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Direct deposit simplifies savings bond investing

Savings bond investors can now open accounts directly with the Treasury Department, have funds deposited by payroll deduction into the account, and then use those funds to buy Series EE or I savings bonds in amounts as small as $25.

While savings bonds are available to many federal employees through payroll deduction and other channels such as banks and savings and loans associations, Treasury is making it possible for employers to deposit payroll deductions directly into an employee's TreasuryDirect account.

BY MIKE MILES

The employee can control how deposited funds are invested through an Internet connection. This new service is primarily targeted at making it easier and less expensive for employers to offer payroll deduction, but it has the additional benefit of providing participating employees with greater flexibility and control over their investments.

TreasuryDirect was introduced two years ago as part of the Treasury Department's effort to modernize the way people buy its securities and to better compete with other fixed-income investment opportunities.

Under the traditional system, employers were required to maintain employee funds earmarked for savings bonds in trust and then purchase the requested bonds in paper form. The employer was required to maintain records and control procedures to account for the funds and the bonds. The new system will make the process as easy for the employer as any other direct deposit transaction -- reducing cost, liability and responsibility. It will also pass the responsibility for buying the bonds to the employee.

The new system will mean that employees no longer have to relinquish the purchasing decisions to their employer. The funds will arrive after each pay day in an account that the employee owns and directly controls. The process works like this:

■ The participant goes online to www.treasurydirect.gov and opens a TreasuryDirect account.

■ The participant asks his employer to withhold a specified amount from each paycheck. He provides the employer with the account and transit routing number for his TreasuryDirect account and instructs the employer to deposit the withheld amounts directly to the account.

■ The funds are held in a non-interest bearing account, called a certificate of indebtedness (COI), pending investment or disbursement.

■ The participant directs investment of the funds through the TreasuryDirect Web site.

To open a TreasuryDirect account, a participant must be at least 18 years old, have a Social Security number, a driver's license or state identification number, and an active checking or savings account.

Funds may be deposited to the account by direct deposit, either from your employer or from your designated bank account. You may designate more than one bank account on your TreasuryDirect account and specify which account you wish to use for each deposit.

When you sell securities, the proceeds are either deposited to your bank account or held in the COI at your direction.

Currently, only Series EE and Series I savings bonds can be purchased, managed and redeemed in a TreasuryDirect account. The Treasury Department plans to eventually add the capability to trade Treasury notes, bills, bonds and TIPS (Treasury Inflation Protected Securities) to TreasuryDirect.

Participants can schedule automatic purchases through TreasuryDirect up to five years in advance. All savings bonds are held in electronic rather than paper form, and purchases can be made for any amount of at least $25, up to the annual maximum limit, which is currently $30,000 per person for each series.

Another interesting feature of the TreasuryDirect account is that its owner may purchase bonds with a variety of registrations in one account. This means that in one account, the account owner may purchase bonds as sole owner, joint owner or in the name of a dependent child. The account also calculates the current value of your holdings and tracks and reports to you any taxable transactions that occur during the year.

As a financial planner, I'm impressed with the capabilities offered by TreasuryDirect and happy to hear that the plan is being made more widely available to employees through payroll deduction. Fixed-income securities are part of most every sound financial strategy, and Treasury-issued securities are the foundation of fixed-income investing.

As an individual investor, you should keep a few things in mind when deciding if, when and how to use TreasuryDirect:

■ TreasuryDirect accounts are not good places to park cash savings. Account holders must choose how to invest the funds. Unless invested in EE or I savings bonds, cash balances do not earn interest. So leaving cash balances in your account means you're probably losing ground to inflation. To avoid the problem of undirected funds, account holders can preselect how they want the funds invested.

■ Payroll deduction is a great way to save. This is a pay-yourself-first strategy you often hear endorsed by financial advisers. The money is saved before you ever get your hands on it.

■ There are no maintenance charges or transaction costs for purchases and redemptions made in a TreasuryDirect account.

■ The Series EE and I savings bonds currently available through TreasuryDirect have tax, risk and return characteristics that can make them an attractive part of a fixed-income portfolio, particularly if the proceeds are used to pay for qualified education expenses.

■ Savings bonds are intended to be, and best suited as, long-term investments. Redemption is prohibited during the first year of ownership and subject to penalties within five years of purchase.

Check with your payroll office about availability of voluntary withholding and direct deposit, and then visit www.treasurydirect.gov to learn more.

If you're unsure about how to proceed, consult a competent financial adviser. ■

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