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**HEADLINE:** FINANCIAL AUDIT-BUREAU OF THE PUBLIC DEBT S FISCAL YEARS 2000 AND 1999 SCHEDULES OF FEDERAL DEBT

**REQUESTOR:** REPORT TO THE SECRETARY OF THE TREASURY

**BYLINE:** DAVID M. WALKER

**BODY:**

March 1, 2001 The Honorable Paul H. O'Neill The Secretary of the Treasury Dear Mr. Secretary: The accompanying auditor's report presents the results of our audits of the Schedules of Federal Debt Managed by the Bureau of the Public Debt for the fiscal years ended September 30, 2000 and 1999. 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 Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Discounts and Premiums managed by the bureau. The auditor's report contains our (1) opinion on the Schedules of Federal Debt for the fiscal years ended September 30, 2000 and 1999, (2) opinion on the effectiveness of related internal control as of September 30, 2000, (3) conclusion on the bureau's compliance in fiscal year 2000 with a selected provision of a significant law we tested, and (4) conclusion on the consistency between information in the Schedules of Federal Debt and the Overview on Federal Debt Managed by the Bureau of the Public Debt. As of September 30, 2000 and 1999, federal debt managed by the bureau totaled about \$ 5,659 billion and \$ 5,641 billion, respectively, for moneys borrowed to fund the government's operations. These balances consisted of approximately (1) \$ 3,439 billion as of September 30, 2000, and \$ 3,668 billion as of September 30, 1999, of debt held by the public and about (2) \$ 2,220 billion as of September 30, 2000, pd \$ 1,973 billion as of September 30, 1999, of intragovernmental holdings. The level of debt held by the public reflects how much of the nation's wealth has been absorbed by the federal government to finance prior federal spending in excess of revenues. It best represents the cumulative effect of past federal borrowing on today's economy and the federal budget. When an actual budget surplus occurs, the annual excess funds are then used to reduce debt held by the public. In other words, actual deficits or surpluses generally approximate the annual net change in the amount of government borrowing from the public. As we recently reported in our Performance and Accountability Series, budget surpluses over the past 3 years have resulted in Treasury reducing debt held by the public. Treasury reducing debt held by the public. Treasury has reduced this debt by redeeming maturing debt, reducing the number of auctions and size of new debt issues, eliminating the 3-year note, conducting buybacks of debt before its maturity date, and redeeming callable securities when the opportunities arose. As a result of Treasury's actions, debt held by the public and managed by the Bureau of the Public Debt, has been reduced by approximately \$ 376 billion since September 30, 1997, with about \$ 229 billion of this decrease occurring in fiscal year 2000. Intragovernmental holdings represent balances of Treasury securities held by individual funds, primarily trust funds, that typically have an obligation to invest their excess annual receipts over disbursements in federal securities.

Most federal trust funds invest in special U.S. Treasury securities that are guaranteed for principal and interest by the full faith and credit of the U.S. government. These securities are nonmarketable, however, they represent a priority call on future budgetary resources. Certain of these trust funds such as the Social Security and federal civilian employee and military retirement trust funds, have been running annual surpluses, which are loaned to the Treasury and reduce the current need for the government to borrow from the public. Primarily as a result of such trust fund surpluses, intragovernmental holdings have increased by approximately \$ 637 billion since September 30, 1997, with about \$ 247 billion of this increase occurring in fiscal year 2000. The transactions relating to the use of the funds surpluses net out on the government's consolidated financial statements because, in effect, they represent loans from one part of the government to another. Importantly, these intragovernmental holdings also constitute future obligations of the Treasury since the Treasury must provide cash to redeem these securities in order for the funds to pay their benefits or other obligations as they come due. When this occurs, the government must fund these redemptions through some combination of reduced future surpluses, if available; lower relative spending for federal programs; higher relative taxes; and/or greater relative borrowing from the public. Debt held by the public and intragovernmental holdings are very different. Debt held by the public approximates the federal government's competition with other sectors in the credit markets. This competition affects current interest rates and private capital accumulation. In addition, interest on debt held by the public is a current burden on taxpayers. In contrast, intragovernmental holdings perform an accounting function but typically do not constitute the government's total future commitment to trust fund financed programs. They primarily represent the cumulative annual surpluses of those trust funds and also reflect future claims on the U.S. Treasury. They do not have the current economic effects of borrowing from the public and do not currently compete with the private sector for available funds in the credit markets. However, when trust funds redeem Treasury securities to obtain cash to fund expenditures, they compete with the private sector and thus have an effect on the economy. Even after 3 years of budgetary surpluses, debt held by the public stands at about \$ 3.4 trillion, or 35 percent of the annual size of the U.S. economy, a level that the United States rarely exceeded before 1940. However, the projected surpluses, if they materialize and depending on how much is saved, could lead to a dramatic reduction in or potential elimination of debt held by the public. Over the longer term, the retirement of the baby boom generation will place significant pressures on the federal budget. These pressures-including, for example, increasing demand for health services-will require reform of existing entitlement programs and/or other policy actions to prevent debt held by the public from dramatically rising again in future decades. We are sending copies of this report to Senator Max Baucus, Senator Robert Byrd, Senator Ben Nighthorse Campbell, Senator Kent Conrad, Senator Pete Domenici, Senator Byron Dorgan, Senator Charles Grassley, Senator Joseph Lieberman, Senator Ted Stevens, Senator Fred Thompson, and to Representative Dan Burton, Representative Stephen Horn, Representative Steny Hoyer, Representative Ernest Istook, Representative Jim Nussle, Representative David Obey, Representative Charles Rangel, Representative Janice Schakowsky, Representative John Spratt, Representative William Thomas, Representative Henry Waxman, and Representative C. W. Bill Young in their capacities as Chairmen, Ranking Members, or Ranking Minority Members of Senate or House Committees and Subcommittees. We are also sending copies of this report to Van Zeck, Commissioner, Bureau of the Public Debt; the Honorable Jeffrey Rush, Jr., Inspector General, Department of the Treasury; the Honorable Jeffrey Rush, Jr., Inspector General, Office of Management and Budget; and other agency officials. Copies will be made available to others upon request. If I can be further assistance, please call me at (202) 512-5500. This report was prepared under the direction of Gary T. Engel, Director, Financial Management and Assurance. Should you or members of your staff have any questions concerning this report, please contact Mr. Engel at (202) 512-3406. Another key contact and staff acknowledgments are in appendix II. Sincerely yours, David M. Walker Comptroller General of the United States To the Commissioner of the Bureau of the Public Debt In connection with fulfilling our requirement to audit the financial statements

of the U.S. government, we audited the Schedules of Federal Debt Managed by the Bureau of the Public Debt (BPD) because of the significance of the federal debt on the federal government's financial statements. This auditor's report presents the results of our audits of the Schedules of Federal Debt Managed by BPD for the fiscal years ended September 30, 2000 and 1999. 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 Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Discounts and Premiums managed by BPD. In our audits of the Schedules of Federal Debt for the fiscal years ended September 30, 2000 and 1999, we found - the Schedules of Federal Debt are presented fairly, in all material respects, in conformity with generally accepted accounting principles; - BPD had effective internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations related to the Schedule of Federal Debt for the fiscal year ended September 30, 2000; and - no reportable noncompliance in fiscal year 2000 with a selected provision of a law we tested. The following sections discuss, in more detail, (1) these conclusions and our conclusion on the Overview on Federal Debt Managed by the Bureau of the Public Debt and (2) the scope of our audits.

**Opinion on Schedules of Federal Debt** The Schedules of Federal Debt including the accompanying notes present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, the balances as of September 30, 2000, 1999, and 1998, for Federal Debt Managed by BPD; the related Accrued Interest Payables and Net Unamortized Discounts and Premiums; and the related increases and decreases for the fiscal years ended September 30, 2000 and 1999.

**Opinion on Internal Control BPD** maintained, in all material respects, effective internal control relevant to the Schedule of Federal Debt related to financial reporting (including safeguarding assets) and compliance with applicable laws and regulations as of September 30, 2000. The internal control provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the Schedule of Federal Debt for the fiscal year ended September 30, 2000, would be prevented or detected on a timely basis. Management asserted that its internal control is effective based on criteria established under 31 U.S.C. 3512 (Federal Managers Financial Integrity Act) and the Office of Management and Budget (OMB) Circular A-123, Management Accountability and Control. We found matters involving computer controls that we do not consider to be reportable conditions. We will communicate these matters to BPD's management, along with our recommendations for improvement, in a separate report to be issued at a later date.

**Compliance With Laws and Regulation** Our tests for compliance in fiscal year 2000 with Statutory Debt Limits, 31 U.S.C. 3101(b), as amended, disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards or OMB audit guidance. However, the objective of our audit of the Schedule of Federal Debt for the fiscal year ended September 30, 2000, was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

**Consistency of Other Information** Information BPD's Overview on Federal Debt Managed by the Bureau of the Public Debt contains information, some of which is not directly related to the Schedules of Federal Debt. We do not express an opinion on this information. However, we compared this information for consistency with the schedules and discussed the methods of measurement and presentation with BPD officials. Based on this limited work, we found no material inconsistencies with the schedules.

**Objectives, Scope, and Methodology** Management is responsible for - preparing the Schedules of Federal Debt in conformity with U.S. generally accepted accounting principles; - establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and - complying with applicable laws and regulations. We are responsible for obtaining reasonable assurance about whether (1) the Schedules of Federal Debt are presented fairly, in all material respects, in conformity with generally accepted accounting principles and (2) management maintained effective related internal control as of September 30, 2000, the objectives of which are the following: - Financial reporting: Transactions are properly recorded, processed, and summarized to permit the preparation of the Schedule of Federal Debt for

the fiscal year ended September 30, 2000, in conformity with generally accepted accounting principles, and assets, as reflected in note 5 to the Schedules of Federal Debt, are safeguarded against loss from unauthorized acquisition, use, or disposition. - Compliance with laws and regulations: Transactions related to the Schedule of Federal Debt for the fiscal year ended September 30, 2000, are executed in accordance with laws governing the use of budget authority and with other laws and regulations that could have a direct and material effect on the Schedules of Federal Debt and any other laws, regulations, and governmentwide policies identified by OMB audit guidance. We are also responsible for testing compliance with selected provisions of laws and regulations that have a direct and material effect on the Schedule of Federal Debt. Further, we are responsible for performing limited procedures with respect to certain other information appearing with the Schedules of Federal Debt. In other to fulfill these responsibilities, we - examined, on a test basis, evidence supporting the amounts and disclosure in the Schedules of Federal Debt Assessed the accounting principles used and significant estimates made by management; evaluated the overall presentation of the Schedules of Federal Debt obtained an understanding of internal control relevant to the Schedule of Federal Debt for the fiscal year ended September 30, 2000, related to financial reporting, (including safeguarding assets as reflected in note 5 to the schedules) and compliance with laws and regulations (including execution of transactions in accordance with budget authority); tested relevant internal controls over financial reporting (including safeguarding assets as reflected in note 5 to the schedules) and compliance, and evaluated the design and operating effectiveness of internal control related to the Schedule of Federal Debt for the fiscal year ended September 30, 2000. Considered the process for evaluating and reporting on internal control and financial management systems under the Federal Managers Financial Integrity Act; and tested compliance in fiscal year 2000 with Statutory Debt Limits, 31 U.S. 3101(b), as amended. We did not evaluate all internal controls relevant to operating objective as broadly described by the Federal Manages Financial Integrity Act, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or on compliance may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become adequate because of changes in conditions or that the degree of compliance with controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate. We did not test compliance with al laws and regulations applicable to BPD. We limited our tests of compliance to selected provisions of laws and regulations that have a direct and material effect on the Schedule of Federal Debt. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes. We performed our work in accordance with U.S. generally accepted government auditing standards and applicable OMB audit guidance. Agency Comments In commenting on a draft of this report, BPD concurred with the facts and conclusions in our report. The comments, are reprinted in appendix I. David M. Walker Comptroller General of the United States January 31, 2001

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