United States Government Accountability Office

GAO

Report to the Secretary of the Treasury

November 2004

FINANCIAL AUDIT

Bureau of the Public Debt's Fiscal Years 2004 and 2003 Schedules of Federal Debt

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Highlights

Highlights of GAO-05-116, a report to the Secretary of the Treasury.

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Why GAO Did This Study

GAO is required to audit the consolidated financial statements of the U.S. government. Due to the significance of the federal debt held by the public to the governmentwide financial statements, GAO has also been auditing the Bureau of the Public Debt's (BPD) Schedules of Federal Debt annually. The audit of these schedules is done to determine whether, in all material respects, (1) the schedules prepared are reliable, (2) BPD management maintained effective internal control relevant to the Schedule of Federal Debt, and (3) BPD complies with selected provisions of significant laws related to the Schedule of Federal Debt.

Federal debt managed by BPD consists of Treasury securities held by the public and by certain federal government accounts, referred to as intragovernmental debt 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 total federal revenues. Intragovernmental debt holdings represent balances of Treasury securities held by federal government accounts, primarily federal trust funds such as Social Security, that typically have an obligation to invest their excess annual receipts over disbursements in federal securities.

www.gao.gov/cgi-bin/getrpt?GAO-05-116.

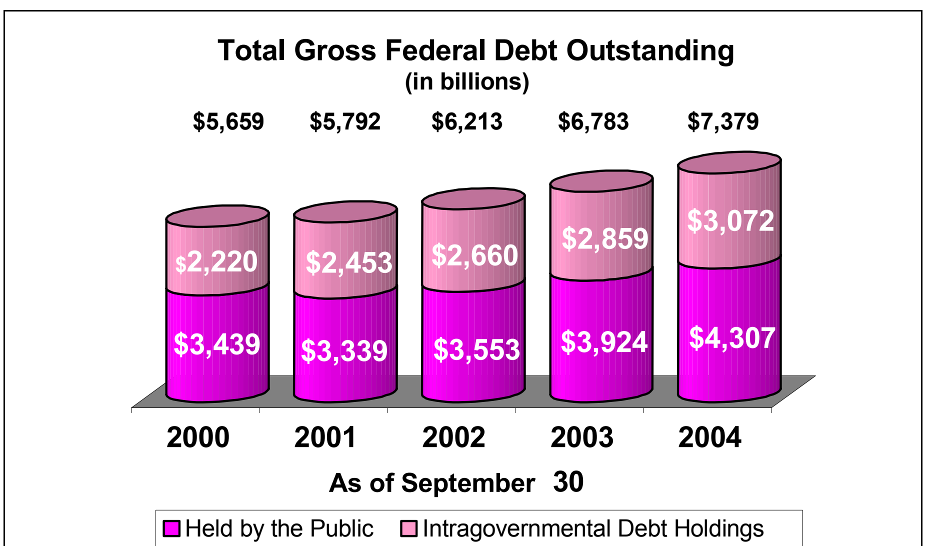
For a fuller understanding of GAO's opinion on BPD's fiscal years 2004 and 2003 Schedules of Federal Debt, readers should refer to the complete audit report, available by clicking the link above, which includes information on audit objectives, scope, and methodology. For more information, contact Gary T. Engel at (202) 512-3406 or engelg@gao.gov.

What GAO Found

In GAO's opinion, BPD's Schedules of Federal Debt for fiscal years 2004 and 2003 were fairly presented in all material respects and BPD maintained effective internal control related to the Schedule of Federal Debt as of September 30, 2004. GAO also found no instances of noncompliance in fiscal year 2004 with the statutory debt limit.

As of September 30, 2004 and 2003, federal debt managed by BPD totaled about $7,379 billion and $6,783 billion, respectively. At the end of fiscal year 2004, debt held by the public as a percentage of the U.S. economy is estimated at 37.5 percent, up from 33.1 percent at the end of fiscal year 2001. Further, certain trust funds (e.g., Social Security) continue to run surpluses, resulting in increased intragovernmental debt holdings. These debt holdings are backed by the full faith and credit of the U.S. government and represent a priority call on future budgetary resources. Gross federal debt has increased 27 percent between the end of fiscal years 2001 and 2004. As a result of the increasing federal debt, on October 14, 2004, Treasury entered into a debt issuance suspension period to avoid exceeding the current $7,384 billion statutory debt limit and requested the Congress take action to raise the debt limit by mid-November 2004.

As shown below, total federal debt increased over each of the last 4 fiscal years. Debt held by the public decreased as a result of cash surpluses for fiscal year 2001, but increased during fiscal years 2002 through 2004, with the return of annual unified budget deficits. Intragovernmental debt holdings steadily increased during this 4-year period primarily due to excess receipts over disbursements in federal trust funds.



Source: BPD.

Contents

Abbreviations

BPD	Bureau of the Public Debt
OMB	Office of Management and Budget
TIPS	Treasury Inflation-Protected Security

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Comptroller General of the United States

United States Government Accountability Office
Washington, D.C. 20548

November 5, 2004

The Honorable John W. Snow
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, 2004 and 2003. 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 bureau.[1]

The auditor's report contains our (1) opinion on the Schedules of Federal Debt for the fiscal years ended September 30, 2004 and 2003, (2) opinion on the effectiveness of related internal control as of September 30, 2004, (3) conclusion on the bureau's compliance in fiscal year 2004 with a selected provision of a 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, 2004 and 2003, federal debt managed by the bureau totaled about $7,379 billion and $6,783 billion, respectively, for moneys borrowed to fund the government's operations. As shown on the Schedules of Federal Debt, these balances consisted of approximately (1) $4,307 billion as of September 30, 2004, and $3,924 billion as of September 30, 2003, of debt held by the public and about (2) $3,072 billion as of September 30, 2004, and $2,859 billion as of September 30, 2003, of intragovernmental debt 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 total federal revenues. It best represents the cumulative effect of past federal borrowing on today's economy and the federal budget. To finance a cash deficit, the government borrows from the

[1]Intragovernmental Debt Holdings represent federal debt issued by Treasury and held by certain federal government accounts, such as the Social Security and Medicare trust funds.

public. When a cash surplus occurs, the annual excess funds can then be used to reduce debt held by the public. In other words, cash deficits or surpluses generally approximate the annual net change in the amount of government borrowing from the public.

Cash surpluses during fiscal years 1998 through 2001 enabled Treasury to reduce debt held by the public by $476 billion, from $3,815 billion as of September 30, 1997, to $3,339 billion as of September 30, 2001. Treasury reduced this debt by redeeming maturing debt, reducing the number of auctions and size of new debt issues, conducting "buybacks" of debt before its maturity date, and redeeming callable securities when the opportunities arose.[2] However, because of the return to deficits, in fiscal years 2002 through 2004, debt held by the public increased by $968 billion, with about $383 billion of this increase occurring in fiscal year 2004. Treasury issued more debt by increasing the number of auctions and the size of new debt issues. During fiscal year 2003, Treasury reintroduced the 3-year note, which will be offered every quarter. In addition, Treasury increased the offerings of the 5-year note from quarterly to monthly offerings; the 10-year note from an offering every quarter to eight offerings a year; and the 10-year Treasury Inflation-Protected Security (TIPS) from three offerings a year to an offering every quarter. During fiscal year 2004, Treasury introduced a 20-year TIPS, first issued on July 30, 2004, and a 5-year TIPS, first issued on October 29, 2004. Both securities will be offered semiannually. Notwithstanding the increases in fiscal years 2002 through 2004, debt held by the public as a percentage of total federal debt has decreased from approximately 71 percent as of September 30, 1997, to approximately 58 percent as of September 30, 2004.

Intragovernmental debt holdings represent balances of Treasury securities held by federal government accounts, primarily federal 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 retirement trust funds, have been

[2]During this period, Treasury eliminated the 3-year note and the 52-week bill. On October 31, 2001, Treasury suspended issuance of the 30-year bond.

running cash surpluses, which are loaned to the Treasury and reduce the current need for the government to borrow from the public in order to finance current operations. As a result of total trust fund surpluses, intragovernmental debt holdings have increased by approximately $1,489 billion during fiscal years 1998 through 2004, from $1,583 billion as of September 30, 1997, to $3,072 billion as of September 30, 2004, with about $213 billion of this increase occurring in fiscal year 2004. Intragovernmental debt holdings as a percentage of total federal debt have increased from approximately 29 percent as of September 30, 1997, to approximately 42 percent as of September 30, 2004.

The transactions relating to the use of the federal government accounts' 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 debt holdings also constitute future obligations of the Treasury since the Treasury must provide cash to redeem these securities in order for the individual accounts to pay their benefits or other obligations as they come due. When this occurs, if sufficient cash surpluses are not available to redeem the securities, the government would either need to increase borrowing from the public, raise future taxes, reduce future spending, retire less debt (if the budget as a whole is in surplus), or some combination thereof.

While both are important, debt held by the public and intragovernmental debt holdings are very different. Debt held by the public approximates the federal government's competition with other sectors in the credit markets. Federal borrowing absorbs resources available for private investment and may put upward pressure on interest rates. In addition, interest on debt held by the public is paid in cash and represents a burden on current taxpayers. It reflects the amount the government pays to its outside creditors. In contrast, intragovernmental debt holdings perform an accounting function but typically do not require cash payments from the current budget or represent a burden on the current economy. In addition, from the perspective of the budget as a whole, interest payments to federal government accounts by the Treasury are entirely offset by the income received by such accounts—in effect, one part of the government pays the interest and another part receives it. This intragovernmental debt and the interest on it represents a claim on future resources and hence a burden on future taxpayers and the future economy when it has to be redeemed to meet obligations under the respective programs. However, these intragovernmental debt holdings do not fully reflect the government's total future commitment to trust fund financed programs. They primarily represent the cumulative historical surpluses of those trust funds and also reflect future priority 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, and Treasury borrows from the public to finance these redemptions, there is competition with the private sector and thus an effect on the economy.

During fiscal year 2003, Treasury faced the challenge of managing the debt within the statutory debt limit. On February 20, 2003, Treasury entered into a debt issuance suspension period. A debt issuance suspension period is any period for which the Secretary of the Treasury has determined that obligations of the United States may not be issued without exceeding the debt limit.[3] Actions taken by Treasury, which were consistent with legal authorities provided to the Secretary, included suspending investment of receipts of the Government Securities Investment Fund (G-Fund) of the federal employees' Thrift Savings Plan, the Civil Service Retirement and Disability Trust Fund (Civil Service fund), and the Exchange Stabilization Fund; redeeming Civil Service fund securities early; suspending the sales of State and Local Government Series nonmarketable Treasury securities; exchanging Treasury securities for Federal Financing Bank securities; and recalling compensating balances held at some commercial banks. In addition, because the debt subject to the limit was so close to the ceiling during this period, Treasury turned to issuing bills with maturity dates of 14 days or less to manage short-term financing needs. On May 27, 2003, legislation was enacted to raise the statutory debt limit by $984 billion to $7,384 billion. Subsequently, Treasury restored all losses to the G-Fund and Civil Service fund in accordance with legal authorities provided to the Secretary of the Treasury.[4] On October 14, 2004, Treasury again determined that a debt issuance suspension period was in effect. So far during the period, Treasury has suspended investment of receipts of the G-Fund and sales of State and Local Government Series nonmarketable Treasury securities to avoid exceeding the debt limit. The Secretary of the Treasury has requested that the Congress take action to raise the debt limit by mid-

[3]5 U.S.C. §§ 8348(j)(5)(B), 8438(g)(6)(B).

[4]In May 2004, we reported on the results of our review of the actions taken and the policies and procedures Treasury implemented during the 2003 debt issuance suspension period. See GAO, *Debt Ceiling: Analysis of Actions Taken during the 2003 Debt Issuance Suspension Period*, GAO-04-526 (Washington, D.C.: May 20, 2004).

November 2004. As of October 25, 2004, the statutory debt limit remains at $7,384 billion.[5]

During our audits, we have noted certain trends—the increase in the amount of Treasury securities held by foreign and international investors and the increased costs to finance the federal government's growing debt. Foreign and international investors are a major holder of debt held by the public. According to amounts reported in the September 2004 *Treasury Bulletin*, Treasury estimates that the amount of Treasury securities held by foreign and international investors has increased by $624 billion, from about $1,135 billion as of June 30, 2002, to $1,759 billion as of June 30, 2004, or an estimated 42 percent of total debt held by the public as of that date. During the same 2-year period, debt held by the public increased by $755 billion, from about $3,464 billion to $4,219 billion. Based on amounts reported in the September 2004 *Treasury Bulletin*, the estimated increase in holdings by foreign and international investors represents about 83 percent of the increase in debt held by the public over the same period. The United States benefits from foreign purchases of Treasury securities because foreign investors fill part of our borrowing needs. However, to service this foreign-held debt, the U.S. government must send interest payments abroad, which adds to the incomes of residents of other countries rather than to the incomes of U.S. residents. In addition, this increasing reliance on foreign investors to finance the deficits of the U.S. government presents a potential risk to the U.S. economy, especially since the U.S. gross national saving rate is low by U.S. historical standards and averages well below that of other major industrialized nations.

Rising interest rates on Treasury securities—although relatively low by historical standards—are contributing to an increased cost to finance the federal government's growing debt. During fiscal year 2004, the interest rate for 13-week Treasury bills increased from a low of 0.87 percent to 1.71 percent as of September 30, 2004. Also, the interest rate on 2-year Treasury notes increased from a low of 1.50 percent to 2.50 percent during this same period. About $2,040 billion, or 47 percent, of Treasury securities held by the public as of September 30, 2004, will mature at least once during the next 2 years. The Congressional Budget Office projects that interest rates on Treasury securities, especially short-term rates, will continue to increase. As such, as the Treasury securities mature over the next 2 years

[5]31 U.S.C. § 3101(b), as amended by Pub. L. No. 107-199, § 1, 116 Stat. 734 (2002) and Pub. L. No. 108-24, 117 Stat. 710 (2003).

and are replaced by new debt, the interest rates on the majority of the new issuances will likely be higher than the September 30, 2004, rates and result in continued increased cost to finance the federal government's debt. Thus, the combined effect of greater levels of debt and higher interest rates will likely place increasing pressure on the federal budget in the years ahead.

The challenge of managing the federal debt is not likely to diminish any time soon. Debt held by the public has continued to grow relative to the economy. At the end of fiscal year 2004, debt held by the public as a share of gross domestic product (GDP) is estimated at 37.5 percent, up from 33.1 percent at the end of fiscal year 2001. In addition, gross federal debt has increased 27 percent during the same period, from $5,792 billion as of September 30, 2001, to $7,379 billion as of September 30, 2004. While growth in the debt held by the public-to-GDP measure does not necessarily create problems in the short term, continued growth in the long term would reduce budgetary flexibility and ultimately lead to an unsustainable fiscal path.

Indeed, GAO's fiscal policy simulations show that over the long term, debt held by the public will rise to unprecedented levels as a share of GDP. These simulations illustrate that the fiscal policies in place today—absent substantive entitlement reform or dramatic changes in tax and spending policies—will result in large, escalating, and persistent deficits that are economically unsustainable over the long term. Without reform, known demographic trends; escalating health care costs; and projected growth in federal spending for Social Security, Medicare, and Medicaid will result in massive fiscal pressures that will hobble the economy. Budget controls instituted to achieve balance in the past have expired, and no agreement has been reached on the appropriate structure or process for focusing on the large and growing fiscal challenges that now face the federal government.

As discussed earlier, federal debt managed by the bureau totaled about $7.4 trillion at the end of the fiscal year, or about $25,000 for every man, woman, and child in this country today. But that number excludes many items, including the gap between promised and funded Social Security and Medicare benefits, veterans' health care, and a range of other commitments and contingencies that the federal government has pledged to support. If these items are factored in, the total burden in current dollars is at least $42 trillion. One of the biggest contributors to this total bill is the new Medicare prescription drug benefit, whose estimated current-dollar cost over the next 75 years is more than $8 trillion. Stated differently, the current total burden for every American is more than $140,000—and every day that burden becomes larger. Our long-term budget simulations show that by 2040, the federal government may have to either cut federal spending by 60 percent or raise taxes to about 2.5 times today's level to pay for the mounting cost of the federal government's current unfunded commitments. Either option would be devastating to the economy and the future standard of living for Americans.

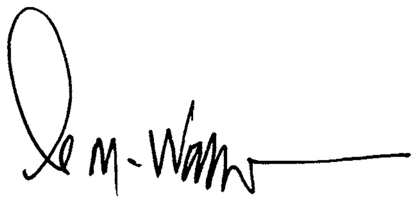
A top-to-bottom review of government activities to ensure their relevance and fit for the 21st century and their relative priority is long overdue. As we have spoken about in the past, the federal government needs a three-pronged approach to (1) restructure existing entitlement programs; (2) reexamine the base of discretionary and other spending; and (3) review and revise the federal government's tax policy, including major tax preferences, and enforcement programs. In addition, new accounting and reporting approaches, budget control mechanisms, and metrics are needed for considering and measuring the impact of spending and tax policies and decisions over the long term.

We are sending copies of this report to the Chairmen and Ranking Minority Members of the Senate Committee on Appropriations; the Senate Committee on Governmental Affairs; the Senate Committee on the Budget; the Subcommittee on Transportation, Treasury, and General Government, Senate Committee on Appropriations; the House Committee on Appropriations; the House Committee on Government Reform; the House Committee on the Budget; the Subcommittee on Transportation, Treasury, and Independent Agencies, House Committee on Appropriations; and the Subcommittee on Government Efficiency and Financial Management, House Committee on Government Reform. We are also sending copies of this report to the Commissioner of the Bureau of the Public Debt, the Inspector General of the Department of the Treasury, the Director of the Office of Management and Budget, and other agency officials. In addition, the report will be available at no charge on the GAO Web site at http://www.gao.gov.

If I can be of 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 or engelg@gao.gov. Another key contact and staff acknowledgments are provided in appendix II.

Sincerely yours,



David M. Walker
Comptroller General
of the United States

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Comptroller General
of the United States

United States Government Accountability Office
Washington, D.C. 20548

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,[1] we audited the Schedules of Federal Debt Managed by the Bureau of the Public Debt (BPD) because of the significance of the federal debt to 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, 2004 and 2003. 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 BPD.[2]

In our audits of the Schedules of Federal Debt for the fiscal years ended September 30, 2004 and 2003, we found the following:

- the Schedules of Federal Debt are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- BPD had effective internal control over financial reporting and compliance with laws and regulations related to the Schedule of Federal Debt as of September 30, 2004; and
- no reportable noncompliance in fiscal year 2004 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.

[1] 31 U.S.C. § 331(e).

[2] Intragovernmental Debt Holdings represent federal debt issued by Treasury and held by certain federal government accounts, such as the Social Security and Medicare trust funds.

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, 2004, 2003, and 2002, for Federal Debt Managed by BPD; the related Accrued Interest Payables and Net Unamortized Premiums and Discounts; and the related increases and decreases for the fiscal years ended September 30, 2004 and 2003.

Opinion on Internal Control

BPD maintained, in all material respects, effective internal control relevant to the Schedule of Federal Debt related to financial reporting and compliance with applicable laws and regulations as of September 30, 2004, that provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the Schedule of Federal Debt would be prevented or detected on a timely basis. Our opinion is based on criteria established under 31 U.S.C. § 3512 (c), (d) (commonly referred to as the Federal Managers' Financial Integrity Act) and the Office of Management and Budget (OMB) Circular A-123, revised June 21, 1995, *Management Accountability and Control.*

We found matters involving information security controls that we do not consider to be reportable conditions.[3] We will communicate these matters to BPD's management, along with our recommendations for improvement, in a separate letter to be issued at a later date.

Compliance with Laws and Regulations

Our tests for compliance in fiscal year 2004 with the statutory debt limit 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, 2004, was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

[3]Reportable conditions are matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operation of internal control, which could adversely affect the organization's ability to meet the internal control objectives described in the Objectives, Scope, and Methodology section of this report.

Consistency of Other 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 the following:

- 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 U.S. generally accepted accounting principles and (2) management maintained effective related internal control as of September 30, 2004, 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, 2004, in conformity with U.S. generally accepted accounting principles.
- Compliance with laws and regulations: Transactions related to the Schedule of Federal Debt for the fiscal year ended September 30, 2004, 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 Schedule of Federal Debt.

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 order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the Schedules of Federal Debt;
- assessed the accounting principles used and any 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 as of September 30, 2004, related to financial reporting and compliance with laws and regulations (including execution of transactions in accordance with budget authority);
- tested relevant internal controls over financial reporting and compliance, and evaluated the design and operating effectiveness of internal control related to the Schedule of Federal Debt as of September 30, 2004;
- 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 2004 with the statutory debt limit (31 U.S.C. § 3101(b), as amended by Pub. L. No. 107-199, § 1, 116 Stat. 734 (2002) and Pub. L. No. 108-24, 117 Stat. 710 (2003)).

We did not evaluate all internal controls relevant to operating objectives as broadly described by the Federal Managers' 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 noncompliance 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 inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate.

We did not test compliance with all laws and regulations applicable to BPD. We limited our tests of compliance to a selected provision of a law that has a direct and material effect on the Schedule of Federal Debt for the fiscal year ended September 30, 2004. 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

October 25, 2004

Overview, Schedules, and Notes

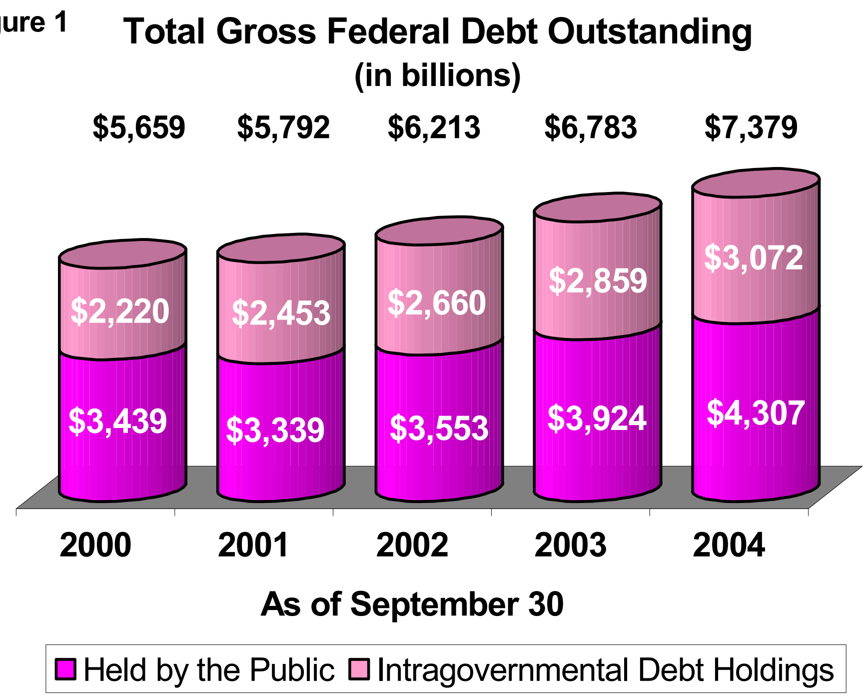
Overview on Federal Debt Managed by the Bureau of the Public Debt

Overview on Federal Debt Managed by the Bureau of the Public Debt

Gross Federal Debt Outstanding[1]

Federal debt managed by the Bureau of the Public Debt comprises debt held by the public and debt held by certain federal government accounts, the latter of which is referred to as intragovernmental debt holdings. As of September 30, 2004 and 2003, outstanding gross federal debt managed by the bureau totaled $7,379 and $6,783 billion, respectively. The increase in gross federal debt of $596 billion during fiscal year 2004 was due to an increase in gross intragovernmental debt holdings of $213 billion and an increase in gross debt held by the public of $383 billion. As Figure 1 illustrates, intragovernmental debt holdings have steadily increased since fiscal year 2000 and debt held by the public decreased in fiscal year 2001, but increased in fiscal years 2002 through 2004. The primary reason for the increases in intragovernmental debt holdings is the annual surpluses in the Federal Old-Age and Survivors Insurance Trust Fund, Civil Service Retirement and Disability Trust Fund, Federal Hospital Insurance Trust Fund, Federal Disability Insurance Trust Fund, and Military Retirement Fund. The fiscal years 2002 through 2004 increases in debt held by the public are due primarily to total federal spending exceeding total federal revenues. As of September 30, 2004, gross debt held by the public totaled $4,307 billion and gross intragovernmental debt holdings totaled $3,072 billion.

Figure 1

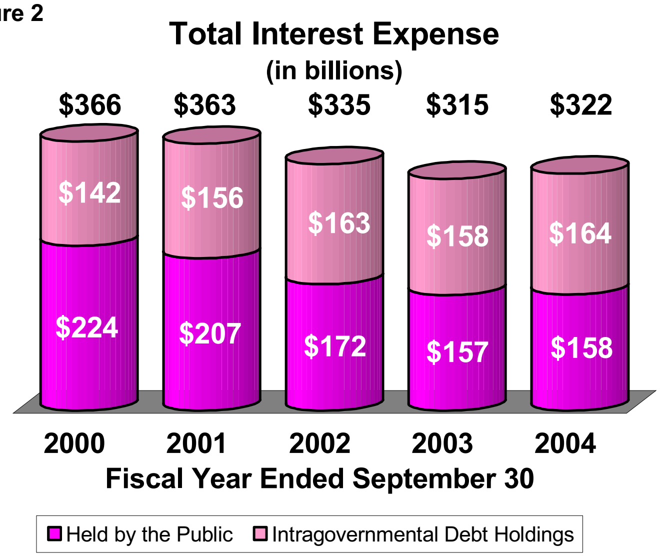


[1] Federal debt outstanding reported here differs from the amount reported in the Financial Report of the United States Government because of the securities not maintained or reported by the bureau and which are issued by the Federal Financing Bank and other federal government agencies.

Interest Expense

Interest expense incurred during fiscal year 2004 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 in 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. During fiscal year 2004, interest expense incurred totaled $322 billion, interest expense on debt held by the public was $158 billion, and $164 billion was interest incurred for intragovernmental debt holdings. As Figure 2 illustrates, total interest expense decreased each year from fiscal year 2001 through 2003, but increased in fiscal year 2004. Average interest rates on principal balances outstanding as of fiscal year end are disclosed in the Notes to the Schedules of Federal Debt.

Figure 2



Debt Held by the Public

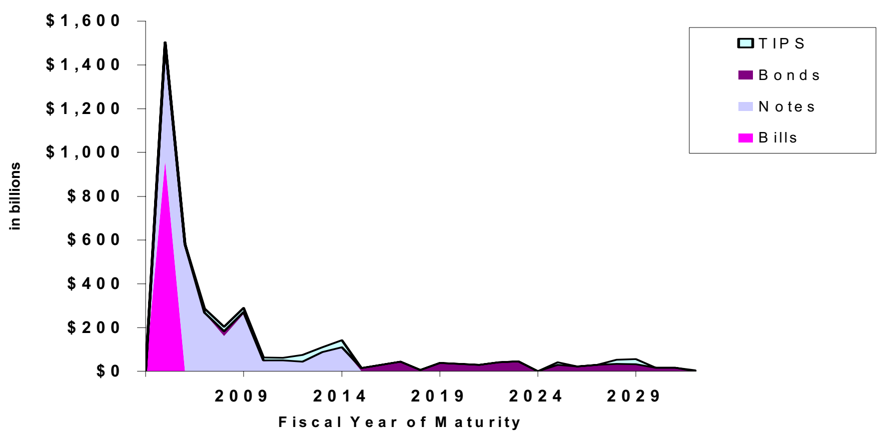
Debt held by the public reflects how much of the nation's wealth has been absorbed by the federal government to finance prior federal spending in excess of total federal revenues. As of September 30, 2004 and 2003, gross debt held by the public totaled $4,307 billion and $3,924 billion, respectively (see Figure 1), an increase of $383 billion. The borrowings and repayments of debt held by the public increased from fiscal year 2003 to 2004 primarily due to Treasury's decision to finance current operations using more short-term securities.

As of September 30, 2004, $3,846 billion, or 89 percent, of the securities that constitute debt held by the public were marketable, meaning that once the government issues them, they can be resold by whoever owns them. Marketable debt is made up of Treasury bills, Treasury notes, Treasury bonds, and Treasury Inflation-Protected Securities (TIPS)[2] 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, 2004, $2,576 billion or 67 percent will mature within the next 4 years (see Figure 3). As of September 30, 2004 and 2003, notes and TIPS held by the public maturing within the next 10 years totaled $2,274 billion and $1,919 billion, respectively, an increase of $355 billion.

The government also issues to the public, state and local governments, and foreign governments and central banks nonmarketable securities, which cannot be resold, and have maturity dates from on demand to more than 10 years. As of September 30, 2004, nonmarketable securities totaled $461 billion, or 11 percent of debt held by the public. As of that date, nonmarketable securities primarily consisted of savings securities totaling $204 billion and special securities for state and local governments totaling $158 billion.

Figure 3

Maturity Dates[3] of Marketable Debt Held by the Public as of September 30, 2004



[2] TIPS were previously included with Notes and Bonds.
[3] Callable securities mature between fiscal years 2010 and 2015, but are reported by their call date.

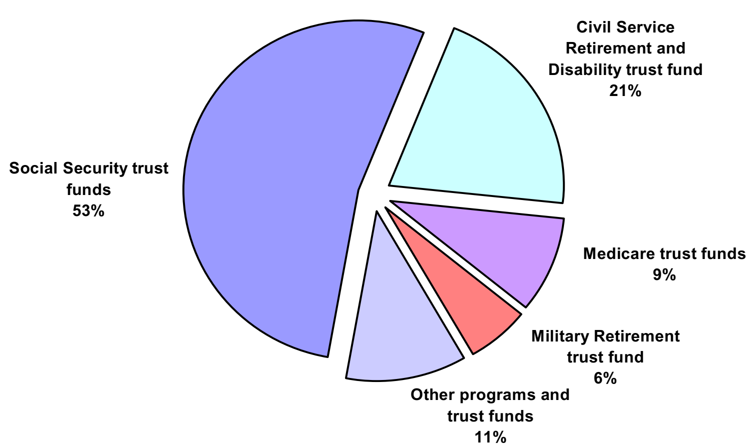
Intragovernmental Debt Holdings

Intragovernmental debt holdings represent balances of Treasury securities held by over 200 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 Civil Service Retirement and Disability trust funds.[4] As of September 30, 2004, such funds accounted for $2,726 billion, or 89 percent, of the $3,072 billion intragovernmental debt holdings balances (see Figure 4). As of September 30, 2004 and 2003, gross intragovernmental debt holdings totaled $3,072 billion and $2,859 billion, respectively (see Figure 1), an increase of $213 billion.

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, 2004



4 The Social Security trust funds consist of the Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund. In addition, the Medicare trust funds are made up of the Federal Hospital Insurance Trust Fund and the Federal Supplementary Medical Insurance Trust Fund.

Significant Events in FY 2004

Increased Issuance of Treasury Inflation-Protected Securities (TIPS)

During fiscal year 2004, Treasury increased the issuances of inflation-indexed securities known as Treasury Inflation-Protected Securities (TIPS). In the May 5, 2004, Quarterly Refunding Statement, Treasury introduced both a 5-year TIPS and a 20-year TIPS. Each security will be issued semiannually with the 5-year TIPS issued in April and October and the 20-year TIPS issued in January and July. A 10-year TIPS will continue to be issued in January, April, July and October. The first 20-year TIPS was issued on July 30, 2004, in the amount of $11 billion and will be reopened in January 2005 and July 2005. Similarly, the 5-year TIPS will be issued in late October 2004, and will be reissued in April 2005 and October 2005.

Treasury System Changes

In the February 2004 Quarterly Refunding Statement, Treasury announced its intentions to compute price awards in auctions to six decimal places per hundred. Calculating prices to six decimals ensures price uniqueness for all discount rates or yields bid in all marketable Treasury securities auctions. This change also makes Treasury's pricing practice consistent with secondary market practices. In addition, the August 2004 Quarterly Refunding Statement announced that the limit on non-competitive Treasury auction awards will be $5 million for all auctions. The previous limit on non-competitive awards, in effect since 1991, was $1 million for bill auctions and $5 million for coupon auctions. These changes were effective on September 20, 2004.

Uniform Offering Circular Rewritten

The Uniform Offering Circular (UOC), in conjunction with the announcement for each auction, provides the terms and conditions for the auction and issuance of marketable Treasury securities to the public. Treasury has rewritten the UOC in plain language because the wide variety of bidders in our securities auctions – broker-dealers, depository institutions, non-financial firms, individuals, etc. – have widely different levels of experience in dealing with federal regulations in general and with securities-related concepts and regulations in particular. On July 28, 2004, the rewritten UOC was published in the Federal Register. Treasury believes that a better understanding of the auction rules may increase direct participation in our auctions and improve the auction process overall, resulting in lower borrowing costs.

Significant Events in FY 2004, cont.

Series HH Savings Bonds Discontinued

As announced on February 18, 2004, the final Series HH Savings Bonds were issued to the public on August 31, 2004. These bonds are current-income securities that pay interest to their owners semiannually. Series HH Savings Bonds issued through August 2004 will continue to earn interest until they reach final maturity 20 years after issue. Treasury withdrew the offering of HH bonds due to the high cost in relation to the relatively small value of transactions. These bonds were initially issued in 1980 and were available in exchange for Series E or EE Savings Bonds. After August 31, 2004, holders of eligible E and/or EE bonds may choose to accept the proceeds of maturing issues or invest them in marketable bills, notes, or TIPS at auction, or they may choose to purchase Series EE or I Savings Bonds.

EasySaver Program To Be Discontinued

EasySaver was introduced in November 1998 to encourage savings and broaden access to Treasury securities. Customers enrolled in EasySaver could buy U.S. Savings Bonds through authorized debits to their bank accounts thus allowing employees of smaller businesses to have access to a regular savings plan like the millions of Americans who buy bonds through payroll savings plans at work. Since some of the same EasySaver features and even more features are available in TreasuryDirect (www.treasurydirect.gov), the Bureau of the Public Debt stopped accepting EasySaver enrollments on December 31, 2003. All existing automatic EasySaver debits will be discontinued in March 2005. Customers are encouraged to enroll in TreasuryDirect to buy, manage, and redeem their securities online.

TreasuryDirect

TreasuryDirect represents a direct relationship between customers — individuals and financial professionals alike — and the U.S. Treasury. The TreasuryDirect website (www.treasurydirect.gov) provides complete information for people who want to buy securities directly from the Treasury — in a way that's easy for everyone to understand. Electronic purchasers can use TreasuryDirect to schedule electronic Series EE and I Savings Bond purchases. TreasuryDirect enhanced its Internet website capability during fiscal year 2004. One new feature offered is a payroll deduction option to purchase a Zero-Percent Certificate of Indebtedness (C of I). While these securities do not earn any interest, they can be used as a source of funds to purchase savings bonds within a TreasuryDirect account after accumulating a minimum of $25 in the C of I or by scheduling a purchase in advance. Customers may purchase electronic Series EE and I Savings Bonds ranging in value from $25 - $30,000 in increments as low as $0.01. There is a $30,000 annual limit per series per person. Customers may redeem a bond one year after purchase, or hold the bond to maturity.

Significant Events in FY 2004, cont.

Depositary Compensation Securities Redeemed, Replaced By Appropriation

In July 2003, Treasury began issuing Depositary Compensation Securities (DCS), a non-marketable security, to compensate those financial institutions serving as financial agents of the United States for essential banking services provided to the Government. These securities were issued to financial agents in an amount sufficient to generate interest payments equal to the monthly expenses for financial agent services provided to Treasury. As part of the fiscal year 2004 Treasury appropriation, a permanent and indefinite appropriation was enacted to reimburse financial institutions serving as financial agents for the United States. As a result, more than $16 billion of DCS were called on February 29, 2004.

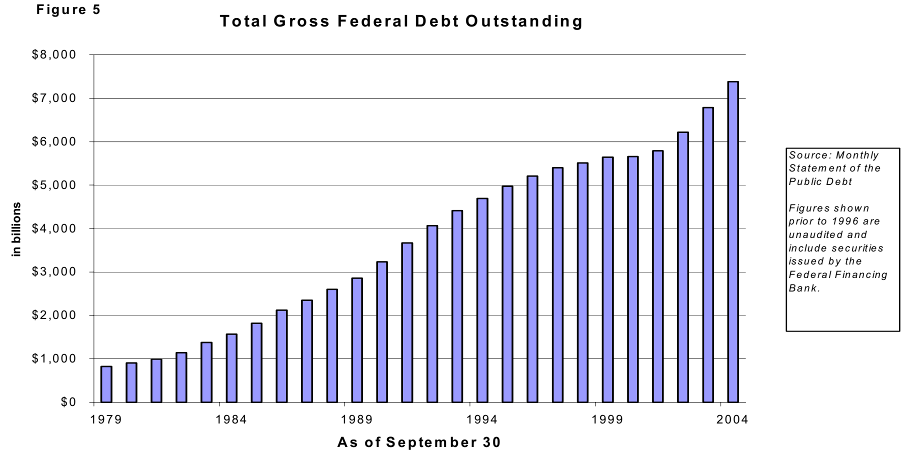
Statutory Debt Limit Being Evaluated

As a consequence of the changes in the government's financing needs, resulting in part from the current economic environment, Treasury Secretary John Snow urged the Congress on August 2, 2004, to raise the debt limit. Delays in raising the current debt limit of $7,384 billion have forced Treasury to enter into a debt issuance suspension period (DISP) that involves Treasury's departure from its normal investment and redemption procedures for certain federal government accounts. Consistent with legal authorities available to the Secretary, on October 14, 2004, Treasury suspended sales of State and Local Government series (SLGS) nonmarketable securities and was unable to fully invest contributions in the Government Securities Investment Fund (G-Fund) of the federal employee 401(k) retirement plan.

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' excess receipts, primarily trust funds. Total gross federal debt outstanding has dramatically increased over the past 25 years from $827 billion as of September 30, 1979 to $7,379 billion as of September 30, 2004 (see Figure 5). Large budget deficits emerged during the 1980'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 rapid pace. As a result, total federal debt increased more than five fold between 1980 and 1997.

Figure 5



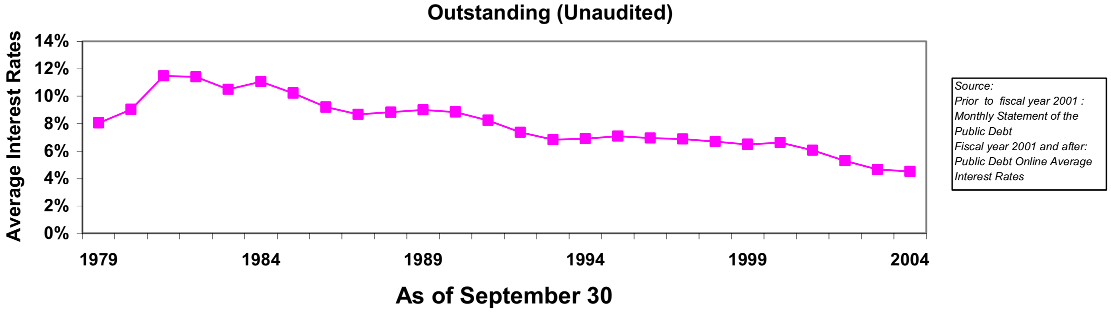
Historical Perspective, cont.

However, 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. As a consequence of the changes in the federal government's financing needs, resulting from increased federal outlays, tax policy decisions, and the deterioration of overall economic performance, from fiscal year 2001 to 2004 debt held by the public rose by $968 billion, from $3,339 billion to $4,307 billion. 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 $852 billion, from $2,220 billion as of September 30, 2000, to $3,072 billion as of September 30, 2004. By law, trust funds have the authority or are required to invest surpluses 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 securities outstanding at the end of the fiscal year.

Figure 6

Average Interest Rates of Federal Debt Outstanding (Unaudited)



Schedules of Federal Debt

Schedules of Federal Debt

Managed by the Bureau of the Public Debt
For the Fiscal Years Ended September 30, 2004 and 2003
(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, 2002	***3,553,180***	***32,874***	***(39,945)***	***2,660,056***	***41,076***	***2,757***
Increases						
Borrowings from the Public	4,299,022		(10,362)			
Net Increase in Intragovernmental Debt Holdings				199,174		3,601
Accrued Interest (Note 4)		143,335			164,379	
Total Increases	**4,299,022**	**143,335**	**(10,362)**	**199,174**	**164,379**	**3,601**
Decreases						
Repayments of Debt Held by the Public	3,928,112					
Interest Paid		144,399			164,701	
Net Amortization (Note 4)			(13,461)			6,670
Total Decreases	**3,928,112**	**144,399**	**(13,461)**	**0**	**164,701**	**6,670**
Balance as of September 30, 2003	***3,924,090***	***31,810***	***(36,846)***	***2,859,230***	***40,754***	***(312)***
Increases						
Borrowings from the Public	4,775,523		(10,667)			
Net Increase in Intragovernmental Debt Holdings				212,478		3,440
Accrued Interest (Note 4)		145,585			167,855	
Total Increases	**4,775,523**	**145,585**	**(10,667)**	**212,478**	**167,855**	**3,440**
Decreases						
Repayments of Debt Held by the Public	4,392,268					
Interest Paid		144,660			166,346	
Net Amortization (Note 4)			(12,735)			3,717
Total Decreases	**4,392,268**	**144,660**	**(12,735)**	**0**	**166,346**	**3,717**
Balance as of September 30, 2004	***$4,307,345***	***$32,735***	***($34,778)***	***$3,071,708***	***$42,263***	***($589)***

The accompanying notes are an integral part of these schedules.

Notes to the Schedules of Federal Debt

Notes to the Schedules of Federal Debt Managed by the Bureau of the Public Debt

For the Fiscal Years Ended September 30, 2004 and 2003

(Dollars in Millions)

Note 1. Significant Accounting Policies

Basis of Presentation

The Schedules of Federal Debt Managed by the Bureau of the Public Debt (BPD) have been prepared to report fiscal year 2004 and 2003 balances and activity relating to monies borrowed from the public and certain federal government accounts to fund the U.S. government's operations. 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.C. authorizes Treasury to prescribe the debt instruments and otherwise limit and restrict the amount and composition of the debt. BPD, an organizational entity within the Fiscal Service of 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, BPD has been given the responsibility to issue Treasury securities to trust funds for trust fund receipts not needed for current benefits and expenses. BPD issues and redeems Treasury securities for the trust funds based on data provided by program agencies and other Treasury entities.

Basis of Accounting

The schedules were prepared in conformity with U.S. generally accepted accounting principles and from BPD's automated accounting system, Public Debt Accounting and Reporting System. 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 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 Public Debt

For the Fiscal Years Ended September 30, 2004 and 2003

(Dollars in Millions)

Note 2. Federal Debt Held by the Public

As of September 30, 2004 and 2003, Federal Debt Held by the Public consisted of the following:

	2004		2003	
	Amount	Average Interest Rates	Amount	Average Interest Rates
Marketable:				
Treasury Bills	$961,449	1.6%	$918,196	1.0%
Treasury Notes	2,109,494	3.5%	1,799,424	3.8%
Treasury Bonds	551,904	8.0%	576,590	8.2%
TIPS	223,008	2.8%	166,120	3.2%
Total Marketable	$3,845,855		$3,460,330	
Nonmarketable	$461,490	5.1%	$463,760	5.3%
Total Federal Debt Held by the Public	$4,307,345		$3,924,090	

Treasury issues marketable bills at a discount 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, 2004 and 2003, respectively. 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, 2004 and 2003. 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, which are tied to the Consumer Price Index, the leading measurement of inflation. TIPS are issued with a term of more than 5 years. 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. Inflation-indexed securities, TIPS, were previously included with Treasury notes and bonds. The fiscal year 2003 amounts and average interest rates have been reclassified to conform with the presentation adopted in fiscal year 2004.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Public Debt

For the Fiscal Years Ended September 30, 2004 and 2003

(Dollars in Millions)

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

As of September 30, 2004, nonmarketable securities primarily consisted of $204,246 million in U.S. Savings Securities, $158,214 million in securities issued to State and Local Governments, $5,881 million in Foreign Series Securities, and $29,995 million in Domestic Series Securities. As of September 30, 2003, nonmarketable securities primarily consisted of $201,606 million in U.S. Savings Securities, $148,366 million in securities issued to State and Local Governments, $11,007 million in Foreign Series Securities, $29,995 million in Domestic Series Securities, and $14,991 million in Depositary Compensation Securities. 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, 2004 and 2003. Nonmarketable securities are issued with a term of on demand to more than 10 years.

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 amounts borrowed from the fund during fiscal years 2004 and 2003 are included in the respective Borrowings from the Public amounts reported on the Schedules of Federal Debt.

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. The FRB owned $698 billion and $654 billion of Federal Debt Held by the Public as of September 30, 2004 and 2003, respectively. These securities are held in the FRB System Open Market Account (SOMA) for the purpose of conducting monetary policy.

Notes to the Schedules of Federal Debt Managed by the Bureau of the Public Debt

For the Fiscal Years Ended September 30, 2004 and 2003

(Dollars in Millions)

Note 3. Intragovernmental Debt Holdings

As of September 30, 2004 and 2003, Intragovernmental Debt Holdings are owed to the following:

		2004	2003
SSA:	Federal Old-Age and Survivors Insurance Trust Fund	$1,452,599	$1,313,427
OPM:	Civil Service Retirement and Disability Fund	631,860 *	601,709 *
HHS:	Federal Hospital Insurance Trust Fund	264,375	251,323
SSA:	Federal Disability Insurance Trust Fund	182,799 *	170,792 *
DOD:	Military Retirement Fund	177,280	172,362
DOL:	Unemployment Trust Fund	45,239	48,188
DOD:	DOD Medicare Retirement Fund	35,864	18,445
FDIC:	Bank Insurance Fund	32,089	31,055
DOE:	Nuclear Waste Disposal Fund	30,518	25,881
OPM:	Employees' Life Insurance Fund	28,107	26,778
HUD:	FHA – Liquidating Account	23,321	23,819
HHS:	Federal Supplementary Medical Insurance Trust Fund	17,439	24,922
DOL:	Pension Benefit Guaranty Corporation Fund	13,166	12,937
DOS:	Foreign Service Retirement & Disability Fund	12,828	12,289
FDIC:	Savings Association Insurance Fund (SAIF)	11,852	11,423
VA:	National Service Life Insurance Fund	10,948	11,246
OPM:	Employees Health Benefits	10,772	9,034
Treasury:	Exchange Stabilization Fund	10,319	10,503
DOT:	Highway Trust Fund	10,212	13,578
DOT:	Airport & Airway Trust Fund	9,892	10,518
Other Programs and Funds		60,229	59,001
Total Intragovernmental Debt Holdings		$3,071,708	$2,859,230

* These amounts include marketable Treasury securities as well as GAS securities as follows:

	GAS Securities	Marketable Treasury Securities	Total
As of September 30, 2004:			
Civil Service Retirement and Disability Fund	$631,749	$111	$631,860
Federal Disability Insurance Trust Fund	182,769	30	182,799
As of September 30, 2003:			
Civil Service Retirement and Disability Fund	$601,429	$280	$601,709
Federal Disability Insurance Trust Fund	170,762	30	170,792

Social Security Administration (SSA); Office of Personnel Management (OPM); Department of Health and Human Services (HHS); Department of Defense (DOD); Department of Labor (DOL); Federal Deposit Insurance Corporation (FDIC); Department of Energy (DOE); Department of Housing and Urban Development (HUD); Department of Transportation (DOT); Department of State (DOS); Department of Veterans Affairs (VA); Department of the Treasury (Treasury).

Notes to the Schedules of Federal Debt Managed by the Bureau of the Public Debt

For the Fiscal Years Ended September 30, 2004 and 2003

(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. The average interest rates for fiscal years 2004 and 2003 were 5.4 percent and 5.5 percent, respectively. The average interest rate represents the original issue weighted effective yield on securities outstanding as of September 30, 2004 and 2003. GAS securities are issued with a term of on demand to 30 years.

Note 4. Interest Expense

Interest expense on Federal Debt Managed by BPD for fiscal years 2004 and 2003 consisted of the following:

	2004	2003
Federal Debt Held by the Public		
Accrued Interest	$145,585	$143,335
Net Amortization of Premiums and Discounts	12,735	13,461
Total Interest Expense on Federal Debt Held by the Public	158,320	156,796
Intragovernmental Debt Holdings		
Accrued Interest	167,855	164,379
Net Amortization of Premiums and Discounts	(3,717)	(6,670)
Total Interest Expense on Intragovernmental Debt Holdings	164,138	157,709
Total Interest Expense on Federal Debt Managed by BPD	$322,458	$314,505

Note 5. Fund Balance With Treasury

	As of September 30, 2004	As of September 30, 2003
Appropriated Funds Obligated	$145	$162

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.

Comments from the Bureau of the Public Debt

DEPARTMENT OF THE TREASURY
BUREAU OF THE PUBLIC DEBT
WASHINGTON, DC 20239-0001

October 29, 2004

Mr. Gary T. Engel
Director
U.S. General Accounting Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Engel:

This letter is our response to your audit of the Schedules of Federal Debt Managed by the Bureau of the Public Debt for the fiscal years ended September 30, 2004 and 2003. We agree with your audit report's conclusions.

Although the past few years have presented new challenges associated with debt issuance suspension periods, we appreciate the experience and professional attitude of your audit team. We would like to thank you and your staff for conducting an efficient and thorough audit of these schedules with increasingly stringent audit requirements. The usability of these reports continues to develop through combined efforts, and we look forward to continuing this productive and successful relationship.

Sincerely,

Van Zeck
Commissioner

www.treasurydirect.gov

GAO Contact and Staff Acknowledgments

GAO Contact

Dawn Simpson, (202) 512-9473

Acknowledgments

In addition to the individual named above, Erik A. Braun, Dean D. Carpenter, Dennis L. Clarke, Chau L. Dinh, Mickie E. Gray, Jennifer L. Hall, Jay McTigue, Lori B. Ryza, Kathryn J. Peterson, and Jason O. Strange made key contributions to this report.

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