



The U.S. Has a Debt Limit?

Jennifer Pollom | November 30, 2009

It's the holiday season in Washington again, and with all the new spending going around that can mean only one thing: an increase in the statutory debt limit. Increases in the amount of debt the U.S. can issue are usually candidates for heated debates, and this year, on the eve of the passage of a \$1 trillion health care spending bill, is no different. Both the Chairman and Ranking Member of the Senate Budget Committee (Sens. Conrad and Gregg, respectively) along with a growing bipartisan group of Senators, are gearing up to oppose the increase in the statutory debt limit that is expected to be included in the Defense Appropriations conference report, due to be considered this December. In light of this upcoming debate, a bit more detail on the debt limit and its implications seems in order.

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First, a bit of background. Federal debt increases in three circumstances: when the government sells debt to the public to finance deficits (debt held by the public), when the government issues debt to certain government accounts, such as Social Security, in exchange for spending the account surpluses (debt held by government accounts), and when the government issues debt to purchase financial assets (traditionally direct loans, and recently financial asset bail outs). The combination of these is the total federal debt.

The statutory debt limit enables Congress to fulfill its constitutional role to control spending, and

imposes a form of fiscal accountability. Affirmatively voting to increase the limit compels Congress and the President to take visible or meaningful action to control the federal debt when the government is running an annual deficit. A statutory limit has restricted the total federal debt since 1917 when Congress passed the Second Liberty Bond Act which helped finance the U.S. entry into World War I.

Before WWI, Congress authorized specific loans or allowed the Treasury to issue specific types of debt instruments, as needed. With the passage of the Second Liberty Bond Act, Congress allowed aggregate constraints on certificates of indebtedness and on bonds allowing the Treasury greater flexibility to respond to changing conditions. In 1939, this new ability was further refined by eliminating separate limits on bonds and other forms of debt, creating one aggregate debt limit. Almost all borrowing by the federal government, which simply creates new debt, is done within the restrictions of a single statutory debt limit (codified in 31 USC 3101(b)). In legislative speak, changes to the debt limit usually involve simply striking the current dollar limit in the statute and inserting a new one. Since 1940, the debt limit has been adjusted 90 times.

As for recent history, Congress has raised the debt limit eight times since 2001. The debt limit has skyrocketed from \$5.95 trillion in FY01 to \$12.1 trillion in FY09 (the current limit). The \$12.1 trillion limit equates to approximately \$39,050 for every American citizen. In comparison, it was raised only once from FY96 to FY01, from \$5.5 trillion to \$5.95 trillion.



An arguably more accurate way to measure the severity of the federal debt is as a percentage of GDP rather than in nominal dollars. Looking at the debt through a GDP lens allows for fluctuations in inflation and economic growth. In terms of GDP, the federal debt was 66% of GDP in FY96, decreased to 57% in FY01, and increased again to a whopping 84% in FY09.

Although increasing the debt limit is politically unpopular, Congress has little choice. According to the Treasury Department, the total public debt stood at \$11.973 trillion as of November 18, 2009. Failing to raise the cap could lead the nation to default before the end of the year – an almost unthinkable event for any politician, or American for that matter. Essentially, Treasury bonds would come due and the government would not have the authority to borrow more money to pay them.

The current increase being debated would raise the limit from \$12.1 trillion to more than \$13.1 trillion. This spring, the House increased the debt limit to \$13.1 trillion as part of the FY10 budget resolution. However, the increase requires Senate to take action as well, so it hasn't taken effect yet. According to Congress Daily, Democratic leaders are actually expected to increase the limit above the House-approved \$13.1 trillion in order to build in a cushion for the additional \$1.5 trillion in deficit spending that's expected to occur next year. Passing a larger increase now would allow Congress to avoid having to pass yet another politically unpopular increase before the midterm elections next year.

The increase in the debt limit usually leads to typical partisan finger-pointing and almost always involves reluctance to cast “on the record” votes, which can have political consequences in today's sound-bite world. To take some of the political sting out of the

votes, both this year and last year, the House has raised the debt limit as part of the budget resolution using a maneuver known as the “Gephardt rule.” The Gephardt rule uses a bit of a legislative loophole to include the debt limit increase in the budget plan for the next year, preventing the House and its Members from having to take a separate vote on increasing the public debt limit. The Senate isn't so lucky. It lacks a similar mechanism, meaning each Senator must cast a potentially perilous vote on raising the public debt.

This year, Democratic leaders are considering including the debt limit increase in the FY10 Defense Appropriations bill, which is expected to be the legislative vehicle for all the year's unfinished appropriations bills. However, a growing number of Senators, including Conrad and Gregg, are threatening to oppose any increase in the debt limit if it is included in an Appropriations bill isn't subject to a full and open amendment process (as would be the case if the debt limit was included in a conference report). These Senators are pressing for the debt limit to be subject to debate so they can offer several amendments. These amendments include a new version of the Conrad-Gregg budget commission, a discretionary spending freeze, a rescission of unspent stimulus funding, and a requirement that any repayment of financial rescue funds be used to reduce the debt. Many of these ideas have been considered before (and many have been discarded). But in a time of skyrocketing American debt, it seems important to consider any possible way to prevent the debt explosion rather than simply continuing to raise the limit because American default is unthinkable. If the debt continues to increase, the U.S. may face tougher choices than these sooner than we expect.