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

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Summary

The statutory debt limit applies to over 98% of all federal debt, whether held by the government itself (by government accounts) or by the public (any individual or entity that is not the federal government). The government's surplus or deficit affects only the change in debt held by the public; changes in debt held by government accounts responds to surpluses or deficits credited to the accounts themselves.

Federal debt subject to limit is again closing in on the current statutory debt limit in spite of four years of surpluses. The surpluses reduced federal debt held by the public but had no effect on the ongoing increases in federal debt held by federal government accounts (which are mostly federal trust funds). Because of the continuing rise in government account held debt and the expectation of a government deficit in fiscal year 2002, the Administration requested, in December 2001, that Congress increase the existing $5.95 trillion limit to $6.7 trillion. The Administration indicated that the limit might begin interfering with the Treasury's ability to carry out its financial responsibilities as early as March 2002.

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 federal government accounts. The government's surpluses or deficits determine the change in debt held by the public. Debt held by government accounts, on the other hand, is unaffected by the government's budget balance. Their holdings of federal debt increase if they report surpluses – which most do – and decrease if they report deficits.

[1] A small amount of federal debt is excluded from debt limit coverage. At the end of fiscal year 2001, total federal debt was $5.834 trillion; debt subject to limit was $5.733 trillion, 98.3% of the total debt.

The primary factor generating the current pressure to raise the debt limit is the almost $900 billion growth in federal debt held by the government's own accounts (almost all in federal trust funds) over the last four years. Over the same four years, debt held by the public has fallen by almost $470 billion. The combination raised the 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 existing $5.95 trillion statutory debt limit. By the end of calendar year 2001, the debt subject to limit was within $80 billion of the limit.

The continuing rapid growth in debt held by government accounts and the deterioration in the budget outlook during the fall of 2001 prompted the Administration in early December 2001, to ask Congress to raise the debt limit by $750 billion to $6.7 trillion. Congress did not act on the request while it finished action on appropriations for fiscal year 2002 in mid-December.

Expectations that debt subject to limit would approach and eventually reach the limit early in 2002, prompted the Administration to make the request. Nearing or reaching the debt limit has the potential to produce a financial crisis for the government. If the Treasury cannot issue new debt (the effect of reaching the limit), the government may not be able to obtain the cash needed to pay its bills (if the government is operating with a deficit) or it may not be able to fully invest the surpluses of designated government accounts in federal debt as 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 keep it from using debt issuance that would allow it to do so. The financing problems for the Treasury could appear as early as March of 2002.

The Current Situation

The federal debt subject to limit, encompassing all but a relatively small amount of the debt issued by the Treasury plus a small amount of federal agency debt, is nearing the current statutory limit of $5,950 billion.[2] Although the government ran surpluses over the last four years (from 1998 through 2001), the surpluses reduced only that portion of federal debt held by the public. As intended, the other portion of federal debt, the portion held by federal government accounts (mostly by federal trust fund accounts), increased over the same four-year period and is expected to continue doing so for years to come. Over the four years of surpluses, debt held by government accounts increased by almost twice as much (by $881 billion) as debt held by the public declined (by $466 billion – see Table 1).[3] By the start of fiscal year 2002, the net effect of the changes put total debt subject to limit within $220 billion of the $5.95 trillion limit. The change from expected surpluses to expected deficits for fiscal year 2002 along with continued increases in debt held by government accounts had raised total debt subject to limit to $5,871 billion by the end of 2001 (calendar year), only $79 billion below the limit.

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[2] The debt limit was last increased 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.

[3] Government publications have not, until 2001, divided 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.

Table 1. Components of Debt Subject to Limit, FY1996-FY2001
(in billions of dollars)

End of Fiscal Year	Debt Subject to Limit			
	Debt Limit	**Total**	**Held by Government Accounts**	**Held by the Public**
1996	$5,500.0	$5,137.2	$1,432.0	$3,705.2
1997	5,950.0	5,327.6	1,571.8	3,745.9
1998	5,950.0	5,439.4	1,748.9	3,690.6
1999	5,950.0	5,567.7	1,976.7	3,594.0
2000	5,950.0	5,591.6	2,220.7	3,370.9
2001	5,950.0	5,732.8	2,452.8	3,279.7
December 31, 2001	5,950.0	5,871.4	2,534.0	3,337.4
FY1997 to FY2001	—	405.2	881.0	-466.2

Source: U.S. Department of the Treasury, Financial Management Service, *Treasury Bulletin*, June 2001 and December 2001. *Daily Treasury Statement* December 31, 2001. 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 their 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 (it remains too large even with this adjustment). 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.

Using the Debt Data from the August 2001 Budget Reports

Evidence exists in the mid-year budget reports from both the Congressional Budget Office (CBO) and the Office of Management and Budget (OMB) that, given the changed budget outlook since their publication, the current debt limit is unlikely to be high enough to accommodate the debt increase now expected for this fiscal year. Both budget reports were released prior to recognition of the severity of the economic situation and the budgetary effects resulting from the September 11 terrorist attacks. Neither report expected the debt limit to be reached this year but did indicate that it would be reached by the end of fiscal year 2003 (CBO) or sometime in fiscal year 2004 (OMB).[4] The changes

[4] The increases in debt held by government accounts would have produced a need to increase the debt limit within two years, *even if the budget had remained in surplus*. This would produce limitations on the Treasury's ability to issue its own debt to the government's own accounts. The government would not be short of any resources to carry out its obligations to the public; it would (continued...)

in the budget outlook after the reports came out, in particular the likely loss of the surplus for fiscal year 2002, changed the timetable for when the debt limit is likely to be reached. According to the Administration's December request for an increase in the debt limit, it could happen as soon as March of 2002.

The August reports contain data that help clarify the turnaround in the debt limit outlook. The CBO report estimated that debt subject to limit would grow by $105 billion and OMB estimated a $103 billion increase. These amounts would have left debt subject to limit slightly more than $100 billion below the current debt limit. The overall increases in debt subject to limit obscured the different directions of change expected in the two components of debt, debt held by government accounts and debt held by the public. The reports showed that debt held by government accounts would increase an estimated $258 billion (OMB) to $261 billion (CBO). Because the reports expected a surplus, they both estimated that debt held by the public would fall by approximately $155 billion.

If one assumes that the government will no longer have a surplus in fiscal year 2002, then debt subject to limit will increase by at least the size of the increases in debt held by government accounts, approximately $260 billion. Such an increase would put the debt subject to limit well above the current debt limit (by between $40 billion and $50 billion). If one further assumes that the government will have a deficit, as the Administration and releases from both congressional Budget Committees have indicated is likely, then debt held by the public will also increase over the course of the year, adding to the increase in debt subject to limit. The increase in debt held by government accounts is probably the minimum amount that debt subject to limit will increase; any budget deficit will increase debt held by the public, moving the date of reaching the limit sooner rather than later in the year. The $79 billion gap existing at the beginning of the year can disappear quickly, constraining the Treasury's ability to fully finance the government's obligations, either externally or internally.

Concluding Comments

Currently, the need to raise the debt limit is mostly attributable to the growth, as designed and desired, in debt held by government accounts. Pressure to raise the debt limit in the past generally came from growth in debt held by the public as the government needed to borrow from the public to finance its deficits. Growth in debt held by government accounts in the past 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 four to five years have been the driving force behind the increases in debt subject to limit and the primary cause of the current need to increase the debt limit.

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[4] (...continued)
be a completely internal financial crisis.