

# CRS Report for Congress

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## Recent Changes in Federal Debt And Its Major Components

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### Summary

The government had surpluses in each of the four years 1998 through 2001. Over those years, the surpluses reduced federal *debt held by the public*, one of two components of total federal debt, by \$453 billion. *Debt held by government accounts*, the other component of total federal debt, *grew* by \$853 billion over the same four years. Total federal debt, the combination of the two components, increased by \$401 billion during the period. Annual change in debt held by government accounts is not affected by the government's overall surplus or deficit. It is determined by law and government accounting practices. This report will be updated as events warrant.

The continuing increase in total (or gross) federal debt in the face of budget surpluses during the 1998 through 2001 period produces an apparent budget paradox.<sup>1</sup> If deficits appear to make federal debt increase, as happened continuously over the previous three decades, why did the surpluses during those four years not make the debt fall? The answer to the question and the resolution of the apparent paradox is that the government's total surplus or deficit affects only the part of total federal debt that is *held by the public*. A deficit requires the government to borrow money from the public, increasing the amount of debt held by the public; a surplus allows the government to repay the public, reducing the amount of debt held by the public. The size of the remaining portion of federal debt, the portion *held by government accounts*, is determined by law and the accounting practices of the government and is not affected by the government's overall surplus or deficit.

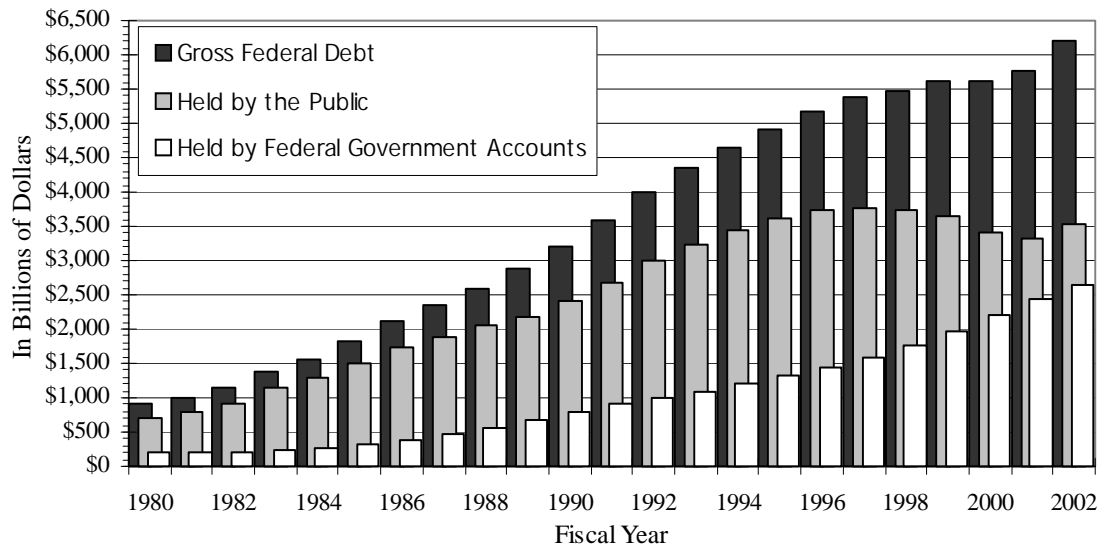
The government's surpluses over fiscal years 1998 through 2001 reduced federal debt held by the public by \$452.8 billion.<sup>2</sup> In the four years prior to the surpluses, 1994

<sup>1</sup> Unless otherwise noted, all years referred to are fiscal years. Data are generally end-of-year or end-of-period; changes are generally measured from the end of one year to the end of the next.

<sup>2</sup> The combination of constant and fairly rapid economic growth and declining deficits beginning in the mid-1990s caused a steep fall in debt held by the public as a share of gross domestic (continued...)

through 1997, with the government's budget in deficit, publicly held debt increased by \$524.1 billion. (For the period 1980 through 1997, continuous federal deficits increased the debt held by the public by over \$3 trillion, from \$711.9 billion in 1980 to \$3,772.8 billion at the end of 1997.) The chart below shows change in total and the two components of federal debt graphically for fiscal years 1980 through 2002.

**Figure 1. Federal Debt, 1980-2002**  
(in billions of dollars)



While federal debt *held by the public* fell during fiscal years 1998 through 2001, federal debt *held by government accounts* increased by \$853.4 billion. These statutorily established specialized government accounts (mostly trust funds) collectively have reported and are expected to continue reporting surpluses throughout the decade. The Treasury, as required by law, credits these accounts with federal debt in the amount of their reported surpluses. This debt accumulates in each account's fund as (potential) future governmental budgetary resources (these holdings of federal debt do *not* provide the account or the government with any financial resources).<sup>3</sup>

The government's total surpluses let the Treasury reduce federal debt held by the public; surpluses credited to government accounts require the Treasury to increase the debt issued to these government accounts. These transactions between and among government accounts and entities are carried out completely within the government itself; they do not require any transactions between the government and the public.

<sup>2</sup> (...continued)

product (GDP). It fell from its post-1960 peak of 49.5% of GDP in 1993 to 46.1% of GDP in 1997, the last year without a surplus. By the end of 2001 it had fallen to 32.7% of GDP.

<sup>3</sup> By changing one of these programs (through legislation), its future need for the accumulated budgetary resources may also change, either rising or falling, depending on the changes in the program. The accumulated amount of debt in the program's account may or may not provide sufficient budgetary resources for future program operations.

During the four years of surpluses, the debt held by government accounts rose substantially faster than debt held by the public fell. As a result, total federal debt grew by \$400.6 billion over these four years. Table 1 shows the amounts for debt held by the public, debt held by government accounts, total federal debt, and the annual change in each for the fiscal years 1990 through 2002.

**Table 1. Federal Debt, 1990-2002**  
(in billions of dollars)

End of Fiscal Year	Held by the Public		Held by Government Accounts		Total	
	Amount	Change from previous year	Amount	Change from previous year	Amount	Change from previous year
1990	\$2,411.8	—	\$794.7	—	\$3,206.6	—
1991	2,689.3	\$277.5	900.2	\$105.5	3,598.5	\$391.9
1992	3,000.1	310.8	1,020.1	119.9	4,002.1	403.6
1993	3,248.8	248.7	1,102.6	82.5	4,351.4	349.3
1994	3,433.4	184.6	1,210.2	107.6	4,643.7	292.3
1995	3,604.8	171.4	1,316.2	106.0	4,921.0	277.3
1996	3,734.5	129.7	1,447.4	131.2	5,181.9	260.9
1997	3,772.8	38.3	1,596.9	149.5	5,369.7	187.8
1998	3,721.6	<b>-51.2</b>	1,757.1	160.2	5,478.7	109.0
1999	3,632.9	<b>-88.7</b>	1,973.2	216.1	5,606.1	127.4
2000	3,410.1	<b>-222.8</b>	2,218.9	245.7	5,629.0	22.9
2001	3,320.0	<b>-90.1</b>	2,450.3	231.4	5,770.2	141.2
2002	3,540.8	220.8	2,658.0	207.7	6,198.8	428.6
Change over the Surplus Years 1998 through 2001		-452.8		853.4		400.6

**Source:** OMB, Budget of the U.S. Government for FY2002, Historical Tables, Table 7.1, Jan. 2002. U.S. Dept. of the Treasury, Final Monthly Treasury Statement, Table 6, Oct. 25, 2002.

## Surpluses or Deficits and Debt Held by the Public

The government's deficit or surplus is the difference between the government's income (receipts) and the government's spending (outlays). Generally, receipts and outlays closely approximate the amount of money (i.e., cash) that the government collects from and spends on the public.<sup>4</sup> As currently defined, a deficit exists when total outlays are greater than receipts; a surplus exists when receipts are greater than outlays.

When the government is in deficit, it borrows money from the public (by selling Treasury issued debt – bills, notes, bonds – through the financial markets to the public).

<sup>4</sup> The public in this context means anyone or any entity that is not part of the federal government. There are slight differences between the government's cash flows and reported outlays or receipts; they are unimportant for this general discussion.

The additional cash acquired by borrowing is needed to pay for the government's obligations that exceed its receipts. Borrowing because of the deficits leads to increases in federal debt held by the public.

In theory, the government could avoid an expected deficit and eliminate the need to borrow from the public by reducing spending or increasing revenues. In practice, at least in the short-term, making the rapid, substantial changes that may be needed to increase receipts or reduce outlays to avoid an expected deficit is extremely difficult. The reality, as shown by the government's actions over the last 30 years, has been an ongoing effort to solve the budget imbalance problem while continuing to raise the needed cash by selling government debt to the public. The many efforts to reduce outlays or increase receipts were never sufficient within short periods of time to eliminate the deficits.<sup>5</sup>

Surpluses reduce the accumulated debt held by the public. With more cash coming in than it needs to pay its bills, the government can, through a fairly automatic by-product of normal Treasury debt financing, shrink the outstanding debt held by the public.<sup>6</sup> In times of surplus, the Treasury will automatically use available cash to pay holders of maturing debt rather than pay them with cash raised by issuing new or replacement debt (a common practice when the government's budget is in deficit). The process of reducing the debt works in a slightly distorted mirror image of what the Treasury does when the government increases its debt when it has a deficit. Instead of offering debt to the financial markets to acquire needed cash, as it does when the government has a deficit, the government now has the cash (from receipts) with which to acquire existing federal debt. The Treasury can remain relatively passive and reduce the debt by waiting for it to mature and use its available surplus cash to pay debt holders, or it can, as it has done over the last several years, repurchase debt directly from the financial markets.<sup>7</sup> The Treasury takes these actions as part of its normal debt management activities without the need for specific instructions from Congress or the President.

As when it has deficits, the government could, through actions by Congress and the President, attempt to eliminate the surplus by increasing spending or decreasing taxes. But as with eliminating deficits, making the legislative adjustments in spending and receipts needed to eliminate the surplus (assuming that objective was desired) in a short period of time would likely prove difficult. Given sufficient time, surpluses, like deficits, can be changed through legislative actions.

## **Future Changes in Federal Debt**

The events in the fall of 2001, along with policy changes adopted both before and after the September 11 terrorist attacks, changed the budgetary expectations for the next

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<sup>5</sup> Congress and the President had also undertaken, as they did through much of the 1980s and most of the 1990s, policy changes that over time were designed to reduce or eliminate the deficit.

<sup>6</sup> The Treasury could also build large cash balances in its general accounts, but such action makes little sense.

<sup>7</sup> By actively entering the market to repurchase government debt, the Treasury is better able to maintain its debt management objectives, including maintaining a desired balance in the maturities of outstanding debt and market liquidity. See CRS Report RS20302, *Paying Down the Federal Debt: A Discussion of Methods*, by James M. Bickley.

several years. Projections of large and growing budget surpluses have been replaced with expectations of deficits, at least for the next several fiscal years, if not longer. This change in outlook will lead to increases in federal debt held by the public (because of the expected deficits) and, as previously assumed, continuing increases in debt held by government accounts. The result, even if the expected deficits are relatively small, will be accelerated increases in total federal debt.