THE DEPARTMENT OF ENERGY LOAN GUARANTEE PROGRAM

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Taxpayers for Common Sense

What are loan guarantees?

Federal loan guarantees provide borrowers the financial backing of the U.S. Treasury enabling them to get below market privately or publicly funded direct loans.

According to the U.S. House of Representatives Rules Committee, a loan guarantee is a "statutory commitment by the federal government to pay part or all of a loan's principal and interest to a lender or the holder of a security in case the borrower defaults."

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The Subsid y of Choice

- Congress
  - Influence markets and industry growth
  - Incentivize specific projects
  - “Free” Money
- Industry
  - Essentially Zero Risk
  - Full faith and credit of the US government
  - Potentially little to no upfront cost
  - Billions more than could ever be given in direct subsidies

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History of the Department of Energy Loan Guarantee Program

- Originally proposed in the failed 2003 Energy Bill for nuclear projects
- Enacted into law in Title XVII of Energy Policy Act of 2005
- Created a program within DOE to provide guarantees for "innovative" energy technologies
- According to the legislation Title XVII is designed to provide financial support for projects that:
  1) Avoid, reduce or sequester air pollutants or greenhouse gases;
  2) Employ new or significantly improved technologies;
  3) Provide a reasonable prospect of repayment
- Proponents claim Title XVII was designed to be technology neutral

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Eligible Projects

- Renewable Energy Systems
- Advanced Fossil Energy Technology
- Hydrogen Fuel Cell Technology
- Advanced Nuclear Facilities
- Carbon Capture and Sequestration Practices
- Efficient Electrical Generation, Transmission and Distribution Technologies
- Efficient End-Use Energy Technologies
- Production Facilities for Fuel Efficient Vehicles
- Pollution Control Equipment
- Oil Refineries

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Title XVII Loan Guarantee Program

- Guarantees can be made for up to 80% of the total project cost
- Program must adhere to Federal Credit Reform Act of 1990
- "Subsidy cost" must be self-financed or appropriated by Congress
- Taxpayers have superior rights to property in case of default

Federal Credit Reform Act (FCRA)

- The Federal Credit Reform Act of 1990 is designed to accurately calculate and account for the cost implications of direct and guaranteed loans on the federal budget.
- Requires agencies to control risks and costs of their respective credit program
- Office of Management and Budget ensures agency programs adhere to FCRA requirements

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Subsidy Cost

- Subsidy Cost is the expected long-term liability or cost to the Federal government in issuing the loan guarantee.
  - Extremely difficult to calculate
  - Inherent conflict because the higher the subsidy cost the less attractive the loan guarantee
  - Projects differ in cost and size, cover large variety of technologies, and applicants will have different credit experience; therefore the DOE is likely to miscalculate individual projects' cost.
  - DOE will likely underestimate loan guarantee fees relative to costs
  - Methodology for accessing this cost is not available to the public

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DOE Regulations

- Before DOE could issue loan guarantees Congress directed DOE to release final regulations.
- DOE Guidelines in Dec 2006
- Notice of Proposed Rulemaking in May 2007
- DOE releases final rule October 2007

DOE Final Rule

- The final rule "establishes the procedures, policies and requirements" for the program
- Guarantees up to 100% of a loan for up to 80% of the project cost
- Requires use of Federal Financing Bank for projects that request 100% guarantee
- Adopts solicitation-based process for applications

Loan Guarantee Program Budget Authority

- $42.5 billion in currently available budget authority
  - $4 billion appropriated for FY2007
  - $38.5 billion included in FY2008 Omnibus Appropriations bill expires March 6, 2009
- $47 billion proposed in FY2009 Omnibus available until committed
- New total likely $51 billion in budget authority

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Project Breakouts for Existing Authority

- $18.5 billion nuclear power facilities
- $8 billion for coal gasification and coal power generation with carbon capture and sequestration
- $10 billion renewable energy and transmission projects (Omnibus raises to $18.5 billion)

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Loan Guarantees in the Stimulus

- Appropriates $6 billion in subsidy costs
- Assumes $60 billion in projects
- Precedent setting for the program

DOE Solicitations

- Dec 2006: Initial Pre-Applications
- June 2008: Nuclear Facilities-$18.5 billion
  - 14 applications
  - $122 billion in guarantees requested
  - 21 new reactors
- June 2008: Front-End Nuclear Fuel Cycle- $2 billion
- June 2008- Renewable Energy Systems
- September 2008: Advanced Fossil Energy
- 11 Pre-applicants likely to receive loan guarantees this spring

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Government Accountability Office (GAO) Concerns

- The GAO, Congress's investigative arm, has tracked the program closely. In their latest analysis GAO found that current program:
  - lacks the resources and internal structure to review and process loan guarantee applications.
  - has yet to initiate a plan to consult with outside experts in financial, legal, environmental and other fields
  - has not determined the programs needs or to begun to establish contracts with outside consultants
  - lacks sufficient staffing and management

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Government Accountability Office (GAO) Concerns (continued)

- GAO latest analysis also finds that current program:
  - plans to accept non-cash equity such as land or other assets
  - lacks performance measures to track the program's effectiveness and to account for the program's full administrative costs
  - has not established a system to find lenders or oversee

- GAO concluded DOE was not "well-positioned" to run the lgp and recommended Congress limit the program

DOE Inspector General Report

- The Inspector General (IG) issued a critical report on the program in 2007, calling it "a significant risk to taxpayers"

- On February 17, 2009 the IG released a new report that also found shortcomings in the current program including a lack of:
  - formalized procedures for distributing loan guarantees
  - evaluation process to approve applications and select eligible lenders

- The IG found the DOE had yet to establish procedures to estimate losses if a loan guarantee recipient were to default on their loan

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Taxpayer Concerns with the Title XVII Program

- Provides guarantees to highly risky projects private markets won't support
- Supports coal and nuclear projects with track record of failure
- Structural and Operational problems: subsidy cost, staffing, failed history of DOE loan guarantee programs
- CBO estimates 50% default rate for nuclear projects
- GAO estimates a 50% default rate and a 50% recovery rate, leaving a 25% loss to federal taxpayers for the program overall

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Future Taxpayer Threats

- Increased Budget Authority
- Removal of all time deadlines
- Appropriation of subsidy cost
- Exemption from FCRA
- Removal of taxpayer superiority of rights

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