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Debt-Limit Extraordinary Measures

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A Debt-Limit Primer

A number of factors put a check on federal government operations, including the debt limit, which statutorily caps debt held by the public and debt held by government accounts. An aggregate debt limit was first created in 1917. During the 21st century, Congress has modified the limit 15 times, most of these direct increases. Since 2013, however, Congress has been suspending the limit and prospectively increasing it to accommodate any debt outstanding.

The government's most recent 16-month debt-limit suspension is set to expire on March 15, 2017, after which the Treasury Department can use "extraordinary measures" – financial tools developed by Treasury that allow the department to pay the bills while the government considers raising the debt ceiling. The government is moving toward another debt-limit decision this fall, when extraordinary measures are projected to be exhausted.

Current Debt-Issuance Suspension

In November 2015, with the Bipartisan Budget Act of 2015 (P.L. 114-74), the government permitted the Treasury to issue new debt as needed until March 15, 2017, after which time no additional debt could be incurred. The amount borrowed during this period adds to the previous debt limit of $18.1 trillion. On March 16, a new debt limit will be established to account for debt issued during the suspension. As of February 28, $1.8 trillion has been borrowed, meaning the new debt limit will be at least $19.9 trillion.

By statute, the Treasury counts toward the limit nearly all debt issued to the public and intragovernmental holdings, with publicly held debt clearly representing the largest portion. As of February 28, marketable and non-marketable debt that is subject to the limit and held by the public equaled $14.4 trillion.

The Treasury has incurred the other part of the debt, intragovernmental holdings, largely by borrowing from trust funds. The government automatically converts surpluses of the funds into loans to the Treasury for use in other activities. As of February 28, this sum of all intragovernmental holdings subject to the debt limit equaled $5.5 trillion.

Use of Extraordinary Measures

Extraordinary measures delay payment of certain obligations, giving Treasury operational room under the debt limit. How much headroom Treasury needs depends on the cash flow it requires each month that would otherwise have been supplied by issuing debt. Outlays are generally paid on a regular monthly basis; however, revenue for the federal government waxes and wanes depending on when most corporate and individual income tax returns are due.

The total produced by the special accounting instruments should Treasury declare a “debt-issuance-suspension period” will likely exceed $250 billion. Thus, the current CBO forecast is for extraordinary measures to be completely exhausted this fall, depending on the expected flow of revenues and outlays.

A comprehensive statement regarding extraordinary measures is found in a March 13, 2015, letter from then-Treasury Secretary Jacob Lew to the Senate and House leadership. The four principal extraordinary measures are:

- **Suspend the issuance of State and Local Government Series (SLGS) Treasury securities.** This action preserves, rather than creates, headroom under the limit, since the issuance of SLGS securities would become a liability of the Treasury and count under the debt limit.
- **Declare a debt-issuance-suspension period and take certain actions in the civil service retirement and disability fund and Postal Service retiree health benefits fund.** Once the debt limit has been reached, the secretary of the Treasury is empowered by statute to cease issuing Treasury securities in exchange for retirement fund investments. This action preserves headroom. In addition, the secretary can redeem certain existing investments, which provides cash for Treasury operations.
- **Suspend daily investment of the Thrift Savings Plan (TSP) G Fund.** The G Fund is one of the TSP funds in which federal employees can invest a portion of their salaries. The fund invests in Treasury securities that count against the debt limit. The secretary of the Treasury can suspend reinvestment of all or part of the G Fund when investment of the fund would cause the debt limit to be breached. This suspension immediately creates headroom under the limit, and federal employees are made whole after the government raises the debt limit.
- **Suspend daily investments in the Exchange Stabilization Fund (ESF).** Treasury uses the ESF to clear its transactions in foreign currencies. The dollar balances in the fund are held in

securities that mature each day. Suspension of the daily balance immediately creates headroom under the debt limit.

These measures, along with a small number of other special accounting tools, allow Treasury to pay the government's bills and to service federal debt for many months. Still, there is a probability that no later than this fall extraordinary measures will become insufficient to maintain payments, requiring government action. This forecast does not take into consideration any large, unexpected bills coming due or sudden drop in the flow of revenues that may occur.

Timing and Market Reaction

Research from academics and a July 2015 Government Accountability Office report strongly indicate that the movement toward expiration is accompanied by an increase in the government's cost of issuing new debt.

Securities brokers and money-market managers constantly create financial products that include relatively risk-free Treasury bills, notes, and bonds. These Treasury products serve as collateral or hedges in transactions that require an asset whose value is little affected by risk.

For financial products that mature at or near the time the federal government might not be able to pay all its bills, the Treasury asset no longer appears risk-free. Because it no longer has a more-or-less-certain value, brokers search for something else to anchor their products. As a result, the demand for Treasury products falls, and the yield that Treasury must guarantee buyers rises. This dynamic increases the borrowing costs of the Treasury leading up to the exhaustion of extraordinary measures.

While additional costs can stem from the mere threat of default, U.S. citizens and foreign observers should remain confident that every measure will be taken to pay the country's bills on time. Even when borrowing authority has expired, the U.S. payment record is nearly perfect.