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INSIGHT

The Debt Limit in 2021

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Debt limit episodes—which can be defined as starting when the statutory limit on federal debt restricts some of the U.S. Treasury's normal debt operations and ending when new legislation to modify the limit is enacted—have been a recurrent federal fiscal feature in the past two decades. Since 2002, the debt limit has been modified 18 times. The Bipartisan Budget Act of 2019 (P.L. 116-37), enacted in August 2019, suspended the debt limit through July 31, 2021.

Recent debt limit episodes share similarities, although the issue in 2021 has a few unique characteristics. First, the COVID-19 pandemic remains a source of economic uncertainty, and the fiscal responses it spurred have accelerated the pace of federal debt accumulation. Second, the U.S. Treasury sharply increased its cash balances in 2020 to accommodate those fiscal responses. Third, since 2015, Bipartisan Budget Acts that adjusted statutory caps on discretionary spending imposed by the Budget Control Act of 2011 (BCA; P.L. 112-25) also suspended the debt limit. The expiration of those discretionary spending caps at the end of FY2021 rendered moot the need for legislation to modify them. Thus, the legislative vehicle used for the past few debt limit modifications is unavailable in 2021.

Federal Debt and the Debt Limit

When in force, the debt limit covers over 99% of federal debt. Federal debt grows when outlays exceed revenues and when the federal credit balance sheet expands. Federal debt outstanding in mid-July 2021 totaled about $28.5 trillion. Most of that debt—$22.3 trillion—is held by the public, including $5.1 trillion in Federal Reserve holdings. Another $6.2 trillion is held as *intragovernmental debt*, mostly in various federal trust funds such as Social Security and federal retirement programs, which hold special Treasury securities that can be redeemed later to pay program expenses.

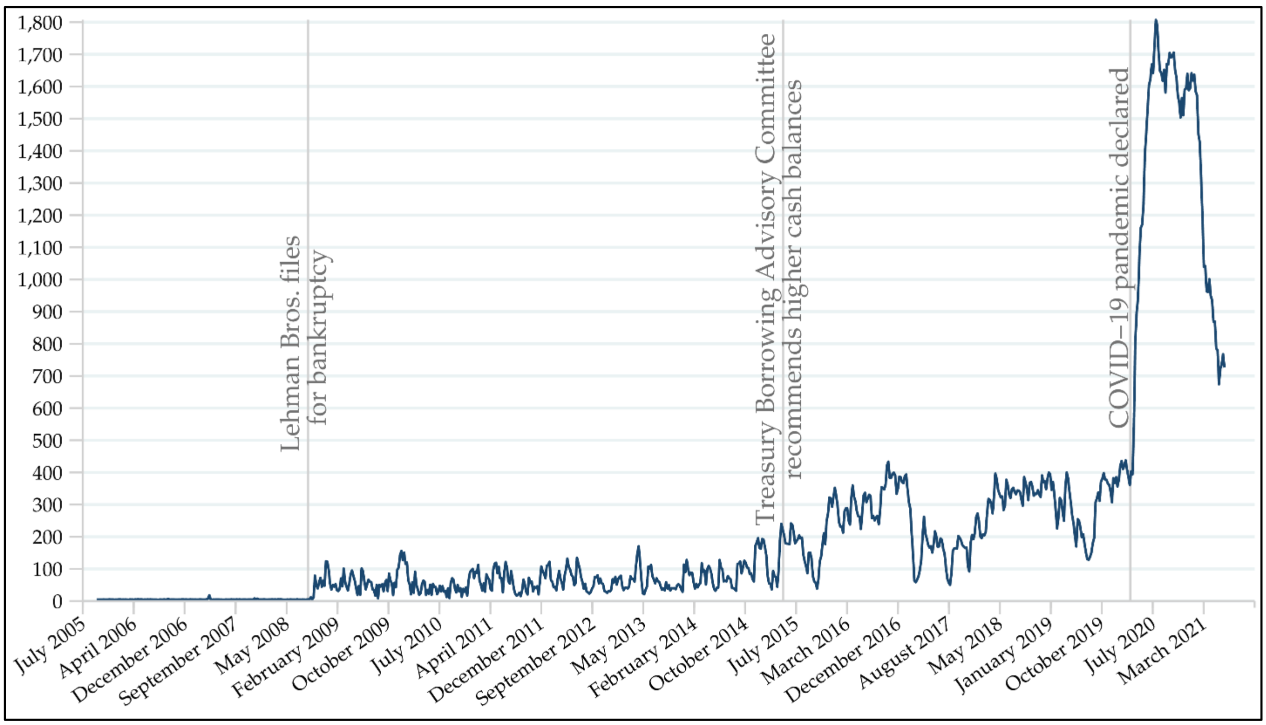
The Treasury Secretary and Extraordinary Measures

On Monday, August 2, 2021, the debt limit will be reset to a level accommodating federal financial commitments since the current suspension began. Once the debt limit would restrict issuance of special securities to the Civil Service retirement trust fund, Treasury Secretary Janet Yellen can then invoke authorities to use "extraordinary measures" by declaring a "debt issuance suspension period." The U.S. Treasury may then suspend investments in Civil Service and U.S. Postal Service retirement funds to help meet other federal obligations. Federal financial operations then continue normally, although debt limit restrictions complicate Treasury's debt and cash management. Once a debt limit episode is resolved, Treasury must report on how it used extraordinary measures.

Treasury Cash Balances

During a debt limit episode, Treasury can pay obligations as long as it retains borrowing capacity, cash balances, and funds available through its extraordinary measures. Treasury's cash balances are now much higher than a decade ago, as **Figure 1** shows. Before the Lehman Brothers investment bank collapsed in September 2008, Treasury cash balances were kept to minimal levels. Balances then fluctuated at levels mostly below $100 billion, although low interest rates reduced the opportunity cost of holding cash. In 2015, a Treasury advisory committee recommended increasing cash balances to cover an average week's outlays as a precaution against financial disruptions on the scale of those following the September 11, 2001, attacks or 2012's Hurricane Sandy. Cash balances rose sharply after the March 2020 declaration of COVID-19 as a pandemic, as then-Treasury Secretary Steven Mnuchin acted to enable rapid disbursement of CARES Act (P.L. 116-136) payments. Treasury states that cash balances will be brought down to $450 billion when the debt limit suspension expires at the end of July 2021.

Figure 1. Treasury Cash Balances, $Billion, FY2006-FY2021

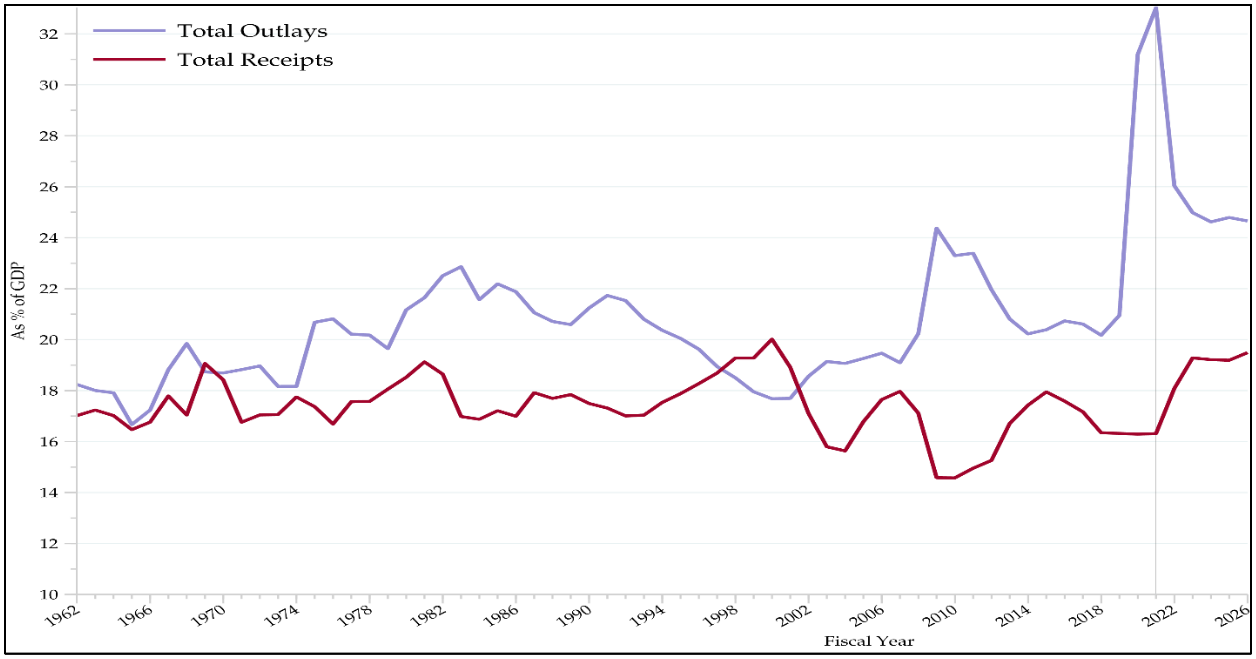


Source: CRS calculations based on U.S. Treasury's *Daily Treasury Statement*. Levels are weekly averages of cash balances of the U.S. Treasury's Federal Reserve Account.

How Long Can Treasury Pay Federal Bills?

At some point, Treasury's cash balances and borrowing capacity will be exhausted, implying that some federal obligations could not be paid on time, unless the debt limit were modified. Predicting when that might occur is especially hard in 2021. Economic recovery and growth in government revenues is rapid, although subject to "elevated" levels of uncertainty, according to the Federal Reserve. About $1.5 trillion in COVID-related budgetary resources remains unspent, which may heighten uncertainty on the pace of federal outlays. The gap between outlays and revenues—that is, the deficit—is at historically high levels in FY2021 (**Figure 2**). Secretary Yellen testified that absent action on the limit, default could become a serious risk by August 2021. Others estimate that Treasury might continue regular payments into November 2021, but warn that such projections are highly uncertain.

Figure 2. Federal Outlays and Receipts As a Percentage of GDP, FY1962-FY2026



Source: CRS calculations based on Office of Management and Budget (OMB), Congressional Budget Office (CBO), and Bureau of Economic Analysis (BEA) data and projections. FY2021-FY2026 outlay and revenue projections reflect Administration proposals. Gross domestic product (GDP) projections are from CBO's July 2021 budget update.

Congressional Options

Congress has used different means to control federal debt at different times. Since February 2013, Congress has suspended the debt limit several times. The Bipartisan Budget Acts of 2015 (BBA 2015; P.L. 114-74), 2018 (BBA 2018; P.L. 115-123), and 2019 (BBA 2019; P.L. 116-37) each suspended the debt limit and adjusted statutory caps on discretionary spending then in place upward, among other provisions. Those caps on discretionary budget authority, set in the BCA, expired at the end of FY2021, although sequestration of nonexempt mandatory spending has been extended.

In the decades before 2013, debt limit legislation typically specified a set dollar amount on outstanding debt. In 2011, the Budget Control Act allowed for three increases in the debt limit, with two subject to congressional resolutions of disapproval. Congress has at times passed stand-alone debt limit measures and, at other times, has packaged debt limit modifications with other provisions.

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