



Accounting and Information
Management Division

B-280769

August 28, 1998

The Honorable James A. Leach
Chairman, Committee on Banking and Financial Services
House of Representatives

Subject: Year 2000 Computing: EFT 99 Is Not Expected to Affect Year 2000
Remediation Efforts

Dear Mr. Chairman:

This letter responds to your request that we assess whether the Electronic Funds Transfer 99 (EFT 99) program is interfering with the capacity of the Financial Management Service (FMS) and financial institutions to complete Year 2000 remediation efforts. As you know, the EFT 99 program seeks to convert most federal payments from paper checks to electronic transactions starting January 2, 1999. A key aspect of this conversion is the establishment of electronic transfer accounts (ETA) for the millions of benefit recipients who do not have bank accounts so they can receive their payments electronically. FMS is overseeing governmentwide implementation of the program.¹

At the same time, FMS and individual financial institutions, the entities most affected by the requirements of EFT 99, are also busy addressing their top

¹FMS, which is a bureau within the Department of the Treasury, serves as the government's financial manager, central disburser, and collections agency, as well as its accountant and reporter of financial information. For fiscal year 1997, FMS reported processing over 850 million disbursements totaling more than \$1 trillion. FMS is also responsible for administering the world's largest collections system. Each year the government collects more than \$1.5 trillion, from sources such as individual and corporate taxes and Customs duties.

information technology priority—Year 2000 conversion.² If FMS and financial institutions do not address this problem in time, millions of individual benefit payments and trillions of dollars in electronic commerce could be affected.

BACKGROUND

Each year the federal government makes nearly one billion payments, for items such as federal employees' salaries, payments to vendors and federal contractors, benefit payments such as social security and veterans benefits, and other miscellaneous payments. A key provision of the Debt Collection Improvement Act of 1996³ requires that starting January 2, 1999, all federal payments—except for tax refunds—must be made using electronic funds transfer (EFT).⁴ However, the law also gives the Secretary of the Treasury broad authority to provide waivers to exempt certain individuals, classes of individuals, or certain types of payments from the EFT requirements.

In response to this provision, the Department of the Treasury established the EFT 99 program. The program requires that all new federal payment recipients—anyone who begins receiving payments after July 26, 1996—must receive their payments electronically. The program also requires, as mandated in the act, that all payment recipients to begin receiving payments electronically starting January 2, 1999.

However, on June 25, 1998, Treasury announced that all unbanked benefit recipients will receive a waiver from the EFT requirement until an ETA account meeting Treasury's specifications is available. In addition, once ETAs are available, recipients will be allowed to decide whether they want to sign up for ETAs or continue receiving a paper check. Treasury also announced that

²The Year 2000 problem is rooted in the way dates are recorded and computed. For the past several decades, systems have typically employed a two digit field to represent the year, such as "98" for 1998, to save electronic storage space and reduce operating costs. Using this date convention, however, the year 2000 can be misinterpreted as 1900, which could cause a system to malfunction or produce inaccurate information.

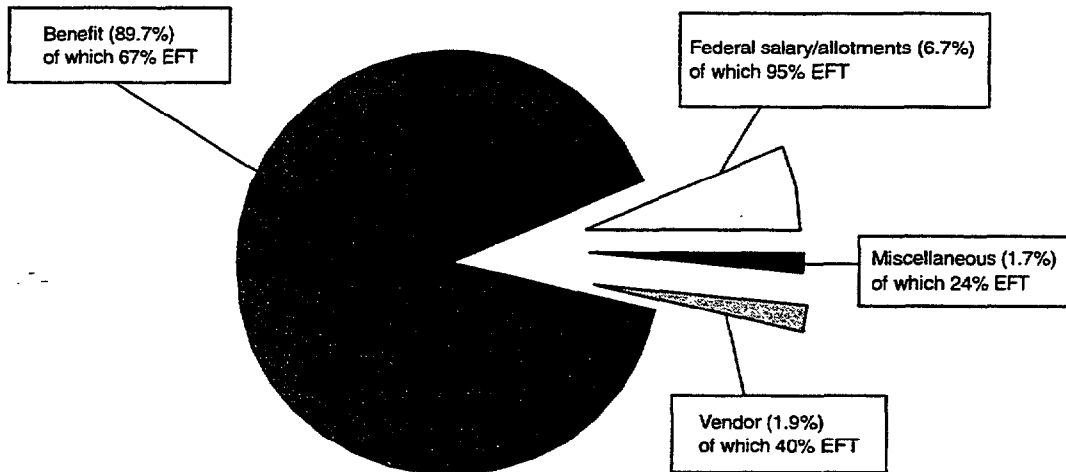
³The Debt Collection Improvement Act was part of the Omnibus Consolidated Rescissions and Appropriations Act of 1996 (Public Law 104-134).

⁴EFT refers to any transfer of funds between accounts through an electronic terminal, telephone, computer, or magnetic tape, without the use of checks or other paper.

current paper check recipients will not be automatically switched to electronic payment unless they request the change.

At the end of June 1998, FMS reported that more than two thirds of its total non tax disbursements were made electronically. Figure 1 shows the percentage of non tax payments in each category and the extent to which the payments are made electronically.

Figure 1: Percentage of Non tax Treasury-disbursed Payments (as of June 30, 1998)



Source: FMS. We did not independently verify this information.

A primary challenge facing Treasury in implementing the EFT 99 program is providing electronic disbursements for benefit recipients who do not have an account at a financial institution. Treasury estimates that currently 6 million to 8 million benefit recipients do not have bank accounts. For these recipients, Treasury plans to create electronic transfer accounts. Although the specific ETA account structure has not been finalized, Treasury expects that these

accounts will be similar to traditional Direct Deposit accounts.⁵ Once the account structure is defined, financial institutions will have the option of offering the accounts.

EFT 99 REQUIREMENTS ARE NOT
EXPECTED TO AFFECT FMS'
YEAR 2000 REMEDIATION EFFORTS

EFT 99 requirements are not expected to affect FMS' Year 2000 remediation efforts. FMS has made payments electronically for many years and thus the applications software and telecommunications infrastructure necessary for initiating electronic payments and transmitting them to financial institutions are already in place. In addition, the process of converting recipients from paper to electronic payment is relatively easy and is done by the program agencies (not by FMS). Consequently, FMS does not expect to make any system changes in preparation for EFT 99.

FMS began providing electronic payments over 20 years ago. In the years since then, it has developed a set of payment systems that are capable of providing both electronic and paper payments. Consequently, FMS officials said that no new system development or enhancement will be necessary to meet requirements of the law.

In addition, most of the electronic disbursements originated by FMS are processed through the Federal Reserve using the ACH network, which is connected to over 20,000 financial institutions. An FMS official noted that because so many financial institutions are already linked to the ACH network, meeting the requirements of EFT 99 and establishing ETAs should be relatively simple.

EFT 99 requirements should also not affect FMS' Year 2000 efforts because converting benefit recipients from paper to electronic payment is a relatively easy process that is conducted by program agencies (such as the Social Security Administration (SSA), Veterans Affairs, or Department of Labor), not FMS. Specifically, upon being notified that a recipient wants to switch from paper to electronic payments, the agency makes all necessary information changes and

⁵Direct Deposit, which was established over 20 years ago, uses the Automated Clearing House (ACH)—a group of networks utilized to facilitate EFT transactions within the financial community—to move funds electronically from an originator (in this case the government) to a receiver (the recipient's financial institution). Direct Deposit is the most widely used EFT program in the federal government with over 20,000 participating financial institutions.

forwards the updated payment information file to FMS. An official from SSA's Office of Finance Assessment and Management said that converting benefit recipients from paper to electronic payment is not difficult and that EFT 99's impact on SSA's workload should not be significant.

Finally, the volume of unbanked benefit recipients who will need to be switched from paper to electronic payments is likely to be much less than originally planned because of Treasury's recently announced waivers to the regulation. Initially, FMS and Treasury expected that when the ETAs became available, most benefit recipients without a bank account would be converted from paper to electronic payment. FMS' Assistant Commissioner for Federal Finance said that given the new waiver policy, he estimates that prior to the year 2000 only 20 to 30 percent of recipients without bank accounts will switch to using ETAs.

EFT 99 REQUIREMENTS ARE ALSO NOT EXPECTED TO AFFECT FINANCIAL INSTITUTIONS' YEAR 2000 EFFORTS

Like FMS, the Year 2000 conversion efforts of financial institutions are not expected to be affected by EFT 99. The systems infrastructure for receiving electronic payments from FMS through the Federal Reserve is already established and many institutions already offer accounts that are similar to those being proposed for the ETAs.

In addition, the financial institutions said that if conflicts do arise between completing Year 2000 efforts or offering ETAs, they will not offer ETAs. For example, a representative of the American Bankers Association noted that if the ETA structure is similar to accounts already maintained by financial institutions, then establishing the accounts should not interfere with Year 2000 efforts. He also said that if ETAs differ from existing account structures, few banks may choose to offer them because they will not be able to dedicate resources to develop a new account structure.

Some of the financial institutions expressed concern that because the account structure for ETAs has not yet been announced, they cannot determine how much system development will be necessary to tailor their accounts to meet ETA account specifications. These institutions said that the longer that the definition of ETAs is delayed, the more likely it is that banks will not initially offer the accounts. Treasury originally expected to announce the ETA account structure in the spring of 1998, then delayed it until the summer of 1998. Treasury officials now expect to announce the structure in the fall of 1998 and estimate that accounts will become available in 1999.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our review was to determine whether EFT 99 and the establishment of ETAs is likely to impede the timely completion of FMS' and financial institutions' Year 2000 remediation efforts. To determine the extent to which FMS' Year 2000 efforts will be affected, we interviewed officials from FMS, including the Chief Information Officer, Assistant Commissioner for Management/Chief Financial Officer, Assistant Commissioner for Federal Finance, and the Acting Deputy Commissioner. We also reviewed EFT 99 program and FMS Year 2000 program documentation, including plans and status reports. Finally, we talked to officials from SSA's Office of the Deputy Commissioner for Finance Assessment and Management to determine the workload associated with converting SSA benefit recipients from paper to electronic payments.

To determine the extent to which EFT 99 will impact the Year 2000 efforts of financial institutions, we interviewed representatives from the Independent Bankers Association of America (IBAA) and the American Bankers Association (ABA). We also interviewed representatives from several financial institutions recommended to us by the ABA or other financial institutions, including First Union Bank, Britton and Koontz 1st National Bank of Natchez, Mississippi, and Citibank. These financial institutions, which include both large regional and national banks and smaller community banks, were recommended because of their interest in ETAs or their experiences developing similar accounts. Finally, we reviewed the letters received by FMS from individuals and organizations commenting on the interim EFT regulation, including federal payment recipients, consumer organizations, government agencies, financial institutions, and non bank financial service providers.

Our audit work was performed between June 1998 and August 1998 in accordance with generally accepted government auditing standards.

We provided a draft of this letter to officials from FMS, ABA, and IBAA for their review and comment. These officials agreed with the report's message and offered several minor points of clarification. We have incorporated their clarifying comments where appropriate.

B-280769

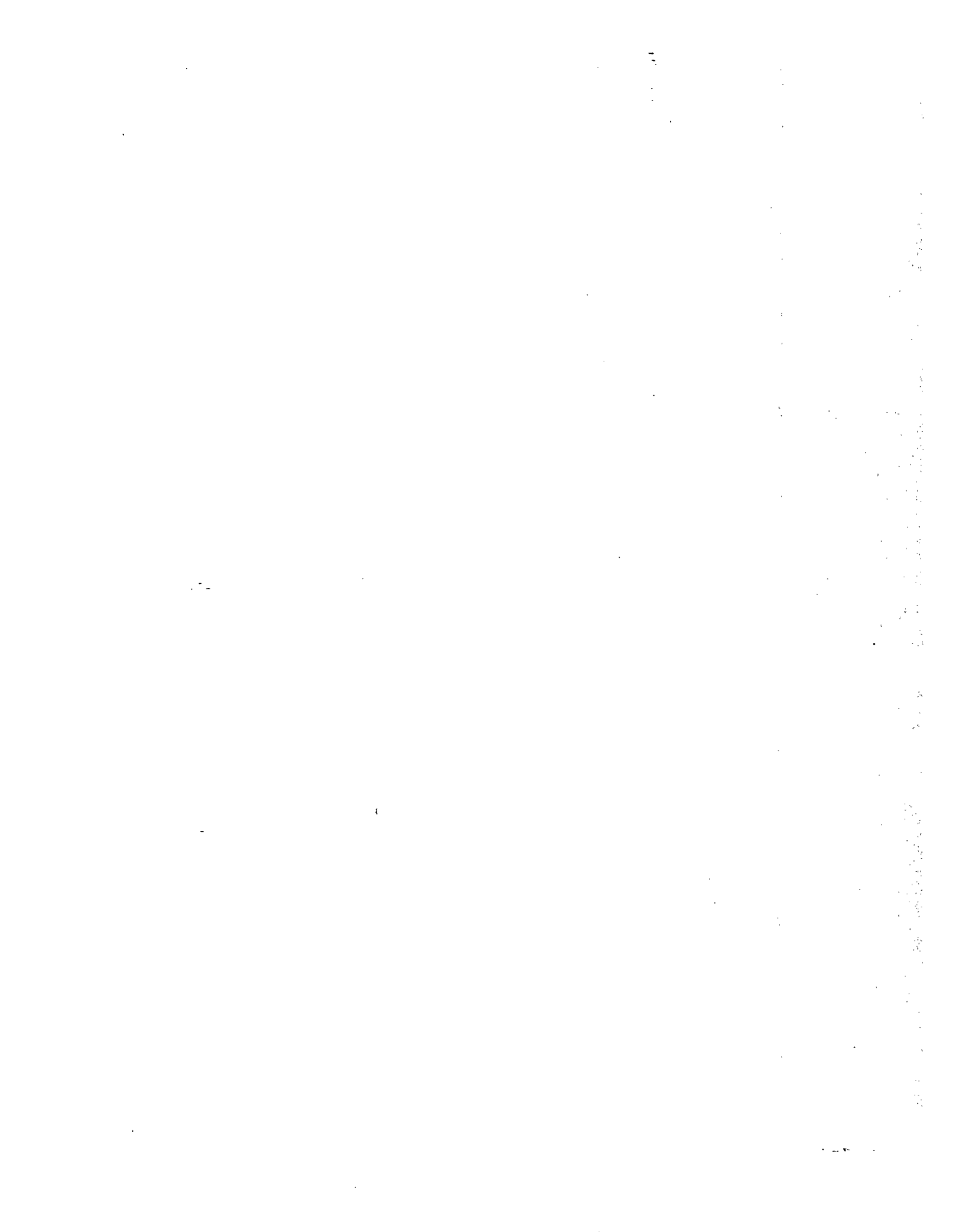
Contributors to this letter include Shane Hartzler and Katherine Chu. If you or your staff have any questions regarding information provided in this letter, please contact me at (202) 512-6256.

Sincerely yours,



Randolph C. Hite
Associate Director
Governmentwide and Defense
Information Systems

(511128)



Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are \$2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. VISA and MasterCard credit cards are accepted, also. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:

U.S. General Accounting Office
P.O. Box 37050
Washington, DC 20013

or visit:

Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC

Orders may also be placed by calling (202) 512-6000 or by using fax number (202) 512-6061, or TDD (202) 512-2537.

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (202) 512-6000 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

For information on how to access GAO reports on the INTERNET, send an e-mail message with "info" in the body to:

info@www.gao.gov

or visit GAO's World Wide Web Home Page at:

<http://www.gao.gov>

**United States
General Accounting Office
Washington, D.C. 20548-0001**

**Bulk Rate
Postage & Fees Paid
GAO
Permit No. G100**

**Official Business
Penalty for Private Use \$300**

Address Correction Requested
