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The Debt Limit: The Need for Increases

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Summary

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

Surpluses generally reduce debt held by the public. The surpluses over the four fiscal years 1998-2001 reduced debt held by the public by $448 billion. More than offsetting this debt reduction, 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 ($853 billion minus $448 billion) raised total federal debt by $405 billion. During 2002, debt subject to limit increased enough to reach the then current statutory debt limit, $5.95 trillion, in early April and again in May 2002. The limit was increased to $6.4 trillion in June 2002.

In December 2002, the Administration began warning Congress that the debt limit would need to be increased again, this time in the first half of 2003. As the limit was approached in February 2003, the Administration resorted to measures at its disposal to avoid reaching the limit. The adoption (April 11, 2003) of the conference report (H.Rept. 108-71) on the budget resolution (H.Con.Res. 95) for FY2004 generated legislation (H.J.Res.51) — deemed passed by the House — increasing the debt limit by $984 billion to $7.4 trillion. The increase would be the largest dollar increase in the debt limit ever enacted.

The Senate received the legislation on April 11, but did not begin its debate on the measure until May 23. The Senate rejected eight proposed amendments before passing the debt limit increase on May 23. The President signed the resolution into law on May 27 (P.L. 108-24). The new limit is expected to provide sufficient borrowing authority for the Treasury into the summer or fall of 2004.

This report will be updated as events warrant.

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The Debt Limit: The Need for Increases

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 Retirement. The government's 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.

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
2002	6,400.0	6,161.4	2,644.2	3,517.2
May 2003	7,384.0	6,498.7	2,755.9	3,742.8
Change During the Period of Surplus, FY1998 — FY2001		**405.0**	**853.4**	**-448.5**

Source: U.S. Department of the Treasury, Financial Management Service, *Treasury Bulletin*, June 2001 and March 2002. Bureau of the Public Debt *Monthly Statement of Public Debt*, September 2002 and May 2003. 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 the 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

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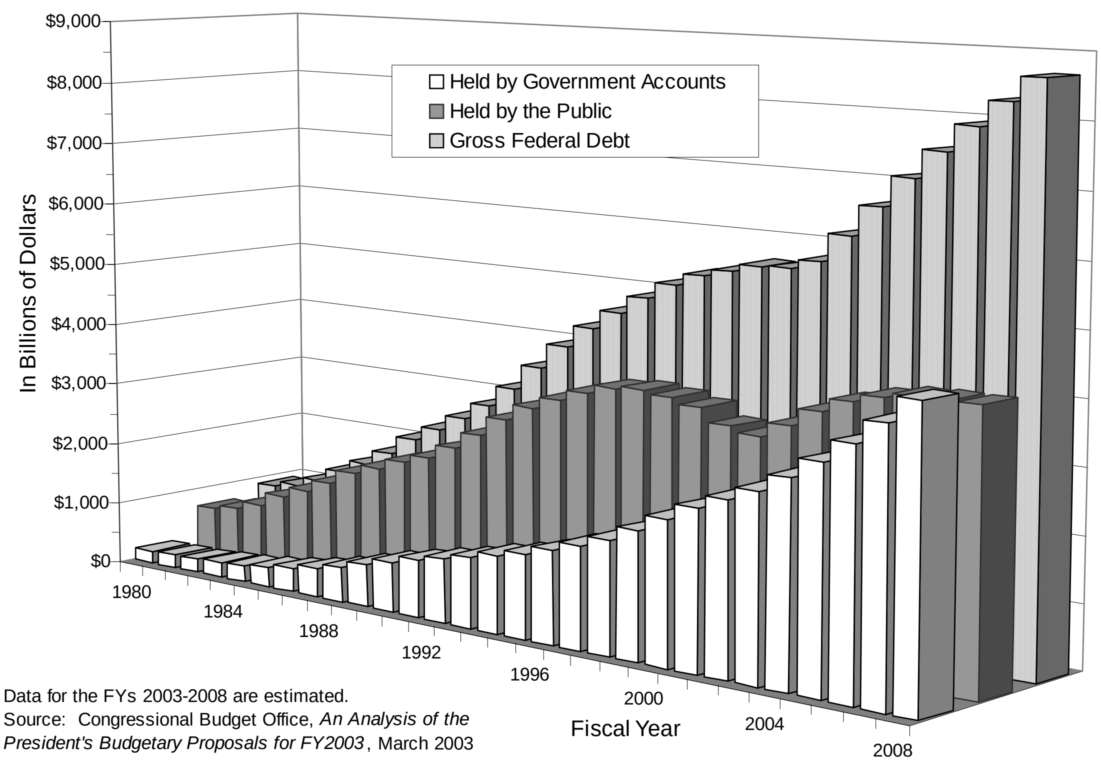
[1] Less than 1% of total the debt is excluded from debt limit coverage. On May 7, 2003, total debt was $6,460,345 million; debt subject to limit was $6,399,975 million, 99.1% of total debt.

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 provide adequate information to reveal the pattern of change in the two categories over the seven years shown.

Nearing or reaching the debt limit interferes with the Treasury's normal ability to finance federal activities or meet government obligations. The government's income and outlays vary over the course of the year, producing monthly surpluses and deficits that affect the level of debt, whether the government has a surplus or deficit for the entire year. The government accounts holding federal debt also can experience monthly deficits and surpluses, even if most of them show annual surpluses. 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 (under a short-term cash flow problem or from an annual deficit) or it may 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.

Figure 1. Components of Federal Debt



Data for the FYs 2003-2008 are estimated.
Source: Congressional Budget Office, *An Analysis of the President's Budgetary Proposals for FY2003*, March 2003

The federal debt held by the government's own accounts grew by $853 billion over the four years of budget surpluses, FY1998 through FY2001, and continues to grow; debt held by the public fell by $448 billion over the same period and has been growing since FY2001 because of the budget deficits (see **Table 1**). The growth in the components of debt are shown graphically in **Figure 1** (above). The data and the estimates are from CBO's March 2003 budget report.[2] These CBO baseline estimates provided data for the fiscal years 2003 through 2013, but **Figure 1** shows only the years through FY2008 (the same period covered by the President's budget). Legislation adopted after the March CBO report (the FY2003 supplemental and the tax cut) will increase current and future deficits. The higher deficits, and resulting larger debt held by the public, will be included in the CBO budget report expected in August 2003.

As can be seen in the chart, debt held by government accounts has grown steadily since 1980, mostly as a result of changes in Social Security adopted in 1983. Debt held by the public (which changes in response to total surpluses or deficits) grew through FY1997, and fell as the government had surpluses from FY1998 through FY2001, before growing once again with the return of deficits in FY2002 and the expected deficits through at least FY2008.[3] CBO's March 2003 estimates show the amount of debt held by government accounts exceeding the debt held by the public in FY2008 and for the fiscal years through 2013 (under baseline assumptions at that time).

The Situation in 2002

The ongoing increases in debt held by government accounts produced most of pressure on the debt limit early in 2002. The re-emergence of deficits in FY2002, which led to increases in debt held by the public, added to the pressure on the debt limit later in the first six months of 2002.[4] The increases in federally held debt and decreases in debt held by the public produced a net increase of $405 billion in debt subject to limit over the fiscal years 1998 through 2001. At the beginning of FY2002 (October 1, 2001), debt subject to limit was within $217 billion of the then $5.95 trillion debt limit.[5] Between then and the end of May 2002, debt subject to limit increased by another $217 billion, divided between a $117 billion increase in debt held by government accounts and a $100 billion increase in debt held by the public, putting the debt very close to the $5.95 trillion limit. **Table 2** shows debt by month for FY2002 and FY2003 with month-to-month changes calculated.

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[2]CBO. *An Analysis of the President's Budgetary Proposals for Fiscal year 2004*, March 2003.

[3]Once the Social Security system begins drawing on its holdings of debt, debt held by government accounts is very likely to begin falling while, without substantial policy changes, debt held by the public will grow rapidly as the government likely experiences growing and persistent deficits.

[4] 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 Table 1 use CRS calculated amounts that approximate the amounts of debt subject to limit held in these two categories for fiscal years prior to 2001.

[5]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.

In the fall of 2001, the Administration 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 2001, 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 first six months of FY2002, 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.

Table 2. Components of Debt Subject to Limit by Month in FY2002-FY2003

(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	$5,732,802		$2,436,521		$3,296,281	
Oct. 2001	5,744,523	$11,721	2,451,815	$15,294	3,292,709	$-3,572
Nov. 2001	5,816,823	72,300	2,469,647	17,832	3,347,176	54,467
Dec. 2001	5,871,413	54,590	2,516,012	46,365	3,355,401	8,225
Jan. 2002	5,865,892	-5,521	2,525,755	9,743	3,340,138	-15,263
Feb. 2002	5,933,154	67,262	2,528,494	2,739	3,404,659	64,521
March 2002	5,935,108	1,954	2,528,318	-176	3,406,789	2,130
April 2002	5,914,816	-20,292	2,549,438	21,120	3,365,378	-41,411
May 2002	5,949,975	35,159	2,553,350	3,912	3,396,625	31,247
June 2002	6,058,313	108,338	2,630,646	77,296	3,427,667	31,042
July 2002	6,092,050	33,737	2,627,980	-2,666	3,464,070	36,403
Aug. 2002	6,142,835	50,785	2,620,946	-7,034	3,521,890	57,820
Sept. 2002	6,161,431	18,596	2,644,244	23,298	3,517,187	-4,703
Oct. 2002	6,231,284	69,853	2,680,812	36,568	3,550,472	33,285
Nov. 2002	6,294,480	63,196	2,680,788	-24	3,613,692	63,220
Dec. 2002	6,359,412	64,932	2,745,787	64,999	3,613,625	-67
Jan. 2003	6,355,812	-3,600	2,753,301	7,514	3,602,511	-11,114
Feb. 2003	6,399,975	44,163	2,750,471	-2,830	3,649,504	46,993
March 2003	6,399,975	0	2,722,812	-27,659	3,677,163	27,659
April 2003	6,399,975	0	2,731,042	8,230	3,668,933	-8,230
May 2003	6,498,658	98,683	2,755,895	24,853	3,742,763	73,830
Change in FY2003, year to date		**$337,227**		**$111,651**		**$225,576**
Change, end of Sept 01-May 03		**$765,856**		**$319,374**		**$446,482**

Source: U.S. Treasury, Bureau of the Public Debt, *Monthly Statement of the Public Debt*, September 2001-May 2003.

On April 4, 2002, the Treasury, to avoid exceeding the limit, used authority provided through existing legislation to suspend reinvestment of government securities in the G-Fund of the federal employees' Thrift Savings Plan (TSP). 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 existing debt subject to limit and allowed the Treasury to issue new debt and meet the government's obligations. On April 16, after the influx of April 15 tax revenues, the Treasury "made whole" the G-Fund by restoring all of the debt that had not been issued to the TSP over this period and crediting the fund with interest it would have earned on that debt.[6] (As the Treasury awaited the influx of tax 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, debt-subject-to-limit had fallen $35 billion below the limit. The Treasury continued to issue debt during May, ending the month with debt subject to limit $15 million below the statutory limit (see **Table 2**).

Resolving the Debt Limit Issue in 2002

By mid-May 2002, federal debt subject to limit effectively reached the statutory limit of $5,950 billion. The previous brush with the debt limit took place from early to mid-April. That earlier episode was short-term and resolved itself with the large tax payments received on and after April 15. When the debt limit was again reached in mid-May 2002, the Treasury, for the second time in 2002, used its available statutory authority to temporarily avoid a default 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, if it had lasted long enough, possibly could have led to additional actions that had not yet been 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."[7] The release went on to state that

> a "debt issuance suspension period" will begin no later than May 16 [2002] .... [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.[8]

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 again able to issue debt to meet the government's obligations. The Treasury also stated that these "extraordinary" actions would suffice only, at the longest, through June 28, 2002. By that date, without an increase in the debt limit, the Treasury indicated that

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[6]For a short discussion of the Treasury's previous uses of its short-term ability to avoid 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 U.S. General Accounting Office, *Debt Ceiling: Analysis of Actions During the 1995-1996 Crisis*, GAO/AIMD-96-130, Aug. 1996.

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

[8]Ibid.

it would need to take other actions to avoid breaching the ceiling.[9] By the end of June and into the first days of July, with large payments and other obligations 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.

Congress took action over May and June 2002, that eventually led 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. At that time, a $450 billion increase in the debt limit was thought to 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 2002 debt limit crisis.

The Situation in 2003

On Christmas Eve, 2002, the Treasury sent a letter to Congress requesting an unspecified increase in the debt limit by late February 2003, indicating that the $6.4 trillion debt limit would be reached about that time. The 108th Congress, just getting organized early in 2003, did not focus on the near-term need to raise the limit. Through the winter and into the spring, the Treasury repeatedly requested that the debt be raised to avoid a serious financial problem. By February 20, 2003, the Treasury had resorted to its management of the debt holdings of certain government accounts, as it had in 2002. These actions included the replacement of internally held government debt with non-debt instruments and not issuing new debt to these accounts, allowing the Treasury to issue additional debt to the public to acquire the cash it needed to pay for the government's commitments (or to issue new debt to other federal accounts).

Through the rest of February and into May, the Treasury held debt subject to limit $15 million below the limit. The adoption of the conference report on the FY2004 budget resolution (H.Con.Res. 95; H.Rept. 108-71) on April 11, 2003, in the House triggered the "Gephardt rule" (House Rule XXVII) that deems passed

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[9]By June 21, 2002, the Treasury had postponed a regular auction of securities but had not announced any other actions.

legislation (H.J.Res. 51) raising the debt limit by enough — $984 billion — to meet the financing needs for the policies contained in the budget resolution.[10]

The Senate received the debt-limit legislation on the same day, but did not consider the legislation until May 23, after receiving further warnings of imminent default from the Treasury. After rejecting eight proposed amendments, the Senate adopted the legislation unchanged, sending it on to the President. The President signed the legislation on May 27, raising the debt limit to $7.384 trillion (P.L.108-24). On the day the Senate cleared the increase in the debt limit, debt subject to limit was $25 million below the $6.4 trillion limit. By the end of May 2003, debt subject to limit had reached $6,498.7 billion.

Concluding Comments

Between the increase in the debt limit in August 1997, to $5.95 trillion, and the beginning of FY2002, the surpluses in the budget resulted in reductions in debt held by the public. Since the beginning of FY2002 (and through May 2003), the reappearance of deficits increased debt held by the public by $463 billion. Debt held by government accounts has grown steadily throughout the period. These increases raised the debt-subject-to-limit to $6,399,975 million, almost to the limit then of $6.4 trillion by the end of February 2003.

The Treasury was able to avoid exceeding the limit from February 2003 into mid-May 2003. At that time, it warned Congress that without an immediate increase in the debt limit, the Treasury would be unable to meet the government's existing obligations beginning on May 28. Although the Treasury has the authority to manage selected internal accounts holding federal debt, the method is limited and runs out of resources at some point. That point was reached in late May this year.

The 10-year budget forecasts produced in 2001 of large and growing surpluses through FY2011 included estimates and projections of the resulting rapid reduction in debt held by the public. The same 2001 forecasts projected continuous, 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 forecast growth in total debt. The estimates indicated that the moderate growth in total debt would delay the 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, triggering the need to increase the debt limit). When the expectations of large surpluses collapsed, late in the fall of 2001, so did the expectations of reductions in debt held by the public. Total debt resumed a fairly rapid rate of growth, making an increase in the debt limit necessary much sooner than previously thought.

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[10] See CRS Report 98-453, *Debt-Limit Legislation in the Congressional Budget Process*, by Bill Heniff Jr., and CRS Report RL31913, *Developing Debt-Limit Legislation: The House's 'Gephardt Rule'*, by Bill Heniff Jr.

The persistence of deficits over most of the last half century requiring the government to borrow from the public, plus the constant growth in government held debt, particularly after FY1983, increased debt subject to limit. The growth has periodically put pressure on Congress to raise the debt limit. The need to raise the debt limit in FY2002, the year after four years of surpluses during which debt held by the public fell, was driven primarily by the continuous increases in debt held by government accounts and secondarily by the return of government budget deficits in FY2002. The debt financing of the deficit in FY2003 plus the constant rise in debt held by government accounts drove the debt against the existing $6.4 trillion debt limit early in 2003. The Treasury was able to avoid actually breaching the limit into May. Congress adopted a debt limit increase of $934 billion on May 23, 2003, that is expected to provide enough room for the expected growth in both publicly held and government account held debt through the summer or fall of 2004.