credit of the U.S. Government. Intragovernmental debt holdings primarily consist of balances in the Social Security, Medicare, Military Retirement and Health Care, and Civil Service Retirement and Disability trust funds.[2] As of September 30, 2014, such funds accounted for $4,581 billion, or 91 percent, of the $5,025 billion intragovernmental debt holdings balances (see Figure 4). As of September 30, 2014 and 2013, gross intragovernmental debt holdings totaled $5,025 billion and $4,756 billion, respectively (see Figure 1), an increase of $269 billion. This increase is primarily the result of the suspension of investments to the CSRDF and Postal Benefits Fund as of September 30, 2013 related to the extraordinary actions taken due to the delay in raising the debt limit that continued to exist as of September 30, 2013. On October 17, 2013, the Continuing Appropriations Act, 2014 (Public Law No 113-46) was enacted suspending the debt limit through February 7, 2014. On October 17, 2013, $118 billion and $5 billion were reinvested into the CSRDF and Postal Benefits Fund, respectively, which included amounts uninvested as of September 30, 2013.

The majority of intragovernmental debt holdings are Government Account Series (GAS) securities. GAS securities consist of par value securities and market-based securities, with terms ranging from on demand out to 30 years. Par value securities are issued and redeemed at par (100 percent of the face value), regardless of current market conditions. Market-based securities, however, can be issued at a premium or discount and are redeemed at par value on the maturity date or at market value if redeemed before the maturity date.

Figure 4

Components of Intragovernmental Debt Holdings
as of September 30, 2014



[2] The Social Security trust funds consist of the Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund. The Medicare trust funds are made up of the Federal Hospital Insurance Trust Fund and the Federal Supplementary Medical Insurance Trust Fund. The Military Retirement and Health Care Funds consist of the Military Retirement Fund and the DOD Medicare-Eligible Retiree Health Care Fund.

Significant Events in Fiscal Year 2014

Delays in Raising the Statutory Debt Limit

A delay in raising the statutory debt limit, which began on May 20, 2013, continued into fiscal year 2014. From October 1 through October 16, 2013, Treasury departed from its normal debt management procedures and invoked legal authorities to avoid exceeding the debt limit. Extraordinary actions taken by Treasury during this period to ensure the debt limit was not exceeded included (1) suspending investments in the G-Fund and CSRDF, (2) suspending new issuances of SLGS securities, (3) exchanging $9,305 million of Treasury securities held by the CSRDF for securities issued by the Federal Financing Bank and (4) suspending investments to the Exchange Stabilization Fund.

On October 17, 2013, the Continuing Appropriations Act, 2014 (Public Law No 113-46) was enacted, which suspended the statutory debt limit through February 7, 2014. Treasury discontinued its use of extraordinary actions and resumed normal debt management operations. On October 17, 2013, and in accordance with relevant laws, Fiscal Service restored uninvested principal amounts to the G-Fund, CSRDF and the Postal Benefits Fund in the amounts of $173,948 million, $117,693 million and $4,601 million, respectively. The Exchange Stabilization Fund was fully reinvested on October 17, 2013 and does not have interest restoration legislation. In accordance with relevant laws, Fiscal Service restored the interest related to the uninvested principal during the period May 20, 2013 through October 16, 2013, to the G-Fund on October 18, 2013, the next interest payment date, in the amount of $653 million. Interest related to the uninvested principal during the period of May 20, 2013 through October 16, 2013, for CSRDF and Postal Benefits Fund was restored on December 31, 2013, the next interest payment date, in the amounts of $539 million and $24 million, respectively.

The statutory debt limit was increased on February 8, 2014 to $17,211,558 million based on the change in qualifying federal debt securities outstanding as of October 17, 2013, compared to those outstanding as of February 8, 2014. As such, on Monday, February 10, 2014, Treasury departed from its normal debt management procedures and invoked legal authorities to avoid exceeding the debt limit. Extraordinary actions taken by Treasury to meet the government's obligations as they came due without exceeding the debt limit included (1) suspending investments in the G-Fund and CSRDF, (2) redeeming certain investments held by CSRDF earlier than normal and (3) suspending new issuances of SLGS securities. On February 15, 2014, the Temporary Debt Limit Extension Act, (Public Law 113-83) was enacted which suspended the statutory debt limit through March 15, 2015. On February 18, 2014, and in accordance with relevant laws, Fiscal Service restored uninvested principal amounts to the G-Fund and the CSRDF in the amounts of $67,972 million and $532 million, respectively. In accordance with relevant laws, Fiscal Service restored the interest related to the uninvested principal during the period February 10, 2014 through February 14, 2014 to the G-Fund on February 18, 2014, the next interest payment date, in the amount of $28 million. Interest related to the uninvested principal during the period of February 10, 2014 through February 14, 2014, for CSRDF was restored on June 30, 2014, the next interest payment date, and was less than $1 million.

Significant Events in Fiscal Year 2014, cont.

Floating Rate Notes

In August 2012, Treasury announced its plan to develop a FRN program to complement the existing suite of securities issued and to help achieve the objective of financing the government at the lowest cost over time. On January 23, 2014, Treasury announced the first FRN, a two year note. This was then followed by the auction and settlement on January 29 and 31, 2014, respectively. The first issuance of this note yielded $15 billion in outstanding securities due to mature on January 31, 2016. The FRN is the first new security that Treasury has offered since TIPS were first auctioned in 1997 and may be issued with maturities of at least one year, but not more than ten years. It is also anticipated that Treasury will, for the first time, issue FRNs to Government Account Series customers in fiscal year 2015.

The FRN is a security that pays interest quarterly and has an interest rate that can change over time. Treasury FRNs are indexed to the highest accepted discount rate (high rate) of the most recent 13-week Treasury bill auction. The interest rate will be the spread plus the index rate, which resets daily based on the most recent auction of 13-week bills and will be subject to a minimum daily interest accrual rate of zero percent. The minimum and maximum purchase and award amounts and the award methodology are the same as for other marketable securities. Treasury announces specific terms and conditions of each issue, such as the auction date, issue date, and the public offering amount, prior to each auction.

End of Paper EE and I Savings Bond Reissues

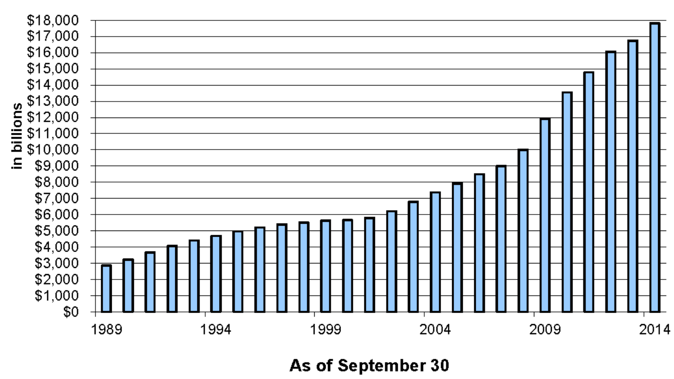
On February 18, 2014, Fiscal Service implemented electronic-only reissues of Series EE and I Savings bonds. The move is a continuation of the *Paperless Treasury* initiative announced in 2010. Paper Series EE and I Savings bonds reissues are requested by customers to change registrations or to replace lost, stolen, or damaged bonds. Under the new program, there will be no reissues of paper Series EE or I Savings bonds. Customers will instead receive electronic reissues of Series EE and I Savings bonds through TreasuryDirect. This change reduces the number of paper bonds printed by 62 percent based on the total number of paper bonds printed in fiscal year 2012 and represents a significant step toward ending all paper savings bond issues. With this phase complete, Fiscal Service will now focus on ending the remaining 38 percent of paper savings bond issues such as tax-time paper savings bonds issued through income tax refunds using IRS Form 8888.

Historical Perspective

Federal debt outstanding is one of the largest legally binding obligations of the Federal Government. Nearly all the federal debt has been issued by the Treasury with a small portion being issued by other federal government agencies. Treasury issues debt securities for two principal reasons, (1) to borrow needed funds to finance the current operations of the Federal Government and (2) to provide an investment and accounting mechanism for certain federal government accounts' (primarily federal trust funds) excess receipts. Total gross federal debt outstanding has dramatically increased over the past 25 years from $2,857 billion as of September 30, 1989, to $17,810 billion as of September 30, 2014 (see Figure 5). Large budget deficits continued during the 1990's due to tax policy decisions and increased outlays for defense and domestic programs. Through fiscal year 1997, annual federal deficits continued to be large and debt continued to grow at a steady pace.

Figure 5

Total Gross Federal Debt Outstanding



Source: Monthly Statement of the Public Debt

Figures shown prior to 1996 are unaudited and include securities issued by the Federal Financing Bank.

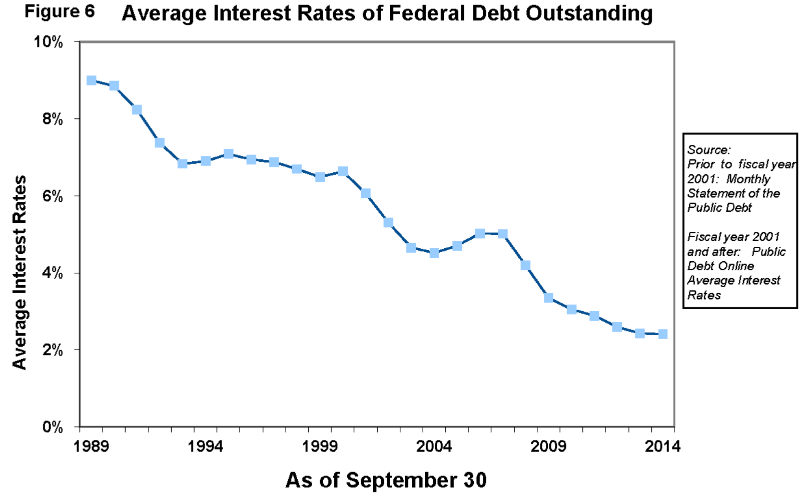
By fiscal year 1998, federal debt held by the public was beginning to decline. In fiscal years 1998 through 2001, the amount of debt held by the public fell by $476 billion, from $3,815 billion to $3,339 billion. However, federal debt held by the public began to increase in fiscal year 2002, primarily as a result of higher federal outlays. Federal debt held by the public increased by 51.2 percent from fiscal year 2002 through fiscal year 2007. From fiscal year 2008 through fiscal year 2014, federal debt held by the public more than doubled, rising by $7,736 billion. This increase was primarily a result of the last economic recession and the federal government's actions to stabilize financial markets and promote economic recovery. Since fiscal year 2002, debt held by the public has increased from $3,339 billion as of September 30, 2001 to $12,785 billion as of September 30, 2014.

Historical Perspective, cont.

Even in those years where debt held by the public declined, total federal debt increased because of increases in intragovernmental debt holdings. Over the past 4 fiscal years, intragovernmental debt holdings increased by $497 billion, from $4,528 billion as of September 30, 2010, to $5,025 billion as of September 30, 2014. By law, federal government accounts, including trust funds, have the authority or are required to invest their excess annual receipts (including interest earnings) over disbursements in federal securities. As a result, the intragovernmental debt holdings balances primarily represent the cumulative surplus of funds due to the trust funds' cumulative annual excess of tax receipts, interest credited, and other collections compared to spending.

As shown in Figure 6, interest rates have fluctuated over the past 25 years. The average interest rates reflected here represent the original issue weighted effective yield on debt held by the public and intragovernmental debt holdings outstanding at the end of the fiscal year.

Figure 6 Average Interest Rates of Federal Debt Outstanding



Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

Schedules of Federal Debt

Managed by the Bureau of the Fiscal Service
For the Fiscal Years Ended September 30, 2014 and 2013
(Dollars in Millions)

	Federal Debt					
	Held by the Public			Intragovernmental Debt Holdings		
	Principal (Note 2)	Accrued Interest Payable	Net Unamortized Premiums/ (Discounts)	Principal (Note 3)	Accrued Interest Payable	Net Unamortized Premiums/ (Discounts)
Balance as of September 30, 2012	**$11,269,586**	**$57,222**	**($19,225)**	**$4,789,051**	**$45,548**	**$56,250**
Increases						
Borrowings from the Public	8,155,584		(10,112)			
Net Increase in Intragovernmental Debt Holdings						21,004
Accrued Interest (Note 4)		242,689			185,437	
Total Increases	**8,155,584**	**242,689**	**(10,112)**	**0**	**185,437**	**21,004**
Decreases						
Repayments of Debt Held by the Public	7,448,891					
Net Decrease in Intragovernmental Debt Holdings				33,336		
Interest Paid		248,716			187,856	
Net Amortization (Note 4)			(4,893)			7,807
Total Decreases	**7,448,891**	**248,716**	**(4,893)**	**33,336**	**187,856**	**7,807**
Balance as of September 30, 2013	**11,976,279**	**51,195**	**(24,444)**	**4,755,715**	**43,129**	**69,447**
Increases						
Borrowings from the Public	7,485,194		(9,368)			
Net Increase in Intragovernmental Debt Holdings				269,279		7,535
Accrued Interest (Note 4)		255,517			182,165	
Total Increases	**7,485,194**	**255,517**	**(9,368)**	**269,279**	**182,165**	**7,535**
Decreases						
Repayments of Debt Held by the Public	6,676,502					
Interest Paid		252,881			182,902	
Net Amortization (Note 4)			(4,433)			9,160
Total Decreases	**6,676,502**	**252,881**	**(4,433)**	**0**	**182,902**	**9,160**
Balance as of September 30, 2014	**$12,784,971**	**$53,831**	**($29,379)**	**$5,024,994**	**$42,392**	**$67,822**

The accompanying notes are an integral part of these schedules.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

For the Fiscal Years Ended September 30, 2014 and 2013

(Dollars in Millions)

Note 1. Significant Accounting Policies

Basis of Presentation

The Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Fiscal Service) have been prepared to report fiscal year 2014 and fiscal year 2013 balances and activity relating to monies borrowed from the public and certain federal government accounts under 31 U.S.C. §§ 3101-3113 to fund the operations of the U.S. government. Permanent, indefinite appropriations are available for the payment of interest on the federal debt and the redemption of Treasury securities.

Reporting Entity

The Constitution empowers the Congress to borrow money on the credit of the United States. The Congress has authorized the Secretary of the Treasury to borrow monies to operate the federal government within a statutory debt limit. Title 31, U.S. Code authorizes Treasury to prescribe the debt instruments and otherwise limit and restrict the amount and composition of the debt. Fiscal Service, an organizational entity within the Department of the Treasury, is responsible for issuing Treasury securities in accordance with such authority and to account for the resulting debt. In addition, Fiscal Service maintains an investment program for federal government accounts, including trust funds, that have legislative authority to invest temporary cash reserves not needed for current benefits and expenses. Fiscal Service issues and redeems Treasury securities for these federal government accounts based on data provided by the respective program agencies and other Treasury entities. Fiscal Service also issues other specific securities outside of the authority of 31 U.S.C. §§ 3101-3113, such as HOPE Bonds, that are not reported on the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service.

Basis of Accounting

The schedules were prepared in accordance with U.S. generally accepted accounting principles and from Fiscal Service's automated debt accounting system. Accounting principles generally accepted for Federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB), which is the official body for setting accounting standards of the Federal government. The FASAB issued the Statement of Federal Financial Accounting Standards (SFFAS) No. 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board* in July 2009. SFFAS No. 34 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of general purpose financial reports of federal reporting entities that are presented in accordance with Federal generally accepted accounting principles.

Interest costs are recorded as expenses when incurred, instead of when paid. Certain Treasury securities are issued at a discount or premium. These discounts and premiums are amortized over the term of the security using an interest method for all long term securities and the straight line method for short term securities. The Department of the Treasury also issues Treasury Inflation-Protected Securities (TIPS). The principal for TIPS is adjusted daily over the life of the security based on the Consumer Price Index for all Urban Consumers.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

For the Fiscal Years Ended September 30, 2014 and 2013

(Dollars in Millions)

Note 2. Federal Debt Held by the Public

As of September 30, 2014 and 2013, Federal Debt Held by the Public consisted of the following:

	2014		2013	
	Amount	Average Interest Rates	Amount	Average Interest Rates
Marketable:				
Treasury Bills	$ 1,409,627	0.1 %	$1,527,909	0.1%
Treasury Notes	8,160,196	1.8 %	7,750,336	1.8%
Treasury Bonds	1,534,068	4.9 %	1,363,114	5.1%
TIPS	1,044,676	0.9 %	936,041	1.1%
Floating Rate Notes	122,985	0.1%	-	-
Total Marketable	$ 12,271,552		$11,577,400	
Nonmarketable	$ 513,419	2.3 %	$398,879	2.4%
Total Federal Debt Held by the Public	$ 12,784,971		$11,976,279	

Treasury issues marketable bills usually at a discount, but may also issue at par, and pays the par amount of the security upon maturity. The average interest rate on Treasury bills represents the original issue effective yield on securities outstanding as of September 30, 2014 and 2013. Treasury bills are issued with a term of one year or less.

Treasury issues marketable notes and bonds as long-term securities that pay semi-annual interest based on the securities' stated interest rate. These securities are issued at either par value or at an amount that reflects a discount or a premium. The average interest rate on marketable notes and bonds represents the stated interest rate adjusted by any discount or premium on securities outstanding as of September 30, 2014 and 2013. Treasury notes are issued with a term of 2 – 10 years and Treasury bonds are issued with a term of more than 10 years.

Treasury also issues TIPS that have interest and redemption payments that are tied to the Consumer Price Index for all Urban Consumers, a widely used measure of inflation. TIPS are issued with a term of 5 years or more. At maturity, TIPS are redeemed at the inflation-adjusted principal amount, or the original par value, whichever is greater. TIPS pay a semi-annual fixed rate of interest applied to the inflation-adjusted principal. The average interest rate on TIPS represents the stated interest rate on principal plus inflation, adjusted by any discount or premium on securities outstanding as of September 30, 2014 and 2013. The TIPS Federal Debt Held by the Public inflation-adjusted principal balance includes inflation of $97,149 million and $88,524 million as of September 30, 2014 and 2013, respectively.

In January 2014, Treasury began issuing a new marketable security, the Floating Rate Note (FRN), which pays interest quarterly based on the interest rate at the time of payment. The interest rate of FRNs can change over time and is indexed to the highest accepted discount rate of the most recent 13-week marketable bill auction. These securities, like marketable notes and bonds, are issued at either par value or at an amount that reflects a discount or premium. The average interest rate on marketable FRNs represents the highest accepted discount rate of the most recent 13-week marketable auction as of September 30, 2014, adjusted by any discount or premium on securities outstanding as of that date. These notes are currently issued with a term of 2 years.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

For the Fiscal Years Ended September 30, 2014 and 2013

(Dollars in Millions)

Note 2. Federal Debt Held by the Public (continued)

Federal Debt Held by the Public includes federal debt held outside of the U. S. government by individuals, corporations, Federal Reserve Banks (FRB), state and local governments, and foreign governments and central banks. As of September 30, 2014, the FRB had total holdings of $1,919,365 million, which (1) excludes $534,667 million in Treasury securities used in overnight reverse repurchase transactions and (2) includes a net of $2,289 million in Treasury securities held by the FRB as collateral for securities lending activities. As of September 30, 2013, the FRB had total holdings of $1,930,247 million, which (1) excludes $145,184 million in Treasury securities used in overnight reverse repurchase transactions and (2) includes a net of $3,148 million in Treasury securities held by the FRB as collateral for securities lending activities. Treasury securities are held by the FRB in the FRB System Open Market Account (SOMA) for the purpose of conducting monetary policy.

Treasury issues nonmarketable securities at either par value or at an amount that reflects a discount or a premium. The average interest rate on the nonmarketable securities represents the original issue weighted effective yield on securities outstanding as of September 30, 2014 and 2013. Nonmarketable securities are issued with a term of on demand out to 40 years.

As of September 30, 2014 and 2013, nonmarketable securities consisted of the following:

	2014	2013
Domestic Series	$ 29,995	$ 29,995
Foreign Series	2,986	2,986
State and Local Government Series	105,668	124,079
United States Savings Securities	176,762	180,022
Government Account Series	196,520	60,445
Other	1,488	1,352
Total Nonmarketable	$ 513,419	$398,879

Government Account Series (GAS) securities are nonmarketable securities issued to federal government accounts. Federal Debt Held by the Public includes GAS securities issued to certain federal government accounts. One example is the GAS securities held by the Government Securities Investment Fund (G-Fund) of the federal employees' Thrift Savings Plan. Federal employees and retirees who have individual accounts own the GAS securities held by the fund. For this reason, these securities are considered part of the Federal Debt Held by the Public rather than Intragovernmental Debt Holdings. The GAS securities held by the G-Fund consist of overnight investments redeemed one business day after their issue. The net increase in the fund's principal balance during fiscal year 2014 is included in the Borrowings from the Public amount reported on the Schedules of Federal Debt. The net decrease in the fund's principal balance during fiscal year 2013 is included in the Repayments of Debt Held by the Public amount reported on the Schedules of Federal Debt.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

For the Fiscal Years Ended September 30, 2014 and 2013

(Dollars in Millions)

Note 3. Intragovernmental Debt Holdings

As of September 30, 2014 and 2013, Intragovernmental Debt Holdings are owed to the following:

		2014	2013
SSA:	Federal Old-Age and Survivors Insurance Trust Fund	$2,712,805	$2,655,599
OPM:	Civil Service Retirement and Disability Fund	843,557	713,761
DOD:	Military Retirement Fund	483,111	421,327
HHS:	Federal Hospital Insurance Trust Fund	202,207	206,010
DOD:	DOD Medicare-Eligible Retiree Health Care Fund	200,372	188,664
SSA:	Federal Disability Insurance Trust Fund	70,113	100,791
HHS:	Federal Supplementary Medical Insurance Trust Fund	68,391	67,385
DOE:	Nuclear Waste Disposal Fund	51,527	50,598
FDIC:	The Deposit Insurance Fund	48,750	36,864
OPM:	Postal Service Retiree Health Benefits Fund	48,468	42,324
OPM:	Employees Life Insurance Fund	43,213	41,951
DOL:	Unemployment Trust Fund	35,919	29,478
OPM:	Employees Health Benefits Fund	23,556	23,427
Treasury:	Exchange Stabilization Fund	22,649	22,669
DOS:	Foreign Service Retirement and Disability Fund	17,792	17,364
DOL:	Pension Benefit Guaranty Corporation	17,444 *	22,575 *
DOT:	Airport and Airway Trust Fund	12,759	11,808
NCUA:	National Credit Union Share Insurance Fund	11,024	10,643
DOT:	Highway Trust Fund	10,696	1,957
Other Programs and Funds		100,641	90,520
Total Intragovernmental Debt Holdings		$ 5,024,994	$4,755,715

* As of September 30, 2013, the Pension Benefit Guaranty Corporation (PBGC) amount consisted of $4,883 million of marketable Treasury securities as well as $17,692 million of GAS securities. As of September 30, 2014, the PBGC amount consisted only of GAS securities. On October 1, 2013, PBGC began reporting its investments in marketable Treasury securities through a newly established Deposit Fund. As such, PBGC's investments in marketable Treasury securities as of September 30, 2014 are included in the Debt Held by the Public balances reported on the Schedules of Federal Debt.

Social Security Administration (SSA); Office of Personnel Management (OPM); Department of Defense (DOD); Department of Health and Human Services (HHS); Department of Energy (DOE); Federal Deposit Insurance Corporation (FDIC); Department of Labor (DOL); Department of the Treasury (Treasury); Department of State (DOS); Department of Transportation (DOT); National Credit Union Administration (NCUA).

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

For the Fiscal Years Ended September 30, 2014 and 2013

(Dollars in Millions)

Note 3. Intragovernmental Debt Holdings (continued)

Intragovernmental Debt Holdings primarily consist of GAS securities. Treasury issues GAS securities at either par value or at an amount that reflects a discount or a premium. GAS securities are issued with a term of on demand out to 30 years. GAS securities include TIPS, which are reported at an inflation-adjusted principal balance using the Consumer Price Index for all Urban Consumers. As of September 30, 2014 and 2013, the inflation-adjusted principal balance included inflation of $121,483 million and $108,908 million, respectively. The average interest rates on Intragovernmental Debt Holdings, excluding TIPS, for fiscal years 2014 and 2013 were 3.3 and 3.6 percent, respectively. The average interest rate on TIPS for both fiscal years 2014 and 2013 was 1.3 percent. The average interest rate represents the original issue weighted effective yield on securities outstanding as of September 30, 2014 and 2013.

Note 4. Interest Expense

Interest expense on federal debt for fiscal years 2014 and 2013 consisted of the following:

	2014	2013
Federal Debt Held by the Public		
Accrued Interest	$255,517	$242,689
Net Amortization of Premiums and Discounts	4,433	4,893
Total Interest Expense on Federal Debt Held by the Public	259,950	247,582
Intragovernmental Debt Holdings		
Accrued Interest	182,165	185,437
Net Amortization of Premiums and Discounts	(9,160)	(7,807)
Total Interest Expense on Intragovernmental Debt Holdings	173,005	177,630
Total Interest Expense on Federal Debt Managed by Fiscal Service	$432,955	$425,212

The valuation of TIPS is adjusted daily over the life of the security based on the Consumer Price Index for all Urban Consumers. This daily adjustment is an interest expense for federal debt managed by Fiscal Service. Accrued interest on Federal Debt Held by the Public includes inflation adjustments of $19,682 million and $16,548 million for fiscal years 2014 and 2013, respectively. Accrued interest on Intragovernmental Debt Holdings includes inflation adjustments of $12,381 million and $10,754 million for fiscal years 2014 and 2013, respectively.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service

For the Fiscal Years Ended September 30, 2014 and 2013

(Dollars in Millions)

Note 5. Fund Balance with Treasury

	As of September 30, 2014	As of September 30, 2013
Appropriated Funds Obligated	$16	$56

The Fund Balance with Treasury, a non-entity, intragovernmental account, is not included on the Schedules of Federal Debt and is presented for informational purposes.

Note 6. Suspension of Issuances and Subsequent Restorations of Uninvested Principal and Interest Amounts

A delay in raising the statutory debt limit existed as of September 30, 2013. When delays in raising the statutory debt limit occur, Treasury often must deviate from its normal debt management operations and take a number of extraordinary actions to meet the government's obligations as they come due without exceeding the debt limit. Many extraordinary actions taken by Treasury during the period of May 20, 2013 through September 30, 2013, resulted in federal debt securities not being issued to certain federal government accounts. Consequently, the resulting uninvested principal as of September 30, 2013, totaling $247,827 million and related interest totaling $801 million are not reported on the Schedule of Federal Debt. Uninvested principal amounts for the Government Securities Investment Fund (G-Fund), Civil Service Retirement and Disability Fund (CSRDF), and Postal Service Retirees Health Benefits Fund (Postal Benefits Fund) were $119,880 million, $123,346 million, and $4,601 million, respectively, as of September 30, 2013. Additionally, the related interest for the G-Fund, CSRDF, and Postal Benefits Fund that would have been accrued and/or paid during the period of May 20, 2013 through September 30, 2013, would have been $476 million, $304 million, and $21 million, respectively, on September 30, 2013.

On October 1, 2013, the Secretary of the Treasury notified Congress that Treasury had begun using the final extraordinary actions and that these actions would be exhausted no later than October 17, 2013. On October 17, 2013, the Continuing Appropriations Act, 2014 (Public Law No 113-46) was enacted suspending the statutory debt limit through February 7, 2014. On October 17, 2013, in accordance with relevant laws, Fiscal Service restored uninvested principal amounts to the G-Fund, CSRDF, and Postal Benefits Fund in the amounts of $173,948 million, $117,693 million, and $4,601 million, respectively. In accordance with relevant laws, Fiscal Service restored the related interest to the G-Fund on October 18, 2013, in the amount of $653 million, and to CSRDF and Postal Benefits Fund on the next semi-annual interest payment date of December 31, 2013, in the amounts of $539 million and $24 million, respectively. The amounts restored included uninvested principal and related interest that existed as of September 30, 2013, which were appropriately excluded from the Schedule of Federal Debt as of September 30, 2013, since securities had not been issued at that time to the affected federal government accounts.

Appendix I: Management's Report on Internal Control over Financial Reporting Relevant to the Schedule of Federal Debt

DEPARTMENT OF THE TREASURY
WASHINGTON, DC 20239-0001

Management's Report on Internal Control over Financial Reporting
Relevant to the Schedule of Federal Debt

The Bureau of the Fiscal Service's (Fiscal Service) internal control over financial reporting relevant to the Schedule of Federal Debt is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of the Schedule of Federal Debt in accordance with U.S. generally accepted accounting principles; and (2) transactions related to the Schedule of Federal Debt are executed in accordance with laws governing the use of budget authority and with other applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on the Schedule of Federal Debt.

Fiscal Service management is responsible for maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the Schedule of Federal Debt that is free from material misstatement, whether due to fraud or error. Fiscal Service management evaluated the effectiveness of Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2014, based on the criteria established under 31 U.S.C. 3512(c), (d) (commonly known as the Federal Managers' Financial Integrity Act).

Based on that evaluation, we conclude that, as of September 30, 2014, Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt was effective.

Sheryl R. Morrow
Commissioner,
Bureau of the Fiscal Service

Cynthia Z. Springer
Deputy Commissioner,
Fiscal Accounting and Shared Services

Matthew J. Miller
Assistant Commissioner,
Fiscal Accounting Operations

Patricia M. Greiner
Chief Financial Officer and
Assistant Commissioner, Management

Kimberly A. McCoy
Deputy Commissioner, Finance and Administration
Chief Information Officer, and
Assistant Commissioner, Information and Security Services

November 3, 2014

DEPARTMENT OF THE TREASURY

Appendix II: Comments from the Bureau of the Fiscal Service

DEPARTMENT OF THE TREASURY
WASHINGTON, DC 20239-0001

November 4, 2014

Mr. Gary T. Engel
Director, Financial Management and Assurance
Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. Engel:

This letter is in response to your audit of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service for the fiscal years ended September 30, 2014 and 2013. We agree with the conclusions of your audit report.

This year was especially challenging as we were faced with the accounting for two Debt Issuance Suspension Periods (DISPs), the issuance of the new Floating Rate Note, and the implementation of the Summary Debt Accounting System (SDAS). We appreciate the knowledge and experience displayed by your audit team as we continued to encounter unique reporting requirements, while striving to maintain strong internal controls in our new system environment. Your team's experience with our accounting operations allowed for continued accuracy and consistency in our reporting. We would like to thank you and your staff for the thorough audit of these schedules as we finalize the eighteenth year of our professional relationship. We look forward to sustaining a productive and successful relationship with your staff.

Sincerely,

Sheryl R. Morrow
Commissioner
Bureau of the Fiscal Service

DEPARTMENT OF THE TREASURY

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's website (http://www.gao.gov). Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to http://www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on Facebook, Flickr, Twitter, and YouTube. Subscribe to our RSS Feeds or E-mail Updates. Listen to our Podcasts. Visit GAO on the web at www.gao.gov.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Website: http://www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Katherine Siggerud, Managing Director, siggerudk@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548