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It’s Time to Permanently Abolish the DOE Green-Energy Loan Programs

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by Veronique de Rugy February 11, 2017 8:23 PM

Next Wednesday, the House Committee on Science, Space, and Technology’s Subcommittee on Energy and its Subcommittee on Oversight are jointly holding a hearing to examine the future of the Department of Energy’s loan-guarantee programs. In particular, they will be looking at the programs authorized under Title VXII (Section 1703’s and Section 1705’s loan-guarantee programs) and Advanced Technology Vehicle Manufacturing (ATVM) loans. You may know them as the programs that gave us epic failures such as Solyndra, Abound Solar, and Fisker Automotive — but also the loans that subsidized Tesla Motors and Nissan, as well as those of Goldman Sachs and energy giants NRG Energy and Prologis.

I am glad that someone is still paying attention to these loan programs considering that since 2009 over $30 billion were issued under the three programs and taxpayers are potentially on the hook for most of that amount. ($22 billion is for Section 1703 and 1705 alone). In addition, while the 1705 loan program expired in 2011, 1703 and ATVM still have billions in authorized funds remaining. In Fiscal Year 2017, DOE still has $24.7 billion in loan-guarantee authority under 1703 and $13.2 billion under ATMV. That’s a lot of potential damages.

As I and others have noted, the problems with loan guarantees such as Sections 1705 and 1703 are much more fundamental than the cost of one or more failed projects. In fact, the economic literature shows that every loan-guarantee program transfers risk from lenders to taxpayers, are likely to inhibit innovation, and they increase the overall cost of borrowing. At a 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, they 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.

Politicians, of course, love these loans because they are able to use them to reward interest groups while hiding the costs of this government-granted privilege. Congress can authorize billions of dollars in guaranteed or direct loans with minimal visible impact on the federal budget because of the way the government accounts for loan programs. Moreover, unlike the Solyndra case, most failures take years to play out, or never happen at all because the company wasn't an overly risky bet in the first place and had plenty of access to capital — such as in the case of 90 percent of the 1705 loan-program recipients. Loan programs allow politicians to collect the rewards of granting a loan to a special interest while skirting political blame years later when or if the project defaults. It's like buying a house on credit without having a trace of the transaction on your credit report.

It is also easy to understand why companies and company executives benefit from these loans and may seek them out. Even if they can access capital in the first place, it lowers their borrowing costs and it gives them an edge over their competitors independent of the merits. However, this shouldn't obscure the fact that this preferential treatment comes at the expense of the taxpayer, competitors, consumers, and ultimately at the expense of our markets and political system.

For all these reasons, the right thing to do is to permanently terminate these loan programs. This is, of course, true of all energy subsidies and not just green-energy ones. There is no reason to panic. As Chris Edwards explains:

> 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. . . .
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> 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, my advice to Congress is the following:

- Cancel all remaining loan authority under section 1703 and ATVM ($24.7 billion for 1703 and $13.2 billion)

- Abolish the program permanently

- Continue to appropriate funds to the DOE's Loan Programs Office, which would administer the winding down of the loan portfolios ($15.7 billion in 1705 guarantees, $6.2 billion in 1703 guarantees, and $8.4 billion in ATVM loans). Alternatively, transfer the loan obligations to the Department of Treasury to administer or auction off to the private sector.

That's great policy and great economics. And because it's a firm step toward putting an end to cronyist programs, it's also good politics.