The Committee on Energy and Commerce

Internal Memorandum

October 12, 2011

TO: Members, Subcommittee on Oversight and Investigation

FROM: Subcommittee on Oversight and Investigations Staff

RE: Hearing on "Continuing Developments Regarding the Solyndra Loan Guarantee"

On Friday, October 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 "Continuing Developments Regarding the Solyndra Loan Guarantee." The hearing will provide an update on the Committee's investigation since the last hearing on September 22, 2011. The hearing will focus on the Department of the Treasury's role in reviewing the Solyndra loan guarantee, particularly with regard to the Department of Energy's (DOE) decision to restructure the Solyndra loan guarantee in February 2011 and subordinate the first $75 million recovered in the event of a liquidation to two Solyndra investors.

## I. WITNESSES

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

Gary Grippo
Deputy Assistant Secretary for Fiscal Operations and Policy
U.S. Department of the Treasury

Gary H. Burner
Chief Financial Officer
U.S. Department of the Treasury Federal Financing Bank

## II. DISCUSSION

### A. *The Department of Treasury Review of DOE Loan Guarantees*

The Department of the Treasury plays two roles with respect to loan guarantees issued by the Department of Energy, one ministerial and one consultative.

The Energy Policy Act of 2005 (Act) authorized the Secretary of DOE to make loan guarantees to companies investing in either innovative clean technologies or commercial-scale renewable energy. Section 1702(a) of that Act addresses the consultative role of the Treasury. Specifically, the Act provides that the DOE Secretary "shall make guarantees under this or any other Act for projects on such terms and conditions as the Secretary determines, after consultation with the Secretary of the Treasury, only in accordance with this section." Section 1702 then sets forth certain requirements for the terms and conditions of the loan guarantee, including provisions relating to the amount, repayment, the interest rate, the term, and default.

The final rule implementing Title XVII of the Energy Policy Act was issued by the DOE on December 4, 2009.[1] Three sections of the rule address Treasury's consultative role at different points in the loan guarantee review process: the evaluation of applications, the closing of the loan guarantee, and deviations from the loan guarantee agreement. Section 609.7 addresses the programmatic, technical, and financial evaluation of DOE loan guarantee applications. That part requires that "[c]oncurrent with its review process, DOE will consult with the Secretary of the Treasury regarding the terms and conditions of the potential loan guarantee." The rule also requires that the DOE consult with Treasury "[p]rior to, or on, the closing date" as to the "terms and conditions of the Loan Guarantee Agreement." 10 C.F.R. § 609.9(d)(4). Finally, in the event that DOE authorizes a deviation from the requirements of the rule, "DOE will consult with OMB and the Secretary of the Treasury before DOE grants a deviation that would constitute a substantial change in the financial terms of the Loan Guarantee Agreement and related documents."

At a briefing, Treasury staff informed Committee staff that Treasury typically reviews the term sheet for DOE loan guarantees prior to conditional commitment. Typically, DOE will provide Treasury with the term sheet, the financial model for the loan guarantee project, credit rating information, and cash flows as well as other financial information. Treasury staff explained that Treasury does not make decisions regarding the creditworthiness of the applicant or the eligibility of the technology for the program, but confines its review to the terms of the guarantee and the financial aspects of the model.

The final rule also addresses Treasury's ministerial roles, which are the payment of disbursements to loan guarantee recipients by the Federal Financing Bank (FFB) and the setting of interest rates for the guarantees. Section 609.10(d)(4)(i) provides that "[w]here DOE guarantees 100 percent of the Guaranteed Obligation, the loan shall be funded by the Federal Financing Bank. For those guarantees that are financed through the FFB, in order for disbursements to be made by FFB to the loan guarantee recipient, DOE or the loan servicer is responsible for ensuring that the conditions precedent to disbursing the loan guarantee are met. Those conditions precedent would include monitoring the construction of the project, ensuring that the collateral securing the deal is uncompromised, and reviewing financial and other reports regarding the project. *See* 10 C.F.R. §609.11(c). Once the DOE or the loan servicer determines that the conditions precedent to funding have been satisfied, DOE sends an Advance Request to the FFB with the amount of the disbursement, the date of the disbursement, and payment information, such as the bank and account routing numbers. The FFB then confirms the account

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[1] This rule amended the previous rule issued by the DOE on October 23, 2007.

and banking information and makes the disbursement; it does not play any role in reviewing the information provided by the loan guarantee applicant or approving the disbursement.

Section 609.10 also addresses the interest rate, stating that the "interest rate . . . is determined by DOE, after consultation with the Treasury Department, to be reasonable, taking into account the range of interest rates prevailing in the private sector for similar obligations of comparable risk guaranteed by the government. For all of its loans, FFB charges a "Lending Rate" which, according to 12 U.S.C. § 2285(b), may not be "less than a rate determined by the Secretary of the Treasury taking into consideration . . . the current average yield on outstanding marketable obligations of the United States of comparable maturity. . . ."

The Lending Rate is calculated by combining the Base Rate and a Spread. To determine the base rate, Treasury uses a formula which considers the terms of the loan guarantee, including the disbursement dates, the maturity date of the loan, and repayment frequency. Treasury then uses a yield curve, which is published on Treasury's website, to plot the base rate. Once the Base Rate is calculated, the FFB adds a spread, which is the difference in interest rates between Treasury securities and other securities in the market that have been issued or guaranteed by Federal agencies. It is a reflection of the amount above Treasury rates that a private-sector lender would charge for lending money that is guaranteed by the Federal government.

For loan guarantees, the interest rate is calculated at each date of disbursement. In a briefing with Committee staff, Treasury officials stated that rates charged by the FFB are not negotiable. They are a product of a formula, the yield curve, and the spread. For example, the amounts of two loan guarantees may be identical, but the interest rates charged on the disbursements of the loan guarantees may differ if the term, maturity, and repayment dates of the two guarantees are different.

B. *Treasury's Review of the Solyndra Loan Guarantee*

As set forth in the statute and the implementing regulations, Treasury played both a consultative and a ministerial role with respect to the Solyndra loan guarantee.

With respect to DOE's review of the Solyndra term sheet prior to conditional commitment, Treasury informed Committee staff that its review was similar to what was described above: it reviewed the term sheet and other financial information. With respect to the restructuring of Solyndra's loan guarantee this year, Treasury staff told Committee staff that Treasury was not directly involved.

Documents produced to the Committee by the DOE and OMB confirm that Treasury played a very limited role with respect to the Solyndra restructuring. On February 10, 2011, Gary Burner, Chief Financial Officer of the FFB, emailed Susan Richardson, General Counsel of the DOE Loan Programs Office, and Frances Nwachuku, Loan Programs Office Director of Portfolio Management, and informed them that OMB had informed Treasury of the restructuring of the Solyndra guarantee, and that "these adjustments may include subordination of Solyndra's $535 million reimbursement obligation to DOE and possibly the forgiveness of interest." Burner went on to state that DOE was apparently required to seek the approval of the Department of

Justice (DOJ) pursuant to 31 U.S.C. § 3711 and 31 C.F.R. Part 902, and asked if DOE planned to refer the matter to DOJ. Ms. Nwachuku responded, stating that she believed there was a "gross misunderstanding of the outcome of the negotiated restructuring of the Solyndra obligation to DOE." Ultimately, the DOE did not seek DOJ approval.

In August 2011, DOE again began discussions with Solyndra's investors to determine if a second restructuring was feasible after those investors declined to inject additional equity into the company under the current restructuring terms. On August 17, 2011, Mary J. Miller, Treasury Assistant Secretary for Financial Markets, emailed Jeffrey D. Zients, Deputy Director of OMB, regarding Treasury's role in reviewing the Solyndra guarantee. In that email, Miller stated: "…[s]ince July of 2010, Treasury has asked DOE for briefings on Solyndra's financial condition and any restructuring of terms. The only information we have received about this has been through OMB, as DOE has not responded to any requests for information about Solyndra." Further, Assistant Secretary Miller also questioned whether DOE's decision to subordinate its interest in Solyndra to Solyndra's investors was proper, stating "[o]ur legal counsel believes that the statute and the DOE regulations both require that the guaranteed loan should not be subordinate to any loan or other debt obligation. The DOE regulations also state that DOE shall consult with OMB and Treasury before any 'deviation' is granted from the financial terms of the Loan Guarantee Agreement. In February, we requested in writing that DOE seek the Department of Justice's approval of any proposed restructuring. To our knowledge, that has never happened." Miller went on to explain that while she "expect[s] that DOE has a view about why loan subordination can occur without DOJ approval or Treasury consultation, I wanted to correct any impression that we have acquiesced in the steps to date."

On September 14, 2011, the Treasury Office of Inspector General opened an inquiry into the role of the Federal Financing Bank in processing and funding the Solyndra loan guarantee.

## III. ISSUES

- What was the extent of the Department of the Treasury's involvement in the review of the Solyndra loan guarantee at the time of conditional commitment, at closing, and at restructuring?
- Did the Department of Energy satisfy the requirements of the Energy Policy Act of 2005 and its implementing regulations to consult with the Department of the Treasury with respect to the Solyndra loan guarantee?
- Does the Department of the Treasury believe that the restructuring of the Solyndra loan guarantee is a violation of the Energy Policy Act of 2005 and its regulations?
- Does the Department of the Treasury believe that DOE was required to seek the Department of Justice's approval of the Solyndra loan guarantee restructuring?

## IV. CONTACTS

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