



November 2016

FINANCIAL AUDIT

Bureau of the Fiscal Service's Fiscal Years 2016 and 2015 Schedules of Federal Debt

GAO Highlights

Highlights of [GAO-17-104](#), a report to the Secretary of the Treasury

Why GAO Did This Study

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

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

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

View [GAO-17-104](#). For more information, contact Dawn B. Simpson at (202) 512-3406 or simpsondb@gao.gov.

November 2016

FINANCIAL AUDIT

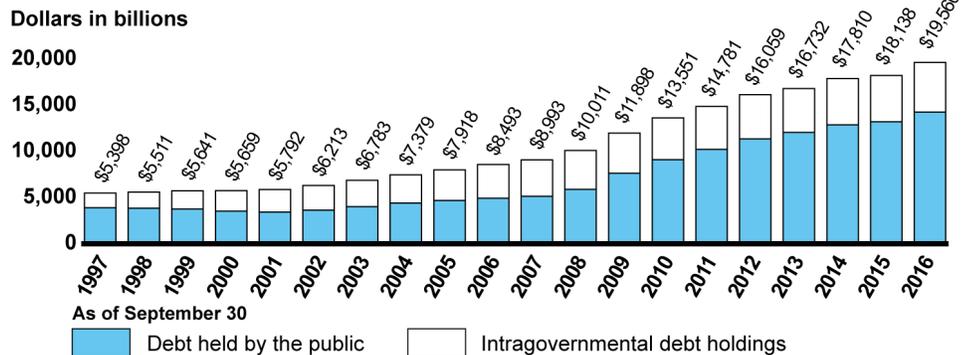
Bureau of the Fiscal Service's Fiscal Years 2016 and 2015 Schedules of Federal Debt

What GAO Found

In GAO's opinion, the Bureau of the Fiscal Service's (Fiscal Service) Schedules of Federal Debt for fiscal years 2016 and 2015 were fairly presented in all material respects, and Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016. GAO's tests disclosed no instances of reportable noncompliance for fiscal year 2016 with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt.

From fiscal year 1997, the first year of audit, through September 30, 2016, total federal debt managed by Fiscal Service has increased by 262 percent, and the debt limit has been raised 16 times, from \$5,950 billion to \$18,113 billion.

Total Federal Debt Outstanding, September 30, 1997, through September 30, 2016



Note: A small amount of total federal debt is not subject to the debt limit.
Source: GAO analysis of Bureau of the Fiscal Service information. | GAO-17-104

Because of delays in raising the debt limit, the Department of the Treasury (Treasury) deviated from its normal debt management operations and took a number of extraordinary actions—consistent with relevant laws—from March 16, 2015, through October 30, 2015, to avoid exceeding the debt limit. Many extraordinary actions taken by Treasury during this delay period resulted in federal debt securities not being issued to certain federal government accounts. Legislation temporarily suspending the debt limit was enacted on November 2, 2015, and Treasury subsequently restored the uninvested principal and related interest to the affected federal government accounts, thereby increasing the federal debt. The suspension of the debt limit is in effect through March 15, 2017, and if an increase in the debt limit is not enacted prior to this date, the debt limit will be increased by the change in qualifying federal debt securities outstanding on November 2, 2015, compared to those outstanding on March 16, 2017. As GAO has previously reported, delays in raising the debt limit have created uncertainty and disruptions in the Treasury market and challenges for Treasury debt and cash management. To avoid such disruptions and to help inform fiscal policy debate in a timely way, GAO has noted in reports related to the debt limit—most recently in July 2015—that the Congress should consider alternative approaches that better link decisions about the debt limit with decisions about spending and revenue at the time those decisions are made.

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Abbreviations

| | |
|--------------------------|--|
| Fiscal Service | Bureau of the Fiscal Service |
| FMFIA | Federal Managers' Financial Integrity Act |
| GDP | gross domestic product |
| Schedule of Federal Debt | Schedule of Federal Debt Managed by the Bureau of the Fiscal Service |
| Treasury | Department of the Treasury |

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November 10, 2016

The Honorable Jacob J. Lew
Secretary of the Treasury

Dear Mr. Secretary:

The accompanying independent auditor's report presents the results of our audits of the fiscal years 2016 and 2015 Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Schedule of Federal Debt). The independent auditor's report contains (1) our opinion that the Schedules of Federal Debt for the fiscal years ended September 30, 2016, and 2015, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles; (2) our opinion that the Bureau of the Fiscal Service (Fiscal Service) maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016; and (3) the results of our tests of Fiscal Service's compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements related to the Schedule of Federal Debt, which identified no instances of reportable noncompliance.

The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and Discounts managed by the Department of the Treasury's (Treasury) Fiscal Service, and include accompanying notes. As of September 30, 2016, and 2015, federal debt managed by Fiscal Service totaled \$19,560 billion and \$18,138 billion, respectively, primarily for borrowings to fund the federal government's operations. As shown on the Schedules of Federal Debt, these balances consisted of approximately (1) \$14,173 billion as of September 30, 2016, and \$13,124 billion as of September 30, 2015, of debt held by the public and (2) \$5,387 billion as of September 30, 2016, and \$5,014 billion as of September 30, 2015, of intragovernmental debt holdings.

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

public represents federal debt issued by Treasury and held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments. The majority of debt held by the public consists of marketable Treasury securities, such as bills, notes, bonds, floating rate notes, and Treasury Inflation-Protected Securities that are sold through auctions and can be resold by whoever owns them. Treasury also issues a smaller amount of nonmarketable securities, such as savings securities and State and Local Government Series securities.

As we have noted in previous years, Treasury reporting shows that foreign ownership of Treasury securities represents a significant portion of debt held by the public.¹ As of June 30, 2016, the reported amount of Treasury securities held by foreign and international investors represented an estimated 45 percent of debt held by the public. This percentage is close to the 47 percent of debt held by the public as of June 30, 2015, but considerably higher than the estimated 30 percent of debt held by the public as of June 30, 2001. Treasury estimated that the amount of Treasury securities held by foreign and international investors has increased from \$983 billion as of June 30, 2001, to \$6,281 billion as of June 30, 2016—an increase of \$5,298 billion.² Estimates of foreign ownership of Treasury securities are derived from information reported under the Treasury International Capital reporting system, not from the financial system used to prepare the Schedule of Federal Debt.³ These estimates are not reported on the Schedules of Federal Debt, and as such, we do not audit these amounts.

Intragovernmental debt holdings represent federal debt owed by Treasury to federal government accounts—primarily federal trust funds such as Social Security and Medicare—that typically have an obligation to invest their excess annual receipts (including interest earnings) over disbursements in federal securities. Most federal government accounts

¹GAO, *Financial Audit: Bureau of the Fiscal Service's Fiscal Years 2015 and 2014 Schedules of Federal Debt*, GAO-16-160 (Washington, D.C.: Nov. 13, 2015).

²Department of the Treasury, *Major Foreign Holders of Treasury Securities*, accessed November 3, 2016, <http://www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt>.

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

invest in special nonmarketable Treasury securities that represent legal obligations of the Treasury and are guaranteed for principal and interest by the full faith and credit of the U.S. government. The federal government uses the federal government accounts' invested cash surpluses to assist in funding other federal government operations. Unlike debt held by the public, intragovernmental debt holdings are not shown as balances on the federal government's consolidated financial statements because they represent loans from one part of the federal government to another. Under U.S. generally accepted accounting principles, when the federal government's financial statements are consolidated, those offsetting balances are eliminated.

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

We have audited the Schedule of Federal Debt since fiscal year 1997. Over this period, total federal debt has increased by 262 percent. Also during this period, the statutory debt limit has been raised 16 times, from \$5,950 billion to \$18,113 billion.⁵ Notably, delays in raising the debt limit have occurred in each of the last 6 fiscal years resulting in Treasury deviating from its normal debt management operations and taking extraordinary actions consistent with relevant laws to avoid exceeding the debt limit.⁶ During the last 4 fiscal years, total federal debt has increased by \$3,501 billion, or 22 percent, from \$16,059 billion as of September 30, 2012, to \$19,560 billion as of September 30, 2016. Of the total increase,

⁴For more information regarding the federal debt, see GAO, *Fiscal Outlook: Understanding The Federal Debt*, accessed November 3, 2016, http://www.gao.gov/fiscal_outlook/understanding_federal_debt/overview.

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

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

\$2,903 billion was from an increase in debt held by the public and \$598 billion was from an increase in intragovernmental debt holdings.

During fiscal year 2016, total federal debt increased by \$1,422 billion, consisting of a (1) \$1,049 billion increase in debt held by the public and (2) \$373 billion increase in intragovernmental debt holdings. For fiscal year 2016, a delay in raising the debt limit that began in fiscal year 2015 continued through October 30, 2015. Following the expiration of an earlier temporary debt limit suspension period, on March 16, 2015, Treasury began taking extraordinary actions consistent with relevant laws to avoid exceeding the debt limit.⁷ These extraordinary actions included suspending investments to certain federal government accounts. The Overview on Federal Debt Managed by the Bureau of the Fiscal Service (Overview) provides details on the extraordinary actions taken by Treasury from October 1, 2015, through October 30, 2015.

On Monday, November 2, 2015, the Bipartisan Budget Act of 2015 was enacted, temporarily suspending the debt limit from the date of enactment through March 15, 2017.⁸ After the start of the current temporary debt limit suspension period, Treasury restored the uninvested principal and interest resulting from Treasury's use of extraordinary actions to the affected federal government accounts in accordance with relevant laws, thereby increasing the federal debt. The amounts restored included uninvested principal and interest that existed as of the end of fiscal year 2015, which were appropriately not reported on the fiscal year 2015 Schedule of Federal Debt because securities had not been issued at that time to the affected federal government accounts. The Overview and note 5 to the Schedules of Federal Debt provide details on Treasury's restoration of uninvested principal and related interest subsequent to the start of the current temporary debt limit suspension period. The fiscal year 2016 increase in debt held by the public of \$1,049 billion was greater than the reported fiscal year 2016 federal deficit of \$587 billion primarily because of the above-noted restoration of principal and interest, as well as increases in the government's cash balance and federal direct student loans. If an increase in the debt limit is not enacted before the end of this suspension period, the debt limit will be increased by the change in

⁷The Temporary Debt Limit Extension Act had suspended the debt limit from February 15, 2014, through March 15, 2015, and, effective March 16, 2015, set the limit at the total face amount of debt outstanding on that date. Pub. L. No. 113-83, § 2, 128 Stat. 1011 (Feb. 15, 2014).

⁸Pub. L. No. 114-74, § 901, 129 Stat. 584, 620 (Nov. 2, 2015).

qualifying federal debt securities outstanding on November 2, 2015, compared to those outstanding on March 16, 2017, in accordance with the Bipartisan Budget Act of 2015.

As we have previously reported, the debt limit does not restrict the Congress's ability to enact spending and revenue legislation that affects the level of federal debt or otherwise constrains fiscal policy, but it does restrict Treasury's authority to borrow to finance the decisions already enacted by the Congress and the President.⁹ The United States benefits from the confidence investors have that debt backed by the full faith and credit of the United States will be honored. However, as we have also previously reported, delays in raising the debt limit have created uncertainty and disruptions in the Treasury market and challenges for Treasury debt and cash management. To avoid such disruptions and to help inform fiscal policy debate in a timely way, GAO has noted in reports related to the debt limit—most recently in July 2015—that the Congress should consider alternative approaches that better link decisions about the debt limit with decisions about spending and revenue at the time those decisions are made.¹⁰

After 3 years of declining deficits, the reported federal deficit increased for fiscal year 2016 to \$587 billion, up from \$439 billion for fiscal year 2015, which was the smallest recorded deficit since 2007. The deficits for the past 4 years and the need to refinance maturing debt meant that federal financing needs continued to grow over the period. Debt held by the public as a percentage of gross domestic product (GDP) of roughly 77 percent at the end of fiscal year 2016 was an increase from the roughly 74 percent at the end of fiscal year 2015. While today's relatively lower interest rates have kept interest costs down, interest rates are expected to increase as the economy continues to recover, resulting in increasing pressure on the budget. Over the longer term, debt held by the public as a share of GDP is expected to continue to grow as a result of the structural imbalance between revenue and spending driven on the spending side by demographics and rising health care costs. Increasing

⁹GAO, *Debt Limit: Market Response to Recent Impasses Underscores Need to Consider Alternative Approaches*, [GAO-15-476](#) (Washington, D.C.: July 9, 2015); *Debt Limit: Analysis of 2011-2012 Actions Taken and Effect of Delayed Increase on Borrowing Costs*, [GAO-12-701](#) (Washington, D.C.: July 23, 2012); and *Debt Limit: Delays Create Debt Management Challenges and Increase Uncertainty in the Treasury Market*, [GAO-11-203](#) (Washington, D.C.: Feb. 22, 2011).

¹⁰[GAO-15-476](#).

numbers of baby-boom generation members are becoming eligible for Social Security retirement benefits and for Medicare. In addition, health care spending has been growing faster than the overall economy over the past several decades and is expected to continue to grow at an increased rate as more members of the baby-boom generation retire and become eligible for federal health programs. The aging of the population and rising health care costs will continue to put upward pressure on spending and, absent action to address the growing imbalance between spending and revenue, the federal government faces an unsustainable growth in debt.

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

If you or your staff have any questions concerning this report, please contact me at (202) 512-3406 or simpsondb@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report.

Sincerely yours,



Dawn B. Simpson
Acting Director
Financial Management
and Assurance



Independent Auditor's Report

To the Commissioner of the Bureau of the Fiscal Service

In our audits of the fiscal years 2016 and 2015 Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Schedule of Federal Debt), we found

- the Schedules of Federal Debt for the fiscal years ended September 30, 2016, and 2015, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;
- the Bureau of the Fiscal Service (Fiscal Service) maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016; and
- no reportable noncompliance for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested related to the Schedule of Federal Debt.

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

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

In connection with fulfilling our requirement to audit the consolidated financial statements of the U.S. government, we have audited the Schedules of Federal Debt because of the significance of the federal debt to the federal government's consolidated financial statements.² The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and

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

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

Discounts managed by the Department of the Treasury's (Treasury) Fiscal Service, and include accompanying notes.³ We also have audited Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016, based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

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

Management's Responsibility

Fiscal Service management is responsible for (1) the preparation and fair presentation of the Schedules of Federal Debt in accordance with U.S. generally accepted accounting principles; (2) preparing and presenting other information included in documents containing the audited Schedules of Federal Debt and auditor's report, and ensuring the consistency of that information with the audited Schedules of Federal Debt; (3) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of Schedules of Federal Debt that are free from material misstatement, whether due to fraud or error; (4) evaluating the effectiveness of internal control over financial reporting based on the criteria established under FMFIA; and (5) providing its assertion about the effectiveness of internal control over financial reporting as of September 30, 2016, based on its evaluation, included in the accompanying Management's Report on Internal Control over Financial Reporting Relevant to the Schedule of Federal Debt in appendix I.

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

Auditor's Responsibility

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

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

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

internal control over financial reporting relevant to the Schedule of Federal Debt that are less severe than a material weakness.⁴

Definitions and Inherent Limitations of Internal Control over Financial Reporting

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

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

Opinion on the Schedules of Federal Debt

In our opinion, the Schedules of Federal Debt present fairly, in all material respects, Federal Debt Managed by Fiscal Service and the related Accrued Interest Payables and Net Unamortized Premiums and Discounts as of September 30, 2016, and 2015, and the related increases and decreases for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

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

Opinion on Internal Control over Financial Reporting

In our opinion, Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016, based on criteria established under FMFIA.

During our fiscal year 2016 audit, we identified deficiencies in Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt that we do not consider to be material weaknesses or significant deficiencies.⁵ Nonetheless, these deficiencies warrant management's attention. We have communicated these matters to management and, where appropriate, will report on them separately.

Other Matter

Other Information

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

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

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

Management's Responsibility

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

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

Auditor's Responsibility

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

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

Our tests for compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements disclosed no instances of noncompliance for fiscal year 2016 that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our tests was not to provide an opinion on compliance with laws, regulations, contracts, and grant agreements applicable to Fiscal Service. Accordingly, we do not express such an opinion.

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

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

Agency Comments

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



Dawn B. Simpson
Acting Director
Financial Management
and Assurance

November 3, 2016

Overview, Schedules, and Notes

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

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

Gross Federal Debt Outstanding

Federal debt managed by the Bureau of the Fiscal Service (Fiscal Service) comprises debt held by the public and debt held by certain federal government accounts (issued under 31 U.S.C. §§ 3101-3113), the latter of which is referred to as intragovernmental debt holdings. As of September 30, 2016 and September 30, 2015, outstanding gross federal debt managed by Fiscal Service totaled \$19,560 billion and \$18,138 billion, respectively.¹ The increase in gross federal debt of \$1,422 billion during fiscal year 2016 was due to an increase in gross intragovernmental debt holdings of \$373 billion and an increase in gross debt held by the public of \$1,049 billion. As Figure 1 illustrates, overall intragovernmental debt holdings and debt held by the public increased by \$598 billion and \$2,903 billion, respectively, from September 30, 2012 to September 30, 2016. The primary reason for the increases in intragovernmental debt holdings is the excess annual receipts (including interest earnings) over disbursements in the Social Security, Medicare, Military Retirement and Health Care, and Civil Service Retirement and Disability (CSRDF) trust funds.² The increases in debt held by the public are due primarily to total federal spending exceeding total federal revenues. There were delays in raising the debt limit in both fiscal years 2013 and 2015, which continued into fiscal years 2014 and 2016 respectively, during which the Department of the Treasury (Treasury) had to take extraordinary actions to meet the government's obligations as they came due without exceeding the debt limit. The extraordinary actions included (1) the suspension of investments in CSRDF, Postal Service Retiree Health Benefits Fund (Postal Benefits Fund), and the Exchange Stabilization Fund (ESF), (2) redeeming certain investments held by CSRDF earlier than normal, and (3) exchanging Treasury securities held by the CSRDF for securities issued by the Federal Financing Bank. Due to these extraordinary actions, intragovernmental debt holdings decreased by \$33 billion between September 30, 2012 and September 30, 2013 and also decreased by \$11 billion between September 30, 2014 and September 30, 2015. Once the delays in raising the debt limit ended, the uninvested principal and related interest were restored, thereby raising intragovernmental debt holdings, and normal debt management operations resumed.

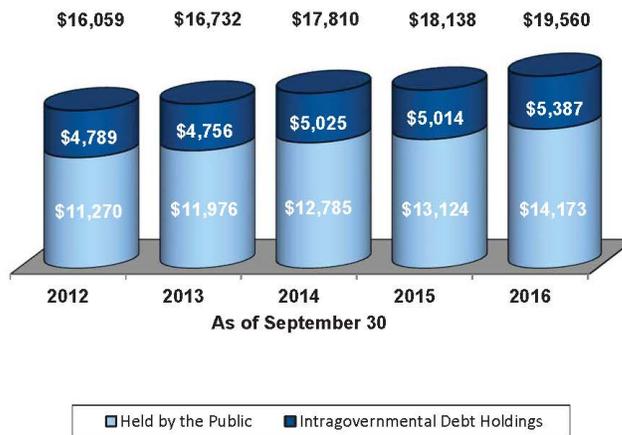
¹ Federal debt outstanding reported here differs from the amount reported in the Financial Report of the United States Government because of the securities not maintained or reported by Fiscal Service which are issued by the Federal Financing Bank and other specific securities issued outside the authority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

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

Gross Federal Debt Outstanding, cont.

On November 2, 2015, the Bipartisan Budget Act of 2015 (Public Law No. 114-74) was enacted which suspended the debt limit through March 15, 2017. Per the act, the debt limit will be increased on March 16, 2017 by the change in qualifying federal debt securities outstanding on November 2, 2015, compared to those outstanding on March 16, 2017. Gross federal debt (with some adjustments) is subject to a statutory debt limit. As of September 30, 2016 and September 30, 2015, outstanding debt obligations subject to the statutory debt limit were \$19,538 billion and \$18,113 billion, respectively.

Figure 1 Gross Federal Debt Outstanding
(in billions)



Interest Expense

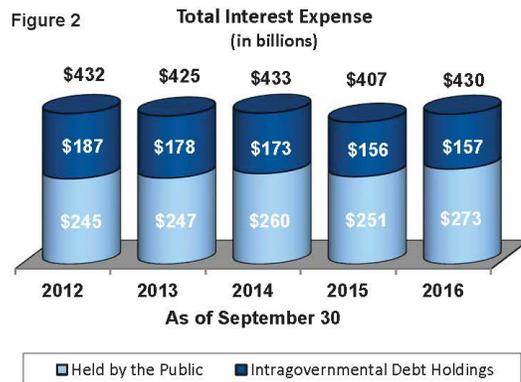
Interest expense incurred during fiscal year 2016 consists of (1) interest accrued and paid on debt held by the public or credited to accounts holding intragovernmental debt during the fiscal year, (2) interest accrued during the fiscal year, but not yet paid on debt held by the public or credited to accounts holding intragovernmental debt, and (3) net amortization of premiums and discounts. The primary components of interest expense are interest paid on the debt held by the public and interest credited to federal government trust funds and other federal government accounts that hold Treasury securities. The interest paid on the debt held by the public affects the current spending of the federal government and represents the burden of servicing its debt (i.e., payments to outside creditors). Interest credited to federal government trust funds and other federal government accounts, on the other hand, does not result in an immediate outlay of the Federal Government because one part of the government pays the interest and another part receives it. However, this interest represents a claim on future budgetary resources and hence an obligation on future taxpayers. This interest, when reinvested by the trust funds and other federal government accounts, is included in the programs' excess funds not currently needed in operations, which are invested in federal securities. For fiscal year 2016, interest expense incurred totaled \$430 billion; this consisted of interest expense on debt held by the public of \$273 billion, and \$157 billion in interest incurred for intragovernmental debt holdings.

As Figure 2 illustrates, interest expense decreased from fiscal year 2012 to 2013 primarily from a decrease in the average interest rates for Treasury notes, bonds, and Treasury Inflation-Protected Securities (TIPS). From fiscal year 2013 to 2014, total interest expense increased from \$425 billion to \$433 billion. This increase resulted from an increase of \$13 billion in interest expense on debt held by the public offset by a \$5 billion decrease in interest expense on intragovernmental debt holdings. The \$13 billion increase in interest expense on debt held by the public resulted from the overall increase in the outstanding debt held by the public offset by a decrease in the average interest rates for Treasury bonds and TIPS. The \$5 billion decrease in interest expense in intragovernmental debt holdings resulted primarily from the decrease in the average interest rates on intragovernmental debt holdings.

From fiscal year 2014 to 2015, total interest expense decreased from \$433 billion to \$407 billion. This decrease resulted from a decrease in interest expense on debt held by the public and intragovernmental debt holdings of \$9 billion and \$17 billion, respectively. The \$9 billion decrease in interest expense on debt held by the public primarily resulted from (1) a decrease in inflation adjustments and (2) the continued decrease in average interest rates for Treasury bonds and TIPS, offset by the overall increase in outstanding debt. The \$17 billion decrease in interest expense on intragovernmental debt holdings primarily resulted from (1) a decrease in inflation adjustments and (2) a decrease in the average interest rates on intragovernmental debt holdings.

Interest Expense, cont.

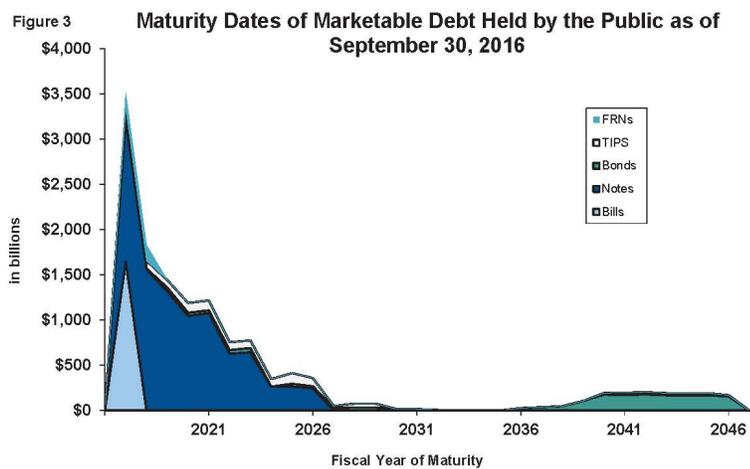
From fiscal year 2015 to 2016, total interest expense increased from \$407 billion to \$430 billion. This increase resulted from an increase in interest expense on debt held by the public and intragovernmental debt holdings of \$22 billion and \$1 billion, respectively. The \$22 billion increase in interest expense on debt held by the public primarily resulted from (1) an increase in the outstanding debt held by the public and (2) an increase in inflation adjustments. The \$1 billion increase in interest expense on intragovernmental debt holdings resulted from (1) an increase in outstanding intragovernmental debt holdings, (2) the restoration of interest to CSRDF and Postal Benefits Fund, and (3) an increase in inflation, which were offset by a decrease in the average interest rate. Average interest rates on principal balances outstanding as of September 30, 2016 and 2015, are disclosed in the Notes to the Schedules of Federal Debt.



Debt Held by the Public

Debt held by the public primarily represents the amount the Federal Government has borrowed to finance cumulative cash deficits. During fiscal year 2016, Treasury used the existing suite of securities to meet the borrowing needs of the Federal Government. Treasury increased its offerings of Treasury bills to help achieve the objective of lowest cost of funding over time and enhance market functioning and liquidity. These actions contributed to Treasury bills increasing by \$290 billion in fiscal year 2016 and to Treasury notes, bonds, TIPS, and Floating Rate Notes (FRNs) also increasing by \$258 billion, \$137 billion, \$74 billion, and \$47 billion, respectively in fiscal year 2016. As of September 30, 2016 and 2015, gross debt held by the public totaled \$14,173 billion and \$13,124 billion, respectively (see Figure 1), an increase of \$1,049 billion. This increase was primarily the result of borrowings needed to finance the government's fiscal year 2016 deficit. Due primarily to an increase in short term debt issuances, as compared to the prior year, the total dollar amount of activity for both borrowings and repayments of debt held by the public increased for fiscal year 2016.

As of September 30, 2016, \$13,638 billion, or 96 percent, of the securities that constitute debt held by the public were marketable, meaning that once the Federal Government issues them, they can be resold by whoever owns them. Marketable debt is made up of Treasury bills, Treasury notes, Treasury bonds, TIPS, and FRNs with maturity dates ranging from less than 1 year out to 30 years. Of the marketable securities currently held by the public as of September 30, 2016, \$7,969 billion, or 58 percent, will mature within the next 4 years (see Figure 3). As of September 30, 2016 and 2015, total marketable debt held by the public maturing within the next 10 years totaled \$11,838 billion and \$11,178 billion, respectively, an increase of \$660 billion.



Debt Held by the Public, cont.

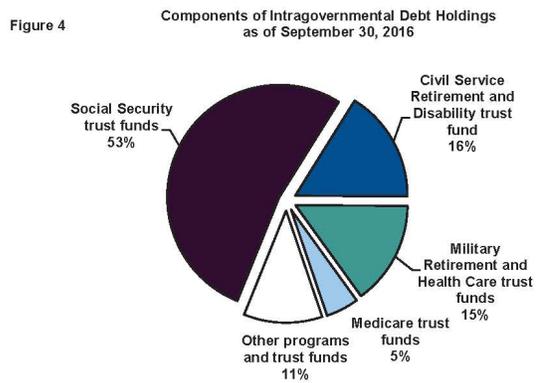
The Federal Government also issues to the public nonmarketable securities, which cannot be resold, and have maturity dates ranging from on demand out to 40 years. As of September 30, 2016, nonmarketable securities totaled \$535 billion, or 4 percent of debt held by the public. As of that date, nonmarketable securities primarily consisted of Government Account Series (GAS) securities totaling \$226 billion, savings securities totaling \$168 billion, and State and Local Government Series (SLGS) securities totaling \$109 billion. From fiscal year-end 2015 to 2016, total nonmarketable securities increased from \$292 billion to \$535 billion. This increase is primarily the result of the suspension of investments to the Government Securities Investment Fund (G-Fund) of the federal employees' Thrift Savings Plan and SLGS related to the extraordinary actions taken due to the delay in raising the debt limit that continued to exist as of September 30, 2015. On November 2, 2015, the Bipartisan Budget Act (Public Law No. 114-74) was enacted suspending the debt limit through March 15, 2017. On November 2, 2015, \$205 billion was restored to the G-Fund. Issuances of new SLGS securities resumed on November 3, 2015.

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

Intragovernmental Debt Holdings

Intragovernmental debt holdings represent balances of Treasury securities held by over 240 individual federal government accounts with either the authority or the requirement to invest excess receipts in special U.S. Treasury securities that are guaranteed for principal and interest by the full faith and credit of the U.S. Government. Intragovernmental debt holdings primarily consist of balances in the Social Security, Medicare, Military Retirement and Health Care, and Civil Service Retirement and Disability trust funds. As of September 30, 2016, such funds accounted for \$4,777 billion, or 89 percent, of the \$5,387 billion intragovernmental debt holdings balances (see Figure 4). As of September 30, 2016 and 2015, gross intragovernmental debt holdings totaled \$5,387 billion and \$5,014 billion, respectively (see Figure 1), an increase of \$373 billion. This increase is primarily the result of (1) an increase in the Military Retirement and Health Care trust funds of \$68 billion, (2) an increase in the Highway Trust Fund of \$57 billion, (3) an increase in the Social Security trust funds of \$34 billion, (4) an increase in the Federal Housing Administration, Mutual Mortgage Insurance Capital Reserve Account of \$22 billion, and (5) the suspension of investments to the CSRDF and Postal Benefits Fund related to the extraordinary actions taken due to the delay in raising the debt limit that continued to exist as of September 30, 2015. On November 2, 2015, the Bipartisan Budget Act of 2015 (Public Law No. 114-74) was enacted suspending the debt limit through March 15, 2017. As a result, on the same day, \$143 billion and \$5 billion were reinvested into the CSRDF and Postal Benefits Funds, respectively, which included amounts uninvested as of September 30, 2015.

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



Significant Events in Fiscal Year 2016

Delay in Raising the Statutory Debt Limit

A delay in raising the statutory debt limit, which began on March 16, 2015, continued into fiscal year 2016. From October 1 through October 30, 2015, Treasury departed from its normal debt management procedures and invoked legal authorities to avoid exceeding the debt limit. Extraordinary actions taken by Treasury during this period to ensure the debt limit was not exceeded included (1) suspending investments in the G-Fund, CSRDF, Postal Benefits Fund, and ESF, (2) redeeming certain investments held by CSRDF earlier than normal, (3) suspending new issuances of SLGS securities, (4) exchanging \$2.7 billion of Treasury securities held by the CSRDF for securities issued by the Federal Financing Bank, and (5) postponing the 2-year note auction originally scheduled for Tuesday, October 27, 2015.

On November 2, 2015, the Bipartisan Budget Act (Public Law No 114-74) was enacted, which suspended the statutory debt limit through March 15, 2017. Treasury discontinued its use of extraordinary actions and resumed normal debt management operations. On November 2, 2015, and in accordance with relevant laws, Fiscal Service restored uninvested principal amounts to the G-Fund, CSRDF, and Postal Benefits Fund in the amounts of \$205 billion, \$143 billion, and \$5 billion, respectively. ESF was fully reinvested on October 21, 2015, and remained fully invested through October 30, 2015. There is no legislation which allows the restoration of interest to ESF. In accordance with relevant laws, Fiscal Service restored the interest related to the uninvested principal during the period March 16, 2015 through October 30, 2015, to the G-Fund on November 3, 2015, the next interest payment date, in the amount of \$1.72 billion. Interest related to the uninvested principal during the period of March 16, 2015 through October 30, 2015, for CSRDF and Postal Benefits Fund were restored on December 31, 2015, the next semi-annual interest payment date, in the amounts of \$0.94 billion and \$0.03 billion, respectively.

Highway Trust Fund Appropriation

On December 4, 2015, the Fixing America's Surface Transportation (FAST) Act was signed into law becoming Public Law No. 114-94. This law provided appropriations totaling \$70 billion to the Highway Trust Fund in fiscal year 2016. The funds were received in January 2016 and invested in the Highway Trust Fund Highway Account and the Highway Trust Fund Mass Transit Account in the amounts of \$51.9 billion and \$18.1 billion, respectively.

Historical Perspective

Federal debt outstanding is one of the largest legally binding obligations of the Federal Government. Nearly all the federal debt has been issued by the Treasury with a small portion being issued by other federal government agencies. Treasury issues debt securities for two principal reasons, (1) to borrow needed funds to finance the current operations of the Federal Government and (2) to provide an investment and accounting mechanism for certain federal government accounts' (primarily federal trust funds) excess receipts. As shown in Figure 5, gross federal debt outstanding has increased over the past 25 years from \$3,665 billion as of September 30, 1991, to \$19,560 billion as of September 30, 2016.

Even in those years where debt held by the public declined, gross federal debt increased because of increases in intragovernmental debt holdings. By law, federal government accounts, including trust funds, have the authority or are required to invest their excess annual receipts (including interest earnings) over disbursements in federal securities. As a result, the intragovernmental debt holdings primarily represent the cumulative surplus of funds due to the trust funds' cumulative annual excess of tax receipts, interest credited, and other collections compared to spending.

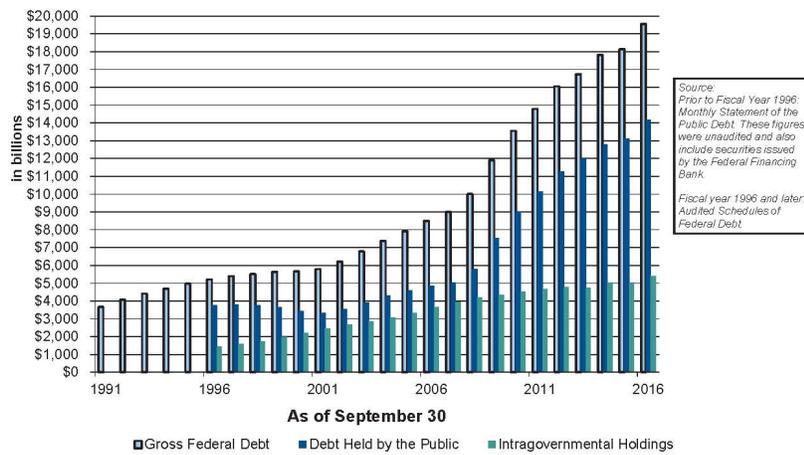
Budget deficits continued through 1997, which resulted in the continued increase in the gross federal debt from \$3,665 billion to \$5,398 billion as of September 30, 1991 and September 30, 1997, respectively. For fiscal years 1998 through 2001, the federal budget was in a surplus. During this period, the amount of debt held by the public fell by \$476 billion, from \$3,815 billion to \$3,339 billion. However, the gross federal debt continued to increase due to increases in intragovernmental holdings of \$870 billion, from \$1,583 billion to \$2,453 billion, from fiscal year 1998 through fiscal year 2001.

Beginning in fiscal year 2002, the federal budget returned to an annual deficit position, which resulted in an increase in debt held by the public. Federal debt held by the public increased from \$3,339 billion to \$5,049 billion from fiscal year 2002 through fiscal year 2007, an increase of 51.2%. From fiscal year 2008 through fiscal year 2016, federal debt held by the public more than doubled, rising by \$9,124 billion. Since fiscal year 2002, debt held by the public has increased from \$3,339 billion as of September 30, 2001 to \$14,173 billion as of September 30, 2016. Intragovernmental debt holdings increased from \$2,453 billion to \$5,387 billion during the same time period.

As shown in Figure 5, fiscal years 2014 and 2016 show a significant increase in the gross federal debt as compared to the previous year's increase due to the delays in raising the debt limit that occurred during fiscal years 2013 and 2015. These delays required Treasury to take extraordinary measures to remain below the statutory debt limit. Extraordinary measures decreased the outstanding debt subject to the statutory debt limit, to allow Treasury to issue new securities to the public as a means of generating cash to pay the obligations of the federal government. This activity caused the gross federal debt to be lower than it otherwise would have been if a delay were not in effect. Consequently, the gross federal debt increased after the delays ended and the uninvested principal and related interest were restored.

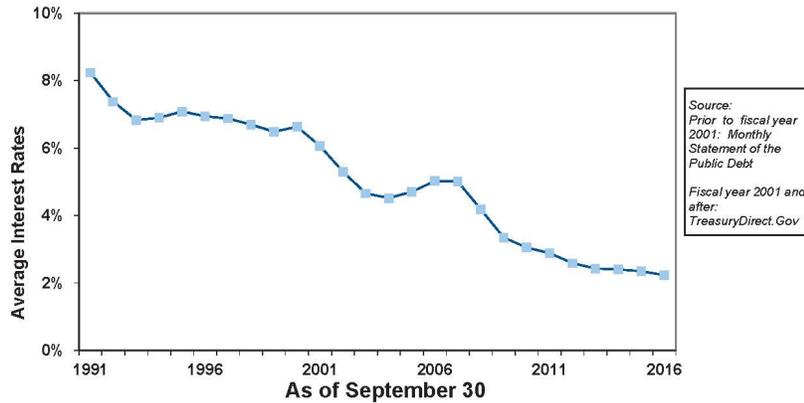
Historical Perspective, cont.

Figure 5 Gross Federal Debt Outstanding



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

Figure 6 Average Interest Rates of Federal Debt Outstanding



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

Schedules of Federal Debt

Managed by the Bureau of the Fiscal Service
 For the Fiscal Years Ended September 30, 2016 and 2015
 (Dollars in Millions)

| | Federal Debt | | | | | |
|---|-----------------------|--------------------------------|--|---------------------------------|--------------------------------|--|
| | Held by the Public | | | Intragovernmental Debt Holdings | | |
| | Principal (Note 2) | Accrued Interest Payable | Net Unamortized Premiums/ (Discounts) | Principal (Note 3) | Accrued Interest Payable | Net Unamortized Premiums/ (Discounts) |
| <i>Balance as of September 30, 2014</i> | \$12,784,971 | \$53,831 | (\$29,379) | \$5,024,994 | \$42,392 | \$67,822 |
| Increases | | | | | | |
| Borrowings from the Public | 7,044,951 | | (7,448) | | | |
| Net Increase in Intragovernmental Debt Holdings - Premiums Accrued Interest (Note 4) | | 245,355 | | | 165,037 | 16,293 |
| Total Increases | 7,044,951 | 245,355 | (7,448) | 0 | 165,037 | 16,293 |
| Decreases | | | | | | |
| Repayments of Debt Held by the Public | 6,706,075 | | | | | |
| Net Decrease in Intragovernmental Debt Holdings - Principal Interest Paid Net Amortization (Note 4) | | 243,455 | (5,449) | 11,033 | 166,867 | 8,776 |
| Total Decreases | 6,706,075 | 243,455 | (5,449) | 11,033 | 166,867 | 8,776 |
| <i>Balance as of September 30, 2015</i> | 13,123,847 | 55,731 | (31,378) | 5,013,961 | 40,562 | 75,339 |
| Increases | | | | | | |
| Borrowings from the Public | 8,401,775 | | (11,318) | | | |
| Net Increase in Intragovernmental Debt Holdings Accrued Interest (Note 4) | | 264,105 | | 373,036 | 164,755 | 4,858 |
| Total Increases | 8,401,775 | 264,105 | (11,318) | 373,036 | 164,755 | 4,858 |
| Decreases | | | | | | |
| Repayments of Debt Held by the Public | 7,352,198 | | | | | |
| Interest Paid Net Amortization (Note 4) | | 262,726 | (8,896) | | 165,625 | 7,460 |
| Total Decreases | 7,352,198 | 262,726 | (8,896) | 0 | 165,625 | 7,460 |
| <i>Balance as of September 30, 2016</i> | \$14,173,424 | \$57,110 | (\$33,800) | \$5,386,997 | \$39,692 | \$72,737 |

The accompanying notes are an integral part of these schedules.

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

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

For the Fiscal Years Ended September 30, 2016 and 2015

(Dollars in Millions)

Note 1. Significant Accounting Policies

Basis of Presentation

The Schedules of Federal Debt Managed by the Bureau of the Fiscal Service (Fiscal Service) have been prepared to report fiscal year 2016 and fiscal year 2015 balances and activity relating to monies borrowed from the public and certain federal government accounts under 31 U.S.C. §§ 3101- 3113 to fund the operations of the U.S. government. Permanent, indefinite appropriations are available for the payment of interest on the federal debt and the redemption of Treasury securities.

Reporting Entity

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

Basis of Accounting

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

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

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

For the Fiscal Years Ended September 30, 2016 and 2015

(Dollars in Millions)

Note 2. Federal Debt Held by the Public

As of September 30, 2016 and 2015, Federal Debt Held by the Public consisted of the following:

| | 2016 | | 2015 | |
|---------------------------------------|----------------------|------------------------|----------------------|------------------------|
| | Amount | Average Interest Rates | Amount | Average Interest Rates |
| Marketable: | | | | |
| Treasury Bills | \$ 1,644,759 | 0.4 % | \$ 1,355,231 | 0.1 % |
| Treasury Notes | 8,624,253 | 1.8 % | 8,366,026 | 1.8 % |
| Treasury Bonds | 1,825,339 | 4.4 % | 1,688,208 | 4.7 % |
| TIPS | 1,209,814 | 0.8 % | 1,135,363 | 0.8 % |
| Floating Rate Notes | 334,139 | 0.4 % | 287,039 | 0.1% |
| Total Marketable | <u>\$ 13,638,304</u> | | <u>\$ 12,831,867</u> | |
| Nonmarketable | <u>\$ 535,120</u> | 2.0 % | <u>\$ 291,980</u> | 2.5 % |
| Total Federal Debt Held by the Public | <u>\$ 14,173,424</u> | | <u>\$ 13,123,847</u> | |

Treasury issues marketable bills usually at a discount, but may also issue at par, and pays the par amount of the security upon maturity. The average interest rate on Treasury bills represents the original issue effective yield on securities outstanding as of September 30, 2016 and 2015. Treasury bills are issued with a term of one year or less.

Treasury issues marketable notes and bonds as long-term securities that pay semi-annual interest based on the securities' stated interest rate. These securities are issued at either par value or at an amount that reflects a discount or a premium. The average interest rate on marketable notes and bonds represents the stated interest rate adjusted by any discount or premium on securities outstanding as of September 30, 2016 and 2015. Treasury notes are issued with a term of 2 to 10 years and Treasury bonds are issued with a term of more than 10 years.

Treasury issues TIPS that have interest and redemption payments that are tied to the Consumer Price Index for all Urban Consumers, a widely used measure of inflation. TIPS are issued with a term of 5 years or more. At maturity, TIPS are redeemed at the inflation-adjusted principal amount, or the original par value, whichever is greater. TIPS pay a semi-annual fixed rate of interest applied to the inflation-adjusted principal. The average interest rate on TIPS represents the stated interest rate on principal plus inflation, adjusted by any discount or premium on securities outstanding as of September 30, 2016 and 2015. The TIPS Federal Debt Held by the Public inflation-adjusted principal balance includes inflation of \$90,815 million and \$90,035 million as of September 30, 2016 and 2015, respectively.

Treasury issues marketable Floating Rate Notes (FRNs), which pay interest quarterly based on the interest rate at the time of payment. The interest rate of FRNs can change over time and is indexed to the highest accepted discount rate of the most recent 13-week marketable bill auction. These securities, like marketable notes and bonds, are issued at either par value or at an amount that reflects a discount or premium. The average interest rate on marketable FRNs represents the highest accepted discount rate of the most recent 13-week marketable auction as of September 30, 2016, and 2015, adjusted by any discount or premium on securities outstanding as of these dates. These notes are currently issued with a term of 2 years.

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

For the Fiscal Years Ended September 30, 2016 and 2015

(Dollars in Millions)

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

Federal Debt Held by the Public includes federal debt held outside of the U. S. government by individuals, corporations, Federal Reserve Banks (FRB), state and local governments, and foreign governments and central banks. As of September 30, 2016, the FRB had total holdings of \$1,750,245 million, which (1) excludes \$713,885 million in Treasury securities used in overnight reverse repurchase transactions and (2) includes a net of \$673 million in Treasury securities held by the FRB as collateral for securities lending activities. As of September 30, 2015, the FRB had total holdings of \$1,845,344 million, which (1) excludes \$618,451 million in Treasury securities used in overnight reverse repurchase transactions and (2) includes a net of \$1,848 million in Treasury securities held by the FRB as collateral for securities lending activities. Treasury securities are held by the FRB in the FRB System Open Market Account (SOMA) for the purpose of conducting monetary policy.

Treasury issues nonmarketable securities at either par value or at an amount that reflects a discount or a premium. The average interest rate on the nonmarketable securities represents the original issue weighted effective yield on securities outstanding as of September 30, 2016 and 2015. Nonmarketable securities are issued with a term of on demand out to 40 years.

As of September 30, 2016 and 2015, nonmarketable securities consisted of the following:

| | 2016 | 2015 |
|-----------------------------------|------------------|------------------|
| Domestic Series | \$ 29,995 | \$ 29,995 |
| Foreign Series | 264 | 264 |
| State and Local Government Series | 109,211 | 78,115 |
| United States Savings Securities | 167,524 | 172,826 |
| Government Account Series | 226,349 | 9,138 |
| Other | 1,777 | 1,642 |
| Total Nonmarketable | \$535,120 | \$291,980 |

Government Account Series (GAS) securities are nonmarketable securities issued to federal government accounts. Federal Debt Held by the Public includes GAS securities issued to certain federal government accounts. One example is the GAS securities held by the Government Securities Investment Fund (G-Fund) of the federal employees' Thrift Savings Plan. Federal employees and retirees who have individual accounts own the GAS securities held by the fund. For this reason, these securities are considered part of the Federal Debt Held by the Public rather than Intragovernmental Debt Holdings. The GAS securities held by the G-Fund consist of overnight investments redeemed one business day after their issue. The net increase in the fund's principal balance during fiscal year 2016 is included in the Borrowings from the Public amount reported on the Schedules of Federal Debt. The net decrease in the fund's principal balance during fiscal year 2015 is included in the Repayments of Debt Held by the Public amount reported on the Schedules of Federal Debt.

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

For the Fiscal Years Ended September 30, 2016 and 2015

(Dollars in Millions)

Note 3. Intragovernmental Debt Holdings

As of September 30, 2016 and 2015, Intragovernmental Debt Holdings are owed to the following:

| | <u>2016</u> | <u>2015</u> |
|---|---------------------|---------------------|
| SSA: Federal Old-Age and Survivors Insurance Trust Fund | \$2,796,712 | \$2,766,649 |
| OPM: Civil Service Retirement and Disability Fund | 874,137 | 718,952 |
| DOD: Military Retirement Fund | 591,046 | 530,960 |
| DOD: Medicare-Eligible Retiree Health Care Fund | 213,482 | 205,793 |
| HHS: Federal Hospital Insurance Trust Fund | 192,209 | 195,458 |
| FDIC: Deposit Insurance Fund | 71,524 | 60,096 |
| DOT: Highway Trust Fund | 64,629 | 7,667 |
| HHS: Federal Supplementary Medical Insurance Trust Fund | 63,336 | 66,128 |
| DOL: Unemployment Trust Fund | 53,776 | 44,368 |
| DOE: Nuclear Waste Disposal Fund | 52,424 | 51,812 |
| OPM: Postal Service Retiree Health Benefits Fund | 51,495 | 45,237 |
| SSA: Federal Disability Insurance Trust Fund | 45,880 | 41,638 |
| OPM: Employees Life Insurance Fund | 45,167 | 43,958 |
| HUD: FHA, Mutual Mortgage Insurance Capital Reserve Account | 36,441 | 14,733 |
| OPM: Employees Health Benefits Fund | 23,726 | 23,018 |
| DOL: Pension Benefit Guaranty Corporation | 23,697 | 18,492 |
| Treasury: Exchange Stabilization Fund | 22,680 | 20,773 |
| DOS: Foreign Service Retirement and Disability Fund | 18,346 | 18,144 |
| HUD: Guarantees of Mortgage-Backed Securities Capital Reserve Account | 15,802 | 12,772 |
| DOT: Airport and Airway Trust Fund | 13,400 | 12,716 |
| NCUA: National Credit Union Share Insurance Fund | 12,305 | 11,584 |
| Other Programs and Funds | 104,783 | 103,013 |
| Total Intragovernmental Debt Holdings | <u>\$ 5,386,997</u> | <u>\$ 5,013,961</u> |

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

Intragovernmental Debt Holdings primarily consist of GAS securities. Treasury issues GAS securities at either par value or at an amount that reflects a discount or a premium. GAS securities are issued with a term of on demand out to 30 years. GAS securities include TIPS, which are reported at an inflation-adjusted principal balance using the Consumer Price Index for all Urban Consumers. As of September 30, 2016 and 2015, the inflation-adjusted principal balance included inflation of \$128,431 million and \$122,397 million, respectively. The average interest rates on Intragovernmental Debt Holdings, excluding TIPS and FRNs, for fiscal years 2016 and 2015 were 2.8 and 3.1 percent, respectively. The average interest rates on TIPS for both fiscal years were 1.3 percent. The average interest rate represents the original issue weighted effective yield on securities outstanding as of September 30, 2016 and 2015.

*Notes to the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service
For the Fiscal Years Ended September 30, 2016 and 2015
(Dollars in Millions)*

Note 4. Interest Expense

Interest expense on federal debt for fiscal years 2016 and 2015 consisted of the following:

| | <u>2016</u> | <u>2015</u> |
|--|-------------|-------------|
| Federal Debt Held by the Public | | |
| Accrued Interest | \$264,105 | \$245,355 |
| Net Amortization of Premiums and Discounts | 8,896 | 5,449 |
| | <hr/> | <hr/> |
| Total Interest Expense on Federal Debt Held by the Public | 273,001 | 250,804 |
| Intragovernmental Debt Holdings | | |
| Accrued Interest | 164,755 | 165,037 |
| Net Amortization of Premiums and Discounts | (7,460) | (8,776) |
| | <hr/> | <hr/> |
| Total Interest Expense on Intragovernmental Debt Holdings | 157,295 | 156,261 |
| | <hr/> | <hr/> |
| Total Interest Expense on Federal Debt Managed by Fiscal Service | \$430,296 | \$407,065 |

The valuation of TIPS is adjusted daily over the life of the security based on the Consumer Price Index for all Urban Consumers. This daily adjustment is an interest expense for federal debt managed by Fiscal Service. Accrued interest on Federal Debt Held by the Public includes inflation adjustments of \$9,985 million and \$2,282 million for fiscal years 2016 and 2015, respectively. Accrued interest on Intragovernmental Debt Holdings includes inflation adjustments of \$5,506 million and \$1,063 million for fiscal years 2016 and 2015, respectively.

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

For the Fiscal Years Ended September 30, 2016 and 2015

(Dollars in Millions)

Note 5. Suspension of Issuances and Subsequent Restoration of Uninvested Principal and Interest Amounts

A delay in raising the statutory debt limit existed as of September 30, 2015. When delays in raising the statutory debt limit occur, Treasury often must deviate from its normal debt management operations and take a number of extraordinary actions to meet the government's obligations as they come due without exceeding the debt limit. Many extraordinary actions taken by Treasury during the period of March 16, 2015 through September 30, 2015, resulted in federal debt securities not being issued to certain federal government accounts. Consequently, the resulting uninvested principal as of September 30, 2015, totaling \$350,476 million and related interest totaling \$2,052 million are not reported on the Schedules of Federal Debt. Uninvested principal amounts for the G-Fund, Civil Service Retirement and Disability Fund (CSRDF), Postal Service Retiree Health Benefits Fund (Postal Benefits Fund), and the Exchange Stabilization Fund (ESF) were \$203,246 million, \$140,602 million, \$4,757 million, and \$1,871 million, respectively, as of September 30, 2015. Additionally, the related interest for the G-Fund, CSRDF, and Postal Benefits Fund that would have been accrued and/or paid during the period of March 16, 2015 through September 30, 2015, would have been \$1,345 million, \$683 million, and \$24 million, respectively, on September 30, 2015. In accordance with relevant laws, ESF is not entitled to forgone interest.

On October 15, 2015, the Secretary of the Treasury notified Congress that extraordinary actions would be exhausted no later than November 3, 2015. On Monday November 2, 2015, the Bipartisan Budget Act of 2015 (Public Law 114-74) was enacted suspending the statutory debt limit through March 15, 2017. On November 2, 2015, Treasury discontinued its use of the extraordinary actions and resumed normal debt management operations. On this date, in accordance with relevant laws, Fiscal Service restored uninvested principal amounts to the G-Fund, CSRDF, and Postal Benefits Fund of \$204,839 million, \$143,033 million, and \$4,757 million, respectively. All principal not invested for ESF had been reinvested as of October 21, 2015. In accordance with relevant laws, Fiscal Service restored the interest related to the uninvested principal during the period of March 16, 2015 through October 30, 2015, to the G-Fund on November 3, 2015, in the amount of \$1,717 million. Interest related to the uninvested principal during the period of March 16, 2015 through October 30, 2015, for CSRDF and Postal Benefits Fund were restored on the next semi-annual interest payment date of December 31, 2015. These amounts were \$938 million and \$33 million, respectively.

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



DEPARTMENT OF THE TREASURY
BUREAU OF THE FISCAL SERVICE
WASHINGTON, DC 20227

November 3, 2016

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

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

Fiscal Service management is responsible for maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the Schedule of Federal Debt that is free from material misstatement, whether due to fraud or error. Fiscal Service management evaluated the effectiveness of Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016, based on the criteria established under 31 U.S.C. 3512(c), (d) (commonly known as the Federal Managers' Financial Integrity Act).

Based on that evaluation, we conclude that, as of September 30, 2016, Fiscal Service's internal control over financial reporting relevant to the Schedule of Federal Debt was effective.

Sheryl R. Morrow
Commissioner,
Bureau of the Fiscal Service

Kimberly A. McCoy
Deputy Commissioner,
Fiscal Accounting and Shared Services

Matthew J. Miller
Assistant Commissioner,
Fiscal Accounting

Patricia M. Greiner
Chief Financial Officer and Assistant
Commissioner for Management (CFO)

Stephen L. Manning
Chief Information Officer and Assistant
Commissioner, Information and Security Services

Appendix II: Comments from the Bureau of the Fiscal Service



DEPARTMENT OF THE TREASURY
BUREAU OF THE FISCAL SERVICE
WASHINGTON, DC 20227

November 4, 2016

Ms. Dawn B. Simpson, Acting Director
Financial Management and Assurance
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Ms. Simpson:

This letter is in response to your audit of the Schedules of Federal Debt Managed by the Bureau of the Fiscal Service for the fiscal years ended September 30, 2016 and 2015. We agree with the conclusions of your audit report.

We appreciate the knowledge and experience displayed by your audit team as we finalize the twentieth year of our professional relationship. Your team's experience with our accounting operations provides timeliness and efficiency to the audit process. We would like to thank you and your staff for the thorough audit of these schedules. This year was particularly unique as we were faced with a Debt Issuance Suspension Period (DISP) to begin the fiscal year, but operated under a suspension of the Statutory Debt Limit which was in effect for the majority of the fiscal year. We look forward to sustaining a productive and successful relationship with your staff.

Sincerely,

A handwritten signature in blue ink that reads "Sheryl R. Morrow".

Sheryl R. Morrow
Commissioner
Bureau of the Fiscal Service

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