



## Given the Current Debt Ceiling Limit, Who Will Get Paid?

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What happens if Republicans and Democrats are unable to craft a deficit reduction agreement by early August? Barring a short-term extension of Uncle Sam's current debt limit of \$14.29 trillion, the Treasury has indicated August 3, 2011 is the date the U.S. government defaults could begin.

### How this could play out

Without authority to further borrow, our government is presumably limited to spending no more than its cash inflows. According to a recently released study by the Bipartisan Policy Center (BPC), the projected cash inflows for the period August 3 to August 31 are \$172.4 billion, while the approved expenditures are over \$306.7 billion for the same time period. That suggests that \$134.3 billion, or nearly half of the scheduled payments would be delayed or subject to default. The Treasury Department would be charged with picking and choosing which payments to make, and it's not difficult to imagine the chaos and legal challenges that would result. It becomes even more problematic when managed on a day-to-day basis as Treasury's revenues vary from day to day, while substantial payments are due on specific dates.

### Can we pay our soldiers?

The BPC study also provides some informative breakdown of the scheduled August expenditures, while contemplating how Treasury might prioritize their payment. Two alternative scenarios each include the expected payment of the four following programs totaling \$141 billion:

- Treasury Security interest - \$29.0 billion
- Social Security Benefits - \$49.2 billion
- Medicare and Medicaid - \$50.0 billion
- Unemployment Benefits - \$12.8 billion

Who then gets paid from the remaining \$31 billion of cash revenues? Consider just a sampling of these other August debts:

- Military Active Duty Pay - \$2.9 billion
- Federal Salaries and Benefits - \$14.2 billion
- IRS Refund Payments - \$3.9 billion
- Defense vendors - \$31.7 billion
- Housing and Urban Development Programs - \$6.7 billion

Although most economists believe it is unthinkable that the government would allow this to play out, the daily meetings between President Obama and congressional leaders underscore the risks of not reaching an agreement on the nation's debt. Beyond the threats of forcing the country back into recession or a further weakening of the dollar, there are real implications to the U.S. Treasury market and likely higher interest rates. The credit rating agencies must consider whether to downgrade U.S. debt obligations if the borrowing limit is not raised.

With sufficient government revenues to meet existing interest payments on U.S. Treasuries, there is presumably no likelihood of defaulting on those debts. However, with an estimate of more than \$500 billion in Treasuries maturing

throughout August, the government must have sufficient access to the markets to raise that amount from new issues and repay its maturing obligations. At what price? And what happens to the appetite for holders of U.S. debt, many of which are located outside of our country?

Without a real precedent for handling this potential crisis, let's hope our lawmakers find the common ground necessary to negotiate a deal.

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