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FULL FAITH AND CREDIT ACT

The Full Faith and Credit Act

H.R. 421: The Full Faith and Credit Act directs the United States Treasury, in the event the debt ceiling is reached, to pay principal and interest due on debt held by the public before making any other payments. The Treasury will have ten times more revenue than needed to cover interest and debt service this year, so there is no reason for the federal government to default on its obligations.

Amazingly, Treasury Secretary Geithner recently indicated that he might permit the United States to default if Congress does not increase the statutory debt ceiling this year. Maintaining the good credit of the United States is essential to economic prosperity and national security. A default on our debt would have catastrophic consequences, including loss of the nation's triple-A credit rating, sky-high interest rates, and rapid inflation. This fallout would thwart any effort to return to robust job growth, prosperity, and balanced budgets. Enacting the Full Faith and Credit Act will ensure that default is the absolute last option available to the Treasury.

Sen. Pat Toomey (PA) has introduced the Full Faith and Credit Act in the Senate, while Rep. Tom McClintock (CA-4), RSC Chairman Jim Jordan (OH-4), Rep. Virginia Foxx (NC-5), and Rep. Scott Garrett (NJ-5) are leading the charge in the House of Representatives.

About the Bill:
H.R.421: The Full Faith and Credit Act - Bill Text
H.R.421: The Full Faith and Credit Act - Myth vs. Reality Fact Sheet
Press Release: RSC Members Introduce Bill to Prevent Default on the Debt
Sen. Toomey Op-Ed in the Wall Street Journal

Outside Support:
Letter of Support from Americans for Prosperity

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112TH CONGRESS
1ST SESSION

H. R. ____

To require that the Government prioritize all obligations on the debt held by the public in the event that the debt limit is reached.

IN THE HOUSE OF REPRESENTATIVES

Mr. MCCLINTOCK (for himself, Mr. JORDAN, Ms. FOXX, and Mr. GARRETT) introduced the following bill; which was referred to the Committee on ____________________

A BILL

To require that the Government prioritize all obligations on the debt held by the public in the event that the debt limit is reached.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Full Faith and Credit Act".

SEC. 2. PRIORITIZE OBLIGATIONS ON THE DEBT HELD BY THE PUBLIC.

In the event that the debt of the United States Government, as defined in section 3101 of title 31, United States Code, reaches the statutory limit, the authority of the Department of the Treasury provided in section 3123 of title 31, United States Code, to pay with legal tender the principal and interest on debt held by the public shall take priority over all other obligations incurred by the Government of the United States.

Treasury Notes

Treasury: Proposals to "Prioritize" Payments on U.S. Debt Not Workable; Would Not Prevent Default

By: Neal Wolin 1/21/2011

In his January 6, 2011 letter urging that Congress act to protect America's creditworthiness by increasing the statutory debt limit, Secretary Geithner made clear that any default on legal debt obligations of the U.S. would be unthinkable. In response, Members of Congress of both parties have indicated agreement that the United States must honor its obligations. However, Treasury disagrees with suggestions by some that Congress could somehow evade this responsibility by passing legislation to "prioritize" payments on the national debt above other legal obligations of the United States.

While well-intentioned, this idea is unworkable. It would not actually prevent default, since it would seek to protect only principal and interest payments, and not other legal obligations of the U.S., from non-payment. Adopting a policy that payments to investors should take precedence over other U.S. legal obligations would merely be default by another name, since the world would recognize it as a failure by the U.S. to stand behind its commitments. It would therefore bring about the same catastrophic economic consequences Secretary Geithner has warned against, including sharp rises in mortgage interest rates and other borrowing costs for families; reductions in the value of homes, 401(k)s and other retirement savings; and negative effects on the dollar and the safe haven status of Treasury bonds and other Treasury securities. Such a policy would also be unacceptable to American servicemen and women, retirees, and all other Americans, who would rightly reject the notion that their payment has been deemed a lower priority by their government. For these reasons, the Department of Treasury has always emphasized – regardless of which party has held the White House or either house of Congress – that the only way to prevent default and protect America's creditworthiness is to enact a timely increase in the debt limit.

Neal Wolin is Deputy Secretary of the Treasury.

Posted in: Category 1

TREASURY FACTS

On December 17, 1903, as part of their work at the Kill Devil Hills Life-Saving Station, five Treasury employees were the first eyewitness to Wilbur and Orville Wright historic flight in Kit Hawk, North Carolina.

FEATURED VIDEO

YouTube video: First Lady Michelle Obama visits the Treasury Department

First Lady Michelle Obama visits the Treasury Department
On July 7, 2010, First Lady Michelle Obama visited the Treasury Department where she joined Secretary Geithner in thanking Treasury employees for the...
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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

April 4, 2011

The Honorable Harry Reid
Democratic Leader
United States Senate
Washington, DC 20510

Dear Mr. Leader:

I am writing to update you on the Treasury Department's projections regarding when the statutory debt limit will be reached and to inform you about the limits of the available measures at our disposal to delay that date temporarily.

In our previous communications to Congress, we provided regular estimates of the likely time period in which the debt limit could be reached. We can now make that projection with more precision. The Treasury Department now projects that the debt limit will be reached no later than May 16, 2011. This is a projection based on the expected level of tax receipts, the timing of our commitments and obligations over the next several weeks, and our judgment concerning the level of cash balances we need to operate. Although these projections could change, we do not believe they are likely to change in a way that would give Congress more time in which to act. Treasury will provide an update of this projection in early May.

If the debt limit is not increased by May 16, the Treasury Department has authority to take certain extraordinary measures, described in detail in the appendix, to temporarily postpone the date that the United States would otherwise default on its obligations. These actions, which have been employed during previous debt limit impasses, would be exhausted after approximately eight weeks, meaning no headroom to borrow within the limit would be available after about July 8, 2011. At that point the Treasury would have no remaining borrowing authority, and the available cash balances would be inadequate for us to operate with a sufficient margin to meet our commitments securely.

As Secretary of the Treasury, I would prefer to avoid resorting to these extraordinary measures. The longer Congress fails to act, the more we risk that investors here and around the world will lose confidence in our ability to meet our commitments and our obligations.

If Congress does not act by May 16, I will take all measures available to me to give Congress additional time to act and to protect the creditworthiness of the country. These measures, however, only provide a limited degree of flexibility—much less flexibility than when our deficits were smaller.

As the leaders of both parties in both houses of Congress have recognized, increasing the limit is necessary to allow the United States to meet obligations that have been previously authorized and appropriated by Congress. Increasing the limit does not increase the obligations we have as a Nation; it simply permits the Treasury to fund those obligations that Congress has already established.

If Congress failed to increase the debt limit, a broad range of government payments would have to be stopped, limited or delayed, including military salaries and retirement benefits, Social Security and Medicare payments, interest on the debt, unemployment benefits and tax refunds. This would cause severe hardship to American families and raise questions about our ability to defend our national security interests. In addition, defaulting on legal obligations of the United States would lead to sharply higher interest rates and borrowing costs, declining home values and reduced retirement savings for Americans. Default would cause a financial crisis potentially more severe than the crisis from which we are only now starting to recover.

For these reasons, default by the United States is unthinkable. This is not a new or partisan judgment; it is a conclusion that has been shared by every Secretary of the Treasury, regardless of political party, in the modern era.

Treasury has been asked whether it would be possible for the Treasury to sell financial assets as a way to avoid or delay congressional action to raise the debt limit. This is not a viable option. To attempt a "fire sale" of financial assets in an effort to buy time for Congress to act would be damaging to financial markets and the economy and would undermine confidence in the United States.

Selling the Nation's gold, for example, would undercut confidence in the United States both here and abroad. A rush to sell other financial assets, such as the remaining financial investments from the Emergency Economic Stabilization Act programs, would impose losses on American taxpayers and risk damaging the value of similar assets held by private investors without generating sufficient revenue to make an appreciable difference in when the debt limit must be raised. Likewise, for both legal and practical reasons, it is not feasible to sell the government's portfolio of student loans.

Nor is it possible to avoid raising the debt limit by cutting spending or raising taxes. Because of the magnitude of past commitments by Congress, immediate cuts in spending or tax increases cannot make the necessary cash available. And, reductions in future spending commitments cannot supply the short-term cash needed. In order to avoid an increase in the debt limit, Congress would need to eliminate annual deficits immediately.

As the Congressional Research Service stated in its February 11, 2011 report:

> "If the debt limit is reached and Treasury is no longer able to issue federal debt, federal spending would have to be decreased or federal revenues would have to be increased by a corresponding amount to cover the gap in what cannot be borrowed. To put this

> into context, the federal government would have to eliminate all spending on discretionary programs, cut nearly 70% of outlays for mandatory programs, increase revenue collection by nearly two-thirds, or take some combination of those actions in the second half of FY2011 (April through September 30, 2011) in order to avoid increasing the debt limit. Additional spending cuts and/or revenue increases would be required, under current policy, in FY2012 and beyond to avoid increasing the debt limit."[1]

None of those budget policy choices is feasible or responsible. As a consequence, given that Congress has imposed on itself the requirement for periodic increases, there is no alternative to enactment of an increase in the debt limit.

I am encouraged that the leaders of both parties in both houses of Congress have clearly stated in public over the last few weeks and months that we cannot default on our obligations as a nation and therefore have to increase the debt limit. Because the date by which we need to increase the limit is growing nearer, I hope that the leadership in both houses will help us impress upon all Members the gravity of this issue and the imperative of timely action.

President Obama is strongly committed to working with both parties to restore fiscal responsibility, and he looks forward to working with Congress to achieve that critically important objective. In the meantime, it is critical that Congress act to increase the debt limit so that the full faith and credit of the United States is protected.

I hope this information is helpful as you plan the legislative schedule for the coming weeks.

Sincerely,

Timothy F. Geithner

Identical letter sent to:
The Honorable John A. Boehner, Speaker of the House
The Honorable Nancy Pelosi, House Democratic Leader
The Honorable Mitch McConnell, Senate Republican Leader

cc: The Honorable Dave Camp, Chairman, House Committee on Ways and Means
The Honorable Sander M. Levin, Ranking Member, House Committee on Ways and Means
The Honorable Max Baucus, Chairman, Senate Committee on Finance
The Honorable Orrin Hatch, Ranking Member, Senate Committee on Finance
All other Members of the 112th Congress

Enclosure

[1] CRS Report R41633, February 11, 2011

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

APPENDIX

Descriptions of the Extraordinary Measures

Previous Secretaries of the Treasury, in both Republican and Democratic administrations, have taken extraordinary measures in order to prevent the United States from defaulting on its obligations as Congress deliberated on increasing the statutory debt limit.[2] Four of these extraordinary measures are available this year. Other measures taken by previous Treasury Secretaries, however, are either unavailable or of limited use.

The extraordinary measures currently available are: (1) suspending sales of State and Local Government Series (SLGS) Treasury securities; (2) determining that a "debt issuance suspension period" exists, which would permit the redemption of existing, and the suspension of new, investments of the Civil Service Retirement and Disability Fund (CSRDF); (3) suspending reinvestment of the Government Securities Investment Fund (G Fund); and (4) suspending reinvestment of the Exchange Stabilization Fund (ESF). These measures are described in more detail below.

These measures, all of which have been employed during previous debt limit impasses, have the effect of creating or conserving headroom beneath the debt limit. Importantly, these extraordinary measures—even taken together—are of limited use. On average, the public debt of the United States increases by approximately $125 billion per month (although there are significant variations from month to month). In total, the extraordinary measures free up approximately $165 billion in headroom under the limit before June 30, 2011, as described below. In addition, if the United States does not exhaust the $165 billion before June 30, 2011, the law governing the CSRDF permits Treasury to take one more action on June 30, which would create an additional $67 billion in headroom on that date.

Under Treasury's current projections, these extraordinary measures would be exhausted after approximately eight weeks, meaning no headroom to borrow within the limit would be available after about July 8, 2011. This estimate is dependent on a number of factors, such as the total amount of tax receipts, which cannot be known with certainty until they actually come in during the second half of April, and the fact that large payments like Social Security and interest payments on Treasury securities are made at certain times of the month.

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[2] The Treasury Department has already taken an action, relating to the Supplementary Financing Program, that has delayed the date that the debt limit will be reached. In January, Treasury announced that it would allow the outstanding $200 billion in Treasury bills issued under the Supplementary Financing Program (which count against the debt limit) to mature in an orderly fashion without being refunded by new bills. By taking this action, Treasury has reduced the debt by $200 billion, so as to postpone the date the debt limit is reached. This action has already been completed and the resulting reduction in debt has already been factored into Treasury's projections; it cannot further postpone the date the debt limit is reached.

It should also be noted that these extraordinary measures are less useful than in previous debt limit impasses. In the 1995-1996 debt limit impasse, for example, the monthly increase in debt was not as large, and the extraordinary measures were therefore able to postpone the date by which the debt limit needed to be increased for several months. The same was true during the 1985 and 2003 debt limit impasses. And, as noted below, some extraordinary measures that were used in the past are no longer available or of limited use today.

1. State and Local Government Securities (SLGS)

The Treasury Department has authority to suspend its issuance of State and Local Government Series Treasury securities (SLGS). This, however, is a limited measure that does not free up borrowing authority.

SLGS are special purpose Treasury securities issued to state and local government entities. In ordinary times, the Treasury Department issues SLGS to state and local governments to assist these governments in complying with Federal tax laws when they have cash proceeds to invest from their issuance of tax exempt bonds. When Treasury issues these securities, they count against the debt limit.[3] There is no statutory or other requirement for the Treasury Department to issue SLGS; they are issued in order to assist state and local governments, and Treasury may suspend SLGS sales during or in anticipation of a debt limit impasse.

This action does not free up headroom under the debt limit. Rather, it conserves headroom (*i.e.*, it eliminates increases in debt that would count against the debt limit if issued).[4] Utilizing this measure reduces uncertainty in projecting the growth of the debt.[5]

2. Civil Service Retirement and Disability Fund

Once the debt limit has been reached, Treasury has authority to take actions regarding investments under the Civil Service Retirement and Disability Fund (CSRDF). This includes declaring a "debt issuance suspension period" with respect to the CSRDF investments.[6]

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[3] The total amount of SLGS outstanding at the end of February 2011 was $182.4 billion.

[4] In other words: when Treasury issues these securities, these securities count against the debt limit; suspending issuance therefore conserves headroom.

[5] Approximately $3 - $12 billion in SLGS is issued per month although this amount is subject to substantial variation from month to month.

[6] The final three measures—relating to Civil Service Retirement and Disability Fund, the Government Securities Investment Fund of the Thrift Savings Plan, and the Exchange Stabilization Fund—all involve the management of the portion of the debt held by U.S. Government accounts, not the debt that is held by the public. The debt of the United States consists of two components: (1) debt held by the public (*e.g.*, the Treasury securities that are periodically auctioned by Treasury); and (2) debt held by U.S. Government accounts. This second category includes, for example, the investments by the Social Security trust fund and other trust funds, and consists of special Treasury securities that are issued directly to those trust fund accounts. The debt held by U.S. Government accounts is approximately $4.6 trillion—in other words, it constitutes roughly a third of the debt.

a. Declaring a "Debt Issuance Suspension Period"

The CSRDF provides defined benefits to retired and disabled Federal employees covered by the Civil Service Retirement System. The fund is invested in special-issue Treasury securities, which count against the debt limit. Congress has given Treasury statutory authority to take certain actions in the event of a debt limit impasse. Specifically, the statute authorizes the Secretary of the Treasury to determine that a "debt issuance suspension period" exists and, once he has done so, Treasury can (1) redeem certain existing investments in the CSRDF, and (2) suspend new investment.

The Secretary of the Treasury does not have unlimited discretion to declare a debt issuance suspension period. Under the statute that governs the CSRDF, the term "debt issuance suspension period" means the period of time that the Treasury Secretary determines that Treasury securities cannot be issued without exceeding the debt limit. The determination of the length of the period must be based on the facts as they exist at the time.

Declaring a debt issuance suspension period is a limited measure that relates only to the CSRDF; it has no impact on any other investments or any other portion of the debt. Moreover, it only provides limited additional time. Assuming a two-month debt issuance suspension period, this measure would free up approximately $12 billion in headroom.[7]

Even if the Secretary were to declare a much longer debt issuance suspension period, this would provide only limited additional headroom. Declaring a 12-month debt issuance suspension period, for example, would only free up approximately $72 billion in additional headroom.[8] In other words, because the debt increases on average by approximately $125 billion per month, a 12-month debt issuance suspension period (which frees up roughly $72 billion in headroom) would postpone the date by which the debt limit must be increased by only a matter of weeks.

During a debt issuance suspension period, civil service benefit payments would continue to be made as long as the United States has not yet exhausted the extraordinary measures. Once the extraordinary measures have been exhausted, however, the U.S. Government will be limited in

[7] The statute governing the CSRDF gives Treasury authority to redeem existing Treasury securities held by the CSRDF in an amount up to the amount of civil service benefit payments authorized to be made from the CSRDF during the debt issuance suspension period. 5 U.S.C. § 8348(k). Treasury makes approximately $6 billion in civil service benefit payments from the CSRDF each month. Therefore, declaring a two-month debt issuance suspension period would allow Treasury to redeem approximately $12 billion of the Treasury securities held by the CSRDF, freeing up approximately $12 billion in headroom. The statute also authorizes Treasury to suspend new investments by the CSRDF during a debt issuance suspension period. The CSRDF receives approximately $2 billion in new employer and employee contributions each month. Therefore, during each month of a debt issuance suspension period, approximately $2 billion in headroom that would otherwise be used is conserved.

[8] As explained above, Treasury makes approximately $6 billion in civil service benefit payments each month. A 12-month debt issuance suspension period would allow Treasury to redeem approximately $6 billion 12 times, or approximately $72 billion, of the Treasury securities held by the CSRDF, freeing up approximately $72 billion in headroom. Additionally, each month it would also conserve approximately $2 billion in headroom.

its ability to make payments across the government. After the debt limit impasse has ended, the statute provides that the CSRDF is made whole.[9]

b. One-time measure available on June 30 if the United States has not exhausted the measures before that date

If the United States has not exhausted the measures before June 30, the statute governing the CSRDF provides an additional one-time measure on that date that frees up headroom.

The same statute that authorizes Treasury to redeem existing investments during a debt issuance suspension period also authorizes Treasury to suspend new investments by the CSRDF during such a period. On June 30, approximately $67 billion in CSRDF investments mature. Ordinarily the proceeds of the maturing investments would be reinvested. But with the investment-suspension authority available, Treasury may suspend the reinvestment of the maturing investments. Suspending the reinvestment would free up approximately $67 billion in headroom.

It should be understood that this suspension of reinvestment that frees up headroom is a one-time measure: it is only available on June 30.[10] The benefit of this additional headroom, moreover, is offset in part by the fact that on that same day Treasury is required to make $12 billion in interest payments on certain of its securities held by the public.

3. G Fund

Once the debt limit has been reached, Treasury may also suspend the daily reinvestment of the Treasury securities held by the Government Securities Investment Fund (G Fund) of the Federal Employees' Retirement System Thrift Savings Plan.

The G Fund is a money market defined-contribution retirement fund for Federal employees. The Fund is invested in special-issue Treasury securities, which count against the debt limit. The entire balance matures daily and is ordinarily reinvested. Congress has granted Treasury the statutory authority to suspend reinvestment of all or part of the balance of the G Fund when the Secretary determines that the Fund cannot be fully invested without exceeding the debt limit.[11]

Using this measure immediately frees up headroom under the debt limit. Because the G Fund balance is approximately $130 billion, using this measure can immediately create up to approximately $130 billion in headroom.

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[9] After the debt limit impasse has ended, Treasury is required to put the CSRDF investment portfolio into the position it would have been in if the impasse had not occurred, and to restore lost interest on the next regularly scheduled interest payment date on the Treasury securities held by the CSRDF.
[10] In addition, this measure conserves headroom. On June 30, there is an interest payment of approximately $18 billion scheduled to be made to the fund. If this interest were invested, it would use up headroom. Because the statute governing the CSRDF authorizes Treasury to suspend new investments, Treasury may suspend the investment of this interest payment, which would conserve approximately $18 billion of headroom.
[11] 5 U.S.C. § 8438(g).

During the period of the investment suspension, payments from the G Fund continue to be made as long as the United States has not yet exhausted the extraordinary measures. Once the United States has exhausted the extraordinary measures, however, the U.S. Government will be limited in its ability to make payments across the government. After the debt limit impasse has ended, the G Fund is made whole.[12]

4. Exchange Stabilization Fund

Treasury may also suspend the daily reinvestment of Treasury securities held by the Exchange Stabilization Fund (ESF).

The ESF has a number of uses, including purchasing or selling foreign currencies. A portion of the ESF is held in U.S. dollars, and the dollar-balance of the ESF is invested in special-issue Treasury securities. The entire dollar-balance matures daily. There is no requirement that the Treasury Department invest the ESF, so Treasury may discontinue investing the dollar-balance of the ESF during a debt limit impasse.

Suspending the daily reinvestment of the dollar-balance of the ESF immediately frees up headroom under the debt limit. Because the dollar-balance of the ESF is approximately $23 billion, this would create up to approximately $23 billion in headroom.

After a debt limit impasse, the interest lost by the ESF is not restored: there is no existing authority to reimburse the ESF for lost interest during the period that the dollar-balance is not invested.

* * *

As described above, the four extraordinary measures can free up approximately $230 billion in headroom. This would postpone the date by which the debt limit needs to be increased by approximately 8 weeks, or until about July 8, 2011.

Other Measures Used by Previous Treasury Secretaries Are No Longer Available or of Limited Use

The other measures that previous Treasury Secretaries have used in past debt limit impasses in order to postpone the date by which the debt limit needed to be increased are either not available or of limited use.

First, although previous Treasury Secretaries have suspended the issuance of U.S. savings bonds to the public, doing so now would be of little benefit. Suspending the issuance of U.S. savings bonds would not free up any headroom under the debt limit. As is the case with suspending sales of SLGS, suspending the sales of savings bonds would only eliminate increases in debt that would count against the debt limit if the securities were issued. Moreover, suspending such sales conserves very little headroom.[13] Second, measures relating to the Federal

[12] Treasury is required to restore lost interest on the next business day.

[13] Sales of savings bonds increase the amount of debt by less than $220 million per month on average.

Financing Bank (FFB) are of limited use.[14] Third, a measure previously used, involving the calling in of cash that Treasury kept on deposit at banks, is no longer available: Treasury no longer keeps these balances.[15] Finally, Congress has in the past provided one-time tools in the midst of a debt limit impasse;[16] those authorities expired 15 years ago.

Other Assets

Although the U.S. Government owns other assets, such as gold, there are prudential or legal limitations on its ability to sell these assets. Selling the Nation's gold to meet payment obligations would undercut confidence in the United States both here and abroad, and would be extremely destabilizing to the world financial system.

With respect to the portfolio of mortgage-backed securities owned by Treasury, Treasury recently announced that it would begin gradually selling these assets, at the rate of up to $10 billion per month subject to market conditions.[17] Treasury's assessment is that selling this amount maximizes value to taxpayers without adversely affecting the market or mortgage rates. A "fire sale" of these assets would be adverse to the interests of taxpayers and could jeopardize the still-fragile housing market. Similarly, although the United States retains investments received in connection with the Troubled Asset Relief Program, Treasury is in the process of exiting these investments in an orderly manner. A "fire sale" of these investments would not maximize value for the taxpayer and could be detrimental to the economy in general. Finally, as mentioned above, for both legal and practical reasons, sale of the government's portfolio of student loans is not feasible. Secretaries of the Treasury of both parties have concluded that asset sales are not a prudent or viable alternative to increasing the debt limit.

[14] In the past, Treasury was able to free up headroom under the debt limit by entering into multi-step exchange transactions with FFB and the CSRDF, swapping obligations that do not count against the debt limit for an equal amount of Treasury securities held by the CSRDF that do count against the debt limit. In each case, FFB used the Treasury securities that it received from the CSRDF to pay down its borrowings from Treasury. When Treasury received from FFB the Treasury securities, they were extinguished, creating the headroom. The potential to use such an exchange transaction is of limited use at this time because FFB has a limited amount of obligations available to exchange.

[15] In the past, Treasury had an ability to increase its cash balance without increasing debt by calling in the non-interest-bearing balances that Treasury formerly kept on deposit at banks to compensate them for fiscal services they provided to Treasury. That option is no longer available because Treasury discontinued keeping those "compensating balances" after Congress appropriated funding to Treasury in 2004 to pay directly for fiscal services.

[16] Specifically, in 1996, in order to enable Treasury to pay the March 1996 Social Security benefits, Congress passed legislation that permitted Treasury to issue a limited amount of Treasury securities that were temporarily excluded from being counted against the debt limit. In addition, Congress passed legislation that temporarily excluded from being counted against the debt limit the new Treasury securities that Treasury issued to federal trust funds in March 1996 to invest new trust fund receipts and to reinvest the proceeds of maturing trust fund investments. Those exclusions from the debt limit expired on March 30, 1996.

[17] The proceeds from these sales are already built into the Treasury projections.

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

January 6, 2011

The Honorable Harry Reid
Majority Leader
United States Senate
Washington, DC 20510

Dear Mr. Leader:

I am writing in response to your request for an estimate by the Treasury Department of when the statutory debt limit will be reached, and for a description of the consequences of default by the United States.

Never in our history has Congress failed to increase the debt limit when necessary. Failure to raise the limit would precipitate a default by the United States. Default would effectively impose a significant and long-lasting tax on all Americans and all American businesses and could lead to the loss of millions of American jobs. Even a very short-term or limited default would have catastrophic economic consequences that would last for decades. Failure to increase the limit would be deeply irresponsible. For these reasons, I am requesting that Congress act to increase the limit early this year, well before the threat of default becomes imminent.

As you know, in February of 2010 Congress passed legislation to increase the debt limit to $14.29 trillion. As of this writing, the outstanding debt that is subject to the limit stands at $13.95 trillion, leaving approximately $335 billion of "headroom" beneath the current limit. Because of the inherent uncertainty associated with tax receipts and refunds during the spring tax filing season, as well as other variable factors, it is not possible at this point to predict with precision the date by which the debt limit will be reached. However, the Treasury Department now estimates that the debt limit will be reached as early as March 31, 2011, and most likely sometime between that date and May 16, 2011. This estimate is subject to change depending on the performance of the economy, government receipts, and other factors. This means it is necessary for Congress to act by the end of the first quarter of 2011.

At several points in past years, Treasury has taken exceptional actions to delay the date by which the limit was reached in order to give Congress additional time to raise the limit. These extraordinary actions include: suspending sales of State and Local Government Series (SLGS) Treasury securities[1];

[1] SLGS are special purpose Treasury securities issued to state and local government entities that have cash proceeds to invest from their issuance of tax exempt bonds. There is no statutory or other requirement that Treasury issue SLGS, so Treasury may suspend SLGS sales during a debt limit impasse.

suspending reinvestment of the Government Securities Investment Fund (G-Fund)[2]; suspending reinvestment of the Exchange Stabilization Fund (ESF)[3]; and determining that a "debt issuance suspension period" exists, permitting redemption of existing, and suspension of new, investments of the Civil Service Retirement and Disability Fund (CSRDF)[4]. Treasury would prefer not to have to engage again in any of these extraordinary measures. If we are forced to do so again, these measures could delay the date by which the limit is reached by several weeks. Once these steps have been taken, no remaining legal and prudent measures would be available to create additional headroom under the debt limit, and the United States would begin to default on its obligations.

As discussed in greater detail below, raising the debt limit is necessary to allow the Treasury to meet obligations of the United States that have been established, authorized, and appropriated by the Congress. It is important to emphasize that changing the debt limit does not alter or increase the obligations we have as a nation; it simply permits the Treasury to fund those obligations Congress has already established.

In fact, even if Congress were immediately to adopt the deep cuts in discretionary spending of the magnitude suggested by some Members of Congress, such as reverting to Fiscal Year 2008 spending levels, the need to increase the debt limit would be delayed by no more than two weeks. The limit would still need to be raised to make it possible for the government to avoid default and to meet the other obligations established by Congress.

The national debt is the total amount of money borrowed in order to fulfill the requirements imposed by past Congresses and under past presidencies, during periods when both Republicans and Democrats were in control of different branches of government. These are legal obligations, incurred under the laws of the United States. Responsibility for creating the debt is bipartisan, and responsibility for meeting the Nation's obligations must be shared by both parties.

As the 112th Congress turns to this issue, I want to stress that President Obama believes strongly in the need to restore balance to our fiscal position, and he is committed to working with both parties to put the Nation on a fiscally responsible path. This will require difficult choices and a comprehensive approach to reduce the gap between our commitments and our resources. It will require that the government spend less and spend more wisely. The President has already taken important steps, including enacting the savings in the Affordable Care Act; restoring Pay-As-You-Go budgeting; and undertaking a three-year freeze on non-security discretionary spending. The President's proposals would put us on a path to cut the deficit by more than half in the medium term, and substantially reduce the rate of growth in federal health care costs in the long term. The President looks forward to

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[2] The G-Fund is a money-market-like defined-contribution retirement fund for federal employees. Amounts in the G-Fund are invested in non-marketable Treasury securities, and the entire balance of the fund matures daily. Treasury has authority to suspend reinvestment of all or part of the balance of the G-Fund when the Secretary determines that the fund cannot be fully invested without exceeding the debt limit.

[3] The ESF is used by Treasury to purchase or sell foreign currencies. The dollar-denominated holdings of the ESF are invested in non-marketable Treasury securities, and the entire balance of the dollar-denominated investments matures daily. There is no requirement to keep the dollar balances of the ESF invested.

[4] The CSRDF is a government fund that holds and invests in nonmarketable Treasury securities to provide defined benefits to retired federal employees. Treasury has authority to redeem existing CSRDF investments and suspend new investments when the Secretary determines that the fund cannot be fully invested without exceeding the debt limit.

working with Members of the 112th Congress on additional measures to address our medium- and long-term fiscal challenges.

Because Congress has always acted to increase the debt limit when necessary, and because failure to do so would be harmful to the interests of every American, I am confident that Congress will act in a timely manner to increase the limit this year. However, for the benefit of Members of Congress and the public, I want to make clear, for the record, what the implications of a default would be so there can be no misunderstanding when the issue is debated in the House and Senate.

Reaching the debt limit would mean the Treasury would be prevented by law from borrowing in order to pay obligations the Nation is legally required to pay, an event that has no precedent in American history. Such a default should be understood as distinct from a temporary government shutdown resulting from failure to enact appropriations bills, which occurred in late 1995 and early 1996. Those government shutdowns, which were unwise and highly disruptive, did not have the same long-term negative impact on U.S. creditworthiness as a default would, because there was headroom available under the debt limit at that time.

I am certain you will agree that it is strongly in our national interest for Congress to act well before the debt limit is reached. However, if Congress were to fail to act, the specific consequences would be as follows:

- The Treasury would be forced to default on legal obligations of the United States, causing catastrophic damage to the economy, potentially much more harmful than the effects of the financial crisis of 2008 and 2009.

- A default would impose a substantial tax on all Americans. Because Treasuries represent the benchmark borrowing rate for all other sectors, default would raise all borrowing costs. Interest rates for state and local government, corporate and consumer borrowing, including home mortgage interest, would all rise sharply. Equity prices and home values would decline, reducing retirement savings and hurting the economic security of all Americans, leading to reductions in spending and investment, which would cause job losses and business failures on a significant scale.

- Default would have prolonged and far-reaching negative consequences on the safe-haven status of Treasuries and the dollar's dominant role in the international financial system, causing further increases in interest rates and reducing the willingness of investors here and around the world to invest in the United States.

- Payments on a broad range of benefits and other U.S. obligations would be discontinued, limited, or adversely affected, including:
    - U.S. military salaries and retirement benefits;
    - Social Security and Medicare benefits;
    - veterans' benefits;
    - federal civil service salaries and retirement benefits;
    - individual and corporate tax refunds;
    - unemployment benefits to states;
    - defense vendor payments;
    - interest and principal payments on Treasury bonds and other securities;
    - student loan payments;
    - Medicaid payments to states; and
    - payments necessary to keep government facilities open.

For these reasons, any default on the legal debt obligations of the United States is unthinkable and must be avoided. It is critically important that Congress act before the debt limit is reached so that the full faith and credit of the United States is not called into question. The confidence of citizens and investors here and around the world that the United States stands fully behind its legal obligations is a unique national asset. Throughout our history, that confidence has made U.S. government bonds among the best and safest investments available and has allowed us to borrow at very low rates.

Failure to increase the debt limit in a timely manner would threaten this position and compromise America's creditworthiness in the eyes of the world. Every Secretary of the Treasury in the modern era, regardless of party, has strongly held this view. Given the gravity of the challenges facing the U.S. and world economies, the world's confidence in our creditworthiness is even more critical today.

I hope this information is responsive to your request and will be helpful as Congress considers this important legislation.

Sincerely,

Timothy F. Geithner

cc: The Honorable John A. Boehner, Speaker of the House
The Honorable Nancy Pelosi, House Minority Leader
The Honorable Mitch McConnell, Senate Minority Leader
The Honorable Dave Camp, Chairman, House Committee on Ways and Means
The Honorable Sander M. Levin, Ranking Member, House Committee on Ways and Means
The Honorable Max Baucus, Chairman, Senate Committee on Finance
The Honorable Orrin Hatch, Ranking Member, Senate Committee on Finance
All other Members of 112th Congress