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The Debt Limit: The Need to Raise It After Four Years of Surpluses

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Summary

Increases in total federal debt are driven by government deficits (which increase debt held by the public) and by the surpluses credited to (and federal accounting for) debt-holding federal accounts, mostly federal trust funds such as the Social Security, Medicare, Transportation, and Civil Service trust funds.

Government deficits increase debt held by the public; government surpluses reduce debt held by the public. The government surpluses over the last four fiscal years (1998-2001) reduced debt held by the public by $448 billion. The surpluses credited to debt-holding government accounts (which generally must invest the surpluses in federal debt), increased their holdings by $853 billion over the same period. The combination increased total federal debt by $405 billion. During FY2002 (through May 31, 2002), total debt subject to limit increased another $217 billion. The increases lifted federal debt to the then current statutory debt limit, $5.95 trillion, twice in 2002, most recently in mid-May 2002.

Since December 2001, the Administration repeatedly asked Congress to increase the $5.95 trillion debt ceiling by $750 billion. The Senate passed a $450 billion increase (S. 2578) on June 11; the House approved the bill on June 27 (by one vote). The President signed the legislation on June 28 (P.L. 107-199) raising the limit to $6.4 trillion, ending the most recent debt limit crisis. (This report will be updated as events warrant.)

The statutory debt limit applies to almost all federal debt.[1] It applies to federal debt held by the public, that is debt held outside the federal government itself, and to federal debt held by the government's own accounts, almost all of which are federal trust funds such as Social Security, Medicare, Transportation, and Civil Service. The government's

[1] When measured on a similar basis, just over one percent of total federal debt is excluded from debt limit coverage. On the last day of June 2002, total federal debt was $6.126 trillion; debt subject to limit was $6.058 trillion, 98.9% of the total debt.

overall surpluses or deficits determine the change in debt held by the public. Debt held in government accounts, on the other hand, is unaffected by the government's overall budget balance. The increases or decreases in debt held by government accounts are the product of government accounting practices and the reported surpluses (or deficits) of the accounts holding the debt.

Nearing or reaching the debt limit interferes with the Treasury's normal ability to finance federal activities or meet government obligations. If the Treasury cannot issue new debt (the effect of reaching the limit), the government may be unable to obtain the cash needed to pay its bills (when the government is operating with a deficit). The Treasury may also be unable to invest the surpluses of designated government accounts (the federal trust funds) in federal debt as generally required by law. In either case, the Treasury is in a bind; it is required by law to continue meeting the government's legal obligations, but the debt limit may prevent it from issuing the debt that would allow it to do so.

Table 1. Components of Debt Subject to Limit, FY1996-FY2002
(in billions of dollars)

End of Fiscal Year (or period)	**Debt Limit**	**Debt Subject to Limit**		
		Total	**Held by Government Accounts**	**Held by the Public**
1996	$5,500.0	$5,137.2	$1,432.4	$3,704.8
1997	5,950.0	5,327.6	1,581.9	3,745.8
1998	5,950.0	5,439.4	1,742.1	3,697.4
1999	5,950.0	5,567.7	1,958.2	3,609.5
2000	5,950.0	5,591.6	2,203.9	3,387.7
2001	5,950.0	5,732.6	2,435.3	3,297.3
FY1997 to FY2001	–-	405.0	853.4	-448.5

Source: U.S. Department of the Treasury, Financial Management Service, *Treasury Bulletin*, June 2001 and March 2002. *Daily Treasury Statement* April 30 and May 31, 2002. CRS calculations.

Note: For the fiscal years 1996 through 2000, the amounts held by government accounts and held by the public are approximations. The Treasury began producing this split into holders of debt subject to limit in its publications in 2001. The numbers in the table showing this split for 1996 through 2000 were calculated by subtracting Federal Financing Bank debt (an arm of the Treasury; its debt is not subject to limit) from total debt held by government accounts to approximate the amount of that debt subject to limit (a second subtraction, for unamortized discount, is unavailable, leaving the approximate amount too large by billions of dollars). This adjusted amount was then subtracted from total debt subject to limit to produce an approximate measure of debt held by the public subject to limit. Because the amount held by government accounts is too large, the resulting measure of debt held by the public subject to limit is too small. The approximations in the table are accurate enough to reveal the pattern of change in the two categories over the six years shown.

The $853 billion growth in federal debt held by the government's own accounts over the last four years (FY1998 through FY2001) plus its continued growth in FY2002 generated most of the pressure on the debt limit in the first six months of 2002. Over the same four years, debt held by the public fell by $448 billion (see **Table 1**; see also table note for information on these numbers).[2] The combination raised the total debt subject to limit by $405 billion between the end of fiscal year 1997 and the end of fiscal year 2001, moving it within $220 billion of the then existing $5.95 trillion statutory debt limit.[3] During FY2002, debt subject to limit has increased by another $217 billion, divided between an increase of $117 billion in debt held by government accounts and an increase of $100 billion in debt held by the public (through May 31, 2002). **Table 2** shows debt for this fiscal year by month and the month-to-month change.

Table 2. Components of Debt Subject to Limit by Month in FY2002

(in millions of dollars)

End of Month	**Total**	Change from Previous Period	**Held by Government Accounts**	Change from Previous Period	**Held by the Public**	Change from Previous Period
Sept. 2001	$5,732,580		$2,436,521		$3,296,059	
Oct. 2001	5,744,280	$11,700	2,451,815	$15,294	3,292,466	$-3,593
Nov. 2001	5,816,564	72,284	2,452,444	629	3,364,120	71,654
Dec. 2001	5,871,154	54,590	2,516,013	63,569	3,355,142	-8,978
Jan. 2002	5,865,742	-5,412	2,525,754	9,741	3,339,988	-15,154
Feb. 2002	5,933,002	67,260	2,528,494	2,740	3,404,507	64,519
March 2002	5,913,597	-19,405	2,548,764	20,270	3,364,833	-39,674
April 2002	5,914,816	1,219	2,549,438	674	3,365,378	545
May 2002	5,949,786	34,970	2,553,350	3,912	3,396,436	31,058
Total Change, Sept-May		$217,206		$116,829		$100,377

Source: U.S. Treasury, Bureau of the Public Debt, *Monthly Statement of the Public Debt*, September 2001-May 2002.

On April 4, 2002, the Treasury, to avoid exceeding the limit, used authority provided through existing legislation to suspend reinvestment of government securities (debt) in the G-Fund of the federal employees' Thrift Savings Plan. The Treasury exchanged between $5 billion and $35 billion in federal securities for the same amount of credit balances. This action lowered the amount of debt subject to limit and allowed the Treasury to sell debt to the public for cash necessary to pay the government's bills. On April 16, after the influx of the April 15th tax revenues, the Treasury "made whole" the G-Fund by restoring all the debt not invested over this period and crediting the fund with interest it would have earned on that debt.[4] (As the Treasury awaited the influx of tax

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[2] Until 2001, government publications did not divide debt subject to limit into the portions held by the public and held by government accounts. This discussion and the table use CRS calculated amounts that approximate the amounts of debt subject to limit held in these two categories for fiscal years prior to 2001.

[3] The previous increase in the debt limit was on August 5, 1997, as part of the Balanced Budget Act of 1997 (P.L. 105-33). The limit was raised from $5.5 trillion to $5.95 trillion.

[4] For a short discussion of the Treasury's previous uses of its short-term ability to avoid (continued...)

payments due on April 15, the debt subject to limit stood at $5,949,975 million, less than $25 million below the limit.) By the end of April and after the tax payments in mid-April, debt subject to limit fell to $35 billion below the limit. The Treasury continued to issue debt during May, leaving the debt subject to limit $15 million below the statutory limit at the end of the month (see **Table 2**).

In the fall of 2001, the Administration had recognized that the deterioration in the budget outlook and continued growth in debt held by government accounts was likely to lead to the debt limit being reached sooner rather than later. In early December, it asked Congress to raise the debt limit by $750 billion to $6.7 trillion. As the debt moved closer to and reached the debt limit over the last six months, the Administration repeatedly requested that Congress adopt an increase in the debt limit and warned Congress of the adverse financial consequences of not raising the limit.

The Current Situation

By mid-May 2002, federal debt subject to limit effectively reached the statutory limit of $5,950 billion. For the second time this year, the Treasury took extraordinary actions to avoid defaulting on government obligations. The previous brush with the debt limit took place from early to mid-April. This earlier episode was short-term and resolved itself with the large tax payments received on and after April 15. Since reaching the debt limit again in mid-May, the Treasury again used its available statutory authority to temporarily avoid the possibility of defaulting on the government's obligations.

The situation that began in mid-May was more serious than the earlier episode. It required the Treasury to resort to the financing actions used earlier and possibly could have led to additional actions not yet used. The situation could not be relieved without an increase in the debt limit. On May 14, the Treasury issued another request to Congress to raise the debt limit or produce some other statutory change that would allow the Treasury to issue new debt. The Treasury, in a news release, stated that, "absent extraordinary actions, the government will exceed the statutory debt ceiling no later than May 16."[5] The release went on to state that "a 'debt issuance suspension period' will begin no later than May 16 .... [This] allows the Treasury to suspend or redeem investments in two trust funds, which will provide flexibility to fund the operations of the government during this period."[6] By reducing the amount of federal debt held by these government accounts (and replacing it with non-interest bearing, non-debt instruments), the Treasury was able to sell debt to the public, providing the cash needed to finance federal activities or to issue debt to other federal trust fund accounts as required by law. The Treasury also stated that these "extraordinary" actions will suffice only, at most,

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[4] (...continued)
breaching the debt limit, see CRS Report 98-805, *Public Debt Limit Legislation: A Brief History and Controversies in the 1980s and 1990s*, by Philip Winters; for a comprehensive report see the GAO report, *Debt Ceiling: Analysis of Actions During the 1995-1996 Crisis*, Aug. 1996, GAO/AIMD-96-130.

[5] U.S. Department of the Treasury. Treasury News. *Treasury Statement on the Debt Ceiling*, May 14, 2002.

[6] Ibid.

through June 28, 2002. By late-June, without an increase in the debt limit, the Treasury indicated that it would need to take other actions to avoid breaching the ceiling.[7] By the end of June and into the first days of July with large payments and other obligation due, the Treasury stated that it would be out of all available options to issue debt and fulfill government obligations. The situation would then put the government on the verge of defaulting on some of those obligations.

Congress took action over May and June 2002, that eventually did lead to an increase in the debt limit. The House-passed supplemental appropriations for FY2002 (H.R. 4775; May 24, 2002) included, after extended debate, language allowing any eventual House-Senate conference on the legislation to add an increase in the debt limit. The Senate did not add debt-limit-increase language to its version of the supplemental appropriations bill, S. 2551 (incorporated as an amendment to H.R. 4775, June 3, 2002). The Senate leadership indicated a strong reluctance to include a debt limit increase in the supplemental appropriation bill. Instead, the Senate adopted a bill, S. 2578, raising the debt limit by $450 billion (to $6.4 trillion) without debate on June 11. A $450 billion increase in the debt limit would provide enough borrowing authority for government operations through at least the rest of calendar year 2002 and possibly into the summer of 2003. With the warning of possible imminent default looming over it, the House passed the $450 billion increase in the debt limit (by one vote) on June 27. The President signed the bill into law on June 28 (P.L. 107-199), ending the most recent debt limit crisis.

Concluding Comments

Between the previous increase in the debt limit (August 1997) and the beginning of this fiscal year (2002), the government's surpluses reduced debt held by the public. Since the beginning of FY2002 (and through May 31, 2002), the government's budget deficit has increased debt held by the public by $100 billion. Debt held by government accounts has grown steadily over the entire period and has increased by $117 billion so far this fiscal year (2002).

The budget forecasts in 2001 of large and growing surpluses through FY2011 showed rapid reductions in debt held by the public. The same forecasts (like the ones this year) showed steady growth in debt held by government accounts. The combination of the shrinkage in debt held by the public and growth in debt held by government accounts moderated the expected growth in total debt. The moderate growth pushed the eventual need to increase the debt limit late into the decade (the continued increases in debt held by government accounts would eventually overwhelm the reductions in debt held by the public). When the expectations of large surpluses disappeared along with the resulting reductions in debt held by the public (beginning in the fall of 2001 and confirmed in the budget reports early in 2002), total debt began growing more rapidly, making a debt limit increase an immediate rather than a distant concern.

The budget turnaround from last year's forecasts resulted from both economic and budgetary factors. These included deteriorated economic conditions, changes in technical

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[7] As of June 21, 2002, the Treasury has postponed a regular auction of securities but has not announced any other actions.

components of the budget models, and policy changes to both spending and revenues.[8] The ongoing and unexpected shortfall in revenues so far this fiscal year (2002), a result mostly of economic factors, has contributed substantially to the year's deficit.

Pressure to raise the debt limit over the last 50 years generally came from growth in debt held by the public as the government needed to borrow from the public to finance deficits. Growth in debt held by government accounts in the past, particularly before the 1983 changes to Social Security, was usually a relatively minor, but not insignificant factor in the growth of total debt subject to limit. In the current instance, in spite of an expected deficit and the resulting increase in debt held by the public, the increases in debt held by government accounts over the last five years (and continuing) have driven the growth in debt subject to limit and were the primary cause of the recent need to raise the debt limit.

[8] For FY2002, the $333 billion change in the budget balance since last January (2001) as estimated by CBO, came from $148 billion in economic changes, $94 billion in technical changes, $53 billion in higher spending (policy changes) including higher interest costs, and $38 billion in revenue reductions resulting from the June 2001 tax act. See CBO, *The Budget and Economic Outlook: Fiscal Years 2003-2012*, Jan. 2002, p. xiv.