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The President's Legal Authority at the Debt Limit

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Some time between the middle and the end of October, the federal government will reach a hard limit on the amount of debt it can issue, and its ability to finance governmental operations will be affected. Confusion about the debt limit abounds, and this *Issue Brief* will address some common questions.

What Is the Debt Limit? The United States debt limit, or debt ceiling, is the statutorily defined amount of debt the U.S. Treasury can issue, either by borrowing from the public or issuing an intragovernmental receipt to special accounts, such as the Social Security or Medicare trust funds.[1]

The Treasury Department has to have liquidity, or cash on hand, to disburse the funds necessary to meet its contractual obligations. The federal government maintains this liquidity by managing governmental receipts (such as income tax payments) and selling debt (such as Treasury bonds).

Will a Government Shutdown Occur If the Debt Limit Is Not Raised? The debt limit is often confused with the expiration of appropriations bills. Reaching the debt limit is distinct from a government shutdown. A government shutdown occurs when appropriations authorization expires: Unless there is a law saying that money may be spent on a project, money may not be spent on that project.[2] A debate over an appropriations bill is a debate over whether to fund a specific government function. When the government shutdown began, only certain statutorily defined "essential" government functions have continued to operate.[3]

The debate over the debt limit, however, is a debate over *how* to finance governmental operations—reaching the debt limit would not force a government shutdown. Currently, the debt limit is $16.699 trillion.[4] The federal government reached this limit on May 19, 2013, and Treasury has since used statutorily allowed "extraordinary measures" to avoid issuing additional debt and still have the cash on hand to finance day-to-day operations. When the Treasury exhausts these extraordinary measures, the federal government will continue operating. However, the President might decide that federal employees, for example, will not necessarily be issued checks available to cash immediately.

Even without the ability to issue additional debt, the government will continue to accrue legal obligations; it will simply not be able to immediately liquidate (pay cash for) those obligations.[5]

What Happens to the U.S. Debt If We Reach the Debt Limit? It is impossible to tell what would happen if the debt limit is not raised.[6] If Congress and the President are unable to reach an agreement on raising the debt ceiling, markets and credit rating agencies might interpret this negatively as unwillingness of the U.S. government to honor its obligation. If the President chooses to default on all obligations rather than a few (discussed below), this could exacerbate the problem. Market perception of U.S. sovereign debt directly affects bond yields (interest

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rate paid) on U.S. debt, so decisions the President makes can actually save or cost the government money in the long term.

The Prompt Payment Act[7] provides that the "temporary unavailability of funds to make a timely payment" does not excuse delayed payment and that the government is responsible for paying interest charges on such delayed payments. Over time, these interest penalties capitalize, so the federal government ends up paying compound interest. Depending on how the President manages payments, statutory interest payments may be greater or smaller.

What Would the President Prioritize? While there have been proposals to cabin the authority of the executive to prioritize payments,[8] as it stands there is no statute governing how to manage government finances past the debt limit. Since governmental obligations would exceed receipts, exceeding the debt limit logically implies that at least some obligations would be delayed. These obligations would thus, by definition, be in default. There is no general "governmental default" past the debt limit; default would occur with respect to specific obligations that the President chooses not to prioritize.

There are constitutional backstops on the President's otherwise plenary authority to prioritize payments.[9] Of these, the most important is that the President may not prioritize payment in violation of the Due Process Clause of the Fifteenth Amendment. He may not, for example, choose to pay the salaries of federal employees of one race before paying the salaries of federal employees of another race. Subject to this limitation, the President's prioritization choices are essentially unbounded.

The President could, of course, play a game of political brinksmanship and fail to pay *any* obligations until the debt ceiling is raised. He could argue that all obligations are on an equal footing and that prioritizing payments violates some principle of fairness. Former Treasury Secretary Timothy Geithner made statements about the political unworkability of prioritization in the past,[10] but to date, Treasury

1. Mindy R. Levit et al., "Reaching the Debt Limit: Background and Potential Effects on Governmental Operations," Congressional Research Service *Report for Congress*, September 19, 2013, http://www.fas.org/sgp/crs/misc/R41633.pdf (accessed October 9, 2013).
2. 31 U.S. Code § 1341.
3. Hans von Spakovsky, "What Happens During a Government 'Shutdown'?," Heritage Foundation *Issue Brief* No. 4049, September 18, 2013, http://www.heritage.org/research/reports/2013/09/what-happens-during-a-government-shutdown.
4. Budget Control Act of 2011, Public Law 112–25.
5. If a federal employee were to sue to compel payment, there is no doubt that the federal government would be obliged to pay. The remedy for such a lawsuit would be payment but not necessarily *immediate* payment. *See, cf., In re Barr Laboratories*, 930 F.2d 72 (D.C. Cir. 1992).
6. The federal government has "defaulted" on various obligations in the past. Technically, any time the government does not make a payment on time, even due to a clerical error, it has "defaulted" on that obligation. Perhaps the most applicable "default" occurred in 1979, when Treasury failed to make timely payments to holders of various Treasury bills. This default was minor, but because it involved the security of Treasury bills, it had lasting consequences. See Brady Dennis, "Delayed Payments in 1979 Offer Glimpse of Default Consequences," *The Washington Post*, July 10, 2011, http://www.washingtonpost.com/business/economy/delayed-payments-in-1979-offer-glimpse-of-default-consequences/2011/07/10/gIQARRBj7H_story.html?hpid=z1 (accessed October 9, 2013). There are many other examples of federal default. See, e.g., George Chidi, "Error Delays Friday the 13th Paycheck for 40,000 Federal Workers," The Raw Story, September 14, 2013, http://www.rawstory.com/rs/2013/09/14/error-delays-friday-the-13th-paycheck-for-40000-federal-workers/ (accessed October 9, 2013). Errors such as these have no market effects, because they do not implicate U.S. public debt. Routine failure of this kind could, however, rankle investors and implicate U.S. borrowing power.
7. 31 U.S. Code § 3902.
8. The Full Faith and Credit Act of 2013 (H.R. 807), which seeks to pay bondholders and Social Security beneficiaries even past the debt limit, has passed the House but is not a priority in the Senate. Furthermore, the President has indicated he would veto the bill.
9. There are a variety of potentially applicable constitutional provisions. Article II, Section I of the Constitution provides that the President's salary "shall neither be increased nor diminished during the Period for which he shall have been elected." Article III, Section I provides that "judges, both of the supreme and inferior Courts…shall, at stated times, receive for their services, a compensation, which shall not be diminished during their continuance in office." These two provisions might be interpreted to mean that the President must prioritize payment of these constitutional officers. In addition, Section 4 of the Fourteenth Amendment provides, "The validity of the public debt of the United States…shall not be questioned." Strictly speaking, this provision is not germane to what happens beyond the debt *limit*, since the relevant statute only limits the creation of additional public debt rather than dissolving previous debt.
10. U.S. Department of the Treasury, letter of Secretary Geithner to the Senate Majority Leader, January 6, 2011, http://www.treasury.gov/connect/blog/Documents/Letter.pdf (accessed October 9, 2013).

has not disavowed its legal authority in this area. Failing to prioritize debt obligations would have far-reaching consequences, however, including potentially increasing the cost of servicing the debt long after the debt limit crisis ends.

Further, to the extent that this situation would involve having cash on hand and failing to pay *some* receipts, this option implicates the Congressional Budget and Impoundment Act of 1974, which prevents the President from deferring any "budget authority." This phrase is defined to include "borrowing authority, which means authority granted to a federal entity to borrow and obligate *and expend* the borrowed funds."[11] Holding cash until such time that the Treasury can meet all of its payments necessarily includes deferring expenditures of borrowed funds until such time as the debt ceiling is raised, which would implicate these statutory limitations.[12]

The President could also choose to continue payments for "essential" services analogous to those defined in the appropriations context.[13] There is no statutory requirement for this decision, but the idea that there are "core" functions of the federal government that ought to remain liquid is easily understandable. Meeting debt obligations and paying military personnel might be prioritized at the expense of other obligations, such as issuing certain grants and loans to private-sector firms and to state and local governments, for example. So-called mandatory spending, such as Social Security payments, do continue during a government shutdown, but they need not be prioritized at the debt limit.[14]

The President could also pick and choose among programs he likes and those he does not like. He might direct Treasury to pay Department of Defense employees before Department of Education employees, or vice versa. Whatever decision he makes would be essentially unchallengable in court.

Ultimately, however the President chooses to manage payments, delays will accumulate and worsen until either spending is cut or the debt ceiling is raised.

Broad Authority. In brief, the President has broad authority to manage government payments to avoid defaulting on federal obligations. He can choose which payments to make and in which order, and these choices will impact the effects on the average U.S. taxpayer and the economy.

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11. 2 U.S. Code § 684; 2 U.S. Code § 622 (emphasis added).
12. If the President decided to prioritize a major program and needed to withhold receipts temporarily in order to provide a liquidity "cushion" and avoid defaulting on that particular obligation, he would be on stronger footing, since the purpose would be meeting rather than avoiding appropriations obligations.
13. 31 U.S. Code § 1342.
14. While the President is not compelled to prioritize Social Security payments, he is certainly not compelled to *not* pay Social Security payments. President Obama has, however, made statements that he believes he will be forced to delay Social Security checks, which is flatly untrue. See Romina Boccia, "Obama Needlessly Scares Seniors: Social Security Checks and the Debt Limit," The Heritage Foundation, *The Foundry*, October 7, 2013, http://blog.heritage.org/2013/10/07/obama-needlessly-scares-seniors-social-security-checks-and-the-debt-limit/.