

tying borrowing costs to program costs, although it has proved more costly to taxpayers than financing directly by the Treasury. In the case of small credit programs, it also provided an effective alternative to inefficient direct small agency market borrowing or even more inefficient attempts by credit agencies to sell specific loans of small, odd amounts with widely varying characteristics.

The participation certificate has also permitted somewhat more flexibility in Treasury financing. First, it has permitted financing outside the oftentimes stringent public debt ceiling, since until the present fiscal year all participation certificates were outside the debt ceiling. In addition, longer-term securities in the form of participation certificates could be offered at times when direct longer-term Treasury borrowing was precluded by the $4\frac{1}{4}\%$ interest ceiling on Treasury issues running five years (now seven) or more to maturity. Hence, charges have been made that congressional intentions were being thwarted on both the debt ceiling and the interest rate ceiling, as well as the even more basic criticism that the use of participation certificates effectively buried substantial expansion of an important form of Federal expenditures—namely Federal direct loan programs.

In one sense, the sale of shares in a pool of loans is but a short, logical step beyond the sale of the asset itself; but this is a critical step. When an asset is sold, the Federal Government retains no equity in it although it usually guarantees the loans it sells. When it is pooled, however—and participation certificates sold in the pool—the ownership (though not the beneficial equity) is still retained by the Federal Government. Interest payments on the loan continue to flow to the Government and the Government continues not only to incur servicing costs but also to assume fully the risk of default on any individual loan as far as the investor in the participation certificate is concerned.

The Commission is firm in its conviction, therefore, that participation certificates, regardless of their advantages or disadvantages on other scores, represent a means of financing the budget deficit rather than an offset to expenditures in determining the amount of the deficit to be financed. Participation certificates are reflected in this manner in the figures presented in Chapter 6 and in Tables 6 and 6D in Chapter 9.¹

¹ Secretary Fowler and Director Schultze regard the proceeds of sales of participation certificates and sales of credit agency obligations—to the extent that these proceeds and other principal repayments do not exceed aggregate loan disbursements—as proper offsets to loan expenditures. They should be subtracted from gross loan disbursements in arriving at “net lending.” To the extent that its credit programs finance themselves through participations, agency issues, sales of individual assets, or loan repayments, the Federal Government does not call upon the revenues or general borrowing of the Treasury. It is the call upon the Treasury revenues or borrowing which the net lending figure should equal. For the self-financed portion of the loans, the Government is primarily acting as a financial intermediary with much the same impact as the insurance of private loans. Federal guarantees of participation certificates come into play only in the contingency that the underlying assets of the credit programs default. Professor Turner also joins in supporting this statement.