

February 15, 2017

The Honorable Randy Weber  
Chair, Subcommittee on Energy  
The Honorable Darin LaHood  
Chair, Subcommittee on Oversight  
House Committee on Science, Space, and Technology

Joint Energy Subcommittee and Oversight Subcommittee Hearing  
Risky Business: The DOE Loan Guarantee Program

Dear Chairman Weber and Chairman LaHood:

Thank you for the opportunity to contribute to the House Committee on Science, Space, and Technology's joint hearing by the Subcommittee on Energy and the Subcommittee on Oversight on the future of the Department of Energy's (DOE's) loan guarantee programs.

As the committee is aware, the Department of Energy's loan guarantee programs authorized under Title XVII (Section 1703 and Section 1705) of the Energy Policy Act of 2005 and the Advanced Technology Vehicle Manufacturing (ATVM) direct loan program have either yielded failures (for example, Solyndra and Abound Solar) or merely protected the bottom lines of companies that did not need taxpayer handouts to begin with (for example, Ford and Nissan). Indeed, these programs have extended preferential loans to commercial giants like NextEra Energy Resources (a Fortune 200 company), Prologis (a global real estate investment trust), NRG Energy (a Fortune 500 company ranked 196th), and Cogentrix (at the time a wholly owned subsidiary of Goldman Sachs).<sup>1</sup>

I greatly appreciate the committee's continuing focus on these loan programs. More than \$30 billion in loans and loan guarantees have been issued under the three programs since 2009, and taxpayers are potentially liable for most of that amount.<sup>2</sup> Programs under Sections 1703 and 1705 in particular have guaranteed \$22 billion in loan guarantees since 2009.<sup>3</sup>

In addition, while the Section 1705 loan program expired in 2011, Section 1703 and ATVM still have billions of dollars in authorized funds remaining. As of FY2017, the DOE still has \$24.9 billion in loan guarantee authority under 1703 and \$13.2 billion

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<sup>1</sup> Department of Energy, "Portfolio Projects," accessed February 13, 2017.

<sup>2</sup> Government Accountability Office, "DOE Loan Programs: DOE Has Made More Than \$30 Billion in Loans and Guarantees and Needs to Fully Develop Its Loan Monitoring Function," GAO-14-367, May 30, 2014.

<sup>3</sup> Ibid.

under ATMV.<sup>4</sup> The potential exposure of taxpayers is substantial. Also, contrary to what some are claiming,<sup>5</sup> the programs are not profitable when considering the federal government's borrowing costs.<sup>6</sup>

As I and others have noted, the problems with loan guarantees like Sections 1703 and 1705 are much more fundamental than the cost of one or more failed projects.<sup>7</sup> In fact, the economic literature shows that every loan guarantee program transfers the risk from lenders to taxpayers, is likely to inhibit innovation, and increases the overall cost of borrowing.<sup>8</sup>

At minimum, such guarantees distort crucial market signals that determine where capital should be invested, causing unmerited lower interest rates and a reduction of capital in the market for more worthy projects. At their worst, loan guarantees introduce political incentives into business decisions, creating the conditions for businesses to seek financial rewards by pleasing political interests rather than customers. This is called cronyism, and it entails real economic costs.<sup>9</sup>

Loan guarantees are particularly attractive from a political perspective. Congress can approve billions of dollars in loan guarantees with little or no impact on appropriations figures or the deficit because such loans are almost entirely off budget. Moreover, unlike the Solyndra case, most failures either take years to occur or never occur; this is because the many of the companies were not risky borrowers in the first place and had plenty of access to capital—as with 90 percent of the Section 1705 loan program recipients.<sup>10</sup> This allows politicians to appease parochial interests by granting loans to local companies with few negative consequences. The projects will most likely succeed, or it will be years before the projects default.

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<sup>4</sup> Catalogue of Federal Domestic Assistance, “Federal Loan Guarantees for Innovative Energy Technologies,” accessed February 13, 2017.

<sup>5</sup> Paul Krugman, “When Government Succeeds,” *New York Times*, November 16, 2014; and Max Ehrenfreund, “Remember Solyndra? Those Loans Are Making Money,” *Washington Post*, November 13, 2014.

<sup>6</sup> Donald Marron, “Spin Alert: Despite What DOE Says, Its Loans Are Not Making Money,” *Forbes*, November 17, 2014; and Veronique de Rugy, “No, the Program That Gave Us Solyndra Is Obviously Not Profitable,” *The Corner, National Review Online*, November 19, 2014.

<sup>7</sup> Veronique de Rugy, “Assessing the Department of Energy Loan Guarantee Program” (Testimony before the House Committee on Oversight and Government Reform, Mercatus Center at George Mason University, Arlington, VA, June 19, 2012). Also see Chris Edwards, “Energy Subsidies” (Downsizing the Federal Government, Cato Institute, Washington, DC, December 16, 2016); and House Budget Committee, “The Empty Promise of Green Jobs: The Costly Consequences of Crony Capitalism,” September 22, 2011.

<sup>8</sup> Matthew D. Mitchell, *The Pathology of Privilege: The Economic Consequences of Government Favoritism* (Arlington, VA: Mercatus Center at George Mason University, 2012); and Veronique de Rugy, “A Guarantee for Failure: Government Lending under Sec. 1705” (Testimony before the House Committee on Oversight and Government Reform, Subcommittee on Regulatory Affairs, Mercatus Center at George Mason University, Arlington, VA, July 18, 2012).

<sup>9</sup> Mitchell, *The Pathology of Privilege*.

<sup>10</sup> de Rugy, “Assessing the Department of Energy Loan Guarantee Program.”

It is also easy to understand why companies and company executives benefit from these loans and may seek them out. However, this should not obscure the fact that this preferential treatment comes at the expense of taxpayers, competitors, and consumers—and ultimately at the expense of our market and political system.

For all of the above reasons, the right thing to do is to permanently terminate these loan programs, along with all other energy subsidies. As Chris Edwards explains,<sup>11</sup>

This energy revolution was driven by private innovation and competitive markets, and it has created environmental as well as economic benefits. Cleaner natural gas is replacing coal as a fuel source in U.S. electricity production. Over the past decade, coal fell from 49 percent of electricity production to 33 percent, while natural gas rose from 20 percent to 33 percent. . . .

. . . The oil and gas revolution shows that businesses and markets can generate major innovations and progress with their own resources. Furthermore, investors and major corporations have stepped up to the plate and pumped billions of dollars into alternative energy technologies in recent years. The U.S. energy sector is vast, dynamic, and entrepreneurial, and it does not need subsidies to thrive.

With that in mind, a plan to reform the DOE's loan guarantee programs should:

- Cancel all remaining loan guarantee authority under Section 1703 and the ATMV program (approximately \$25 billion for Section 1703 and \$13 billion for ATVM).
- Abolish the programs permanently.
- Continue to appropriate funds to the DOE's Loan Programs Office, which would administer the wind-down of the loan portfolios (\$15.7 billion in Section 1705 guarantees, \$6.2 billion in Section 1703 guarantees, and \$8.4 billion in ATMV). Alternatively, transfer the loan obligations to the Department of the Treasury to administer or auction them off to the private sector.

Eliminating these loan guarantee programs will level the playing field for all firms, end a cycle of counterproductive cronyism, and allow the crucial energy sector to continue to thrive and innovate, with beneficial effects on the environment.

Sincerely,

Veronique de Rugy  
Senior Research Fellow  
Mercatus Center at George Mason University

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<sup>11</sup> Edwards, "Energy Subsidies."