

A Bird's Eye View of the Debt Ceiling

The federal government seems to be constantly running up against the statutory debt limit as the national debt increases, which has major implications for the U.S. economy. Here's a basic overview of this critical issue. See a more detailed explainer [here](#).

What is the debt limit?

The debt ceiling is the legal cap on the total amount of federal debt that the government can accumulate. Before the establishment of the debt ceiling, Congress had to approve through legislation each time the government borrowed funds. The limit was established to simplify the process in the early 20th Century and has been raised about 100 times since then.

What happens if the debt ceiling is reached?

In the immediate term, the Treasury Department can execute accounting maneuvers to avoid going over the limit, known as "extraordinary measures." Once those measures are exhausted, then the government cannot issue any more debt to borrow money. The government will have to rely on cash on hand and incoming revenue to pay obligations, which will not last long since the federal government is currently running deficits. The result will be a government default.

What happens if the U.S. defaults?

A government default likely means that Social Security payments will be missed, government employees will not get paid, and creditors and businesses dealing with the government will not receive what is owed them. A default would have grave consequences for the economy, as investors would refrain from buying government securities because they would no longer be considered a safe investment. Interest rates would go up and markets would be shaken.

What should policymakers do?

Default is not an option as the economic consequences are too severe. Even threatening a default could cause chaos and wreak havoc on the economy. On the other hand, continuing to add to the debt indefinitely is also not an option because that too would harm the economy and standard of living over time. Policymakers need to fix the debt through spending and tax reforms that are phased in over time.

How useful is the debt ceiling if the national debt keeps going up?

Actually, most of the major deficit reduction agreements of recent years have accompanied a debt limit increase. However, in most cases, temporary debt limit increases were enacted to provide time for deficit reduction negotiations to conclude without the threat of default.

Is there a better way?

Yes. There are many options for improving or replacing the debt limit to control the national debt without threatening economic disaster. Some ideas include linking increases to the debt limit to fiscal targets; considering the debt limit when Congress is making spending and revenue decisions, as opposed to afterwards; and applying the debt limit to more economically relevant measures like debt held by the public as a share of the economy. See more ideas [here](#).