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THE DEBT CEILING: WHAT IS AT STAKE

Jason J. Fichtner and Veronique de Rugy
Senior Research Fellows

The debt ceiling (or limit), the legal limit the federal government may borrow, is set currently at $14.294 trillion. In his latest report, Secretary of the Treasury Timothy Geithner predicts that the United States will reach the current debt ceiling around May 16, 2011,[1] and the Congressional Research Service estimates the federal government will have to issue an additional $738 billion in debt above the current statutory limit to finance obligations for the remainder of FY2011.[2]

Congress is currently considering whether it should raise the debt ceiling. This is not new territory. Congress has raised the debt ceiling ten times in the last ten years.[3] However, raising the debt ceiling for the eleventh time in as many years without recognizing and correcting systemic problems would have consequences beyond merely tapping revenue and assets to meet FY2011 budget commitments. Continuing to pass debt ceiling increases without proper spending reforms would be irresponsible.

The United States should not consider defaulting on its debt, nor should it put itself in a position where it has to postpone payment to contractors or "manage" other non-debt obligations. Neither, however, should Congress be forced to raise the debt ceiling under false pretenses. By our calculations, the United States has enough expected cash flow (tax revenue) and assets on hand to avoid either of these unattractive options until at least the end of the current fiscal year in September, perhaps even longer.

REAL INSTITUTIONAL REFORM

The heated rhetoric about whether Congress should raise the debt ceiling obscures the federal government's real problem: an unprecedented increase in government spending during the past 10 years has created a fiscal imbalance.[4] No matter what Congress decides to do about the debt ceiling, the United States must implement institutional reforms that constrain government spending and return it to a sustainable fiscal position.

Real institutional reforms, as opposed to one-time cuts, would change the trajectory of fiscal policy and put the United States on a more sustainable path. Such reforms could include:

1. A constitutional amendment to limit spending. Lawmakers' inabilities to constrain their own spending makes spending limits enforced through the U.S. Constitution preferable.[5]

2. Meaningful budget reforms that limit lawmakers' tendency to spend. In the absence of constitutional rules, budget rules should have broad scope, few and high-hurdle escape clauses, and minimal accounting discretion.[6]

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[1] Timothy Geithner, "Letter to Harry Reid on the Debt Limit" (April 4, 2011), http://www.treasury.gov/connect/blog/Documents/FINAL%20Letter%2004-04-2011%20Reid%20Debt%20Limit.pdf.
[2] Mindy Leavitt et al., *Reaching the Debt Limit: Background and Potential Effects on Government Operations* (Washington DC: Congressional Research Service, February 11, 2011), 4–5, http://www.fas.org/sgp/crs/misc/R41633.pdf.
[3] Office of Management and Budget, *Budget of the United States FY 2011*(Washington, DC: OMB, 2010), Historic Tables 7.1, 7.2, and 7.3, http://www.whitehouse.gov/omb/budget/Historicals.
[4] Congressional Budget Office, *Long-Term Budget Outlook* (Washington, DC: CBO, June 2010) http://cbo.gov/doc.cfm?index=11579.
[5] David M. Primo, "Constitution is Only Way to Cut U.S. Deficit," Bloomberg.com, February 24, 2011.

3. The end of budget gimmicks. Creative bookkeeping is at the center of many countries' financial troubles. Congress should end abuse of the emergency spending rule, reliance on overly rosy scenarios, and all other gimmicks and institute a transparent budget process.[7]

4. A strict cut-as-you-go system that applies to the entire federal budget, not just to a small portion of it. There should be no new spending without offsetting cuts.[8]

5. A BRAC-like commission for discretionary spending. Commissions composed of independent experts often tackle intractable political problems successfully.[9]

6. Annual real spending caps. If Congress cut one cent out of every dollar it currently spends and did it for the next five years, the budget would be balanced before the end of the decade.[10]

REVENUE AND ASSESTS AVAILABLE TO FUND FY2011 COMMITMENTS

If Congress decides not to raise the debt ceiling, however, the United States does not have to default on its debt obligations. If the government reaches the debt ceiling and the Treasury is no longer able to issue federal debt, the federal government could reduce spending, increase federal revenues by a corresponding amount to cover the gap, or find other funding mechanisms.

Relying on any of the following sources of funds or increasing the debt ceiling to meet FY2011 budget commitments illustrates the irresponsible path the country is on and the urgent need for institutional spending reform. Nonetheless, the following assets could be used as a temporary measure to allow Congress and the Administration to negotiate a debt ceiling increase that includes spending reductions and institutional reforms to the budget process to ensure the nation is put back on a sound fiscal path. To be clear, the list below presents the range of possible options available to Congress: they may well be neither good nor desirable options.

Future Expected Cash Flow ($2.2 Trillion)

According to the Congressional Budget Office,[11] the federal government is estimated to collect $2.2 trillion in tax revenue over FY11.

That alone would be enough to cover interest on the debt ($214 billion), thereby avoiding any technical default of the U.S. government; Social Security ($727 billion); Medicare ($572 billion); and Medicaid ($274 billion) and would leave approximately $400 billion for other priorities.

Liquidating Existing Assets ($2.395 Trillion)

The Department of the Treasury has financial measures at its disposal to fund government operations temporarily without having to issue new debt. These include:

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[6] David M. Primo, "Making Budget Rules Bite," *Mercatus on Policy* 72 (Arlington, VA: Mercatus Center at George Mason University, 2010), http://mercatus.org/sites/default/files/publication/MOP72_Making%20Budget%20Rules%20Bite_web.pdf.
[7] Veronique de Rugy, "Budget Gimmicks or the Destructive Art of Creative Accounting" (working paper, Mercatus Center at George Mason University, 2010), http://mercatus.org/sites/default/files/publication/Budget_Gimmick_WP1030.pdf.
[8] Veronique de Rugy and David Bieler, "Is PAYGO a NO-GO?" *Mercatus on Policy* 73 (Arlington, VA: Mercatus Center at George Mason University, 2010), http://mercatus.org/sites/default/files/publication/MOP73_PAYGO_web.pdf.
[9] Jerry Brito, "The BRAC Model for Spending Reform," *Mercatus on Policy* 70 (Arlington, VA: Mercatus Center at George Mason University, 2010), http://mercatus.org/sites/default/files/publication/The%20BRAC%20Model%20for%20Spending%20Reform.pdf.
[10] Jason J. Fichtner, "The 1 Percent Solution" (working paper, Mercatus Center at George Mason University, 2011), http://mercatus.org/sites/default/files/publication/One%20Percent%20Solution.Ficthner_1.pdf.
[11] CBO, *Long Term Budget Outlook.*

1) Non-restricted cash on hand: $113.495 billion (The total operating balance of the United States Treasury as of April 19, 2011).[12]

2) Suspension of the daily reinvestment of Treasury securities held by the Exchange Stabilization Fund: $23 billion.[13]

3) Restricted cash and other monetary assets (gold, international monetary assets, foreign currency): $315.1 billion.[14]

4) TARP assets: $179.2 billion in gross outstanding direct loans; $142.5 billion in equity investments (As of September 30, 2010).[15]

5) The Federal Reserve: Unknown, but estimated by Secretary Geithner to be insignificant.[16] (Special programs at the Treasury may borrow money on the behalf of the Federal Reserve, and this borrowing would not count toward the debt ceiling.)

6) Determination of a "debt issuance suspension period." (This determination would permit the redemption of existing, and the suspension of new, investments of the Civil Service Retirement and Disability Fund (CSRDF).[17]): $766.615 billion (intergovernmental holdings in the Civil Service Retirement and Disability Fund). [18]

7) Redemption of existing investments in other trust funds[19, 20]

    - DOD, Military Retirement Fund: $332.9 billion
    - DOD, Medicare-Eligible Retiree Health Care Fund: $159.9 billion
    - Department of Energy, Nuclear Waste Disposal: $48.0 billion
    - FDIC Funds: $38.3 billion
    - OPM, Postal Service Retiree Health Benefits Fund: $42.9 billion
    - OPM, Employees Life Insurance Fund: $38.6 billion
    - DOT, Highway Trust Fund: $23.8 billion
    - Pension Benefit Guaranty Corporation Fund: $14.9 billion
    - DOL, Unemployment Trust Fund: $12.1 billion
    - OPM, Employees Health: $17.3 billion
    - Department of State, Foreign Service Retirement and Disability Fund: $16.1 billion
    - HUD, Federal Housing Authority Liquidating Account: $7.3 billion
    - All other programs and funds: $102.7 billion

8) Suspend investments of any federal government account surpluses in Treasury securities as required by law: $0 (but conserves headroom by not adding to the debt further).[21]

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[12] U.S. Department of the Treasury, "Daily Treasury Statement," April 19, 2011, https://www.fms.treas.gov/fmsweb/viewDTSFiles?dir=w&fname=11041900.pdf.
[13] Geithner, "Letter to Harry Reid." Such a suspension occurred in 1985 and during the debt limit crisis of 1995–1996.
[14] Department of the Treasury, *2010 Financial Report of the U.S. Government* (Washington, DC: GAO, 2010), 61, http://www.gao.gov/financial/fy2010/10frusg.pdf. Note: The Treasury owns approximately 264.3 million ounces of gold and marks the value of its gold holdings at $42 per ounce, giving a reported value of $11.1 billion. At a spot market price of $1,500 per ounce, Treasury's gold holdings could be valued near $400 billion.
[15] Ibid.
[16] Geithner, "Letter to Harry Reid."
[17] In September 1985, the Treasury took the step of disinvesting the Civil Service Retirement and Disability Trust Fund, the Social Security Trust Funds, and several smaller trust funds
[18] Department of Treasury, "Monthly Statement of the Public Debt of the United States", March 31, 2011, http://www.treasurydirect.gov/govt/reports/pd/mspd/2011/opdm032011.pdf.
[19] According to Thomas L. Hungerford, there are about 200 federal trust funds, but most trust funds are relatively small with balances of less than $100 million. The largest trust funds account for over 98% of the balances of all trust funds, "Federal Trust Funds and the Budget." *Economic Legislation Blog,* http://economic-legislation.blogspot.com/2010/07/federal-trust-funds-and-budget.html.
[20] All trust fund values from the Department of Treasury, "Monthly Statement of the Public Debt of the United States," March 31, 2011.

9) Suspend the issuance of State and Local Government Series Treasury securities: $0 (but conserves headroom by not adding to the debt further).[22]

ABOUT THE AUTHORS

Jason Fichtner is senior research fellow at the Mercatus Center. Previously, he served in several positions at the Social Security Administration (SSA) including deputy commissioner of Social Security (acting), chief economist, and associate commissioner for retirement policy. Prior to the Social Security Administration, Dr. Fichtner was a senior economist with the Joint Economic Committee (JEC) of the United States Congress. Dr. Fichtner's primary research interests are Social Security, federal tax policy, budget issues, as well as policy proposals to increase saving and investment.

Veronique de Rugy is a senior research fellow at the Mercatus Center. She was previously a resident fellow at the American Enterprise Institute, a policy analyst at the Cato Institute, and a research fellow at the Atlas Economic Research Foundation. Dr. de Rugy's research interests include the federal budget, homeland security, taxation, tax competition, and financial privacy issues.

For more information or to meet with the scholars, contact
Robin Landauer, Associate Director for Outreach, (703) 993-4886, rlandaue@gmu.edu
Mercatus Center at George Mason University ● 3351 North Fairfax Drive, 4th Floor ● Arlington, VA 22201

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[21] "In September 1985, the Treasury Department informed Congress that it had reached the statutory debt limit…Treasury took the additional step of "disinvesting" the Civil Service Retirement and Disability Trust Fund, the Social Security Trust Funds, and several smaller trust funds by redeeming some trust fund securities earlier than usual. Premature redemption of these securities created room under the debt ceiling for Treasury to borrow sufficient cash from the public to pay other obligations, including November Social Security benefits…As a result of the 1985 debt limit crisis, Congress subsequently authorized the Treasury to alter its normal investment and redemption procedures for certain trust funds during a debt limit crisis. Such authority was not provided with respect to the Social Security trust funds…In 1996, Congress passed P.L. 104-121 to increase the debt limit and, among other provisions, to codify Congress's understanding that the Secretary of the Treasury and other federal officials are not authorized to use Social Security and Medicare funds for debt management purposes, except when necessary to provide for the payment of benefits or administrative expenses of the programs." Mindy Leavitt et al., *Reaching the Debt Limit: Background and Potential Effects on Government Operations*, (Washington DC: Congressional Research Service, February 11, 2011), 4–5, http://www.fas.org/sgp/crs/misc/R41633.pdf .

[22] Geithner, "Letter to Harry Reid."