July 15, 2009

The Honorable Steven Chu
Secretary of Energy
United States Department of Energy

Dear Secretary Chu:

The National Commission on Energy Policy (NCEP) has actively been exploring new clean energy financing mechanisms that could help to quickly and efficiently channel financial capital to low-carbon energy technologies and projects. One public financing program of priority interest is the Section 1705 Loan Guarantee Program, which will be implemented shortly under your authority at the Department of Energy (DOE). This new program, enabled by the American Recovery and Reinvestment Act of 2009 (Recovery Act), aims to provide a significant injection of capital into the clean energy industry, which is critical given the ongoing difficulties in the financial markets. Recognizing the important role that the Section 1705 Program will have in shaping both the Administration's energy goals and the clean energy community's continued progress, NCEP recently convened a set of prominent energy finance experts and project developers with an interest in the details of the Program's structure to consider enhancing the particulars of its design. This letter lays out the basic insights of our Section 1705 Working Group discussions.

Early indications on the direction of the 1705 Program by DOE officials have generated concern by participants in the marketplace that the program may contain several well-intentioned elements that could prove unworkable in the current capital markets. In an effort to generate helpful suggestions for how the 1705 loan guarantee program could be designed to ensure that the program maintains its design objectives in a manner best suited for the current economic conditions, the NCEP convened group gathered in New York on June 23-24 to discuss these issues and has since been working collectively on the attached background memorandum. The following organizations participated in the NCEP 1705 Working Group and are eager to provide ongoing advice on the program design.

Participants:
BrightSource
Credit Suisse
Deepwater Wind
Deutsche Bank Securities, Inc.
Energy Capital Partners
First Wind
Goldman, Sachs & Co.
Madison Dearborn Partners
Nextlight Renewable Power
Sunpower
TPG Capital, L.P.

Key Information and Insights from the NCEP-Convened Section 1705 Loan Guarantee Working Group:

Credit markets remain tight, making it difficult to execute renewable energy deals. The past year has demonstrated that finding and securing debt for renewable energy project finance projects remains challenging at best. Long-term investment credit is scarce. Because renewable energy projects rely heavily on debt financing from capital markets, the current credit shortfall presents a serious roadblock to completing clean energy projects in the near term.

Flexibility in the financing structure of the loan guarantee program is needed: One of the objectives of the 1705 loan guarantee program is to bridge the credit and financing shortfalls currently facing the market. The 1705 program presumably will attempt to address these challenges by guaranteeing qualifying energy project debt. Ensuring that appropriate incentives are in place to maintain a rigorous selection and investment process should correctly be a priority for the DOE program designers. However, our group is especially concerned that the forthcoming guidelines will require deal structures that have large guaranteed debt components complemented by smaller tranches of unguaranteed debt in an attempt to ensure the credit component can withstand a market test. It is the strong view of our group that reliance on the frozen credit markets will undermine the intent and effectiveness of the 1705 loan guarantee program. Because DOE will likely (and rightly) require reassurance that each project is subject to market scrutiny, the group suggests several alternative approaches to ensure that the project investors have appropriate "skin in the game" without relying on the credit markets. By historical standards, deep credit markets could likely have accommodated these provisions. However, given the current credit environment and the framework under which banks hold or syndicate debt, requiring an unguaranteed portion of debt will shrink the market available for renewable projects dramatically—likely on the order of tens of billions of dollars—and raise the cost of borrowing considerably. Flexibility in the financing requirements is needed until credit markets improve. Therefore, our group suggests that DOE consider providing additional options to 1705 applicants that could free up much needed credit while maintaining an alignment of public and private interests. For example, at-risk banking fees or higher equity to debt ratios could both be used to provide public safeguards and ensure that the appetite to finance renewable projects is robust and not dependent on the capital markets in the near term.

Redundant NEPA requirements risk delaying clean energy projects: By law, recipients of loan guarantees under Section 1705 must comply with NEPA. Depending on the requirements, NEPA regulations hold the potential to significantly delay "shovel-ready" projects, possibly beyond the two year window of the 1705 program. The group we convened wholeheartedly agrees that the safeguards provided by NEPA are necessary conditions for any project. However, many NEPA requirements are duplicative to the environmental assessments required by state and other Federal agencies. In cases where such requirements are overlapping, our group suggests that the NEPA process should be streamlined and redundancies minimized in order to speedily move clean energy projects.

Attributes of a successful 1705 loan guarantee program: A robust loan guarantee program holds the potential to motivate widespread clean energy development, even in tight credit markets. However, given the current market conditions, our group agreed that the 1705 program should contain the following attributes:

- *Flexibility:* Offer an additional lending option that does not require an "unguaranteed option" on the debt component should credit markets remain tight. The program could consider other requirements— such as at risk banking fees and higher equity to debt ratios—that provide additional "skin in the game" and the align interest with the private sector capital. Such options could be developed in a manner that would incent the

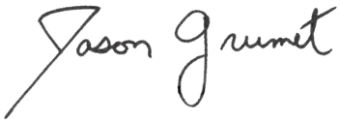
private sector to seek debt from private capital markets first but would provide a guaranteed debt option if credit is scarce.

- *Bank Participation:* Using banks to administer credit applications will utilize the processing capabilities and expertise of financial institutions. Such a delegated lending structure will allow DOE to process more loans in a shorter timeframe. Our group is concerned that the 1705 program may attempt to impose non-market liability standards on lead banks. If liability standards are outside normal commercial practices, the program runs the risk of limiting—and possibly precluding—much needed bank participation.
- *NEPA Streamlining:* Streamline the NEPA process to eliminate unnecessary redundancies where adequate work has already been completed by states or other federal agencies.

In summary, it is clear that the Section 1705 program is enormously important. It will undoubtedly play a critical role in the Recovery Act and help drive the Administration's efforts to address climate change, energy security, and job creation. However, there are serious concerns in the financial and project development community that if the efforts to align the public and private interests in the program require significant dependence on the credit markets (via an unguaranteed segment of the loan) the program will not optimize its potential. The attributes outlined by the NCEP 1705 working group attempt to maintain an equivalent alignment of public and private interest while mobilizing financial capital by relying more on the equity markets and by exposing the bank processing fees to some market risk. The group listed above is eager to help ensure that the full potential of the Section 1705 loan guarantee program can soon be realized and is readily available to work with the DOE to develop a successful 1705 program. We would be pleased to schedule a briefing with your office on the technical details and key insights of our work.

I hope you find this information useful and thank you for considering these suggestions.

Sincerely,



Jason Grumet
Executive Director, National Commission on Energy Policy
President, Bipartisan Policy Center

cc: Matt Rogers, Special Advisor to the Secretary