September 12, 2011

TO: Members, Subcommittee on Oversight and Investigation

FROM: Subcommittee on Oversight and Investigations Staff

RE: Hearing on "Solyndra and The DOE Loan Guarantee Program"

On Wednesday, September 14, 2011, at 9:30 a.m. in room 2123 of the Rayburn House Office Building, the Subcommittee on Oversight and Investigations will hold a hearing entitled "Solyndra and The DOE Loan Guarantee Program." The hearing will provide an overview of the Department of Energy's (DOE) and Office of Management and Budget's (OMB) involvement in the review of a loan guarantee awarded to Solyndra, Inc., a California company, in September 2009, and the restructuring of that deal in February 2011. The hearing will also examine Solyndra's financial position, representations it made to the government about the financial condition of the company, and Solyndra's recent bankruptcy filing.

I. WITNESSES

The Committee has invited four witnesses to testify at the hearing:

Jonathan Silver Director, Loan Programs Office U.S. Department of Energy (DOE)	Jeffry Zients Deputy Director Office of Management and Budget (OMB)
Brian Harrison President and Chief Executive Officer Solyndra, Inc.	W.G. Stover, Jr. Sr. Vice President & Chief Financial Officer Solyndra, Inc.

II. DISCUSSION

A. The DOE Loan Guarantee Program and Review Process

The Energy Policy Act of 2005 authorized the Secretary of DOE to make loan guarantees to companies investing in either innovative clean technologies or commercial-scale renewable energy projects. Under the law, companies that receive loan guarantees under the DOE program must pay a credit subsidy cost. The credit subsidy cost represents the cost of the loan to the taxpayer if the recipient of the guarantee defaults on the loan and reflects several factors, including the cash flows of the loan recipient; the rate of recovery the government expects from the assets pledged as security for the loan; and the risk of default.

In 2009, the American Reinvestment and Recovery Act (ARRA or "stimulus") appropriated approximately $6 billion in funding to pay for the credit subsidy costs of the DOE loan guarantees for certain renewable energy, electric transmission, and leading edge biofuels systems. The DOE Loan Guarantees that are eligible for stimulus funding for their credit subsidy costs are commonly referred to as "Section 1705" loan guarantees.[1] The appropriation of this funding in the stimulus was critical to the ability of DOE to issue loan guarantees for clean energy projects because many loan guarantee applicants had been unable to come up with the funding themselves to pay the credit subsidy costs, which can be considerable.

Since the stimulus provided funding for the credit subsidy costs, DOE has closed 17 Section 1705 loan guarantees, totaling $7.84 billion. The department has also announced conditional commitments to an additional 16 Section 1705-eligible projects totaling $10.4 billion.[2] To be eligible for stimulus funding, the stimulus requires that Section 1705 loan guarantee projects begin construction no later than September 30, 2011. When he testified before the Subcommittee on Oversight and Investigations on March 17, 2011, DOE Chief Financial Officer Steve Isakowitz indicated that DOE intended to close all its conditional guarantees by the deadline.

Applications for DOE Loan Guarantees are received in response to specific solicitations issued by the Loan Guarantee Program. Once an application is filed, DOE reviews the initial application to determine whether the applicant meets the solicitation criteria. If so, those applicants submit a second, more comprehensive application. DOE then conducts due diligence — including legal, environmental, engineering, and market reviews — and sometimes engages outside consultants for these reviews.[3] Once these reviews are complete, the Loan Programs Office then negotiates a term sheet with the applicant company. A credit paper is then drafted and submitted to a DOE "Credit Committee," which is comprised of DOE officials. If the Credit Committee approves the credit paper and term sheet, a DOE "Credit Review Board" then reviews and votes on the matter. The Credit Review Board is comprised of senior DOE officials, including the Deputy Secretary, the General Counsel, the Chief Financial Officer, and other

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[1] Ultimately, Congress transferred $3.6 billion of this funding to other programs, leaving DOE with $2.4 billion for the credit subsidy costs.

[2] By fiscal year 2009, Congress had authorized $51 billion in funding for loan guarantees that meet the criteria set forth in Title 17 of the Energy Policy Act. With the additional funding provided in the stimulus for the credit subsidy costs of these guarantees, the total estimated loan guarantee authority is approximately $70 billion.

[3] In a July 2010 report, the Government Accountability Office found that "DOE's implementation of the program has favored some applicants and disadvantaged others in a number of ways." With regard to due diligence, GAO found that "in at least five of the ten cases in which DOE made conditional commitments, it did so before obtaining all of the final reports from external reviewers, allowing those applicants to receive conditional commitments before incurring expenses that other applicants were required to pay." GAO, *Department of Energy: Further Actions Are Needed to Improve DOE's Ability to Evaluate and Implement the Loan Guarantee Program*, GAO-10-627 (Washington, DC: July 2010).

senior advisors. If the Credit Review Board approves the term sheet, a conditional commitment is made to the company.

Following the conditional commitment, DOE and the loan guarantee applicant begin to negotiate the terms for the final loan guarantee agreement. DOE is also responsible for calculating the credit subsidy score of the guarantee. Under the Financial Credit Reform Act (FCRA) of 1990, the Office of Management and Budget (OMB) is responsible for determining and approving the subsidy estimates associated with loan guarantees awarded by federal agencies. DOE submits its credit subsidy estimate to OMB along with other information about the guarantee. OMB then reviews the underlying information, and asks questions or seeks additional information from DOE about the guarantee. OMB can either approve the credit subsidy calculated by DOE, or can recommend that the cost be increased or decreased based on the perceived risk of the guarantee. Once OMB approves, the loan guarantee is finalized and DOE begins making disbursements to the company. The tenor of the loan and the repayment schedule is set out in the final loan guarantee document.

Following the loan closing, the DOE Loan Programs Office tracks and monitors the loan guarantee project. The loan guarantee agreement spells out the type of information and data the company must provide about the status of the loan project (in some cases, construction updates), as well as engineering reports and other information. These kinds of reports and data must be submitted to the DOE before the Loan Programs Office will authorize the disbursement of funds to the company.

It is important to note that the Loan Programs Office has grown rapidly and its procedures have changed over the last three years. The office hired its first federal employee on August 1, 2007. At the time Solyndra's application went into due diligence in late 2008 and 2009, the Loan Programs Office had 16 federal employees. By late 2009, the office had 44 employees, and as of March 1, 2011, the Loan Programs Office told Committee staff it had 90 federal employees. In addition to federal employees, the Loan Programs Office contracts with private firms and consultants to conduct due diligence of the loan guarantee applications. The fees for this work are paid by the applicants.

B. *Review of Solyndra's Loan Guarantee Application and Conditional Commitment*

Solyndra first applied for a DOE loan application in December 2006, in response to an August 2006 solicitation. The company, located in Fremont, CA, proposed to manufacture thin firm solar modules for flat, commercial rooftops, or flat rooftops. Solyndra used a unique cylindrical design for the panels based on Copper Indium Gallium Selenide, or "CIGS," technology. Solyndra claimed that its product had an advantage over other solar panels because its panels were easier to install, lighter, had cheaper rooftop installation costs, and potentially higher efficiencies due to better wind performance and design. Solyndra planned to use a loan guarantee to build a full-scale production facility (referred to as "Fab 2") capable of building solar panels that would produce 210 megawatts of electricity a year.

In August 2007, a technical review of the application was complete; staff from the Loan Programs Office informed Committee staff that Solyndra's application scored 88 out of 100. Two months later, in October 2007, DOE invited 16 applicants from the 143 that responded to the August 2006 solicitation to submit a full application. Solyndra submitted that application in May 2008, and it was deemed complete in August 2008.

Once the application was deemed complete, formal due diligence of the Solyndra application began, beginning with the independent engineer's review. Emails exchanged between DOE staff in early December 2008 show that Solyndra was one of a handful of projects that was slated to be presented to a Credit Review Board by January 15, 2009. These emails also show that DOE staff did not believe that an independent market analysis would be complete by that time, but that the Loan Programs Office would use "off the shelf" analyses to inform its review of the market for Solyndra's panels. The final draft of the independent engineer's report was submitted on January 5, 2009.

In early January 2009, DOE made a presentation to OMB staff regarding the Solyndra deal and some of its credit concerns. During that time, staff for the Loan Programs Office had drafted a proposed term sheet and credit paper for the Credit Committee's review. The January 2009 credit paper stated that the total Solyndra project cost was $722,701,000: $534,214,000 through the DOE loan guarantee and $204,697,000 from equity. This money would finance Phase I of the Fab 2 manufacturing facility, or three production lines. Once the facility reached full capacity in Phase II, six manufacturing lines would be operational. The Credit Committee paper noted certain concerns with the CIGS technology, including that it was "immature" compared to other thin-firm technologies, and that the company had not yet demonstrated the efficiency and yield levels that would be reached at full-commercial production. In addition, the Credit Committee paper stated that, while Solyndra's prices on a per-watt basis were higher than the projected market prices, Solyndra's price included the cost of installation while its competitors' price did not. It also noted, though, that the company had raised $750 million in private capital, that the photovoltaic market was growing, and that the company was managed by a "highly-experienced team of technical and financial professionals."

The Solyndra application was presented to a DOE Credit Committee on January 9, 2009. While the Credit Committee stated "that the project appears to have merit, there are several areas where the information presented did not thoroughly support a finding that the project is ready to be approved at this time." Specifically, the Credit Committee noted that there was no independent market analysis "addressing the long term prospects for this company beyond the sales agreements already in place." The Credit Committee also stated that "[t]here are questions regarding the nature and strength of the parent guarantee for the completion of this project." The Credit Committee concluded that the "number of issues unresolved makes a recommendation for approval premature at this time," and remanded the project to the Loan Programs Office for "further development of information."

In late January 2009, DOE contracted with an outside consultant to provide a marketing analysis of the Solyndra application. Documents presented to the Committee show that the Loan Programs Office was continuing with its credit policy assessment of the Solyndra deal. On March 6, 2009, the first draft of the independent marketing analysis was submitted. Six days later, on March 12, 2009, a second Credit Committee meeting on the Solyndra application was held, and the Committee voted unanimously to approve the project provided that the Loan Programs Office answer 11 specific questions from the Committee, address certain risks discussed in the independent engineer's report, and provide additional analysis of the company's revenue information.

On March 17, 2009, the DOE Credit Review Board met to consider the proposed conditional commitment to Solyndra. The Credit Review Board members were the Chief of Staff to DOE Secretary Steven Chu; the Senior Advisor to Secretary Chu for ARRA Activities; the DOE Chief Financial Officer; and the DOE Acting General Counsel. After discussing the terms of the deal, the market for Solyndra's products, and DOE's proposed efforts to monitor the loan, the board voted to offer a conditional commitment to Solyndra. The conditional commitment was announced on March 20, 2009.

Following the conditional commitment, Loan Programs Office staff, with the assistance of outside counsel, negotiated the terms and conditions of the final loan guarantee agreement with Solyndra. In addition, Solyndra began working to raise the $198 million in equity that was required for the company to receive the DOE loan guarantee and to satisfy other conditions precedent to closing.

Once the terms and conditions were nearly complete, DOE generated the proposed credit subsidy cost for the Solyndra loan guarantee, and presented this information to OMB staff and officials on August 25, 2009.[4] This presentation included information about the financial status of the company, the structure of the deal, and the potential risks and mitigants of the guarantee. Following that presentation, OMB asked DOE a number of questions about the company in order to determine whether DOE had assigned the proper risk values to the Solyndra guarantee. In particular, OMB questioned whether the risk rating assigned to the Solyndra deal was too high, considering that the debt service for the deal comes from the project, and not the parent company, Solyndra, Inc., and how competitive pressures in the photovoltaic market might impact DOE's recovery analysis.

Ultimately, OMB recommended certain changes to the credit subsidy cost factors to reflect these concerns, which DOE accepted. The Solyndra loan guarantee closed on September 2, 2009. At the time, DOE's Loan Program Office estimated that the guarantee would create 3,000 construction jobs and 1,000 jobs once the facility opened.

C. Solyndra's Financial Problems

Following the closing, DOE continued to monitor Solyndra's financial status and construction progress at the new manufacturing facility. Pursuant to the loan guarantee

[4] OMB first became involved in reviewing the Solyndra guarantee in December 2008. At that time, DOE had begun its active due diligence of the Solyndra loan guarantee. In early January 2009, ahead of a DOE Credit Committee meeting to approve a conditional commitment to Solyndra,. The DOE Credit Committee did not approve the conditional commitment, and therefore DOE made another presentation to OMB ahead of a second Credit Committee meeting in March 2009.

agreement, Solyndra was required to provide monthly engineering reports about its technology and monthly constructions reports.

In 2010, Solyndra experienced a number of financial setbacks. In March 2010, Solyndra's auditor, PricewaterhouseCoopers stated in the company's S-1 amended filing to the Securities and Exchange Commission (SEC) that the "Company had suffered recurring losses from operations, negative cash flows since inception and has a net stockholder's deficit that, among other concerns, raise substantial doubt about its ability to continue as a going concern." Just three months later, in June 2010, the company cancelled a $300 million Initial Public Offering (IPO). Instead, to raise capital, the company issued $175 million of convertible promissory notes to various investors.

In the fall of 2010, DOE told Solyndra that, due to the company's financial problems, the department would refuse its request for a loan disbursement unless Solyndra obtained additional capital. Solyndra, DOE, and two of Solyndra's lead investors — Argonaut Venture Capital and Madrone Capitol Partners —began negotiations to restructure the Solyndra loan guarantee agreement. On November 3, 2010, Solyndra announced that it was closing its older manufacturing facility, resulting in the layoff of 135 temporary employees and approximately 40 full-time employees.

From December 2010 through February 2011, DOE, Solyndra, and two of its investors, Argonaut Venture Capital and Madrone Capitol Partners, negotiated the terms and conditions of an agreement to restructure the Solyndra loan guarantee. Throughout this process, DOE consulted with OMB about the proposed terms and conditions of this arrangement.

On February 23, 2011, the parties signed an agreement to restructure the Solyndra deal. Under that agreement, Solyndra's investors agreed to a $75 million credit facility, with the option of a second $75 million. DOE agreed to extend the term of Solyndra's loan guarantee from seven to 10 years, and to postpone the first repayment installment by one year, from 2012 to 2013. In addition, the agreement provided that, in the event of the company's liquidation before 2013, the investors have the senior secured position with respect to the first $75 million recovered. DOE has the second senior secured position with respect to the next $150 million recovered in liquidation. If Solyndra had not liquidated or declared bankruptcy by 2013, the investors would have lost their senior secured position to DOE.

The restructuring agreement also provides for enhanced monitoring of Solyndra's financial position by the DOE. Under the original agreement, the loan guarantee project was not required to provide financial information about the parent company, Solyndra, Inc. The restructuring agreement required Solyndra to provide weekly information about its cash flow to DOE, as well as monthly financial reports and statements. The DOE also took an "observer" seat on Solyndra's board.

This summer, representatives of Solyndra, including its Chief Executive Officer, Brian Harrison, came to Congress and met with several members of the Committee on Energy and Commerce. During those meetings the week of July 18, Mr. Harrison and other representatives of Solyndra claimed that Solyndra's financial condition was improving, and that Solyndra's revenues were growing. However, during a briefing with Committee staff the week of September 6, DOE Loan Programs Office staff stated that during that same period, the company was preparing to restate some of its projected financial statements to reflect increasing market and pricing pressures on its products, resulting in decreased revenues. When senior management of Solyndra informed the Solyndra board about this planned restatement, Solyndra's investors stated that they were not comfortable with providing the second $75 million credit facility to the company in August unless the terms of the restructuring agreement were changed.

Loan Programs Office staff informed Committee staff that it then began negotiating with Solyndra and its investors over the first few weeks of August about proposed terms for a second restructuring agreement. DOE also contracted with an outside investment banking firm to scope out potential terms and investors for this deal. The Loan Programs Office staff stated that it engaged in an "interagency process" regarding this development with Solyndra, and the possibility of a second restructuring agreement. Ultimately, DOE determined that a second restructuring was not feasible, and informed the company and its investors of this on August 30, 2011. The Solyndra board met shortly after, and voted to announce its bankruptcy. The announcement was made on August 31, 2011.

D. Solyndra Bankruptcy and FBI Raid

Solyndra filed for bankruptcy under title 11 of the United States Code on September 6, 2011, in United States Bankrupcty Court for the District of Delaware.

In its filings, Solyndra states that its significant investors include Argonaut Venture Capital (38.9%); Madrone Capitol Partners (13.00%), U.S. Venture Partners (9.20%) and Rockport Capital Partners (7.33%). The company attributed its decision to file for bankruptcy to the "dramatically reduced solar panel pricing world-wide" caused by an oversupply of solar panels, as well as certain subsidies that have been offered by foreign governments to their solar manufacturers and the reduction in subsidies and incentives for the purchase of solar energy.[5] In Solyndra Chief Financial Officer W.G. Stover's affidavit accompanying the bankruptcy filings, he states that Solyndra will engage in a "four-week exploratory period" during which it will search for a "turnkey buyer" and consider all restructuring options, including liquidation.

Two days after Solyndra filed for bankruptcy, Federal Bureau of Investigation (FBI) agents, acting together with agents from the DOE Office of Inspector General (OIG), executed search warrants on Solyndra's headquarters in Fremont, California, as well as at the home of certain Solyndra executives. Neither the FBI nor the DOE OIG have commented on the details of this criminal investigation, and the warrants remain under seal with the court.

E. White House Memorandum on the DOE Loan Guarantees

The DOE Loan Guarantee Program was the subject of an October 25, 2010, White House Memorandum addressed to the President from Carol Browner (then-Director of the White

[5] Declaration of W.G. Stover, Jr., Senior Vice President and Chief Financial Officer, In Support of First Day Motions, In re*:* Solyndra LLC, *et al*., Debtors, September 5, 2011.

House Office of Energy and Climate Change Policy); Ron Klain (then-Chief of Staff to Vice President Biden); and Larry Summers (then-Director of the National Economic Council). *See* Attachment A. The memorandum sought President Obama's "direction" regarding the implementation of the Loan Guarantee Program, and notes that the program had been subjected to criticism for its "slow implementation" and "making commitments to projects that would have happened anyway and thus fail to advance [the President's] clean energy agenda." In addition, the memorandum states that:

> OMB and Treasury . . . have raised implementation questions, including "double dipping" — the total government subsidy for loan guarantee recipients, which have exceeded 60%, "skin in the game" — the relatively small private equity (as low as 10%) developers put into projects; and non-incremental investment —some loan guarantee projects would appear likely to move forward without the credit support offered by [Section 1705 loan guarantees] including those projects that already exist and for which the loan guarantee simply provides a means for refinancing.

The memorandum also mentions a "policy review" conducted by the White House of the DOE loan guarantees, and explains that this review has sometimes resulted in extending the amount of time a guarantee is under review. It concludes by discussing a number of options to change the way the loan guarantee program is implemented, including limiting OMB's oversight role.

F. The Committee's Investigation

The Committee's investigation of the DOE Loan Guarantee Program began with a February 17, 2011, letter to DOE Secretary Chu requesting a briefing as well as documents and information relating to the Solyndra guarantee. That letter was followed by a March 14, 2011, letter to OMB Director Jacob Lew, also requesting documents and information relating to the Solyndra loan guarantee.

After significant delay in obtaining documents from the OMB responsive to the Committee's March 14 request, the Subcommittee on Oversight and Investigations held a business meeting on July 14, 2011, to authorize the issuance of a subpoena to OMB for documents relating to the Solyndra loan guarantee. The Subcommittee agreed to issue the subpoena by a vote of 14-8. That subpoena was issued on July 15, 2011.

Last week, Chairman Upton and Chairman Stearns sent a letter on September 1, 2011, to White House Counsel Kathryn Ruemmler, requesting communications between the White House and Solyndra and its investors relating to the loan guarantee.

III. ISSUES

The following issues will be examined at the hearing:

- Did the DOE and the OMB conduct a proper review of the Solyndra application?
- Should the DOE and the OMB have anticipated some of the financial problems that Solyndra experienced, which resulted in its bankruptcy?
- Did the DOE and the OMB take adequate steps to protect the taxpayer when it negotiated the terms and conditions of the Solyndra guarantee and its restructuring?

IV. CONTACTS

If you have any questions about this hearing, please contact Karen Christian or Todd Harrison at (202) 225-2927.