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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Secretary Of The Treasury

The Bureau Of Public Debt Should Better Control Savings Bond Sales And Redemptions

GAO's review of the Bureau of Public Debt's internal controls over savings bond sales, redemptions, and blank stock has identified major system weaknesses that result in losses to the Treasury and poor control over large supplies of blank savings bond stock. GAO recommends the centralization of controls over savings bond stock and the establishment of adequate accounting controls and procedures over sales and redemptions.



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UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D.C. 20548

ACCOUNTING AND FINANCIAL
MANAGEMENT DIVISION

B-204343

The Honorable Donald T. Regan
The Secretary of the Treasury

Dear Mr. Secretary:

This report recommends ways to eliminate duplication and inefficiency from the Bureau of Public Debt's U.S. Savings Bond Program. We have discussed the report with Bureau officials and they generally agreed with our findings and recommendations.

The report contains recommendations to you. As you know, 31 U.S.C. 720 requires the head of a federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations no later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We would like to be advised of any actions taken or planned concerning the matters discussed in this report. We will be glad to discuss these matters with you or your representatives.

Sincerely yours,


W. D. Campbell
Acting Director



GENERAL ACCOUNTING OFFICE
REPORT TO THE SECRETARY
OF THE TREASURY

THE BUREAU OF PUBLIC DEBT
SHOULD BETTER CONTROL SAVINGS
BOND SALES AND REDEMPTIONS

D I G E S T

The U.S. Savings Bond Program has been used for years to finance a portion of the public debt and, as of January 1982, was financing about \$67.6 billion. The program has permitted financing at interest rates lower than those prevailing for other types of private and public borrowing. It is the Bureau of Public Debt's responsibility to ensure attainment of the maximum advantages under the program. GAO reviewed the program's accounting and related internal controls to see if they were adequate and to identify any losses resulting from irregularities and abuses. This report discusses the problems GAO found, which have resulted in small monetary losses. The potential exists for greater losses.

INTERNAL CONTROLS
OVER SAVINGS BOND STOCK
SHOULD BE IMPROVED

Savings bonds are sold by 44,000 issuing agents at banks and other financial institutions from pre-printed blank stocks that can be converted easily to negotiable securities. The stock is provided without charge to the agents, and fraudulent or unauthorized bond issuances cannot be detected until after they are redeemed by the Bureau. Because of this, the blank stocks should be controlled in a manner similar to that used for currency, with one Bureau office maintaining accounting control over the agent's stock inventories and related sales. The Bureau, however, uses two different offices to account for sales and related inventories and relies on Federal Reserve banks and branches to control inventory distribution to the agents. Within the decentralized environment, GAO also found that:

- The Federal Reserve banks and branches have not followed recognized control and accounting procedures for the savings bond stocks distributed to issuing agents on a consignment basis, even though they are compensated for this function. Agents have been provided with more than enough stocks to support their sales activities, and have reported bond stock losses and thefts with a face value totaling at least \$8.8 million, a portion of which has already been redeemed by the

government. Most of these losses occurred during a recent 2-year period. GAO believes these shortages are a direct result of poor control over the stocks by the banks and branches. (See pp. 6-8, 10.)

--The Bureau also has not properly accounted for stocks issued to Federal Reserve banks and branches for distribution to agents, or properly investigated the large amounts of stock shortages reported by agents before granting them relief. The Bureau made a considerable effort over a 36-month period to locate all unissued Series E savings bond stock after it was recalled when the government changed to the Series EE bonds. Still, it has not established proper control over unissued bond stock with a face value of several million dollars. In some cases, the Bureau has granted relief to agents for reported bond shortages and later found that the agents had sold the bonds. (See pp. 8-10.)

--Several unexplored opportunities exist to improve accountability over blank stock while reducing costs. Among these would be the centralization of bond stock control at a single Bureau office and the conversion to paper bonds instead of the present card weight bonds, which would simplify transaction handling and permit machine encoding. (See pp. 11-13.)

The bond stock control problems have persisted for years, and GAO estimates that over 6 percent of the issuing agents had stock balances differing from those recorded on Federal Reserve bank and branch records. If the inventory control problems are allowed to persist, GAO believes large shortages of Series EE savings bond stock could develop.

MANAGEMENT ACTIONS CONTRIBUTE TO INEFFICIENCIES BY AGENTS

GAO noted that a major concern of Bureau management has been to keep the issuing agents from leaving the program. This concern has apparently influenced a number of decisions that contributed to abuses and practices leading to both stock and monetary losses. For example, the Bureau delayed a program to assess penalty interest in those cases where issuing agents did not remit bond sales proceeds promptly, even though such assessments were necessary to prevent agents from receiving dual compensation for services.

The Bureau has also followed a practice that permits issuing agents to hold money from savings bond

sales while paying little or no interest for the use of the money. It involves primarily cases where agents are granted relief from stock shortages and are later found to have sold the bonds without remitting sales proceeds. In such cases, the Bureau collects the bond sales price from the issuing agents but not the interest it paid in redemption when that interest is less than \$100. While GAO could establish only a small amount of related losses, it believes the process could result in larger losses if widely known, and sees no reason for the Bureau to continue the practice.

The Bureau relieved an agent from liability for monetary losses in redeeming bond stocks stolen by one of the agent's employees and subsequently redeemed by the government--losses which could eventually total about \$188,000. The relief was granted with questionable authority and on the basis that issuing agents should be held liable for losses or thefts only when it could be proven they were negligent.

The Bureau also has not been effective in controlling the amounts it is owed by others, primarily agents. For example, it has not promptly recorded amounts as receivables and, in the past 3 years, has not taken required actions to ensure prompt collection of amounts recognized as due. Receivables have not been aged, other actions have not been taken to recognize debts of doubtful collectibility, and penalty interest has not been assessed on delinquent amounts owed by debtors.

Finally, the Bureau has followed a practice of paying its agents for services on the basis of number of transactions handled, without regard to the quality of work. This has led to a considerable number of agent errors in selling and redeeming savings bonds and preparing related documents. GAO estimates that the Bureau spends around \$530,000 annually to correct the errors and believes it should consider having agents bear this additional cost, especially those agents with a history of errors in their sales and redemption transactions.

ACCOUNTING PRACTICES PREVENT FULL DISCLOSURE OF OPERATING RESULTS

GAO found several Bureau accounting practices to be inconsistent with laws and recognized procedures. This prevented full disclosure of control problems and related losses. For example:

--Receivables were not established for amounts owed the Bureau from late payments of sales proceeds.

Some of the proceeds relate to bonds that have already been redeemed. (See pp. 18-19.)

- Significant amounts of receivables and payables were being recorded in the same account; an unacceptable practice that distorts the agency's financial position. (See pp. 27-28.)
- All monetary losses were charged to a revolving type fund that does not have sufficient appropriations to cover losses already incurred or anticipated, and the Congress has apparently not been fully advised of the extent to which the fund is used for such purposes. (See pp. 28-29.)
- Required reports of losses have not been submitted to GAO so that it can settle the accounts that have shortages, as required by law. (See p. 29.)
- Additional amounts owed to bond holders for underpayments on bonds have been provided to paying agents to remit to the bondholders even though documents have not been received to relieve the government's liability for these underpayments. (See pp. 29-30.)

RECOMMENDATIONS

To improve accountability and control over savings bond activities, GAO recommends that the Secretary of the Treasury:

- Have the Bureau's Parkersburg office centrally account for consigned savings bonds and sale proceeds.
- Ask the Treasury's Office of Inspector General to evaluate any shortages in Series E bond stock and make sure that proper amounts are recorded in the Bureau's official inventory records for activities holding such bonds.
- Ensure that interest penalties are assessed on issuing agents' late remittance of sales proceeds, as well as any overdue receivables, and that the assessed amounts are promptly collected unless circumstances warrant a waiver.
- Amend the issuing agreement to specify that issuing agents are liable for all monetary losses related to redemption of savings bond stock that is lost or stolen by their employees, and to recover any monetary losses that develop.

- Have receivables resulting from the Bureau's operation properly managed and aged and aggressively collected.
- Require the use of accrual basis accounting for all activities related to savings bonds, including any redemption of savings bonds that results in money being owed the government, as well as the assessment of penalty interest.
- Make sure the Bureau properly uses separate accounts for receivables and payables.
- Refund amounts of bond redemption underpayments directly to the bondholders and recover any resulting costs from the agents responsible for the underpayments.

The Secretary should also fully advise the Congress of activities in the Payment of Government Losses in Shipment Fund, including the amount needed to cover existing and expected losses, and make sure the Bureau's accounting system is changed to properly recognize such losses. Other recommendations are contained in the body of this report.

The Bureau of Public Debt generally agrees with these recommendations and efforts are underway to address or implement needed improvements to financial control. (See pp. 13, 14, 23, 24, 31)

AGENCY COMMENTS

In commenting on the report (see app. II), the Department of the Treasury acknowledged the existence of inventory control and accounting problems in the U.S. Savings Bond Program. The Bureau of Public Debt generally agrees with GAO's recommendations. It has promised to implement them and to review the corrective actions to address the weaknesses identified in this report. These corrective actions, when fully implemented, should lead to a more effective operation.

Treasury's comments also included examples of actions taken in response to our report. These include

- establishment of separate receivable and payable accounts,
- studying the feasibility of centralizing stock control in one office, and
- studying and identifying procedural changes necessary to generate faster collections from agents.

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CHAPTER 1

INTRODUCTION

The U.S. Savings Bond Program is a huge operation that, as of January 1982, financed about \$67.6 billion of the public debt at comparatively low interest rates. The bonds are sold primarily to small investors through a vast network of issuing agents comprising banks, other types of financial institutions, and commercial enterprises with payroll savings plans. The bonds are redeemable 6 months after their issue dates at any financial institution acting as paying agent for the federal government. The program, which is administered by the Bureau of Public Debt, has experienced a high volume of sales and redemption transactions. In recent years, the transactions have totaled more than \$15 billion annually.

This report discusses weaknesses in the accounting systems and related internal controls over the sale and redemption of savings bonds that become, upon issuance, registered securities to be honored by the federal government. The weaknesses are related to activities for which the Bureau spent about \$100 million in fiscal year 1981. This amount was for agent fees for selling and redeeming savings bonds and for a variety of activities essential to register bonds, account for sale and redemption transactions, and control blank stock provided without charge, or on a consignment basis, to issuing agents.

ACCOUNTING REQUIREMENTS FOR SAVINGS BOND SALES AND REDEMPTIONS

Since 1941, the Treasury has offered several types of savings bonds. Among them are Series H, HH, E, and EE bonds. The primary differences between these bonds are in the minimum denomination, interest rate, and maturity period. The Series E and EE bonds are more suited for small investors and, in recent years, most sale and redemption transactions processed under the program have related to those bond series. The program has some unique accounting requirements that, if handled correctly, can reduce opportunities for losses and abuses and promptly detect those that have occurred.

One requirement is related to the practice of providing blank stock free, or on consignment, to issuing agents who make the sales. The consignment technique is appropriate when it is desirable to keep the seller from having to invest large sums in inventories. For savings bonds the technique is particularly appropriate because the issuing agents are providing a service for which they are paid a fee that would not cover the investment cost of purchasing blank bonds. The bond stock provided to the agents, however, should be accounted for by the Bureau until sales are reported and proceeds are received. The Bureau's accounting records should also recognize any real or contingent liabilities related to stock losses and thefts.

Another requirement is associated with the registering of bonds after their sale. Under current procedures, savings bonds are registered in the Bureau's accounting records to show persons or activities to which bonds were sold and sale dates. The registry forms also contain the names, addresses, and identification (usually social security numbers) of the owners, and information about the agents issuing the bonds. The registration of bonds is a very important feature of the system if done correctly; it provides a basis for determining whether the government received funds for savings bonds that are redeemed.

It is also extremely important for accounting and physical control to be maintained over unissued savings bond stocks, because savings bonds will be cashed by any paying agent when they bear an issuing agent's stamp and have the names, addresses, and identification numbers of the owners. This bond feature can result in federal money being paid out for bonds before the sale proceeds are received, even though the bonds cannot be redeemed for 6 months after issuance. Thus, the Bureau's accounting system must provide for the recording of receivables related to such transactions and recognize any losses that eventually develop.

The sale and redemption of savings bonds also involves transactions and calculations that are handled by an extremely high number of nongovernment activities. The Bureau has no direct control over such activities and can detect only those errors resulting in overpayment or underpayment of money in postaudits of transactions. Thus, the Bureau's accounting system must recognize receivables and payables developing from errors or improper transactions. The system must also provide for bond sales and redemptions to be recorded in the appropriation accounts established to pay public debt principal and interest.

We approved a system design for the Bureau in 1968 that provided for the basic accounts needed to control the savings bond sale and redemption transactions. Since then, several changes have been made to the system which have not been submitted to us for approval. For example, the system was modified in 1978 to provide the data needed to pay issuing agents for their services.

MAGNITUDE OF ACTIVITIES INVOLVED IN ACCOUNTING OPERATIONS

The Bureau has overall responsibility for management of the Savings Bond Program, including the physical control over unissued stock and the accounting for all transactions related to stock transfers and bond sales and redemptions. It carries out these accounting and physical control responsibilities through several of its offices, all 24 Federal Reserve banks and branches, more than 44,000 issuing agents, and a similar number of paying agents.

The Bureau uses its headquarters office to procure blank bond stocks from vendors. The headquarters office sends the blank stocks to Federal Reserve banks and branches for distribution to issuing agents, maintains custody of unissued stock, and accounts

for the stock distributed to banks and stored in its vault. The office also maintains the different control records, or general ledger accounts, in which sale and redemption transactions are eventually recorded.

The Federal Reserve banks and branches are used as fiscal agents, with specific responsibilities for providing blank bond stocks to issuing agents and accounting for unissued stocks in the hands of agents. Among other things, they determine the banks' and other institutions' qualifications to be issuing and paying agents, establish and terminate agents' agreements, and issue and redeem bonds upon request. The banks and branches process (1) all sale and redemption transactions handled by other issuing and paying agents, and (2) related documents that affect the amount of money in the U.S. Treasury. The Bureau paid the banks and branches about \$21 million in fiscal year 1981 to do this.

The issuing agents sell bonds from blank stocks furnished them on consignment through the Federal Reserve banks and branches. Their responsibilities include safeguarding the blank stocks, collecting money from sales, preparing documents to deposit proceeds from sales, and remitting the proceeds in accordance with procedures and time frames specified by the Bureau. Most commercial banks, as well as other types of financial institutions and several commercial companies, have been qualified as issuing agents. For these services, the agents are paid a fee ranging from \$.05 to \$.85 for each bond sale, depending partly upon the extent of mechanization available to handle the related paperwork. In fiscal year 1981, payments to the agents totaled about \$15 million.

The paying agents are responsible for paying the correct amounts when bonds are presented for redemption by owners and for preparing the appropriate forms so they can be reimbursed for amounts they pay out. Most commercial banks and other types of financial institutions, such as credit unions and savings and loan associations, are qualified as paying agents and receive \$.34 for each bond redeemed for cash and \$.50 for each one exchanged. In fiscal year 1981, the Bureau paid more than \$44.2 million to cover services provided by the paying agents.

Finally, the Bureau has a facility in Parkersburg, West Virginia, that processes all transactions related to savings bond sales and redemptions. Its functions include registering bonds from documents submitted by issuing agents, monitoring the transmittals of funds after sales, recording all bond redemptions under procedures designed to verify the accuracy of amounts paid out by agents, and processing documents to support adjustments to Treasury's cash accounts when errors are found. These functions account for a large part of the \$23 million the Bureau spent in fiscal year 1981 on administrative costs directly attributable to the Savings Bond Program.

OBJECTIVES, SCOPE, AND METHODOLOGY

This report is based on our review of accounting and physical controls over savings bond operations at Bureau offices; Federal Reserve banks and branches, which act as fiscal agents of the Treasury; and issuing and paying agent facilities. Our primary objectives were to determine whether the accounting and related internal controls over the Savings Bond Program were adequate to protect the federal government's interests and to identify and disclose any losses resulting from irregularities and abuses.

Our review included an evaluation of policies and procedures published by the Bureau to direct the many different activities in carrying out savings bond accounting and physical control functions. We worked at the Bureau of Public Debt's offices in Washington, D.C., and Parkersburg, West Virginia; Federal Reserve banks in New York, Chicago, Cleveland, San Francisco, and Los Angeles; and 17 issuing and paying agents in Ohio, Kentucky, California, and the District of Columbia.

We performed our review in accordance with generally accepted government audit standards. It specifically included the following:

- Examinations of selected Bureau accounting records and financial reports to establish the completeness and accuracy of data being recorded and reported.
- Observations of Bureau operations involved in registering securities and recording redemptions to identify any obvious operational problems.
- Analyses of data provided the Bureau by Federal Reserve banks and branches and their agents to establish its appropriateness for monitoring and reimbursing monetary transactions.
- Reviews of data extracted from the Bureau's data base on bond status to evaluate the efforts to locate large numbers of missing bonds.
- Interviews with appropriate officials in the Bureau, Federal Reserve banks, and agent facilities to gain an understanding of the accounting and internal control responsibilities assigned to them under the Savings Bond Program.

In addition, we randomly selected 600 savings bond issuing agents and sent questionnaires to them to accumulate data on their operations. The questionnaire was specifically designed to identify internal control weaknesses and to disclose instances when excessive stock was being requested and held by agents. We received responses from 531 of the 600 agents (88.5 percent), which gave us the data we used to develop the adverse conditions discussed in chapter 2. The reliability of our sample is explained in appendix I.

CHAPTER 2

WEAKNESSES IN CONTROLS

CONTRIBUTE TO NEGOTIABLE BOND STOCK SHORTAGES

AND OTHER PROBLEMS

The Bureau provides its savings bond issuing agents with preprinted stocks that become negotiable securities when they bear payees' names and addresses, payees' social security numbers, issue dates, and issue agent stamp imprints. As these data can be easily inscribed on unissued bonds and validity cannot be established until after the bonds are redeemed, the Bureau and its agents should have recognized that unissued bond stocks are, in effect, currency and should be controlled accordingly. Yet, we found that:

- Federal Reserve banks and branches have not followed recognized procedures to control and account for savings bond stocks distributed to agents on a consignment basis, even though they are paid to do this. As a result, agents have obtained excessive stock balances. We believe this condition contributed to bond stock shortages with a redemption value of over \$8.8 million reported by issuing agents in a recent 2-year period.
- The Bureau has not properly accounted for stocks issued to Federal Reserve banks for distribution to agents or investigated large amounts of stock shortages reported by agents before granting them relief. Consequently, all unissued Series E savings bond stocks have still not been brought under proper accounting control despite a 36-month effort to do this. Also, relief for liabilities has been granted for some shortages of bond stocks that later were found to have been sold by agents getting the relief.
- Several opportunities exist to improve accountability over blank stock while reducing costs. These have not been fully explored by the Bureau. Among them are centralization of bond stock control at a single Bureau office and conversion from the card stock that is presently used to paper bonds that would permit efficiencies in registering bonds and recording redemptions.

REQUIRED PROCEDURES NOT FOLLOWED IN CONTROLLING BOND STOCKS

Since the Savings Bond Program began, the Bureau has used Federal Reserve banks and branches as its fiscal agents and given them specific responsibility to distribute and control blank savings bond stocks to the vast network of issuing agents. In recent years the banks have been paid to perform these functions (about \$7 million in fiscal year 1981) but performance has not been consistent with Treasury regulations.

Excessive stock provided to agents

Treasury procedures to control stocks revolve around the level of stock authorized to an agent to support its operations. The level set is based on demand for the stocks over a specified period of time, with consideration given to the time it takes to order and ship replacement stocks to the activity. In the case of savings bond stocks, the Bureau has decided that issuing agents should base stock levels on prior sales activities and at any given time should not have more than 3 months stock on hand, including requisitions outstanding. This standard has been published in the Bureau's Fiscal Agency Security Manual which is available for use by the banks and branches.

The Federal Reserve banks we visited were aware of the maximum levels specified in the Bureau manual. They also had records of stock inventories for agents they serviced showing stock balances and a history of prior activities. However, we found that banks and branches had routinely filled requisitions from agents for stocks far in excess of maximum authorized levels. The chart shows some excessive requisitions filled during the last quarter of 1981.

Stock Status

<u>Bank</u>	<u>On hand</u>	<u>Requisitioned</u>	<u>Total</u>	<u>Value</u>
	----- (years) -----			(thousands)
San Francisco	1.3	4.9	6.2	\$126
New York	5.3	4.9	10.2	\$ 83
Chicago	0.4	1.3	1.7	\$ 70
Cleveland	7.8	11.5	19.3	\$ 69

In our questionnaire we asked for data on stocks agents had on hand when their most current requests for additional bonds were submitted to Federal Reserve banks and branches. We also asked for data on monthly sales and the amounts of stock requisitioned, but only 338 of the 531 respondents provided the data on their latest requisition. These data showed that one request had been filled for a 150-year supply of stock by a Federal Reserve bank, and that five other requests had been filled for stock that would support sales by each agent for more than 45 years. The average requisition filled for the 338 agents would support their sales for approximately 27 months.

The 531 responses showed that the average agent's stock balance would support 73 months of sales activities with individual levels ranging from 1 month to 130 years of stock. Overall, we estimate that only 5 percent of the approximately 44,000 issuing agents had restricted their stock levels to the 3-month maximum prescribed by the Bureau, and others exceeded the maximum by amounts shown in the table on the next page.

<u>Number of agents</u>	<u>Percentage of agents</u>	<u>Stock on hand (months)</u>
2,200	5	0 - 3
10,560	24	4 - 12
14,080	32	13 - 36
17,160	39	37 or more
<u>44,000</u>	<u>100</u>	

We also questioned the agents about their knowledge of the maximum stock levels authorized to support their savings bond sales. Of the 520 agents who responded to this question, 84 percent said they had not received guidance from Federal Reserve banks and branches on consignment stock levels that could be retained to support their sales.

Officials at the Federal Reserve banks we visited acknowledged that the agents had stock balances exceeding the authorized levels and that requisitions had been filled by the banks for excessive amounts. Some blamed this on the higher sales trends experienced before the Series EE bonds were introduced. But we noted that the Federal Reserve banks either had no procedure in effect to reject excessive requisitions or used manual procedures, with one clerk responsible for reviewing hundreds of stock requests to ensure that agent balances did not exceed recommended amounts. We were not advised of any plans to mechanize stock requisitioning and recordkeeping to the extent that would be necessary to permit automatic rejections of excessive requisitions based on earlier sales data.

Stock balances not properly confirmed

Another specified stock control is to compare balances recorded on agency control records with balances on records of activities holding the stock. This can be done either through independent audits or by written confirmation procedures, but at the Federal Reserve banks we visited neither of these recognized approaches were being used effectively.

We found the banks to be using various methods to confirm agents' balances, although some banks had no way of determining whether the agents' recorded balances agreed with those shown on bank records. For example, the San Francisco and Cleveland banks were confirming balances by matching agents' reported sales and stock balances with their records, while the Los Angeles and New York banks relied on agents to report account imbalances. At the San Francisco bank, we noted that its records differed with the balances being reported by agents for about 16 percent of 2,600 agents serviced as of August 10, 1981. For agents serviced as of January 27, 1982, its records differed with the balances reported by 452 agents, or about 17 percent. The bank had not begun to reconcile its agents' Series EE stock balances until 15 months after the start of the Series EE program, and then gave it a very low priority. We noted that some agents had been reporting differences

since Series EE bonds were first issued to them in late 1979. A San Francisco bank official explained that the savings bond operation was only a small part of the bank's total operation and, due to staffing restrictions, the bank's primary concern was to carry out operations rather than to reconcile differences in accounting records.

Many bank officials we interviewed acknowledged that the reconciliation of differences in stock balances had been given a low priority. Overall, we estimate that 6 percent of the 44,000 issuing agents had stock balances differing from those recorded for them on records of Federal Reserve banks and branches. This estimate is based on a comparison of data furnished by 531 issuing agents and Federal Reserve banks and branches.

We understand that Federal Reserve banks and branches now furnish monthly statements to each agent, showing sales, damaged stock, and stock on hand. The agents are instructed to reconcile balances and notify the Federal Reserve banks when differences are identified. We noted instances, however, in which agents ignored the monthly statements when this technique was used to confirm balances. Also, we do not believe the technique to be particularly effective because some agents are holding larger balances than those shown on the banks' and branches' records and the agents have no incentive to report this condition. A Bureau official acknowledged that the confirmation approach was not effective and concurred that it would be better to have agents identify their balances and let the Federal Reserve banks and branches determine whether balances agree.

Independent audits are normally considered necessary to ensure that accountable persons accurately report security balances. We found no special requirement for the audits to be made by persons representing either the Bureau or the Federal Reserve banks and branches. Over 40 percent of the agents responding to our questionnaire, and most agents we visited, said their consignment stock had rarely, if at all, been physically inventoried by independent persons. We believe periodic physical inventories are necessary to confirm the existence of stock being reported by agents. We recognize that it is not feasible to inventory all 44,000 agents annually, but this should be a requirement for some of the larger agents, with smaller agents being inventoried less frequently.

STOCK ACCOUNTABILITY AND LOSSES NOT PROPERLY HANDLED

Besides not properly controlling stocks distributed to issuing agents, the Bureau has not maintained proper accountability of bond stocks it has distributed to Federal Reserve banks. Consequently, it has been unable to establish proper accountability over all unissued Series E bond stock even though it has spent considerable effort over the past 36 months attempting to do this. Moreover, the Bureau has not properly investigated stock losses or thefts that agents have reported, especially those reported during the Series E stock recall.

Accountability not established

In late 1979, the Bureau started issuing the Series EE bonds that the government approved to replace the Series E bonds. It began in January 1980 a recall of all unissued Series E stock which, according to Bureau records, had a face value of about \$6.5 billion. The initial recall and related record reconciliation were handled by the Federal Reserve banks and branches. By July 1981, they reported that all but \$1.1 million in unissued stock was accounted for.

About the same time, the Bureau office in Parkersburg had come up with different results in its attempts to account for all unissued Series E stocks. Its efforts showed that as many as 800,000 unissued bonds had to be accounted for. No value could be placed on these bonds at the time of our field work. This number of bonds was derived through a computer program that had compared the serial numbers of bonds delivered by printers against those on which entities had accountability for such things as sales, losses, thefts, or damaged stock. Bureau officials told us that their program to identify the missing bonds contained some errors, and that the total number could be much greater than the number already identified. However, the officials decided to abandon the effort to locate the missing bonds, primarily because of lack of staff time and difficulties in getting computer programming assistance.

The Bureau resumed its efforts to identify missing bonds after we found that the stock and records of Federal Reserve banks and branches and issuing agents did not agree. Another computer program developed by the Bureau initially disclosed about 1.2 million unissued bonds to be accounted for, whereas its records showed Federal Reserve banks and branches to be holding only about 400,000 unissued bonds. Bureau officials could not explain this difference but did obtain informal reports showing the banks and branches as well as its Washington vault to have about 817,000 of the missing bonds with a face value of \$246 million. They did not, however, require physical inventories to verify the accuracy of the reports. We did not attempt to establish the existence of the reported bond stock because of the extensive amount of work involved. Bureau officials, however, acknowledged that about \$22.5 million of the missing stock was not at those locations.

The Bureau found several weaknesses in the bond recordkeeping system in its effort to bring the unissued Series E bond stock under proper accounting control. For example, the system for entering new bond serial numbers in control records had resulted in more bonds being listed for control than were actually printed. Because of this problem, the records showed more than \$40 million in bonds to be controlled that never existed. The Bureau also found that some Federal Reserve banks and branches had bond stocks which the records incorrectly showed as located in other banks or branches. Adding to the confusion, vault personnel were found to not always accurately report stock balances, and the Bureau had to request

clarification on several occasions. At the conclusion of our field work the Bureau was still attempting to locate 147,575 unissued bonds with a face value of over \$22.5 million.

Stock shortages not investigated

Issuing agents have reported bond stock shortages with a face value totaling more than \$8.8 million between January 1980 and July 1982, with about \$8 million reported during the first 18 months of that period. We found that the Bureau has usually granted relief for the stock shortages as long as the serial numbers for lost bonds were furnished with the requests for relief.

For example, in our review of 74 requests for relief from agents serviced by the New York Federal Reserve Bank, we noted that 20 claims did not include sufficient information for the Bureau to determine whether or not the agents' negligence led to the losses or thefts. One request, a claim dated February 8, 1980, simply stated that blank bonds had been stolen and did not explain how the theft occurred or what procedures the agent used to safeguard bond stocks. The accompanying police report also did not include this information. Yet, on May 19, 1980, the Bureau approved the agent's request for relief.

We noted that during the Series E bond recall, issuing agents were permitted to submit requests for relief for bond stock shortages if the bond serial numbers were identified. Over 1,570 requests for relief, totaling about \$8 million, were submitted between January 1980 and June 1981. Most requests were approved and contained the stipulation that the agents would be liable for the value of the bonds in the event they had to be redeemed by the Bureau.

The Bureau's records showed that some agents had requested relief from bond losses that had actually been sold. In such cases, the Bureau denied the agent's request if the bonds had already been redeemed, but a number of relief requests had been approved before the Bureau discovered that the bonds had actually been issued. We believe that if the Bureau would investigate the requests for relief, it would identify poor recordkeeping and physical security practices leading to the losses and could develop information on the financial standing of the agents requesting relief.

Determination of the agent's financial position is usually important as a prerequisite to granting relief for stock losses. Today, however, it is essential because companies and financial institutions are having financial difficulties, merging, or going out of business. A Bureau official told us that relief for bond losses had been granted to several companies that had either gone bankrupt before being granted relief or merged with other companies. He said that in some cases the Bureau had been unable to recover the money for the bonds. We could not determine the monetary losses related to this condition because, as discussed later in this report, the Bureau does not properly account for its losses.

OPPORTUNITIES TO IMPROVE SYSTEM CONTROLS
NOT FULLY EXPLORED

The Bureau's system to control savings bond stock was apparently developed many years ago and contains many laborious manual procedures. During our review we noted the following system changes that would improve controls over unissued savings bond stocks while apparently decreasing operating costs.

The major change would be to have the accounting for unissued bond stock and perhaps even the bond stock distribution functions centralized at the Bureau's Parkersburg office, which now accounts for bond sales proceeds. This office could record the serial numbers of blank bond stock distributed to each agent. This perpetual inventory-type account would be updated via the documentation used to record sales data, instead of using reports from the Federal Reserve banks and branches as is presently done. The centralized account would provide the information needed to properly manage the program, which is not readily available under the current system.

For example, in cases where bonds are redeemed before the sale proceeds are received, the centralized records would permit immediate identification of the agent owing the money. They would also permit identification of agents with excessive stock levels in relation to past sales volume, especially those under payroll plans.

The centralization would also seem to permit economies and efficiencies in:

- Distributing bond stocks to agents. The Bureau is already distributing stock directly to some of its larger issuing agents from its vault in Washington, and it contends that this practice reduces distribution costs. We see no reason to dispute this, because the Federal Reserve banks and branches perform middleman functions that would not be necessary under a centralized distribution approach. These include receiving bonds shipped to them, recording them, and repackaging them for reshipment.
- Collecting forms to register bonds after sale. Under current procedures, agents submit registration stubs and deposit slips to Federal Reserve banks and branches in support of their sales activity. The only apparent use for the stubs is to adjust stock records, check the accuracy of amounts deposited, and identify any instances where sales proceeds were not remitted promptly. The banks and branches in turn ship the stubs to the Bureau's Parkersburg office. Since the Parkersburg office already performs most of these functions, centralizing the stock records would eliminate the need for stubs to be sent to the banks and branches. This appears to be an opportunity for savings, since centralization would eliminate duplicate functions and unnecessary handling and shipping.

--Processing redeemed bonds. All redeemed bonds and appropriate reimbursement vouchers are now sent by paying agents directly to Federal Reserve banks and branches, who apparently use them to verify the accuracy of payments made by the agent. The Bureau's Parkersburg office, however, performs this function after the redeemed bonds are shipped to it by the banks and branches. A centralized control activity would not be necessary to change the way the redeemed bonds are routed, but it would help simplify the accounting process.

In initial discussions of the proposed centralization of stock control, Bureau officials expressed concern that it might create stock distribution problems and raise the Bureau's operating costs. We agree that centralization might increase the operating costs, but the Bureau now pays the Federal Reserve banks to perform functions that could be eliminated. The money thus saved would be available to cover any increased operating costs. The Bureau is now reconsidering the centralized approach idea.

Another improvement would be to reduce the number of issuing agents authorized to hold stock. The huge network of agents was established because the savings bond sales volume was high. However, from the peak of approximately \$8 billion in sales in fiscal year 1978, the sales volume declined by 58 percent, to about \$3.3 billion in fiscal year 1981. Also, the trend in sales has shifted: payroll sales now account for 73 percent of all sales. Consequently, many issuing agents are no longer selling enough bonds to justify keeping any stock on hand. Our review disclosed that more than 9,500 issuing agents reported no sales for the month of April 1982. As early as August 1980, the Bureau noted that many agents were not making enough sales to justify the expenses associated with providing the stocks. It considered the possibility of removing the stocks from low-volume agents and replacing the bond stock with application forms. The actual sale of bonds would be performed only by high-volume activities. This change appears to have merit, but was not implemented by the Bureau.

A proposed Treasury improvement would be to use a paper bond instead of the card currently used. The paper bonds could be designed to be compatible with optical scanning equipment. This would eliminate time-consuming and laborious keypunching. The Bureau is considering this improvement and we believe it has merit.

Finally, the Bureau could improve controls over savings bond stock by changing its procedures for furnishing documents supporting bond sales through payroll savings plans. Current procedures emphasize the timely remittance of cash proceeds but do not specify when supporting documents, such as bond registration stubs, should be furnished. Consequently, the supporting documentation is sometimes furnished long after sales are made. For example, in May 1982 an agent submitted sales documents for 200,000 bonds that were sold more than 2 months earlier, including some for more than 250 bonds sold more than a year earlier. Without the sales documentation the Bureau cannot readily determine whether sales proceeds

have been remitted promptly or at all. Bureau officials agreed that the lag in receipt of the sales documents had caused record-keeping and reconciliation problems. At the end of our field work, however, regulations had not been changed to require supporting documents to accompany deposits of sales proceeds.

RECOMMENDATIONS

We recommend that the Secretary of the Treasury have the Bureau's Parkersburg office centrally account for consigned savings bonds and sales proceeds. The office managing the consignment should be required to:

- Actively enforce Bureau criteria for the amount of savings bond stock that issuing agents can have on hand and on requisition at any given time.
- Thoroughly investigate requests for relief from lost and stolen bonds, particularly large ones, before decisions are made on requests for relief.
- Reconcile and verify agents' stock levels through appropriate procedures, including periodic and independent physical inventories that will ensure accountability for all bond stock held by agents.
- Establish requirements for agents to submit documents supporting payroll sales as soon as practicable after they remit sales proceeds.

We also recommend that the Secretary:

- Make other system improvements that will lower operating costs, such as eliminating stock levels of agents with low sales volume and converting from card weight to paper bonds.
- Ask the Treasury's Office of Inspector General to determine whether shortages exist in Series E bond stock and make sure that proper amounts are recorded on the Bureau's official inventory records for activities holding such bonds.

AGENCY COMMENTS AND ACTIONS

In reporting our findings to the Department of the Treasury, we recognized that the Bureau faces a formidable task in controlling blank savings bonds in the hands of issuing agents. In commenting on our report (see app. II), the Treasury's acting assistant fiscal secretary said the Bureau was studying the feasibility of centralizing stock control in the Parkersburg office and was looking at issues covered by our other recommendations. Our discussions with Bureau officials confirmed this. We also found the Bureau working on a plan to reduce excessive Series EE stock levels now existing at issuing agents. The Bureau has informed us that

the plan has been completed. This inventory reduction should make it much easier for the Bureau to exercise control over the consignment inventory.

While agreeing to improve controls, some Bureau officials have expressed concern about the costs associated with implementing our recommendations. We recognize there will be some costs, but believe that the benefits to be realized from eliminating duplication and inefficiency from operations now costing over \$100 million annually will be well worth the effort.

CHAPTER 3

IMPROVEMENTS NEEDED

IN THE COLLECTION OF SALES PROCEEDS

A major concern of Bureau management has been to keep its issuing and redeeming agents from leaving the Savings Bond Program. We noted a number of practices apparently motivated by this concern that we believe have led not only to stock losses but also monetary losses. Specifically, we noted that:

- Penalty interest has usually not been collected from issuing agents when cash proceeds from sales are deposited late. We estimate that penalties totaling about \$5 million were never assessed or collected in about a 3-year period.
- Issuing agents have been allowed free or low-cost use of savings bond proceeds. This happens when agents sell bonds that they previously reported as lost. While the amounts involved appear to be small, continuation of this practice could result in larger losses.
- An issuing agent has been granted relief from liability for losses that could total more than \$188,000. The losses had resulted from redeeming bond stocks stolen by one of its employees. Relief had been granted with questionable authority and, more importantly, the rationale for the relief sets a precedent that will make it difficult to hold agents liable for future monetary losses.
- Aggressive action has not been taken in the past 3 years to collect the receivables recognized in the Bureau's records. For example, interest charges are not assessed on accounts receivable, and the Bureau has requested an exemption from that requirement.
- Payments have been made to issuing and redeeming agents for a large amount of work that has to be corrected at an additional cost to the Bureau. For example, we estimated that the Bureau spent about \$530,000 to correct errors it found in agents' work covering a 1-year period.

PENALTIES NOT IMPOSED FOR LATE CASH DEPOSITS BY AGENTS

In April 1979, the Bureau planned to begin assessing interest penalties in cases where issuing agents failed to promptly remit proceeds from the sale of savings bonds. Prompt remittance keeps agents from receiving dual compensation for selling bonds. However, implementation of the program was delayed until September 1981; since then, many interest assessments have been waived without adequate basis and the Bureau has been slow to collect amounts not waived. Also, we found that the Federal Reserve banks and branches were not assessing interest as required on late payments

for bonds they issue for agents. We estimate that at least \$5 million in revenue has been lost as a result of those conditions.

Unnecessary delays
in implementing the program

Before November 1978, the Bureau compensated agents for selling savings bonds by allowing them full use of sales proceeds for long periods of time. Then, because the practice was considered too costly to the federal government, the Bureau decided to start paying agents a fee for issuing bonds and requiring them to remit bond sales proceeds promptly to the U.S. Treasury. The payment of fees began in November 1978. A program should have been in place by that date to require prompt remittance of sales proceeds and to identify instances where agents did not remit cash promptly so that an interest penalty could be assessed. The Bureau, however, did not implement the program to assess the interest until September 1981.

Bureau officials told us the interest assessment had not started sooner because the Bureau was not getting complete and accurate information on sales from issuing agents. While there may have been some problems, we believe the sales data could have been accumulated from sales documents being furnished to the Bureau as is now being done. We believe the underlying reason for deferring assessment charges was a concern that the interest assessment would cause some issuing agents to leave the program.

The Bureau realizes that a significant amount of revenue could have been collected had assessments been made on late payments of sales proceeds since April 1979. For example, the Bureau tested payments made by issuing agents between May 1981 and August 1981 and found that more than \$648,000 in interest should have been assessed on late payments during the 4 months. Based on this Bureau test, we estimated that approximately \$4.7 million in revenue was lost between April 1979 and August 1981 due to the Bureau's delay in beginning to assess penalties. Our estimate is based on a test period when an average 10 percent of the sales proceeds were remitted late. We consider it conservative, since about 25 percent of the proceeds were not being remitted promptly in the early part of that period.

We do not understand the Bureau's extensive delay in starting the interest penalty assessment. This is a recognized approach to encourage prompt payments, particularly for savings bond proceeds which, according to Treasury estimates, would provide \$1.5 million in savings monthly if remitted promptly. By delaying the assessment, the Bureau missed the full benefit of prompt remittance. Still, payments were made for the savings bonds issued by agents and those not promptly remitting sales proceeds received dual compensation.

Unjustified waivers and slower collection of assessments

The Bureau has begun to assess interest for late remittances made after September 1981. We found, however, that it sometimes waived, for poor reasons, the amounts assessed. For example, it has waived amounts when agents said they were unaware of the interest assessment program or that their accounting procedures made it impossible to meet remittance deadlines. By May 12, 1982, waivers totaling around \$87,000 had been granted.

Bureau officials said the number of waivers granted since January 1982 have been declining. This may be the case; however, we noted that the Bureau continued to grant waivers for unacceptable reasons. For example, in March 1982--some 7 months after it began assessing interest on late remittances--the Bureau granted a waiver to an agent for more than \$2,000 when the agent claimed unawareness of the regulations requiring prompt remittance. Bureau officials acknowledged that the criteria for granting waivers has not changed.

The issuing agents were advised that penalty interest would be assessed in an early 1979 Treasury publication, "Statement of Rules Governing Remittance of Proceeds of Sales of United States Savings Bonds." In addition, the Bureau held an interest assessment awareness program for all the Federal Reserve banks and branches in May and June 1981 and instructed them to inform their respective issuing agents about the plan to assess interest. We believe these actions were adequate to notify the Bureau's agents of the intent to assess penalties on their late remittances.

Even when assessments are not waived, the Bureau is very slow in collecting the interest penalties from issuing agents. To illustrate, the Bureau had assessed penalties totaling about \$319,000 by May 1982, but had collected only about \$184,000, or about 58 percent, of that amount. Our analysis of the uncollected amount as of May 1982 showed that most of it had been due for more than 30 days and most of the amounts assessed in September 1981 still had not been collected.

Federal Reserve banks and branches did not comply with assessment requirements

Many large companies use Federal Reserve banks and branches to issue savings bonds to their employees through payroll savings plans. Some companies also use a book-entry approach to selling bonds, whereby records are established showing amounts invested by employees in savings bonds. In the book-entry system, the companies should remit sales proceeds to the U.S. Treasury when an employee accumulates enough funds to purchase a specific type of savings bond. The Federal Reserve banks and branches are responsible for assessing interest on late remittances for either the bonds they issue for agents or the book-entry accounts they service for agents.

We noted that the banks and branches--like the Bureau itself--were not assessing all issuing agents with interest for the late remittance of sales proceeds as required. For example:

--The New York Federal Reserve Bank had not assessed interest on a late remittance of funds by one large book-entry system agent. Consequently, the agent usually remitted sales proceeds several days late. Based on prevailing quarterly interest rates, we estimate the government has lost \$435,886 in interest from this agent for the period December 1980 through January 1982.

--The same bank also validated and issued bonds for 55 agents, a common practice nationwide, but did not assess interest on late payments for the bonds. For example, the bank did not assess about \$8,800 in interest over a 4-month period during which sales proceeds were remitted late by one agent.

New York Federal Reserve Bank officials told us they did not have time to assess interest on late payments for bonds the bank printed for issuing agents. They expressed the belief that other Federal Reserve banks similarly did not assess interest on late payments.

A Bureau official said the Bureau could not identify all instances in which agents selling bonds under the book-entry approach had remitted sales proceeds late. According to him, the Bureau monitors only 5 out of 56 agents who sell savings bonds under that method, and procedures provide for the Federal Reserve banks and branches to compute, collect, and report interest assessments for the remaining 51 agents, as well as for the agents for which the banks issue bonds. Bureau officials acknowledged that they were not monitoring the Federal Reserve's activities to ensure compliance with the prescribed procedures.

AGENTS ALLOWED FREE OR LOW-COST USE OF BORROWED MONEY

Over the years, savings bond interest rates have been much lower than those paid on other types of investments, especially in the early months of the investment. We noted a Bureau practice that provides issuing agents with free or low-cost use of money invested in savings bonds.

This happens when relief is granted for savings bond stock shortages that are later found to have been sold by agents. In such cases, the Bureau establishes a sales price that includes any interest it had to pay in redeeming the bonds if the interest was over \$100. If the interest is under \$100, the Bureau asks only for the sales price and foregoes collection of interest and any penalty for late remittance.

The Bureau's only rationale for this practice was that it had been in effect for years and had never become an issue, since no significant monetary losses had resulted from it. The Bureau

does not have records showing the amounts of losses attributed to the practice. Our tests of collections from agents suggest that relatively small amounts have been lost so far by the practice. However, we believe the practice could lead to some large losses if it became widely known.

QUESTIONABLE RELIEF GRANTED FOR MONETARY LOSSES

During our review the Bureau, with questionable authority, granted an issuing agent relief from monetary losses associated with the theft of bond stocks by one of its employees. In doing so, it expressed a rationale that would make it difficult to hold agents liable for future monetary losses.

Relief exceeded delegated authority

Federal agents' efforts to collect debts owed to the federal government are covered by the Federal Claims Collection Act of 1966 (31 U.S.C. 3711). That act requires the Comptroller General and the Attorney General to issue joint regulations implementing the law, which they have done in the Code of Federal Regulations entitled: "The Federal Claims Collection Standards" (4 CFR 101-105).

The codified regulation has the force and effect of law. It says that federal agencies are responsible for debts due the government from their operations and requires a series of actions to attempt collection. When the specified actions fail, the agencies have authority to settle losses totaling \$20,000 or less, in accordance with 4 CFR standards.

Under the law (31 U.S.C. 3125), the Bureau has specific authority to grant relief to owners of securities for any reported losses, thefts, destructions, mutilations, or defacements when the securities are identified by number and description. It also has specific authority to grant paying agents relief for losses related to their redemptions of savings bonds (31 U.S.C. 3126(a)). However, it has no express authority to grant relief for losses by agents collecting money on behalf of accountable officers with the Bureau.

During our review, we found that the Bureau had granted an agent--the Sears Bank and Trust Company--relief from responsibility for monetary losses associated with stock thefts by one of its employees. The case involved a theft of unissued bond stock with a face value of \$453,000 by a Sears employee from a locked cabinet with controlled key access. The employee simply recorded the number of the cabinet and arranged to have a duplicate key made. The employee was later caught, and all but about \$188,000 of the stock was recovered uncashed. At the time the Bureau granted the agent relief from the loss, it had already redeemed more than \$41,000 of the stolen bonds and it may have to pay for the remaining \$147,000 in stock if they are redeemed.

The Bureau decided that relief should be granted on the basis that the agent's negligence did not contribute to the loss. We disagree because the agent was holding the bonds in a key lock safe--a type that does not provide acceptable security for even small amounts of petty cash. Moreover, it is common practice for the bonds to be kept in combination lock safes and sent to agents via registered mail or armored carriers. The agent should have been aware of all these practices and approaches to safeguard the unissued bonds when it signed the trust agreement for receiving the bond stock on consignment.

Impact of decision on future losses

Each issuing agent must sign a trust agreement before it receives blank savings bond stock for sale. Under the trust agreement, an agent assumes "responsibility for all acts of its officers and employees in the custody, sale, and issue of savings bonds, and in accounting for proceeds of their sale." The Bureau's position paper on the Sears case recognized that the trust agreement itself suggests the agents will be held strictly liable for any monetary losses the federal government might incur from actions of the agents' employees.

The Bureau's position paper, however, concluded that a finding of negligence should have been required before the agents were held liable for losses, because its guidance to the agents, incorporated by reference in the trust agreement, suggested that a finding would be the basis for holding them liable for losses. It also noted that its past practice was to hold issuing agents liable for losses resulting from their activities only when negligence was proven. In addition, a negligence standard is prescribed by statute for paying agents.

The standard of liability for issuing agents should not be the same as that imposed on paying agents that have more limited responsibilities in redeeming bonds. The redemption responsibilities are principally to make sure bonds are presented for payment by registered owners and correct amounts are paid out. Such responsibilities involve basing disbursements on the receipt of appropriate support documents (issued bonds) and tying them to a specific agent. Issuing agents, on the other hand, are involved in activities that are creating obligations that the government must honor. They have responsibility for controlling savings bond stocks, collecting proper amounts upon stock sales, and promptly remitting amounts to the Treasury. Inefficiencies in their work can result in losses and thefts of stock that can be easily converted to valid government obligations. If issuing agents are not held strictly liable for any losses or thefts of bonds by their employees, they will have little incentive to safeguard the bonds and the government's interest will not be protected.

In our view, the current trust agreement can reasonably be interpreted to impose strict liability on issuing agents. However, the Bureau has concluded that any suggestion of a strict liability is overcome by other Bureau documents that refer to a negligence

standard. Accordingly, we believe that the issuing agreement and other relevant documents should be amended to specify that issuing agents will be strictly liable for all losses to the government resulting from actions of their employees, and amounts lost should then be collected under the provisions of the Federal Claims Collection Act.

RECEIVABLES ARE NOT EFFECTIVELY CONTROLLED
OR AGGRESSIVELY COLLECTED

As of March 1982, the Bureau had about \$1.7 million in receivables on its records. Because action has not been taken in the past 3 years to collect this amount, a substantial portion of the recorded receivables may not be collectible.

The actions to be taken in collecting debts are specified in the Code of Federal Regulations (4 CFR 101-105). These actions include, among other things, assessing interest on delinquent debts, reporting delinquent accounts to credit bureaus for collection, and collecting debts by offset when feasible. Of course, such actions are not possible until receivables are first aged to identify those in a delinquent status, and the collection efforts are more effective when automated systems are used to support them.

We found that the Bureau was still using manual records to control its receivables. The use of manual records usually makes management of receivables difficult, but these types of records really complicate the Bureau's efforts, since the total owed the Bureau at any time comprises many individual accounts. Apparently because of the large number of accounts, the Bureau's receivables had not been properly aged--the first step in determining collectibility. Bureau officials said they plan to automate the records within the next year.

We analyzed the receivables in Bureau records and found that all of them were being carried as collectible even though some were more than a year old. Other factors raising questions about the collectibility of receivables we reviewed were the lack of addresses and the identification of debtors. We did not attempt to estimate the amounts of receivables in the doubtful collection category because the receivable records are not well enough organized to permit estimating without considerable research. To illustrate, receivable records are controlled by the names of individuals or activities losing bonds rather than by the names of the actual debtors.

Another problem is that the Bureau has not used recognized approaches to collect its receivables. Before February 1979, the Bureau used the Secret Service as its collection agent. Apparently this approach was successful, since the Bureau's records showed that, over the years, about 82 percent of the recorded amounts had been collected. The Secret Service, however, apparently decided its collection activities should be limited to cases in which bonds were redeemed with forged or unauthorized endorsements. The Bureau took no action to collect these receivables through other means.

At the time of our review, it was holding more than 200 improper payments on bonds, totaling over \$47,000, in suspense for the Secret Service to collect. Included were about 130 bonds that had been redeemed or recorded in the Bureau's books for periods ranging from 2 to 10 years.

We noted that the Bureau was sending some demand letters to identified debtors, but the letters did not mention the possibility of the delinquent accounts being referred to collection bureaus, collected by offset, or charged penalty interest. The Bureau has in the past offset amounts owed it by debtors against the interest the Bureau owed them on Series E and EE bonds. However, the Bureau did not pursue this offset approach as a means of collecting amounts owed to it. We also noted that the Bureau did not use credit bureaus to collect delinquent amounts from debtors.

Finally, we noted that the Bureau had not assessed interest penalties on delinquent accounts it recognized. For example, in April 1982 the Bureau had accounts receivable totaling about \$437,000 that were more than 4 months old. At the interest rates prevailing then, the Bureau should have assessed interest penalties totaling about \$5,500 per month, but did not. In fact, it asked to be exempt from the requirement to collect interest on delinquent accounts. Its rationale for this was that the effort to assess and collect interest would not be cost-effective and that the assessment of penalties on issuing agents would reduce goodwill and cause irrevocable harm to the Savings Bond Program.

We disagree with the Bureau's rationale and believe the assessments should be made to encourage prompt payment of debts. Also, the Bureau must have controls to identify the delinquencies. Without controls, it will have no way of knowing which debtors, especially in the case of issuing agents, are not paying money they owe the government.

PAYMENT MADE FOR SERVICES WITHOUT REGARD TO QUALITY

The Bureau has paid agents in recent years (more than \$59 million in fiscal year 1981) to perform the services involved in selling and redeeming savings bonds, including providing documentation to support the related transactions. We noted that much of the documentation provided is incorrect. The Bureau spends considerable time correcting errors and supporting the corrections for the agents.

For example, based on Bureau officials' analyses and the Bureau's records, we estimate that between March 1981 and February 1982, agent error caused more than 200,000 adjustments and cost the federal government about \$530,000. The adjustments involved such things as correction of amounts (1) paid for individual bond redemption, (2) deposited for sales, and (3) furnished to paying agents to cover their redemptions.

We believe agents should be made aware of their errors so that they will establish better controls over the transactions they handle. The Bureau is doing this by providing agents with documents detailing the larger errors they make. We believe, however, that if agents were charged for their mistakes, they would take the necessary steps to reduce errors by training their personnel and strengthening their control of the program.

RECOMMENDATIONS

We recommend that the Secretary of the Treasury take action to:

- Ensure that interest penalties are assessed on issuing agents' late remittance of sales proceeds, as well as any overdue receivables, and that the assessed amounts are promptly collected unless circumstances warrant a waiver.
- Discontinue the Bureau's practice of allowing agents free or low-interest-cost use of the money realized from the sale of savings bonds.
- Amend the issuing agreement to specify that issuing agents are liable for all monetary losses related to redemption of savings bond stock that is lost or stolen by their employees, and to recover any such monetary losses that develop.
- Explore with the Department of Justice the possibility of recovering the losses from the Sears case, notwithstanding the grant by Treasury of relief from liability.
- Institute collection action against the bank employee convicted of the theft of bond stock, pursuant to the Claims Collection Act and implementing standards.
- Have receivables resulting from the Bureau's operation properly managed and aged and aggressively collected.
- Charge agents for correcting their errors when this appears to be a feasible approach to improve the quality of their work in handling sales, redemptions, and related transactions.

AGENCY COMMENTS AND ACTIONS

In discussing our findings with us, Bureau officials emphasized the desirability of the Bureau maintaining a favorable working relationship with its agents, and their belief that some concessions are necessary to keep agents in the program. We recognize this, but are concerned that the Bureau's actions discussed in this chapter, when taken collectively, could be the underlying reason why issuing agents are not exercising proper control over the blank savings bond stocks and are not promptly remitting sales proceeds. They have little incentive, for example, to hold down stock levels or exercise good physical controls if they are not held accountable

for monetary losses related to their operations. On the other hand, they have a reverse incentive to report sales proceeds late when the money can be borrowed at little or no cost and without penalty.

In commenting on our recommendations, the Department of the Treasury said that the Bureau will study and identify procedural changes necessary to generate faster collections from agents. Our discussions with Bureau officials confirmed that emphasis will be placed in this area.

The Department indicated that the practice of allowing agents free use of sales proceeds would be discontinued. It also said that actions were underway to have automated capability to control the Bureau's receivables by December 1983. It said the Bureau would take action to exercise proper control over receivables, and our discussions with Bureau officials confirmed that they plan to aggressively collect the receivables by appropriate means, including offset when feasible.

Bureau officials expressed some concern, however, about our recommendation to have agents pay the Bureau's cost of correcting their errors. Their concern was about the impracticality of devising a charge to recover the cost of correcting each agent's errors. We recognize that this would be difficult, but we believe the costs should be passed on to agents with a history of errors in their transactions. This would encourage better quality work on the part of such agents. Bureau officials acknowledged that this approach might have merit for further study.

With regard to our view that the Bureau should not have granted relief to the Sears Bank and Trust Company for unissued bonds stolen by one of its employees from a key-locked cabinet, the Treasury Department said that our concerns had prompted it to reexamine its policy. After its own review, Treasury will have the Justice Department also review the position taken.

CHAPTER 4

ACCOUNTING PRACTICES INCONSISTENT

WITH LAW AND RECOGNIZED PROCEDURES

Operation of an agency's accounting system should be consistent with applicable laws and Comptroller General principles, standards, and related requirements. When this is the case, the system should be capable of producing the financial information needed by its management and by any external sources exercising control over it, such as the Congress. We found the Bureau's system was producing incomplete and inaccurate data on the savings bond operation because of several practices not in conformity with applicable laws and recognized accounting practices.

CASH BASIS ACCOUNTING USED TO RECORD ACTIVITIES

It is widely accepted that the cash basis of accounting is inadequate for significant activities, since it involves recording transactions only when payments are made or received. In recognition of this, the law (31 U.S.C. 3512(b)) requires federal agencies to use accrual basis accounting. Under the accrual method, the agencies recognize revenue in the period earned and expenses and related liabilities in the period incurred. We found three areas in which the Bureau's practice was cash basis accounting rather than the required accrual basis.

One area was the assessment of penalty interest on late remittance of bond proceeds. When the Bureau started the assessments in September 1981, it decided not to record any related receivables when interest was earned and bills prepared. Instead, it would record revenue when it was received from agents. According to Bureau officials, the cash basis of accounting was to last for a trial period of 6 months, until about March 1982. When our field work was completed in June 1982, however, the cash basis method was still being used. At the end of May, the unrecorded assessments not collected totaled more than \$600,000. We believe the Bureau should act immediately to account for assessments on an accrual basis, since this is required by law and is necessary to provide the data for proper management of receivables. Moreover, the only extra effort involved would be to record amounts billed the agents as receivables in the general ledger and to periodically age the amounts along with other Bureau receivables.

The second area was the redemption of issued and unissued savings bonds for which the Bureau has granted relief on the basis that the bonds were lost, stolen, or inadvertently destroyed. Since the Bureau has either (1) already made payments to settle the relief claims, or (2) has not received sales proceeds, the redemption of these bonds creates a receivable that the Bureau should collect when possible. Considerable research is required on each of the questionable redemptions to identify the debtor. During the research effort, the bonds are not reconciled as receivables but

are controlled through a referral ticket held in a suspense file. All the bonds held in suspense are said to be recorded as receivables, except in cases where research efforts establish that issuing agents actually sold the bonds on which relief was granted. According to Bureau officials, the issuing agents are instructed to send in the sales proceeds and they have done so in most cases. We could not verify this because of the absence of the necessary records.

Once the Bureau sets up a receivable for redeemed bonds on which relief has been granted, it records the receivables in manual ledger accounts. At the end of each month, it records the amount of the erroneous redemptions. When this entry is made, an entry is also made to increase the funds available in the appropriation for the public debt principal, even though no money was received. The receivables then remain in the control account until they are collected from debtors or written off as losses to the Payment of Government Losses in Shipment Fund.

We believe receivables should have been charged to the Government Losses in Shipment Fund when they are dropped from the appropriation for redeeming the public debt. Otherwise, the funds available in the Bureau's appropriation accounts from redeeming the debt will always be overstated.

We noted that from the inception of the program through April 1982, the Bureau had redeemed approximately \$35 million in lost, stolen, forged, or counterfeited bonds for which relief was previously provided. Apparently, the Bureau handled all those redeemed bonds under the cash basis approach, first charging amounts to the suspense account instead of promptly setting up receivables to control collection efforts. The Bureau's records do not contain the data necessary to establish the adequacy of efforts to recover this amount. They do show that only about \$5 million of the amount was written off as uncollectible to the Payment of Government Losses in Shipment Fund. This implies that the remaining \$30 million was collected by the Bureau and deposited in appropriate fund control accounts.

The third area was the Bureau's redemption of Series E and EE savings bonds on which it has no documentation of the sales proceeds being received. We noted during our review that the Bureau was holding in the suspense account about 19,000 redeemed bonds valued at \$1.5 million. A Bureau official told us that some of the bonds had been sold by agents who did not remit sales proceeds. Other redeemed bonds were said to be related to cases in which agents had submitted sales proceeds without providing related sales documents. We found that action had not been completed to (1) identify the bonds on which sales proceeds had been actually received, or (2) establish receivables for the other bonds, even though many of them had been redeemed for many months and some for several years. The Bureau held these redemptions "open" for the extended periods presumably because it believed the amounts would

eventually be collected. In addition, Bureau officials assigned low priority to the research efforts necessary to properly classify the amounts.

SIGNIFICANT AMOUNTS OF RECEIVABLES
AND PAYABLES RECORDED IN SAME ACCOUNT

The accrual accounting method enables an activity to establish separate accounts for its assets, including the receivables it should collect, and for its liabilities, which are the amounts it owes to others. The law (31 U.S.C. 3512) specifically requires federal agencies to maintain their systems so as to show assets, liabilities, and costs of operation. We noted a Bureau activity in which identified receivables and payables were recorded in the same account; consequently, accounting records were not readily available to establish whether payments and collections were actually made on transactions involving significant amounts.

In this activity, the Bureau recorded adjustments for agent errors in an account classified as a "miscellaneous liability account" in the Bureau's general ledger. The account, however, neither specifically identified receivables due the government nor amounts owed by it to agents or former bondholders, because individual receivables and payables were offset against each other in arriving at the amount to be recorded. The amounts shown in the account have usually represented an increase to the federal government's cash account, which is maintained by Federal Reserve banks and branches. This could erroneously suggest the Bureau has collected additional money from agents.

Once the banks and branches accept the charges, the Bureau drops accountability for the individual adjustment and assumes that those activities will either refund or collect money as warranted by the individual adjustment provided to them. We were told that the banks and branches promptly processed adjustments for agents having reserve accounts with them. For collections when an agent did not have a reserve account, the collection activity involved sending a notification to the agent for amounts due and holding the adjustment in suspense until payment was made.

The Bureau's records do not readily provide the data to estimate the extent to which receivables and payables have been misstated by the Bureau's offset practice, but evidence suggests it is substantial. For example, the daily amount recorded for the adjustments in April 1982 totaled about \$5.5 million. This amount usually reflected a net income to Treasury's accounts, but the amount of receivables would be understated to the extent they were offset by the payables.

We brought this deficiency to the attention of Bureau officials in early 1981, and it was later discovered by the Office of Management and Budget during work in the Bureau's debt collection efforts. At the insistence of that office, the Bureau agreed to

establish separate receivable accounts for the adjustments. However, they had not been established by the time our field work was completed in June 1982.

LOSSES CHARGED TO ACCOUNT
WITH INSUFFICIENT FUNDS

The Bureau charges all monetary losses it has decided to write off to the Payment of Government Losses in Shipment Fund. The small amount in the fund is insufficient to cover the monetary losses the Bureau has already incurred or should expect to incur. Also, it appears that the Congress has not been fully advised of how extensively the fund is used to cover losses associated with savings bond sales and redemptions.

The fund is a governmentwide account used to cover losses associated primarily with shipments of government property such as coins, currency, and securities, and certain losses incurred by the U.S. Postal Service. The Bureau has also used the fund to cover all types of losses associated with both the sale and redemption of savings bonds, even though the budget appendix annually submitted to Congress says the fund is used to cover "... losses in connection with the redemption of savings bonds." The appendixes have given no indication of the amounts of actual and expected losses under the program. For example, the fiscal year 1983 budget appendix shows estimated losses to be around \$200,000 for fiscal years 1982 and 1983. The fund is also under the control of another Treasury activity, the Bureau of Government Financial Operations.

The fund is operated essentially as a working capital fund which also receives direct appropriations upon request. At the time of our review, the fund had only \$153,400 to cover losses associated with savings bonds. However, the Bureau had possibly around \$3 million in recorded and unrecorded receivables that developed from its redemption of some savings bonds on which sales proceeds were not received. This amount is made up of savings bonds that have been redeemed for years. For example, many of the securities were redeemed more than 2 years ago and one was redeemed more than 10 years ago. Also, the receivables contain amounts that have not been related to a specific debtor. Thus, a substantial portion of the amount should be recorded as probable losses. The \$153,400 available in the fund is obviously not sufficient when other possibilities for monetary losses are considered.

The other possible monetary losses are related to the large amounts of relief the Bureau has granted for issued and unissued savings bonds that have been reported as lost, stolen, or inadvertently destroyed. Since program inception, the Bureau has apparently granted relief for bonds with a redemption value of about \$173 million, of which about \$40 million had been redeemed at the time of our review. The Bureau's records indicate that it incurred monetary loss of about \$5 million for bonds redeemed on which relief had been granted. The Bureau still has about \$133 million in outstanding savings bonds (at redemption value) on which a significant amount of relief--more than \$51 million--was granted in the

past 5 years. Experience shows that some of the bonds will be redeemed, especially in those cases when relief was granted for bonds reported as lost or stolen by individual owners or issuing agents. The extent of the possible losses should be estimated and provided to the Congress in the budget submission for the Payment of Government Losses in Shipment Fund. We found that this was not being done and information was not readily available to allow us to establish the amount of expected losses.

The Congress should also be advised in budget submissions of the extent to which the fund has been used to pay losses related to savings bond sales and redemptions. We believe this would serve a useful purpose, since it is not clear whether authorizing legislation and related history intended for the fund to be used in the manner it has been.

REQUIRED REPORTS NOT SUBMITTED TO GAO

All federal agencies are required to report to us any losses they incur that exceed \$600 from any single event or series of related events.¹ The purpose of this requirement, which is spelled out in our guidance to federal agencies (7 GAO 28.14), is to provide data we need to discharge the account settlement responsibility imposed on us by law (31 U.S.C. 3526).

We noted that internal regulations drafted by the Bureau recognized the requirement to report to us any large losses incurred in the Savings Bond Program. However, we found only a few cases where losses of \$300 or less have been reported to us in a recent 3-year period. During the same approximate period, the Bureau recognized more than 110 individual losses exceeding \$600 which were not reported.

UNDERPAYMENTS TO BOND HOLDERS RETURNED TO PAYING AGENTS

The Bureau must maintain records to show that its disbursements are made to parties to which the government has valid obligations. The records also must contain sufficient evidence to show whether the government has fully satisfied the obligations in the event the parties file a claim against the government. We noted a Bureau disbursement practice that (1) did not ensure that proper parties were receiving the money for underpayments by agents in redeeming bonds and (2) did not provide the records necessary to prove that the government's related liability was satisfied.

The practice is the Bureau's method of making adjustments in cases when paying agents were found to underpay bondholders. In such cases, the government is liable to the bondholder for any underpayment. The Bureau has found it uneconomical to research any error amounting to \$5 or less, and such transactions are recorded

¹This was subsequently changed to \$750.

in a "small difference account." If the amount is greater than \$5, the Bureau refunds the money to paying agents redeeming the bond under the assumption they will return it to the former bondholder. The Bureau receives no assurance that this is done, however, since it does not require the agents to submit evidence of the bondholder actually receiving the money. The absence of such records also precludes the Bureau from having records readily available to settle any claims filed by bondholders for underpayments.

The Bureau has two alternatives if it is to continue the practice in question. One is to require the paying agents to furnish records showing that payments were made to bondholders. The other is for the agents to retain the records for the retention period (6 years, 3 months) specified for records supporting federal agencies' disbursements and collections. Neither of these alternatives appears desirable, however, when one considers that the Bureau has all the data necessary to refund the underpayments to the bondholders. The Bureau must furnish its agents with copies of documents essential to make the refunds. The cost of providing this service would be eliminated if the Bureau refunded money directly to the person entitled to it--the underpaid bondholder. If additional costs are required to make the refunds, we believe the related amounts should be deducted from the fees agents are paid for redeeming the bonds.

The Bureau's records do not show amounts of bond redemption underpayments that have been refunded to paying agents rather than to bondholders. We did not attempt to make estimates because the necessary data were not readily available.

RECOMMENDATIONS

We recommend that the Secretary of the Treasury:

- Require the use of accrual basis accounting for all activities related to savings bonds, including the assessment of penalty interest and any redemption of savings bonds that results in money being owed to the government.
- Make sure the Bureau properly uses the separate accounts for receivables and payables developed in the Bureau's efforts to correct agents' errors.
- Have monetary losses reported as required by regulation.
- Refund amounts of bond redemption underpayments directly to the bondholders and recover any costs of doing this from the agents responsible for the underpayments.
- Fully advise the Congress of activities in the Payment of Government Losses in Shipment Fund, including the amount needed to cover existing and expected losses, and make sure the Bureau's accounting system is changed to properly recognize such losses.

AGENCY COMMENTS AND ACTIONS

In commenting on our draft report, the Bureau said it has begun a thorough examination of its accounts receivable practices and recordkeeping. It will emphasize identification of various changes that will lead to easier accessibility of pertinent data and complete disclosure of erroneous payments, potential loss items, recoveries from debtors, and uncollectible items written off. In its response to our recommendation that separate receivable and payable accounts be established for the debit and credit adjustments to correct errors by agents, the Bureau said such accounts were established in October 1982. Our followup work confirmed that the accounts have been established, but we did not try to ascertain whether they were being used properly.

On our recommendation that action be taken regarding the Payment of Government Losses in Shipment Fund, Bureau officials agreed on the need to act, but stated that further study is necessary to establish procedures for the use of this fund. We believe the Bureau should report on the funds necessary to cover losses already incurred.

Bureau officials expressed apprehension about our recommendation to refund underpayments by agents on bond redemptions made directly to registered owners of bonds. They said this might not always be possible, since many bonds are redeemed without the current address of the registered owner being provided. As an alternative, Treasury proposed to issue regulations (1) advising agents that they would be held liable for any claims relating to underpayments, and (2) requiring agents to return any amounts not reported to the owners. This alternative would be an improvement over the present approach to handling the refund. However, we believe the money should be returned directly to owners unless the Bureau finds this to be impractical. Bureau officials agreed to look into the possibility of paying individuals directly, particularly when large amounts of money may be involved, and consider the appropriateness of trying to recover funds that agents are unable to deliver.

SAMPLING RESULTS--PROJECTIONS TO UNIVERSE

In order to review the Bureau's network of approximately 44,000 issuing agents scattered throughout the United States, we selected a statistical random sample of a representative part of the universe. A sample size of 600 issuing agents was selected using a systematic random sampling technique. The sample size was chosen to provide a 95-percent confidence level. The results were used to develop the estimates shown in table 1.

Statistical sampling enables us to draw conclusions about a universe on the basis of information about a sample of that universe. The results from a statistical sample are subject to some uncertainty (sampling error) because only a portion of the universe has been selected for analysis. The sampling errors consist of two parts: confidence level and range. The confidence level is the degree of confidence that can be placed in the estimates derived from the sample. The range is the upper and lower limits between which the actual universe value will be found.

For example, a random sample of issuing agents' stock balances showed that the average of all agents' balances was 72.9 months of stock. Using a sampling error formula with a 95-percent confidence level, we can say that if all agents' balances were examined, the actual levels would be within plus or minus 13.7 months of the sample results. Thus, chances would be 95 in 100 that the average agent's balance would be between 69.2 (72.9 - 13.7) and 86.6 (72.9 + 13.9) months. The upper and lower limits (range) for all estimates presented in the report are shown in table 1.

TABLE 1Projection of Sample Results - To Issuing Agents.

<u>Description</u>	<u>Universe estimate</u>	<u>Range (95% confidence)</u>
Average agent's stock balance - months of stock on hand (based on sales)	72.9	59.2 to 86.6
Average agent's requisition amount - months of stock (based on sales and latest requisition amount)	26.9	13.5 to 40.3



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

FISCAL ASSISTANT SECRETARY

23 DEC 1982

Dear Mr. Campbell:

The recent GAO draft report on the United States Savings Bond Program presented a good many findings and recommendations and raised some complex issues. This letter describes the approach being followed in responding to GAO's concerns about controls over unissued bond stock, accounting systems, debt collections, and management practices. It also describes remedial actions directly applicable to some of the audit findings and current plans with respect to others. We will respond further as our analysis progresses and additional decisions are made.

Several audit findings and recommendations concern the quality and effectiveness of controls over bond stock consignment accounts. Several months ago, the Bureau of the Public Debt commissioned a study of savings bond operations. The information and recommendations to be produced by this study are directly related to the matters cited in the audit report: strengthening systems for recording, monitoring, and controlling agent accountability for consignments; improvements in the balancing and verification of agent inventories; application of independent physical audits; policy as to the size of the issuing agent network; terms of issuing agent qualification; and a reconsideration as to stocking low-volume agents. Also, the study group will examine and prepare a recommendation on the feasibility of centralizing stock consignment functions in the Bureau's Savings Bond Operations Office.

I have asked the Bureau to furnish me with recommendations this month as to the appropriate level of stock that agents should be permitted to carry and a plan for bringing agents into compliance, through attrition of inventories and stock recall, over a 6-month period. This will be a large undertaking, but the results should provide an immediate improvement in control. The Bureau will accelerate the study of the other matters mentioned above and furnish a schedule for deliveries of pertinent recommendations.

The \$22.5 million of unreconciled differences has been reduced to \$2.7 million and efforts will continue to account for the remainder. The reconciliation process has disclosed no evidence that any of the bonds in question have been improperly issued or redeemed, or misappropriated.

There were several audit recommendations on accounting systems and practices. I have instructed the Bureau to review its systems in the light of GAO's comments and adopt accrual accounting principles. Documentation relative to the Interest Assessment System is being prepared and will be furnished to

GAO as soon as possible. Also, we will review the criteria applicable to waivers of penalty interest on late remittances of bond issue proceeds and the general policy of not assessing penalty interest on accounts receivable. Our reconsideration of past practices will take into account the auditors' concerns and we hope to resolve the matter with you in the next few weeks.

It was recommended that separate receivable and payable accounts should be established for the debit and credit adjustments against agents. This was implemented by the Bureau in October 1982.

The development of an automated accounts receivable system is under way and scheduled for implementation in April 1983. Pursuant to GAO's recommendations we will provide for proper recording and aging of accounts receivable using this automated system. In addition, the Bureau has begun a thorough examination of accounts receivable practices and recordkeeping. In recognition of the need for improved controls, we will be identifying various changes leading to easier accessibility of pertinent data and complete disclosure of erroneous payments, potential loss items, recoveries from debtors, and uncollectible items written off.

In the area of debt collection, GAO recommends that penalty interest be assessed on all late remittances by issuing agents and on overdue receivables. This issue should be resolved shortly, as mentioned above. Also, the Bureau will identify and implement procedural changes as necessary to generate faster collections from agents. A description of these measures will be furnished to GAO. We are in the process of evaluating alternative debt collection practices, including the employment of credit bureaus, collection agencies, and offset arrangements, and decisions on implementation will be made in due course.

The report cites a practice whereby only the issue price is recovered from an agent for bonds redeemed after stock credit has been granted, if the accrued interest is less than \$100. The Bureau is preparing a recommendation to discontinue this longstanding practice, which I expect to approve.

Efforts will continue toward ensuring compliance with Treasury instructions for interest assessments against certain payroll accounts serviced by the Federal Reserve Banks. Although substantial progress is evident in recent months, this matter will be covered regularly in the Bureau's monthly Bank visitations and in special meetings as necessary.

One case is mentioned where GAO estimates that Treasury lost nearly \$436,000 in interest for the period December 1980 through January 1982. This is being researched and we will report on it as requested by Senator Percy.

There are some basic issues to be dealt with relating to the disposition of the Sears Bank and Trust Company case. In light of the GAO report, Treasury policy is being reexamined with respect to stock credit cases and the appropriate standard to be applied in determining liability of issuing agents. This review will be thorough and comprehensive, including an assessment by the Department of Justice as to whether a standard of absolute liability would be considered defensible from the standpoint of litigation. This reconsideration of Treasury policy will supplement other study efforts dealing with consignment accountability, stock losses by agents, and requests for stock credit, and also represents an appropriate response to GAO's concerns that the resolution of the Sears case would constitute a precedent for future similar cases.

A number of items in the report will require further investigation by the Bureau and/or consultation with the auditors to clarify the facts and determine whether action is warranted -- for example:

Requiring payroll agents to submit sales documents at the same time they remit sales proceeds -

Charging agents for Bureau costs in adjusting agent errors -

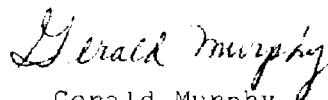
Reporting losses exceeding \$600 -

Refunding underpayments directly to bondowners and recovering costs from agents -

Use of the Government Losses in Shipment Fund.

I'm sure that these matters can be satisfactorily settled given reasonable time for review and joint discussions. The Bureau is instructed to pursue them with the auditors and I will advise you of their resolution.

Sincerely,



Gerald Murphy
Acting Fiscal
Assistant Secretary

Mr. W. D. Campbell
Acting Director
Accounting and Financial
Management Division
United States General Accounting Office
Washington, D.C. 20548



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

FISCAL ASSISTANT SECRETARY

JAN 25 1983

Dear Mr. Campbell:

This supplements my letter of December 23, 1982, and provides additional information as to steps being taken in response to GAO's concerns about controls over unissued savings bond stock.

I have approved a revised timetable for the Bureau of the Public Debt study of savings bonds operations. Revised target dates for the delivery of reports and recommendations from the Bureau are shown below.

- | | |
|--|-----------|
| Part 1: Strengthen and standardize
consignment systems | May 1983 |
| Part 2: Evaluate the size and structure
of the issuing agent network | June 1983 |
| Part 3: Consider feasibility of
centralizing consignment
functions | May 1984 |

Part 1 of the study calls for examination of the systems for recording, monitoring, and controlling agent accountability for consignments, achieving improvements in the balancing and verification of agent inventories, and consideration of the applicability of independent physical audits. A series of recommendations on agent stock levels, representing a partial product of Part 1, has already been approved. These will be described later in this letter.

Part 2 involves a reconsideration of policy as to the size of the issuing agent network, the terms of agent qualification, and whether or not to stock low-volume agents.

Part 3 deals with the GAO recommendations on centralizing the consignment functions in the Parkersburg Office. We believe that the outcome of the deliberations relative to Parts 1 and 2 will impact significantly on our recommendations for Part 3.

The amended timetable accelerates Part 2 by 14 months and Part 3 by 6 months.

The following recommendations, the first to come from the study, have been approved and are being implemented by the Bureau.

A. Stock Level Regulation

1. Agents will be allowed to have no more than a 3-month supply of unissued stock on hand. The maximum dollar level for

an agent will be an average based on sales data over a preceding 12-month period and should be recomputed annually.

2. A maximum supply level of \$6,250 will be assigned to newly qualified agents and agents with past sales history indicating a 3-month average of less than \$6,250. (face value)
3. Temporary exceptions to the maximum stock levels described above will be permitted in cases where an agent furnishes the Federal Reserve Bank adequate written justification in terms of genuine anticipation of significantly increased sales.

B. Agent Compliance

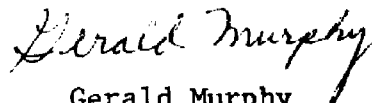
1. Maximum stock levels for each agent will be computed based on sales data for calendar year 1982.
2. The Federal Reserve Banks will be instructed to bring all agents into compliance with the maximum stock levels within a period of 6 months either through attrition of agent inventories or by recalling excess stock.
3. In recalling excess stock, control problems can be avoided by "spoiling" the stock prior to shipment. This is also the most desirable method insofar as recordkeeping and security are concerned. In some cases there may be significant cost associated inasmuch as spoiled stock cannot be used and is destroyed. The amount of such cost cannot now be estimated.

In order to minimize the costs related to spoilage of recalled stock, the Bureau may authorize an additional 3-months time for agent compliance with maximum stock levels in those cases where further attrition of inventories can reasonably be expected to reduce significantly the amount of stock to be recalled.

It is anticipated that the 6-month period for obtaining agent compliance can begin on February 1, 1983. The implementation of these recommendations should go a long way toward satisfying your concerns about stock control.

Enclosed for your information is a copy of the Bureau's letter to Senator Percy, responding to his request for information on an item brought up at the hearing on December 13, 1982.

Sincerely,



Gerald Murphy
Acting Fiscal
Assistant Secretary

Mr. W. D. Campbell
Acting Director
Accounting and Financial
Management Division
United States General Accounting Office
Washington, D.C. 20548

Enclosure



BUREAU OF THE PUBLIC DEBT

DEPARTMENT OF THE TREASURY

FISCAL SERVICE

WASHINGTON, D.C. 20226

January 21, 1983

Dear Mr. Chairman:

During testimony before the Subcommittee on Energy, Nuclear Proliferation and Government Processes on December 13, 1982, I was unable to comment factually on the specifics of an item reported by the General Accounting Office. You asked that I investigate and advise the Subcommittee as to a report that some \$435,000 of penalty interest had not been assessed against a savings bond agent for late remittances of bond issue proceeds in the period December 1980 through January 1982.

The agent in question is the General Electric Company, which operates a very large thrift-type, payroll deduction program on behalf of its employees. During the period in question, sales proceeds totaling \$122,367,111 were deposited with the Treasury's fiscal agent, the Federal Reserve Bank of New York. On average, the 14 payments involved were received 8.4 days beyond their respective due dates. The Interest Assessment Program was not operational until September 1981. Under that Program, penalty interest of \$135,776 could have been assessed for late remittances by the General Electric Company during the period September 1981 through January 1982.

In this case, latenesses may be attributed to two factors: first, a misunderstanding on the part of the Federal Reserve Bank concerning remittance deadlines relative to companies for which the Bank acts as issuing agent vs. remittance deadlines for companies which issue bonds themselves; and, second, an operational breakdown on the Bank's part in enforcing its conception of the rules for remittance.

The Bureau became aware of the situation early in 1982 and took prompt action to clarify and improve the enforcement of its remittance requirements. Since March 1982, General Electric has remitted sales proceeds on a timely basis. In addition, the Bureau has expanded the scope of its oversight of Federal Reserve Bank savings bond remittance processing to ensure that all Banks understand and properly carry out their responsibilities.

I would like to take this opportunity to reaffirm to the Subcommittee that the Bureau will carefully evaluate each of the recommendations contained in the General Accounting Office's

report and will take appropriate actions to assure that its activities are controlled in a manner which minimizes opportunities for fraud, waste, and abuse, and which accommodates the Government's cash management objectives.

Sincerely,

W. M. Gregg
W. M. Gregg
Acting Commissioner

The Honorable
Charles H. Percy
Chairman
United States Senate Subcommittee
on Energy, Nuclear Proliferation
and Government Processes
Washington, D.C. 20510

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