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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, 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. 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 raised total federal debt by $405 billion. During the first half of FY2002, debt subject to limit increased enough to reach the then current statutory debt limit, $5.95 trillion, in both early April and again in May 2002.

Beginning in December 2001, the Administration repeatedly asked Congress to increase the $5.95 trillion debt ceiling, initially by $750 billion. Not until June 11, 2002 did the Senate pass a $450 billion permanent increase (S. 2578 in the 107th Congress); 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 that debt limit crisis. The deficit in FY2002 ($158 billion) and the ongoing increases in debt held by government accounts, led the Administration, in late December 2002, to request that Congress again raise the debt limit, this time, with no amount specified and to raise it before late February 2003. (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

[1] Less than one percent of total the debt is excluded from debt limit coverage. On January 24, 2003, total debt was $6.392 trillion; debt subject to limit was $6.347 trillion, 999.3% of the total debt.

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 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
Change, FY1996 to FY2002		**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. 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 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. 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) 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.

The federal debt held by the government's own accounts grew by $853 billion over the four years, FY1998 through FY2001, and continues to grow; debt held by the public fell by $448 billion over the same period (see **Table 1**). The continuing 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.[2] The effect of the changes raised total debt subject to limit by $405 billion between the end of fiscal year 1997 and the end of fiscal year 2001. At the beginning of FY2002, debt subject to limit was within $220 billion of the then existing $5.95 trillion debt limit.[3] Between the beginning of FY2002 and the end of May 2002, debt subject to limit 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. **Table 2** shows debt by month for fiscal year 2002 and FY2003 with month-to-month changes.

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. 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 issue debt and meet the government's obligations. On April 16, after the influx of April 15th tax revenues, the Treasury "made whole" the G-Fund by restoring all the debt not provided 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 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 to $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**).

Earlier 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, 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.

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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 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.

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
Change in FY2002		**$428,629**		**$207,723**		**$220,906**
Change, Sept 01-Dec. 02		**$626,610**		**$309,266**		**$317,344**

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

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. For the second time in FY2002, 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. 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 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, if it 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."[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 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 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.

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. 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 that debt limit crisis.

The Current Situation

The growth in debt subject to limit since the June 2002 adoption of the last increase in the limit has again brought the outstanding amount close to the current $6.4 trillion limit. The *Daily Treasury Statement* for January 24, 2003 (from the Financial Management Service in the Department of Treasury) reports that debt subject to limit, $3,346.6 billion, is less than $55 billion below the existing limit. On Christmas Eve, 2002, the Treasury sent a letter to Congress requesting an unspecified increase in the debt limit by late February 2003. The 108th Congress, just getting organized early in 2003, has not indicated publicly how it will deal with a – likely – need to increase the limit. At this time, exactly when the debt limit will be reached is unknown, what actions Treasury will take to maintain the integrity of the government's accounts is unknown, and how long such actions can avoid a default is also uncertain. The Treasury may take actions such as

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

[6] Ibid.

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

those undertaken in 2002 of using existing authority to manage a limited number of government accounts' debt holdings to avoid precipitating a government default. These actions will work only for a limited time. Without an increase in the debt limit by Congress sometime in the relatively near future, the government will be unable to acquire the resources, financial or budgetary, that it will need to operate.

Concluding Comments

Between the previous increase in the debt limit (August 1997) and the beginning of fiscal year 2002, the government's surpluses reduced debt held by the public. Since the beginning of FY2002, the government's budget deficit has increased debt held by the public (by $318 billion). Debt held by government accounts has grown steadily over the entire period and has increased by $309 billion in fiscal year 2002. The increases moved debt-subject-to-limit $627 billion closer to the current limit.

The budget forecasts in 2001 of large and growing surpluses through FY2011 showed rapid reductions in debt held by the public. The same forecasts (as in most years) 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 estimate indicates that the moderate growth delayed 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). When the expectations of large surpluses collapsed, late in the fall of 2001, so did the reductions in debt held by the public. Total debt resumed a more rapid rate of growth, making an increase in the debt limit necessary sooner rather than later.

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 that debt subject to limit and were the primary cause of the need to raise the debt limit in FY2002.