United States Government Accountability Office

GAO

Report to the Secretary of the Treasury

November 2012

FINANCIAL AUDIT

Bureau of the Public Debt's Fiscal Years 2012 and 2011 Schedules of Federal Debt

GAO

Accountability * Integrity * Reliability

GAO-13-114

GAO Accountability * Integrity * Reliability

Highlights

Highlights of GAO-13-114, a report to the Secretary of the Treasury

November 2012

FINANCIAL AUDIT

Bureau of the Public Debt's Fiscal Years 2012 and 2011 Schedules of Federal Debt

Why GAO Did This Study

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

Federal debt managed by BPD consists of Treasury securities held by the public and by certain federal government accounts, referred to as intragovernmental debt holdings. 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, BPD's Commissioner concurred with GAO's conclusions.

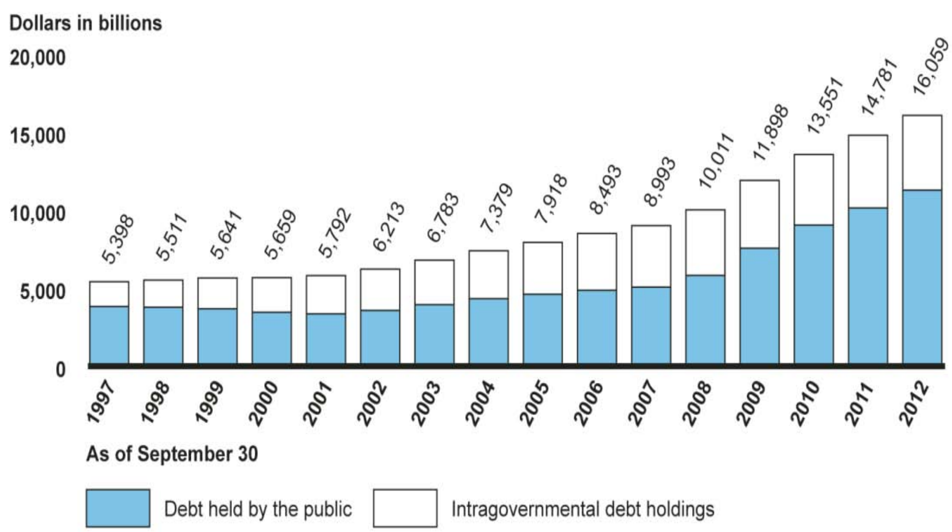
View GAO-13-114. For more information, contact Gary T. Engel at (202) 512-3406 or engelg@gao.gov.

What GAO Found

In GAO's opinion, the Bureau of the Public Debt's (BPD) Schedules of Federal Debt for fiscal years 2012 and 2011 were fairly presented in all material respects, and BPD maintained effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012. GAO's tests of BPD's compliance in fiscal year 2012 with selected provisions of laws related to the Schedule of Federal Debt disclosed no instances of noncompliance.

As of September 30, 2012 and 2011, federal debt managed by BPD totaled $16,059 billion and $14,781 billion, respectively. GAO has audited the Schedule of Federal Debt since fiscal year 1997. Over this period, total federal debt has increased by 197 percent. Also during this period, the statutory debt limit was raised 13 times, from $5,950 billion to its current level of $16,394 billion.

Total Federal Debt Outstanding, September 30, 1997, through September 30, 2012



Source: BPD.

During fiscal year 2012, delays in raising the statutory debt limit occurred prior to the January 2012 increase in the limit, with the Department of the Treasury (Treasury) deviating from its normal debt management operations and taking certain extraordinary actions within its legal authorities to avoid exceeding the debt limit. As part of the process established by the Budget Control Act of 2011, the statutory debt limit was increased by $1,200 billion effective after close of business on January 27, 2012. In July 2012, GAO reported on extraordinary actions Treasury took during 2011 and January 2012 to manage federal debt when delays in raising the debt limit occurred and the effect of delayed increases on Treasury borrowing costs. As with its February 2011 report, GAO also noted in its July 2012 report that Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue to avoid potential disruptions to the Treasury market and to help inform the fiscal policy debate in a timely way.

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Abbreviations

BCA	Budget Control Act of 2011
BPD	Bureau of the Public Debt
ESF	Exchange Stabilization Fund
GDP	gross domestic product

G A O

Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

November 8, 2012

The Honorable Timothy F. Geithner
Secretary of the Treasury

Dear Mr. Secretary:

The accompanying auditor's report presents the results of our audits of the Schedules of Federal Debt Managed by the Bureau of the Public Debt for the fiscal years ended September 30, 2012 and 2011. The Schedules of Federal Debt present the beginning balances, increases and decreases, and ending balances for (1) Federal Debt Held by the Public and Intragovernmental Debt Holdings, (2) the related Accrued Interest Payables, and (3) the related Net Unamortized Premiums and Discounts managed by the Department of the Treasury's (Treasury) Bureau of the Public Debt (BPD).

The auditor's report contains our (1) unqualified opinions on the Schedules of Federal Debt for the fiscal years ended September 30, 2012 and 2011; (2) opinion that BPD maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012; and (3) conclusion that our tests of BPD's compliance with selected provisions of laws related to the Schedule of Federal Debt disclosed no instances of reportable noncompliance.

As of September 30, 2012 and 2011, federal debt managed by BPD totaled $16,059 billion and $14,781 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) $11,270 billion as of September 30, 2012, and $10,127 billion as of September 30, 2011, of debt held by the public and (2) $4,789 billion as of September 30, 2012, and $4,654 billion as of September 30, 2011, 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, 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. As of June 30, 2012, the reported amount of Treasury securities held by foreign and international investors represented an estimated 48 percent of debt held by the public. This percentage is slightly higher than the 46 percent as of June 30, 2011, and remains considerably higher than the estimated 30 percent of debt held by the public as of June 30, 2001. Treasury estimates that the amount of Treasury securities held by foreign and international investors has increased from $983 billion as of June 30, 2001, to $5,311 billion as of June 30, 2012—an increase of $4,328 billion. 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. These estimates are not reported on the Schedules of Federal Debt and as such we do not audit these amounts.[1]

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 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

[1]Treasury, *Major Foreign Holders of Treasury Securities*, accessed November 1, 2012, http://www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt.

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 burden on today's economy as borrowing from the public absorbs resources available for private investment and may put upward pressure on interest rates. In addition, interest on debt held by the public is paid in cash and represents a burden on current taxpayers. Moreover, 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 typically do not require cash payments from the current budget or represent a burden on the current economy. In addition, from the perspective of the budget as a whole, Treasury's interest payments to federal government accounts are entirely offset by the income received by such accounts. However, this intragovernmental debt and related interest reflects a burden 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.[2]

We have audited the Schedule of Federal Debt since fiscal year 1997. Over this period, total federal debt has increased by 197 percent. Also during this period, the statutory debt limit was raised 13 times, from $5,950 billion to $16,394 billion. During the last 4 fiscal years, total federal debt has increased by $6,048 billion, or 60 percent, from $10,011 billion as of September 30, 2008, to $16,059 billion as of September 30, 2012. The rapid growth in federal debt during this period presented debt management challenges for Treasury.[3] The economic downturn along with the federal government's response to it contributed to this rapid buildup in federal debt held by the public. As a result, the increases to

[2]For more information regarding the federal debt, see GAO, *Federal Debt: Answers to Frequently Asked Questions*, accessed November 1, 2012, www.gao.gov/special.pubs/longterm/debt.

[3]For more information, see GAO, *Debt Management: Treasury Was Able to Fund Economic Stabilization and Recovery Expenditures in a Short Period of Time, but Debt Management Challenges Remain*, GAO-10-498 (Washington, D.C.: May 18, 2010).

total federal debt over the past 4 fiscal years represent the largest dollar increases over a 4-year period in history. During fiscal year 2012 alone, total federal debt increased by $1,278 billion. Of the fiscal year 2012 increase, $1,143 billion was from the increase in debt held by the public and $135 billion was from the increase in intragovernmental debt holdings. Notably, the statutory debt limit was raised on seven different occasions during the last 4 fiscal years, increasing by about 54 percent, from $10,615 billion to its current level of $16,394 billion. As of September 30, 2012, debt subject to the limit totaled $16,027 billion.[4]

During fiscal year 2012, Treasury faced an additional challenge of managing federal debt close to the statutory debt limit. Delays in raising the statutory debt limit occurred prior to the January 2012 increase in the limit, with Treasury deviating from its normal debt management operations and taking certain extraordinary actions within its legal authorities from January 4, 2012, through January 27, 2012, to avoid exceeding the debt limit. These actions included suspending investments to the Government Securities Investment Fund of the Federal Employees' Retirement System (G-Fund)[5] and the Exchange Stabilization Fund (ESF).[6] As part of the process established by the Budget Control Act of 2011 (BCA), the statutory debt limit was increased by $1,200 billion to its current level of $16,394 billion effective after close of business on January 27, 2012.[7] Subsequent to the January 2012 increase in the statutory debt limit, Treasury fully restored the G-Fund to the position it would have been in had the suspensions of debt not occurred. Treasury also invested the uninvested principal for January 2012 to the ESF. However, Treasury did not restore interest losses to the ESF because it lacks legislative authority to do so. Additionally, as a result of extraordinary actions taken in fiscal year 2011 to manage federal debt

[4]Debt subject to the limit is primarily comprised of total federal debt managed by BPD, as reported on the Schedule of Federal Debt, less unamortized discounts on Treasury bills and Zero Coupon Treasury bonds.

[5]The G-Fund contains contributions made by federal employees toward their retirement as part of the Thrift Savings Plan program.

[6]The ESF is used to help provide a stable system of monetary exchange rates.

[7]On August 2, 2011, Congress and the President enacted the Budget Control Act of 2011 (Pub. L. No. 112-25), which established a process that resulted in debt limit increases in three increments—$400 billion effective on August 2, 2011, $500 billion effective after close of business on September 21, 2011, and $1,200 billion effective after close of business on January 27, 2012.

within the statutory debt limit, Treasury restored interest losses to the Civil Service Retirement and Disability Fund[8] and the Postal Service Retiree Health Benefits Fund[9] on December 30, 2011, in accordance with the legal authorities provided to the Secretary of the Treasury. In July 2012, we reported on the extraordinary actions Treasury took during 2011 and January 2012 to manage federal debt when delays in raising the debt limit occurred and the effect of delayed increases on Treasury borrowing costs. As with our February 2011 report, we also noted in our July 2012 report that Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue to avoid potential disruptions to the Treasury market and to help inform the fiscal policy debate in a timely way.[10]

Federal financing needs remain high, in part due to the persistent effects of the economic downturn and its impact on the federal deficit. The reported federal deficit for fiscal year 2012 was $1,089 billion, down from the fiscal year 2011 reported federal deficit of $1,297 billion. Correspondingly, debt held by the public increased from roughly 68 percent of gross domestic product (GDP) at the end of fiscal year 2011 to roughly 73 percent at the end of fiscal year 2012. The pace at which federal debt held by the public increases over the next several years depends largely on whether current laws, such as spending limits pursuant to the BCA[11] and the expiration of certain tax cuts enacted in 2001 and 2003, take effect. Over the longer term, debt held by the public as a share of GDP is expected to grow as a result of the structural imbalance between revenue and spending driven by rising health care costs and demographics. Increasing numbers of baby-boom generation

[8]The Civil Service Retirement and Disability Fund contains contributions made by federal government agencies and their civilian employees toward retirement benefits.

[9]The Postal Service Retiree Health Benefits Fund contains contributions made by the United States Postal Service toward its retirees' health benefits.

[10]For more information, see GAO, *Debt Limit: Analysis of 2011-2012 Actions Taken and Effect of Delayed Increase on Borrowing Costs*, GAO-12-701 (Washington, D.C.: July 23, 2012).

[11]The BCA (Pub. L. No. 112-25) enacted caps on discretionary spending for fiscal years 2012 through 2021. In addition, the BCA specified additional limits on discretionary spending and automatic reductions in direct spending that would take effect if lawmakers did not enact legislation originating from the Joint Select Committee on Deficit Reduction that would reduce projected deficits by at least $1.2 trillion. Because no such legislation was enacted, those procedures are now scheduled to go into effect.

members are becoming eligible for Social Security retirement benefits and for Medicare. In addition, although health care spending growth recently slowed, it has been growing faster than the overall economy 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.[12]

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

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

Sincerely yours,

Gary T. Engel

Gary T. Engel
Director
Financial Management
and Assurance

[12]For more information, see GAO, *The Federal Government's Long-Term Fiscal Outlook: Spring 2012 Update*, GAO-12-521SP (Washington, D.C.: April 2012).

United States Government Accountability Office
Washington, DC 20548

Independent Auditor's Report

To the Commissioner of the Bureau of the Public Debt

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 Managed by the Bureau of the Public Debt (BPD) because of the significance of the federal debt to the federal government's consolidated financial statements.[1]

This auditor's report presents the results of our audits of the Schedules of Federal Debt Managed by BPD for the fiscal years ended September 30, 2012 and 2011. 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) BPD.[2]

In our audits of the Schedules of Federal Debt Managed by BPD for the fiscal years ended September 30, 2012 and 2011, we found

- the Schedules of Federal Debt are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- BPD maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012; and
- no reportable noncompliance in fiscal year 2012 with selected provisions of laws we tested related to the Schedule of Federal Debt.

[1]31 U.S.C. § 331(e)(2). As a bureau within the Department of the Treasury, federal debt and related activity and balances managed by BPD are also significant to the consolidated financial statements of the Department of the Treasury (see 31 U.S.C. § 3515(b)).

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

The following sections discuss in more detail (1) these conclusions; (2) other information included with the Schedules of Federal Debt; (3) our audit objectives, scope, and methodology; and (4) BPD's comments on a draft of this report.

Opinion on the Schedules of Federal Debt

The Schedules of Federal Debt including the accompanying notes present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, the balances as of September 30, 2012, 2011, and 2010 for Federal Debt Managed by BPD; the related Accrued Interest Payables and Net Unamortized Premiums and Discounts; and the related increases and decreases for the fiscal years ended September 30, 2012 and 2011.

Opinion on Internal Control

BPD maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012, that provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the Schedule of Federal Debt would be prevented or detected and corrected on a timely basis. Our opinion on internal control is based on criteria established under 31 U.S.C. § 3512(c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

We identified deficiencies in BPD's system of internal control that we consider not to be material weaknesses or significant deficiencies.[3] We have communicated these matters to management and, where appropriate, will report on them separately. In late fiscal year 2011, Treasury began consolidating the data centers and related operations of BPD and Treasury's Financial Management Service. Given the significant role that certain information systems have in managing federal debt, it will be important that BPD management assesses risks associated with the

[3]A material weakness is a deficiency, or a combination of deficiencies, in internal control 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 significant deficiency is a deficiency, or 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. 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.

consolidation and ensures that internal control over the information systems in these data centers is effectively designed and implemented.

Compliance with Selected Provisions of Laws

Our tests of BPD's compliance in fiscal year 2012 with selected provisions of laws related to the Schedule of Federal Debt disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards. The objective of our audit was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Other Information

BPD's other information, which consists of the Overview on Federal Debt Managed by the Bureau of the Public Debt, 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. 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.

Objectives, Scope, and Methodology

BPD management is responsible for (1) preparing the Schedules of Federal Debt in conformity with U.S. generally accepted accounting principles; (2) preparing and presenting other information included with 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) establishing and maintaining effective internal control over financial reporting, and evaluating its effectiveness; and (4) complying with applicable laws and regulations. BPD management evaluated the effectiveness of BPD's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012, based on the criteria established under FMFIA. BPD management's assertion based on its evaluation is included in appendix I.

We are responsible for planning and performing the audit to obtain reasonable assurance and provide our opinion about whether (1) the Schedules of Federal Debt are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles and (2) BPD management maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012. We are also responsible for (1) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the Schedule of Federal Debt and (2) applying certain limited procedures to the other information included with the Schedules of Federal Debt.

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the Schedules of Federal Debt;
- assessed the accounting principles used and any significant estimates made by BPD management;
- evaluated the overall presentation of the Schedules of Federal Debt;
- obtained an understanding of BPD and its operations, including its internal control over financial reporting relevant to the Schedule of Federal Debt;
- considered BPD's process for evaluating and reporting on internal control over financial reporting relevant to the Schedule of Federal Debt based on the criteria established under FMFIA;
- assessed the risk of (1) material misstatement in the Schedule of Federal Debt and (2) material weaknesses in BPD's internal control over financial reporting relevant to the Schedule of Federal Debt;
- evaluated the design and operating effectiveness of BPD's internal control over financial reporting relevant to the Schedule of Federal Debt based on the assessed risk;
- tested BPD's internal control over financial reporting relevant to the Schedule of Federal Debt;
- tested compliance in fiscal year 2012 with the (1) statutory debt limit (31 U.S.C. §§ 3101(b), as amended, and 3101A) and (2) suspension of investments from the Government Securities Investment Fund (G-Fund) (5 U.S.C. § 8438(g));
- 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; and
- performed such other procedures as we considered necessary in the circumstances.

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 conformity with U.S. generally accepted accounting principles and (2) transactions related to the Schedule of Federal Debt are executed in accordance with laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the Schedule of Federal Debt.

We did not evaluate all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing statistical reports 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 the effectiveness of internal control over financial reporting and may not be sufficient for other purposes. Consequently, our audit may not identify all deficiencies in internal control over financial reporting that are less severe than a material weakness. Because of inherent limitations, internal control may not prevent or detect and correct misstatements due to error or fraud, losses, or noncompliance. 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.

We did not test compliance with all laws and regulations applicable to BPD. We limited our tests of compliance to selected provisions of laws that have a direct and material effect on the Schedule of Federal Debt for the fiscal year ended September 30, 2012. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

Agency Comments

In commenting on a draft of this report, BPD's Commissioner concurred with our conclusions. BPD's comments are reprinted in their entirety in appendix II.

Gary T. Engel
Director
Financial Management
and Assurance

November 1, 2012

Overview, Schedules, and Notes

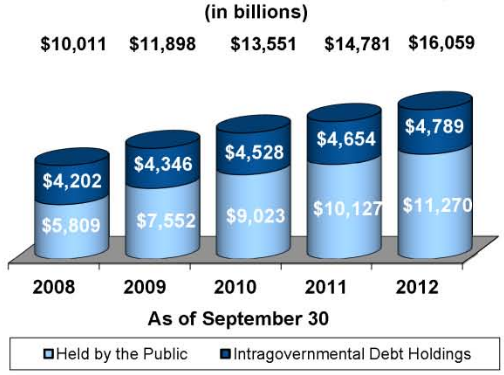
Overview on Federal Debt Managed by the Bureau of the Public Debt

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

Gross Federal Debt Outstanding

Federal debt managed by the Bureau of the Public Debt (BPD) comprises debt held by the public and debt held by certain federal government accounts (under 31 U.S.C. § 3101), the latter of which is referred to as intragovernmental debt holdings. As of September 30, 2012 and 2011, outstanding gross federal debt managed by BPD totaled $16,059 billion and $14,781 billion, respectively.[1] The increase in gross federal debt of $1,278 billion during fiscal year 2012 was due to an increase in gross intragovernmental debt holdings of $135 billion and an increase in gross debt held by the public of $1,143 billion. As Figure 1 illustrates, intragovernmental debt holdings and debt held by the public increased by $587 billion and $5,461 billion, respectively, from September 30, 2008 to September 30, 2012. The primary reason for the increases in intragovernmental debt holdings is the excess annual receipts (including interest earnings) over disbursements in the Federal Old-Age and Survivors Insurance Trust Fund, Civil Service Retirement and Disability Fund, Military Retirement Fund, and DOD Medicare-Eligible Retiree Health Care Fund. The increases in debt held by the public are due primarily to total federal spending exceeding total federal revenues. As of September 30, 2012, gross debt held by the public totaled $11,270 billion and gross intragovernmental debt holdings totaled $4,789 billion.

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

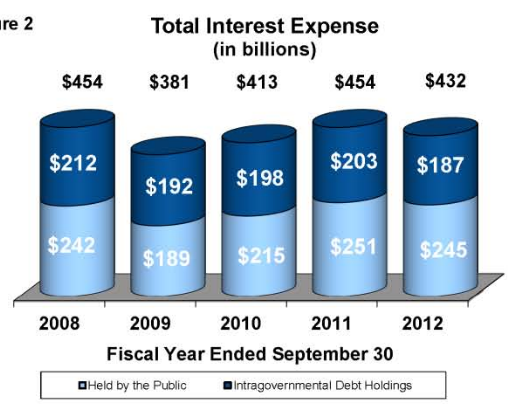


[1] Federal debt outstanding reported here differs from the amount reported in the Financial Report of the United States Government because of the securities not maintained or reported by BPD which are issued by the Federal Financing Bank and other specific securities issued outside of the authority of Title 31, U.S. Code, section 3101.

Interest Expense

Interest expense incurred during fiscal year 2012 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 2012, interest expense incurred totaled $432 billion; this consisted of interest expense on debt held by the public of $245 billion, and $187 billion in interest incurred for intragovernmental debt holdings. As Figure 2 illustrates, due to the economic conditions, there was a significant increase in the demand for government backed securities during fiscal year 2009, which resulted in lower average interest rates and interest expense for that year. For example, the average interest rates on Treasury bills outstanding as of September 30, 2009 and 2008 were 0.3 percent and 1.6 percent, respectively. Interest expense increased for fiscal years 2010 and 2011 due primarily to an increase in Treasury notes and bonds outstanding, which had higher average interest rates than Treasury bills. Interest expense decreased for fiscal year 2012 due primarily to a decrease in the average interest rates for Treasury notes, bonds, and Treasury Inflation-Protected Securities (TIPS). Average interest rates on principal balances outstanding as of September 30, 2012 and 2011, are disclosed in the Notes to the Schedules of Federal Debt.

Figure 2

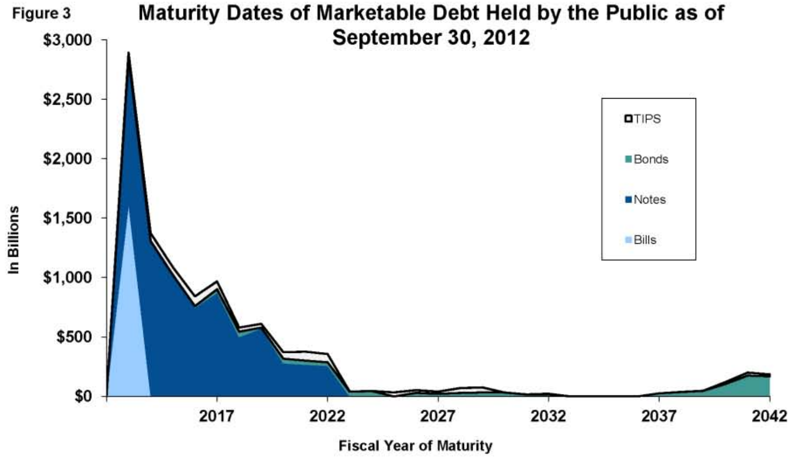


Debt Held by the Public

Debt held by the public primarily represents the amount the Federal Government has borrowed to finance cumulative cash deficits. During fiscal year 2012, Treasury used the existing suite of securities to meet the borrowing needs of the Federal Government while primarily increasing its offerings of Treasury notes over offerings of Treasury bills, Treasury bonds, or TIPS. As a result, Treasury notes increased by $708 billion; whereas, Treasury bills, bonds, and TIPS increased by $137 billion, $178 billion, and $102 billion, respectively, in fiscal year 2012. As of September 30, 2012 and 2011, gross debt held by the public totaled $11,270 billion and $10,127 billion, respectively (see Figure 1), an increase of $1,143 billion. This increase was primarily the result of borrowings needed to finance the government's fiscal year 2012 deficit. As a result of the increase in outstanding gross debt held by the public primarily being in the form of longer term securities, the total dollar amount of activity for both borrowings and repayments of debt held by the public decreased for fiscal year 2012.

As of September 30, 2012, $10,730 billion, or 95 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, and TIPS 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, 2012, $6,225 billion, or 58 percent, will mature within the next 4 years (see Figure 3). As of September 30, 2012 and 2011, notes and TIPS held by the public maturing within the next 10 years totaled $7,646 billion and $6,916 billion, respectively, an increase of $730 billion.

Figure 3 **Maturity Dates of Marketable Debt Held by the Public as of September 30, 2012**



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, 2012, nonmarketable securities totaled $539 billion, or 5 percent of debt held by the public. As of that date, nonmarketable securities primarily consisted of savings securities totaling $184 billion, State and Local Government Series securities totaling $159 billion, and Government Account Series securities totaling $163 billion.

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.

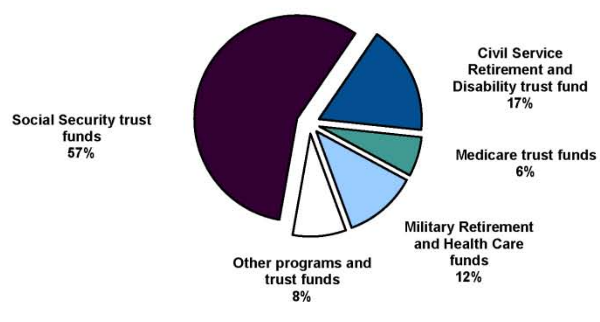
Intragovernmental Debt Holdings

Intragovernmental debt holdings represent balances of Treasury securities held by 239 individual federal government accounts with either the authority or the requirement to invest excess receipts in special U.S. Treasury securities that are guaranteed for principal and interest by the full faith and credit of the U.S. Government. Intragovernmental debt holdings primarily consist of balances in the Social Security, Medicare, Military Retirement and Health Care, and Civil Service Retirement and Disability trust funds.[2] As of September 30, 2012, such funds accounted for $4,389 billion, or 92 percent, of the $4,789 billion intragovernmental debt holdings balances (see Figure 4). As of September 30, 2012 and 2011, gross intragovernmental debt holdings totaled $4,789 billion and $4,654 billion, respectively (see Figure 1), an increase of $135 billion.

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

Figure 4

Components of Intragovernmental Debt Holdings as of September 30, 2012



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

Significant Events in Fiscal Year 2012

Statutory Debt Limit Raised

Prior to the enactment of the Budget Control Act of 2011, which was signed into law on August 2, 2011, (Public Law No. 112-25), delays in raising the statutory debt limit occurred that required Treasury to depart from its normal debt management procedures and invoke legal authorities to avoid exceeding the statutory debt limit. In accordance with relevant legislation, on December 30, 2011, BPD restored the Civil Service Retirement and Disability Fund (Civil Service Fund) and the Postal Service Retiree Health Benefits Fund (Postal Benefits Fund) portfolios for the interest lost from the delays in raising the statutory debt limit, which ended on August 2, 2011. The restoration amounted to nearly $517 million for the Civil Service Fund and $22 million for the Postal Benefits Fund.

After close of business on January 27, 2012, the statutory debt limit was increased by $1.2 trillion, from $15.194 trillion to $16.394 trillion. The increase was authorized under the terms of the Budget Control Act of 2011. However, prior to the statutory debt limit increase, beginning on January 4, 2012, delays in raising the statutory debt limit resulted in Treasury departing from its normal debt management procedures and invoking legal authorities to keep the debt outstanding no closer than $25 million to the statutory debt limit. Treasury maintained the $25 million window by utilizing extraordinary actions within its legal authorities, which included suspending investments of the Exchange Stabilization Fund (ESF) and the Government Securities Investment Fund of the Federal Employees' Retirement System (G-Fund).

In accordance with relevant legislation, on January 30, 2012, BPD restored foregone principal and interest for the G-Fund totaling $36.9 billion and foregone principal to the ESF totaling $22.7 billion. BPD only restored forgone principal to the ESF as the ESF is not entitled to interest losses resulting from authorized actions taken by Treasury to manage federal debt when delays in raising the debt limit occur.

FY 2013 Budget Proposes BPD and Financial Management Service (FMS) Consolidation

In his fiscal year 2013 Budget request, President Obama proposed a consolidation of BPD and FMS, both under Treasury's Office of the Fiscal Assistant Secretary (OFAS), into one organization called the Bureau of the Fiscal Service. Beyond the financial and operational benefits, this effort will enable the Department of the Treasury to better address the financial management needs of the federal government and realize administrative efficiencies while retaining existing core federal financial management responsibilities. Beginning in fiscal year 2014, the combined BPD and FMS cumulative net savings from the proposed consolidation is projected to be $36 million over a five year period. Areas identified for cost reduction included:

- Headquarters staff, by transitioning to one Commissioner responsible for Fiscal Service operations;
- Finance and budget, by transitioning to one Chief Financial Officer;

Significant Events in Fiscal Year 2012, cont.

- Information technology, by transitioning to one Chief Information Officer;
- Legal support, by transitioning to one Chief Counsel; and
- Legislative and Public Affairs, by transitioning to one office.

The proposed consolidation of BPD and FMS will position the Fiscal Service to create a new standard of excellence and leadership for the federal community.

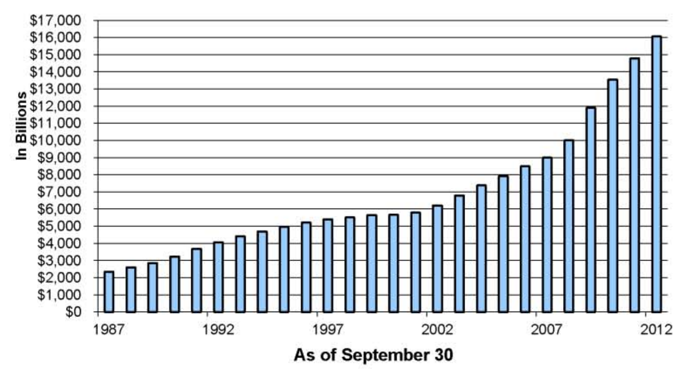
Ready.Save.Grow.

On March 27, 2012, BPD kicked off a public education campaign, Ready.Save.Grow.$_{SM}$, to raise awareness of Treasury securities and to remind the public that, although paper savings bonds can only be purchased with tax refunds, electronic savings bonds remain available through TreasuryDirect. To aid the campaign, BPD is partnering with several non-profit organizations such as AARP, American Savings Education Council, Center for Financial Services Innovation, and Consumer Federation of America. The campaign's website (http://www.treasurydirect.gov/readysavegrow) organizes Treasury investment information in an easy-to-read format for new and prospective investors. The Treasurer of the United States is the spokesperson for the campaign.

Historical Perspective

Federal debt outstanding is one of the largest legally binding obligations of the Federal Government. Nearly all the federal debt has been issued by the Treasury with a small portion being issued by other federal government agencies. Treasury issues debt securities for two principal reasons, (1) to borrow needed funds to finance the current operations of the Federal Government and (2) to provide an investment and accounting mechanism for certain federal government accounts' (primarily federal trust funds) excess receipts. Total gross federal debt outstanding has dramatically increased over the past 25 years from $2,350 billion as of September 30, 1987, to $16,059 billion as of September 30, 2012 (see Figure 5). Large budget deficits emerged during the 1980's due to tax policy decisions and increased outlays for defense and domestic programs. Through fiscal year 1997, annual federal deficits continued to be large and debt continued to grow at a rapid pace. As a result, total federal debt more than doubled between 1987 and 1997.

Figure 5 **Total Gross Federal Debt Outstanding**



Source: Monthly Statement of the Public Debt

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

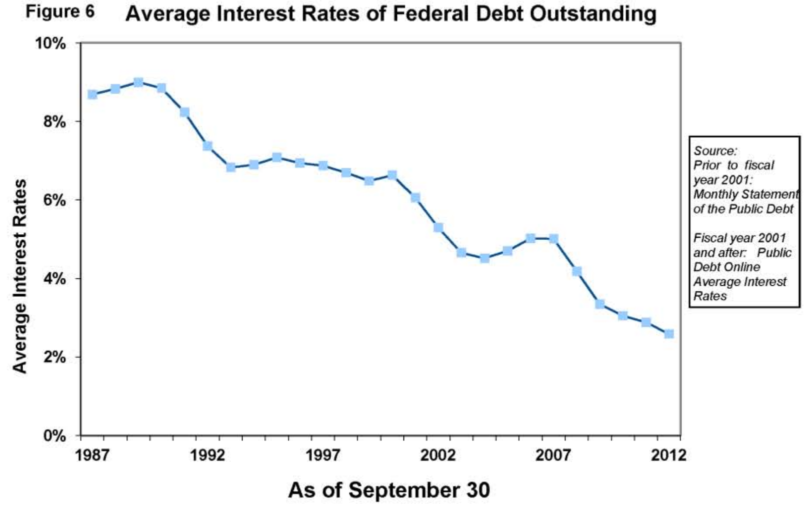
By fiscal year 1998, federal debt held by the public was beginning to decline. In fiscal years 1998 through 2001, the amount of debt held by the public fell by $476 billion, from $3,815 billion to $3,339 billion. However, federal debt held by the public began to increase in fiscal year 2002, primarily as a result of higher federal outlays. Federal debt held by the public increased by 51.2 percent from fiscal year 2002 through fiscal year 2007. From fiscal year 2008 through fiscal year 2012, federal debt held by the public more than doubled, rising by $6,221 billion. This increase was primarily a result of the economic downturn and the federal government's response to it. Since fiscal year 2002, debt held by the public has increased from $3,339 billion as of September 30, 2001 to $11,270 billion as of September 30, 2012.

Historical Perspective, cont.

Even in those years where debt held by the public declined, total federal debt increased because of increases in intragovernmental debt holdings. Over the past 4 fiscal years, intragovernmental debt holdings increased by $587 billion, from $4,202 billion as of September 30, 2008, to $4,789 billion as of September 30, 2012. By law, federal government accounts, including trust funds, have the authority or are required to invest their excess annual receipts (including interest earnings) over disbursements in federal securities. As a result, the intragovernmental debt holdings balances primarily represent the cumulative surplus of funds due to the trust funds' cumulative annual excess of tax receipts, interest credited, and other collections compared to spending.

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

Figure 6 Average Interest Rates of Federal Debt Outstanding



Schedules of Federal Debt

Schedules of Federal Debt

Managed by the Bureau of the Public Debt
For the Fiscal Years Ended September 30, 2012 and 2011
(Dollars in Millions)

	Federal Debt					
	Held by the Public			Intragovernmental Debt Holdings		
	Principal (Note 2)	Accrued Interest Payable	Net Unamortized Premiums/ (Discounts)	Principal (Note 3)	Accrued Interest Payable	Net Unamortized Premiums/ (Discounts)
Balance as of September 30, 2010	**$9,022,808**	**$46,991**	**($33,870)**	**$4,528,083**	**$48,582**	**$38,404**
Increases						
Borrowings from the Public	7,965,202		(2,368)			
Net Increase in Intragovernmental Debt Holdings				126,291		12,364
Accrued Interest (Note 4)		244,218			205,881	
Total Increases	**7,965,202**	**244,218**	**(2,368)**	**126,291**	**205,881**	**12,364**
Decreases						
Repayments of Debt Held by the Public	6,860,979					
Interest Paid		239,739			206,685	
Net Amortization (Note 4)			(6,700)			3,144
Total Decreases	**6,860,979**	**239,739**	**(6,700)**	**0**	**206,685**	**3,144**
Balance as of September 30, 2011	**10,127,031**	**51,470**	**(29,538)**	**4,654,374**	**47,778**	**47,624**
Increases						
Borrowings from the Public	7,761,885		4,995			
Net Increase in Intragovernmental Debt Holdings				134,677		13,242
Accrued Interest (Note 4)		240,097			191,656	
Total Increases	**7,761,885**	**240,097**	**4,995**	**134,677**	**191,656**	**13,242**
Decreases						
Repayments of Debt Held by the Public	6,619,330					
Interest Paid		234,345			193,886	
Net Amortization (Note 4)			(5,318)			4,616
Total Decreases	**6,619,330**	**234,345**	**(5,318)**	**0**	**193,886**	**4,616**
Balance as of September 30, 2012	**$11,269,586**	**$57,222**	**($19,225)**	**$4,789,051**	**$45,548**	**$56,250**

The accompanying notes are an integral part of these schedules.

Notes to the Schedules of Federal Debt

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

For the Fiscal Years Ended September 30, 2012 and 2011

(Dollars in Millions)

Note 1. Significant Accounting Policies

Basis of Presentation

The Schedules of Federal Debt Managed by the Bureau of the Public Debt (BPD) have been prepared to report fiscal year 2012 and fiscal year 2011 balances and activity relating to monies borrowed from the public and certain federal government accounts under 31 U.S.C. § 3101 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. BPD, an organizational entity within the Fiscal Service of the Department of the Treasury, is responsible for issuing Treasury securities in accordance with such authority and to account for the resulting debt. In addition, BPD 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. BPD issues and redeems Treasury securities for these federal government accounts based on data provided by the respective program agencies and other Treasury entities. BPD also issues other specific securities outside of the authority of 31 U.S.C. § 3101, such as HOPE Bonds, that are not reported on the Schedules of Federal Debt Managed by the Bureau of the Public Debt.

Basis of Accounting

The schedules were prepared in conformity with U.S. generally accepted accounting principles and from BPD'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 conformity 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 Public Debt
For the Fiscal Years Ended September 30, 2012 and 2011

(Dollars in Millions)

Note 2. Federal Debt Held by the Public

As of September 30, 2012 and 2011, Federal Debt Held by the Public consisted of the following:

	2012		2011	
	Amount	Average Interest Rates	Amount	Average Interest Rates
Marketable:				
Treasury Bills	$ 1,613,026	0.1 %	$1,475,557	0.1%
Treasury Notes	7,114,960	2.0 %	6,406,983	2.3%
Treasury Bonds	1,194,715	5.4 %	1,016,408	5.8%
TIPS	807,469	1.4 %	705,352	1.9%
Total Marketable	$ 10,730,170		$9,604,300	
Nonmarketable	$ 539,416	2.1 %	$522,731	2.8%
Total Federal Debt Held by the Public	$ 11,269,586		$10,127,031	

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, 2012 and 2011. 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, 2012 and 2011. Treasury notes are issued with a term of 2 – 10 years and Treasury bonds are issued with a term of more than 10 years.

Treasury also issues TIPS that have interest and redemption payments that are tied to the Consumer Price Index for all Urban Consumers, a widely used measure of inflation. TIPS are issued with a term of 5 years or more. At maturity, TIPS are redeemed at the inflation-adjusted principal amount, or the original par value, whichever is greater. TIPS pay a semi-annual fixed rate of interest applied to the inflation-adjusted principal. The average interest rate on TIPS represents the stated interest rate on principal plus inflation, adjusted by any discount or premium on securities outstanding as of September 30, 2012 and 2011. The TIPS Federal Debt Held by the Public inflation-adjusted principal balance includes inflation of $77,909 million and $76,133 million as of September 30, 2012 and 2011, respectively.

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

For the Fiscal Years Ended September 30, 2012 and 2011

(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, 2012, the FRB had total holdings of $1,646,809 million, including a net of $1,523 million in Treasury securities held by the FRB as collateral for securities lending activities. As of September 30, 2011, the FRB had total holdings of $1,665,419 million, including a net of $759 million in Treasury securities held by the FRB as collateral for securities lending activities. These securities are held 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, 2012 and 2011. Nonmarketable securities are issued with a term of on demand out to 40 years.

As of September 30, 2012 and 2011, nonmarketable securities consisted of the following:

	2012	2011
Domestic Series	$ 29,995	$29,995
Foreign Series	2,986	2,986
State and Local Government Series	158,514	151,831
United States Savings Securities	183,661	185,187
Government Account Series	162,880	151,346
Other	1,380	1,386
Total Nonmarketable	$ 539,416	$522,731

Government Account Series (GAS) securities are nonmarketable securities issued to federal government accounts. Federal Debt Held by the Public includes GAS securities issued to certain federal government accounts. One example is the GAS securities held by the Government Securities Investment Fund (G-Fund) of the federal employees' Thrift Savings Plan. Federal employees and retirees who have individual accounts own the GAS securities held by the fund. For this reason, these securities are considered part of the Federal Debt Held by the Public rather than Intragovernmental Debt Holdings. The GAS securities held by the G-Fund consist of overnight investments redeemed one business day after their issue. The net increase in amounts borrowed from the fund during fiscal years 2012 and 2011 are included in the respective Borrowings from the Public amounts reported on the Schedules of Federal Debt.

Fiscal year-end September 30, 2012, occurred on a Sunday. As a result, $53,003 million of marketable Treasury notes, $35 million of Government Account Series securities, and $1 million of State and Local Government Series securities, matured but not repaid are included in the balance of the total debt held by the public as of September 30, 2012. Settlement of this debt repayment occurred on Monday, October 1, 2012.

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

For the Fiscal Years Ended September 30, 2012 and 2011

(Dollars in Millions)

Note 3. Intragovernmental Debt Holdings

As of September 30, 2012 and 2011, Intragovernmental Debt Holdings are owed to the following:

		2012	2011
SSA:	Federal Old-Age and Survivors Insurance Trust Fund	$ 2,586,697	$2,492,531
OPM:	Civil Service Retirement and Disability Fund	819,444	795,371
DOD:	Military Retirement Fund	376,439	326,040
HHS:	Federal Hospital Insurance Trust Fund	228,292	245,939
DOD:	Medicare-Eligible Retiree Health Care Fund	176,113	161,741
SSA:	Federal Disability Insurance Trust Fund	132,345	161,965
HHS:	Federal Supplementary Medical Insurance Trust Fund	69,324	70,446
DOE:	Nuclear Waste Disposal Fund	49,552	48,611
OPM:	Postal Service Retiree Health Benefits Fund	45,347	43,708
OPM:	Employees Life Insurance Fund	41,250	39,678
FDIC:	Deposit Insurance Fund	36,498	34,926
Treasury:	Exchange Stabilization Fund	22,680	22,721
OPM:	Employees Health Benefits Fund	21,259	19,191
DOL:	Pension Benefit Guaranty Corporation	21,114 *	20,974 *
DOL:	Unemployment Trust Fund	20,673	16,030
DOS:	Foreign Service Retirement and Disability Fund	16,893	16,397
DOT:	Airport and Airway Trust Fund	10,425	8,641
NCUA:	National Credit Union Share Insurance Fund	10,297	10,733
DOT:	Highway Trust Fund	9,970	16,302
Other Programs and Funds		94,439	102,429
Total Intragovernmental Debt Holdings		$ 4,789,051	$4,654,374

* These amounts consist of $5,038 million and $5,243 million of marketable Treasury securities as well as $16,076 million and $15,731 million of GAS securities as of September 30, 2012 and 2011, respectively.

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

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

For the Fiscal Years Ended September 30, 2012 and 2011

(Dollars in Millions)

Note 3. Intragovernmental Debt Holdings (continued)

Intragovernmental Debt Holdings primarily consist of GAS securities. Treasury issues GAS securities at either par value or at an amount that reflects a discount or a premium. GAS securities are issued with a term of on demand out to 30 years. GAS securities include TIPS, which are reported at an inflation-adjusted principal balance using the Consumer Price Index for all Urban Consumers. As of September 30, 2012 and 2011, the inflation-adjusted principal balance included inflation of $96,075 million and $87,986 million, respectively. The average interest rates on Intragovernmental Debt Holdings, excluding TIPS, for fiscal years 2012 and 2011 were 3.7 and 4.1 percent, respectively. The average interest rates on TIPS for fiscal years 2012 and 2011 were 1.5 and 1.8 percent, respectively. The average interest rate represents the original issue weighted effective yield on securities outstanding as of September 30, 2012 and 2011.

Fiscal year-end September 30, 2012, occurred on a Sunday. As a result, $2,145 million of GAS securities held by federal government accounts matured but not repaid is included in the balance of the Intragovernmental Debt Holdings as of September 30, 2012. Settlement of this debt repayment occurred on Monday, October 1, 2012.

Note 4. Interest Expense

Interest expense on Federal Debt Managed by BPD for fiscal years 2012 and 2011 consisted of the following:

	2012	2011
Federal Debt Held by the Public		
Accrued Interest	$240,097	$244,218
Net Amortization of Premiums and Discounts	5,318	6,700
Total Interest Expense on Federal Debt Held by the Public	245,415	250,918
Intragovernmental Debt Holdings		
Accrued Interest	191,656	205,881
Net Amortization of Premiums and Discounts	(4,616)	(3,144)
Total Interest Expense on Intragovernmental Debt Holdings	187,040	202,737
Total Interest Expense on Federal Debt Managed by BPD	$432,455	$453,655

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 BPD. Accrued interest on Federal Debt Held by the Public includes inflation adjustments of $10,652 million and $22,735 million for fiscal years 2012 and 2011, respectively. Accrued interest on Intragovernmental Debt Holdings includes inflation adjustments of $7,160 million and $15,220 million for fiscal years 2012 and 2011, respectively.

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

For the Fiscal Years Ended September 30, 2012 and 2011

(Dollars in Millions)

Note 5. Fund Balance with Treasury

	As of September 30, 2012	As of September 30, 2011
Appropriated Funds Obligated	$ 98	$107
Fiduciary Funds Obligated	$0*	$2
Total Fund Balance with Treasury	$ 98	$109

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

* Fiduciary Funds Obligated were definitive agency securities reported in deposit fund 20X6008, Payment of Principal and Interest on securities of Various Government Agencies. BPD no longer processes these securities, and the funds were returned to the agencies. There are no plans to resume accounting for these securities in the future.

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

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

The Bureau of the Public Debt's (BPD) 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 conformity with U.S. generally accepted accounting principles; and (2) transactions related to the Schedule of Federal Debt are executed in accordance with laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the Schedule of Federal Debt.

BPD management is responsible for establishing and maintaining effective internal control over financial reporting. BPD management evaluated the effectiveness of BPD's internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2012, 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, 2012, BPD's internal control over financial reporting relevant to the Schedule of Federal Debt was effective.

David A. Lebryk
Commissioner

Patricia M. Greiner
Chief Financial Officer

Matthew J. Miller
Assistant Commissioner
Office of Public Debt Accounting

Kimberly McCoy
Chief Information Officer

November 1, 2012

Appendix II: Comments from the Bureau of the Public Debt

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

November 2, 2012

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

Dear Mr. Engel:

This letter is in response to your audit of the Schedules of Federal Debt Managed by the Bureau of the Public Debt for the fiscal years ended September 30, 2012 and 2011. We agree with the conclusions of your audit report.

We appreciate the knowledge and experience displayed by your audit team as we finalize the sixteenth 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. With the recent management changes resulting from the proposed consolidation of the Bureau of the Public Debt and the Financial Management Service, we are dedicated to continued excellence and accuracy in our business environment. We look forward to sustaining a productive and successful relationship with your staff.

Sincerely,

David A. Lebryk
Commissioner

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