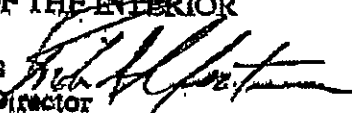




EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

April 3, 2008

MEMORANDUM FOR TIMOTHY R. PEITY
DEPUTY ASSISTANT SECRETARY, WATER
AND SCIENCE
DEPARTMENT OF THE INTERIOR

FROM: Richard A. Mertens 
Deputy Associate Director
Energy, Science and Water

SUBJECT: Loan guarantees to improve Federally owned assets

We appreciate the efforts of the Department of Interior and the Bureau of Reclamation to help water districts meet their responsibilities to operate and maintain water infrastructure. We look forward to continued work with the Department and the Bureau in these efforts.

PL 109-451 authorized the Bureau of Reclamation to provide loan guarantees to finance improvements and major rehabilitation of Reclamation projects. Some of these assets are owned by non-Federal entities, but most are owned by the Federal Government. This distinction has important consequences for the budgetary treatment of loan guarantees issued to finance improvements to these assets. Agencies are required to record obligations up front for the *subsidy cost* of loan guarantees issued to finance non-Federal assets, reflecting the private ownership and risk-sharing between the private sector and the Federal Government. Similarly, agencies are required to record obligations up front for the *full Government contingent liability* of loans that are guaranteed by the Government and used to finance improvements to Federally owned assets, reflecting the Government's ownership and its full risk for repayment of the loans. This treatment for loan guarantees used to improve Federally owned assets is consistent with the Congressional Budget Office's stated position on the budgetary treatment of similar financings of Federal assets through third-parties, outlined in the CBO issue brief *Third-Party Financing of Federal Projects* (2005).¹

The Government bears the full risk of a loan guarantee issued to finance a Federally owned asset because it owns the asset, and benefits from the improvements to the asset. The water district relies solely on receipts generated by that asset to repay the loan. The water district lacking any ownership interest does not have a comparable economic stake in the overall success of the project, as do water districts that own the assets.

¹ Posted at http://www.cbo.gov/ftpdocs/63xx/doc6399/06-01-thirdpartyfinancing_brief.pdf

Such financing arrangements are equivalent to direct Federal borrowing to finance the improvements and using receipts from water users to repay the Federal debt. The scoring reflects this equivalence. Direct Federal borrowing is generally less expensive for the taxpayer because the rates on Treasury bonds are lower than the rates on private-sector, third-party financing.

Given the above distinctions, the cost of a loan guarantee to finance improvements to Federally-owned assets would be 100 percent of the guaranteed amount. Thus, an 80 percent guarantee of a \$10 million loan would require an appropriation of \$8 million of budget authority, up front. If the terms and conditions of the loan guarantee agreement obligated the Federal government to greater liability, the up-front appropriation required would be greater.

This budgetary treatment does not prevent the Bureau of Reclamation from issuing loan guarantees for improvements to Federally owned assets. However, the agency should establish eligibility criteria to ensure that Bureau of Reclamation loan guarantees are utilized when credit is the most effective means of assistance, in accordance with Federal credit policies under OMB Circular A-129.