

# The National Debt Ceiling Increase Standoff Continues – Despite Loud Alarm Bells

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The U.S. Treasury has clearly warned that as early as June the national debt ceiling will likely be reached, and the federal government may have to default on its debt obligations. Continued paralysis, however, plagues Washington and legislators continue to fail to increase the national debt ceiling as the country marks four months into the new fiscal year and the 18<sup>th</sup> congressional session. With the GOP in control of the House since January, the current congress is also earning the distinction as one of the least productive on record, furthering the loss of esteem by the American public.

All obligations and programs previously approved by earlier congressional sessions and the executive branch will no longer be able to be funded after the debt ceiling is reached. Government entities will not be able to function putting in peril all payments to federal employees including those related to social security beneficiaries, Medicare and Medicaid healthcare insurance reimbursements, national security, air controllers and national defense globally.

It is stressed that the existing debt-ceiling adjustment mechanism is seriously flawed as rising debt is a consequence of fiscal decisions that have already been legislated. Furthermore, nearly two-thirds of the federal budget is consumed by so-called mandatory outlays (include Social Security and Medicare programs), which simply rise automatically as prescribed by law.

President Biden and the Democrats of both houses have demanded since the beginning of the year a debt limit hike with no strings attached. Such increases were repeatedly made during the administration of President Trump with Democrats cooperating despite record budget deficits. Debt ceiling increases during his term, according to US Treasury data, totaled \$7.8 billion, 25% of the current national debt. Each addition established new record national debts.

The GOP House Speaker has now proposed an increase in the debt ceiling conditional on deep across the board budget cuts (reportedly on average 22% according to the Office of Management and Budget), without any great specificity until now on which programs and by how much. The GOP has agreed that Social Security and Medicare benefits will not be touched, despite their need for serious attention given projected depletion of resources and technical insolvency in the near future. They are also reluctant to decrease defense spending.

The GOP has expressed, however, their intentions to attack federal health care and food assistance programs qualification requirements as well as other programs that have been the focus of past Democrats legislative successes. These include such key areas as education, climate change, energy, labor, research programs and paradoxically, even the manpower of the Internal Revenue Service.

Democrats have warned that those proposals are non-starters as they signify deep cuts to benefits aimed at working- and middle-class citizens. Furthermore, significant cuts at this moment would hamper economic growth. Estimates of the toll of such cuts include 30 million fewer veteran outpatient visits, 10 million people under Medicaid losing health insurance coverage, layoffs of 108,000 teachers in schools with low-income students and kids with disabilities, 200,000 fewer children in Head Start educational development programs and 1.7 million low-income women and children losing nutritional assistance.

The 2024 budget proposal of the President conserves those programs and places increased focus on increasing tax revenue from corporations (currently contribute only 9% of tax revenues) and high-income individual taxpayers (earning greater than \$400,000 annually). Both of these groups received significant tax reductions during the Trump years, a period which incurred high social cost obligations due to the COVID-19 pandemic and significant increases in the cost of national defense.

The House Speaker's proposal to date leaves untouched the Pentagon and possibly services for veterans. However, his proposal is further complicated by well-known divisions within the House GOP on the debt negotiation proposal to be submitted to the President with publicized ideas heavily influenced by the demands of the ultra-right Freedom Caucus minority.

A group of bipartisan moderates in the U.S. Congress, this part of a group named the Problem-Solvers Caucus (64 members equally divided between Democrats and Republicans) have made a new proposal to avert the disaster of the federal government defaulting on its debt this year. It has the following key points:

- Suspend the debt ceiling limit through the rest of the year 2023 and up to 18 months while Congress proceeds with its usual budget and appropriations process
- During the 18-month period this group of centrists would establish an external independent "fiscal commission" to develop a package to stabilize long-term deficits and debt. The commission's report would be completed by December 2024 and its recommendations voted on by February 28 of 2025 to ensure the fiscal health of the country. This idea sounds similar to the Bowles-Simpson Commission, a bipartisan Presidential Commission on deficit reduction created in 2010 by President Barack Obama which had serious recommendations, but which went largely ignored

The Problem-Solving Caucus has been instrumental during prior congressional sessions to develop agreements that aided in the passing of important legislation including deals on COVID-19 relief, immigration reform, health care, infrastructure, and other important policy issues. Seventy-five percent of the caucus members reportedly support this proposal.

This suggestion is one of several that will possibly emerge as the final debt ceiling deadline nears. This highlights the existing confrontation between President Biden and House Speaker Kevin McCarthy. The leadership of both parties have to date, however, dismissed this idea and have described the idea as counterproductive.

The latest key provisions of the debt proposal announced on April 18<sup>th</sup> by Majority Speaker McCarthy are the following:

1. **Raise the debt ceiling into 2024 - by \$1.5 trillion, or through March 2024, whichever occurs first, while making cuts to government spending.**
2. **Massive spending cuts** – These cuts would slash the federal budget back to levels adopted in the 2022 fiscal year, which could amount to \$130 billion in spending cuts for 2024. It also proposes to cap any growth in federal agencies' future budgets at 1 percent, this implying budget cuts of as much as 22% in discretionary budget accounts outside of defense.
3. **New work requirements for welfare** - Millions of low-income Americans who receive food stamps and health insurance from the federal government would have to work longer hours or satisfy certain income or work thresholds in exchange for benefits under the new GOP bill. It does not address those unable to work because of health conditions.
4. **Block student debt cancellation** - The plan aims to block the President's program to cancel thousands of dollars in college debt, a program long sought by cash-strapped students. President Biden announced in August his plan to wipe out \$10,000 in debt for Americans who earn less

than \$125,000 annually, and \$20,000 for lower-income borrowers. The Supreme Court under a suit brought by several states has heard arguments in February in a case that could see the program thrown out regardless of what Congress does.

5. **Claw back IRS funds** - The plan targets at least some of the \$80 billion allocated to improve the staffing and resources of the Internal Revenue Service and help the government pursue unpaid taxes. Democrats originally approved the money last year as part of the Inflation Reduction Act to ease a backlog of returns at the tax agency while empowering it to investigate wealthy Americans and corporations that fail to pay what they owe in taxes. The CBO found that the new IRS spending would help reduce the deficit by \$120 billion over the next decade.
6. **Repeal green energy programs, including some EV tax credits** - Republicans have made no secret about their opposition to the Inflation Reduction Act's investments to fight climate change. The plan would repeal a broad range of tax policies intended to incentivize the deployment of green energy. That includes a partial end to tax credits for new and used electric vehicles.
7. **Take back unspent covid aid and other measures** - the plan would include:
  1. Clawing back of unspent money authorized in previous coronavirus aid packages. Federal officials have estimated that amount is probably less than \$100 billion.
  2. Adopting what is called the Reins Act, which would grant Congress major new authority to review and overturn health, labor and other rules issued by federal agencies. The Reins Act would require Congress to approve any federal rule or regulation the Office of Management and Budget determines to have an economic impact of \$100 million or more according to before it is imposed on the American people.
  3. Permitting legislation that could ease the way for more oil and gas drilling.

At this late date and hour, there is reported skepticism that an agreement will in fact be reached between President Biden and House Speaker McCarthy. Unlike the agreement reached in 2011 on the same issue between the two rival parties (at which moment President Biden was Vice-President), this time the House Speaker faces major hurdles in uniting his party for any one budget proposal, with its extreme right minority having undue influence. In addition, President Biden remains unwilling to glorify a ludicrous bill containing outlandish budget cuts with little chance to be approved by the Senate.

In the meantime, as the critical default hour commencing in June approaches the alarm bells get louder for the country and its financial markets.