United States Government Accountability Office

Report to the Chairman, Committee on the Budget, House of Representatives

July 2022

CREDIT REFORM

Transparency Needed for Evaluation of Potential Federal Involvement in Projects Seeking Loans

Accessible Version

GAO-22-105280

GAO Highlights

Highlights of GAO-22-105280, a report to the Chairman, Committee on the Budget, House of Representatives

July 2022

CREDIT REFORM

Transparency Needed for Evaluation of Potential Federal Involvement in Projects Seeking Loans

Why GAO Did This Study

FCRA was enacted to improve the accuracy of the cost of federal credit programs reported in the federal budget, among other things. It requires agencies to measure the government's cost of federal credit programs over the length of a loan. This facilitates better cost comparisons between credit and noncredit programs. FCRA applies only to loans and loan guarantees made to non-federal borrowers.

GAO was asked to review how the non-federal borrower concept is applied in practice. This report examines (1) OMB's policies for evaluating whether federal loan programs would potentially fund a federal borrower or federal activities; and (2) processes that selected agencies—EPA and the U.S. Departments of Agriculture and Transportation—use to screen loan applications for potential federal activities.

GAO analyzed policy and program documents and interviewed officials from six direct loan programs for infrastructure projects with the most obligations in fiscal year 2020. GAO also reviewed OMB policies and processes and interviewed OMB staff.

What GAO Recommends

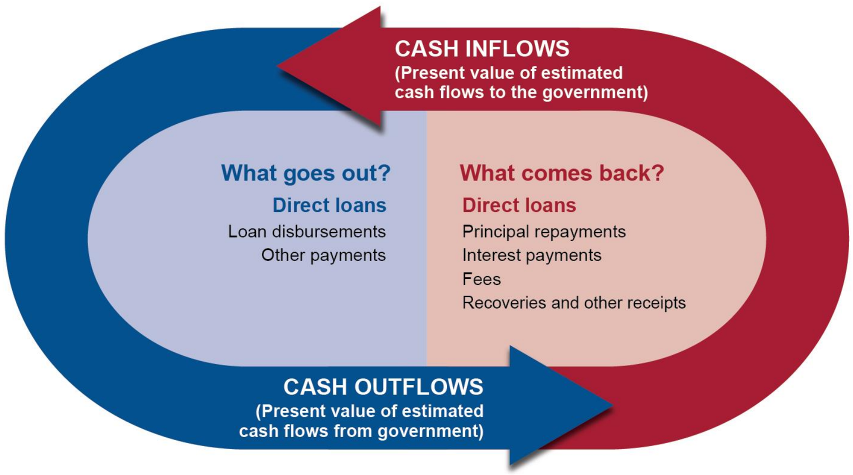
GAO recommends that OMB publish government-wide criteria agencies should consider when evaluating federal involvement in a potential project to help determine whether it is eligible for the special budgetary treatment under FCRA. OMB neither agreed nor disagreed with GAO's recommendation. OMB provided technical comments, which GAO incorporated as appropriate.

View GAO-22-105280. For more information, contact Jeff Arkin at (202) 512-6806 or arkinj@gao.gov.

What GAO Found

The Federal Credit Reform Act of 1990 (FCRA) allows special budgetary treatment for federal loans made to non-federal borrowers. Specifically, the subsidy cost of the loan (cash outflows minus inflows) is reflected in the budget in the year the loan is made. Prior to FCRA, the total amount of a direct loan was recorded as a cost in the year it was made. Repayments were not recorded until the years they were received. Under the special budgetary treatment FCRA affords, federal agencies can issue an amount of loans that is larger than the related appropriations they receive. For example, in fiscal year 2021, $7 billion in appropriations supported roughly $236 billion in direct loans.

Figure: Loan Subsidy Cost Components



Source: GAO. | GAO-22-105280

The concept of non-federal borrower is not defined in FCRA. According to Office of Management and Budget (OMB) staff, classification of a borrower as non-federal depends on not only if the recipient is a non-federal entity but also if a loan is sought for a non-federal activity. If a proposed project is a federal activity, it is ineligible for special budgetary treatment under FCRA.

Of the six direct loan programs in GAO's review, one had published criteria for evaluating whether proposed financing applications would fund federal activities. Specifically, the Environmental Protection Agency (EPA), OMB, and the Department of the Treasury jointly published such criteria for EPA's Water Infrastructure Finance and Innovation Act (WIFIA) program. OMB staff said the concepts applied in the WIFIA criteria are generally applicable for all federal lending programs. However, OMB has not published government-wide criteria for evaluating potential federal involvement in projects seeking a federal loan.

Agency officials managing the other five programs in GAO's review were unaware that OMB considers the WIFIA criteria to be applicable to all federal loan programs. Without government-wide criteria, there could be inconsistent treatment of loans across the federal government. This, in turn, could make it harder for policymakers to assess and compare the cost of federal programs.

Contents

Abbreviations

CBO	Congressional Budget Office
Corps	U.S. Army Corps of Engineers
DOD	Department of Defense
DOT	Department of Transportation
EPA	Environmental Protection Agency
FCRA	Federal Credit Reform Act of 1990
OMB	Office of Management and Budget
Treasury	Department of the Treasury
USDA	U.S. Department of Agriculture
WIFIA	Water Infrastructure Finance and Innovation Act

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

July 28, 2022

The Honorable John A. Yarmuth
Chairman
Committee on the Budget
House of Representatives

Dear Mr. Chairman:

The federal government uses credit programs—direct loans and loan guarantees—to support specific social and public policy objectives.[1] For example, the federal government provides loans to students and their families to help meet postsecondary education costs and guarantees certain home mortgages to promote homeownership. The Federal Credit Reform Act of 1990 (FCRA) was enacted to improve the accuracy of the cost of federal credit programs reflected in the federal budget, among other things.[2] By requiring agencies to measure the government's cost of federal credit programs over the length of a loan, FCRA facilitates better cost comparisons both among credit programs and between credit and noncredit programs, such as federal grants.

Before fiscal year 1992, when FCRA took effect, liabilities for credit programs were reflected in the budget on a cash-flow basis (i.e., the expected amount of cash paid out minus the cash received in a given year). As a result, direct loans initially appeared to cost the same as grants because agencies were required to obligate the total amount of a loan when it was made. The direct loan repayments were recorded in later years when they were received. In contrast, a loan guarantee would appear free at the time it was made. An obligation was only recorded if a default had occurred, which may have been many years after the guarantee was made.

[1]A direct loan is defined as a disbursement of funds by the government to a non-federal borrower under a contract that requires the repayment of such funds either with or without interest. A loan guarantee is defined as any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-federal borrower to a non-federal lender. This does not include the insurance of deposits, shares, or other withdrawable accounts in financial institutions.

[2]Pub. L. No. 101-508, tit. XIII, § 13201(a), 104 Stat. 1388, 1388-609 (1990) (*codified as amended*, 2 U.S.C. §§ 661-661f).

Under FCRA, the estimated cost to the government over the life of the loan is obligated in the year that the direct loan or loan guarantee is made. For direct loans, this cost—referred to as the subsidy cost— is calculated as the net present value of estimated cash flows from the government (e.g., loan disbursements and claim payments to lenders) minus estimated cash flows to the government (e.g., principal repayments, interest payments, fees, and recoveries on defaulted loans) over the life of the loan. Since the subsidy cost of a direct loan is the amount of the loan less estimated repayments or fees, it will generally be less than the full amount of the loan. In fiscal year 2021, $7 billion in appropriations supported roughly $236 billion in direct loans.

The application of FCRA helps ensure all federal obligations are recorded in full at the time the obligations are incurred and helps maintain a clear and transparent picture of all obligations of the federal government. It also provides policymakers with the best possible information about trade-offs made when making budgetary decisions. In other words, allowing a federal borrower to receive the special budgetary treatment afforded by FCRA could understate the cost to the government and therefore make it more difficult for policymakers to compare federal spending across programs.

A core concept of FCRA is that the special budgetary treatment it affords only applies to loans and loan guarantees made to non-federal borrowers. However, the definition of a non-federal borrower is not specified in FCRA.

Given the lack of a definition of a non-federal borrower, you asked us to study how the concept is applied in federal lending programs. This report examines (1) the Office of Management and Budget's (OMB) policies for evaluating whether federal loan programs would potentially fund a federal borrower or federal activities, and (2) processes that selected federal agencies use to screen applications for their loan programs for potential federal activities.

To examine OMB policies for evaluating whether federal loan programs would potentially fund a federal borrower or federal activities, we reviewed relevant legislation, guidance, and program documents and interviewed staff from OMB. We also selected six direct federal loan programs across three agencies and asked the agency officials about their awareness and application of OMB's policies and criteria.

To select these six loan programs, we focused on loan programs that support infrastructure projects because individual loans from these programs tend be larger, in dollar terms, than those for other loan programs, such as student loans and small business loans, which tend to loan smaller amounts of money to thousands of borrowers. Also, the potential for federal participation is likely more relevant for infrastructure projects. For example, federal agencies, such as the U.S. Army Corps of Engineers (Corps), may be directly involved in the construction or management of certain infrastructure projects. We also focused on direct loans—and not loan guarantees—to allow for comparisons across similar types of infrastructure loan programs.

We narrowed our selection to direct loan programs supporting infrastructure projects with the largest actual obligations in fiscal year 2020—the most recent available data on actual obligations at the time of our selection—from the Analytical Perspectives volume of the President's Budget for fiscal year 2022.[3]

The six direct loan programs we selected based on these criteria are shown in table 1.[4]

[3]These programs obligated more than $16 billion combined in fiscal year 2020. This amount represents about 3 percent of the fiscal year 2020 total obligations for direct loans. However, this amount accounts for 3.8 percent of obligations for direct loans in fiscal year 2020, excluding the student loan program – the largest loan program – which awards direct loans to individuals.

[4]To select case study programs, we first selected direct loan accounts that support infrastructure programs. Specifically, we selected five accounts with the largest actual fiscal year 2020 obligations based on the Fiscal Year 2022 President's Budget Federal Credit Supplement. We then focused on the loan programs that each account supports. One of the accounts we selected within USDA supports two distinct program areas, resulting in six case study programs. In developing our selection criteria, we consulted staff from the Congressional Research Service, the Congressional Budget Office, and OMB.

Table 1: Overview of Direct Loan Programs Selected for Case Study Review

Department	Bureau	Program	Purpose and Activities
Environmental Protection Agency (EPA)	Office of Water	Water Infrastructure Finance and Innovation Act Program	Provides capital for eligible water and wastewater infrastructure projects.
U.S. Department of Agriculture (USDA)	Rural Utilities Service	Rural Electric Program	Provides capital to maintain, expand, upgrade, and modernize America's vast rural electric infrastructure.
		Rural Telecommunications Program	Provides capital to rural telecommunications and broadband providers to build broadband networks and deliver service to rural areas.[a]
		Rural Water and Waste Disposal Program	Provides capital to support clean and reliable drinking water systems, sanitary sewage disposal, sanitary solid waste disposal, and storm water drainage to households and businesses in eligible rural areas.
U.S. Department of Transportation (DOT)	Build America Bureau	Transportation Infrastructure Finance and Innovation Act Program	Provides capital to finance critical improvements in the nation's transportation system including highways, port access, and other infrastructure.
		Railroad Rehabilitation and Improvement Financing Program	Provides capital to finance (1) development of railroad infrastructure, including acquiring, improving, or rehabilitating intermodal or rail equipment or facilities; (2) development or establishment of new intermodal or railroad facilities; and (3) transit-oriented development, among other activities.

Source: GAO analysis of EPA, USDA, and DOT data. | GAO-22-105280

[a]According to USDA, this program area includes multiple underlying programs, including the Telecommunications Infrastructure Loan Program. Consistent with USDA's practice, for purposes of our report, we refer to the overarching program as the Rural Telecommunications Direct Loan Program, or Rural Telecommunications Program.

To describe selected agencies' processes for screening federal loan applications for potential federal activities, we asked the officials about their policies and procedures for evaluating the eligibility of loan applicants. We also interviewed officials from the Corps, since it is also authorized to provide loans and loan guarantees under the Water Infrastructure Finance and Innovation Act for its own infrastructure program. While the agencies that administer the loan programs we selected may also manage other federal credit programs, we limited our review to policies and processes in place related to our case study programs. Our selected case studies are a non-generalizable sample. The findings related to our case studies are intended to serve as illustrative examples and are not generalizable to all federal credit programs.

We conducted this performance audit from June 2021 to July 2022 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Agencies use federal credit programs to provide assistance to non-federal borrowers through direct loans and loan guarantees (see figure 1).

Figure 1: Types of Federal Credit Programs

Source: GAO. | GAO-22-105280

Text of Figure 1: Types of Federal Credit Programs

Direct Loan	Example
A disbursement of funds by the federal government to a non-federal borrower under a contract that requires the repayment of such funds with or without interest.	Students may receive direct loans from the Department of Education Direct Student Loan Program to assist them in obtaining postsecondary education.

Loan Guarantee	Example
Any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-federal borrower to a non-federal lender. Does not include the insurance of deposits, shares, or other withdrawable accounts in financial institutions.	A home buyer may receive a mortgage loan from a private bank that has insured the mortgage loan with a loan guarantee from the Department of Housing and Urban Development's Federal Housing Administration.

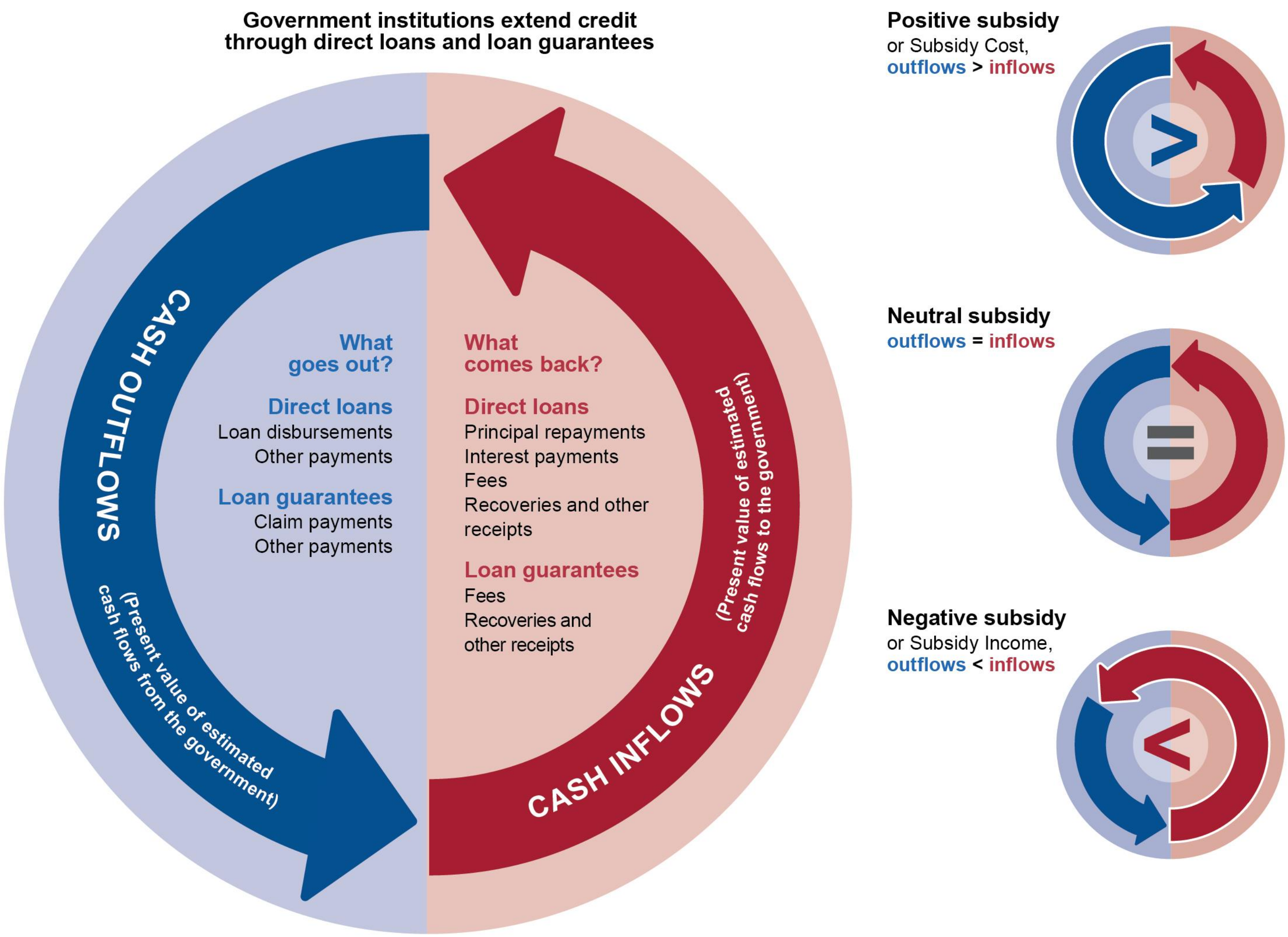
Source: GAO. | GAO-22-105280

Federal credit programs are reflected in the federal budget using special budgetary treatment that FCRA affords. This treatment results in a more accurate record of the cost of loan programs to the federal government than the approach used prior to the implementation of FCRA. In calculating the subsidy cost that will be reflected in the budget, discount rates that reflect the federal government's cost of financing are used to determine the net present value of estimated cash flows.[5]

As shown in figure 2, if the present value of estimated cash outflows exceeds cash inflows, there is a subsidy cost. If the present value of estimated cash inflows exceeds cash outflows, there is a negative subsidy cost, referred to as subsidy income.

[5]FCRA states that in estimating net present values under credit reform, the discount rate represents the average interest rate on marketable Treasury securities of similar maturity to the cash flows of the direct loan or loan guarantee for which the estimate is being made.

Figure 2: Calculation of Subsidy Cost for Direct Loans and Loan Guarantees



Source: GAO. | GAO-22-105280

Data for Figure 2: Calculation of Subsidy Cost for Direct Loans and Loan Guarantees

1) Government institutions extend credit through direct loans and loan guarantees

    a) CASH OUTFLOWS

        i) (Present value of estimated cash flows from the government)

ii) What goes out?

(1) Direct loans

(2) Loan disbursements

(3) Other payments

(4) Loan guarantees

(5) Claim payments

(6) Other payments

b) CASH INFLOWS

i) (Present value of estimated cash flows to the government

ii) What comes back?

(1) Direct loans

(2) Principal repayments

(3) Interest payments

(4) Fees

(5) Recoveries and other receipts

(6) Loan guarantees

(7) Fees

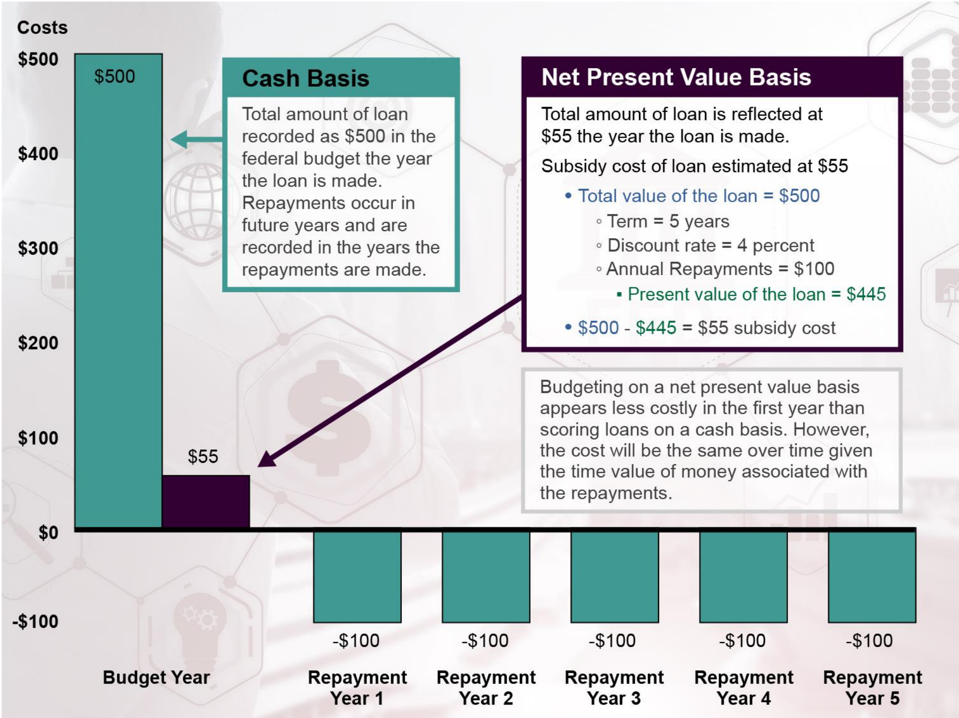
(8) Recoveries and other receipts

- Positive subsidy or Subsidy Cost, outflows > inflows
- Neutral subsidy outflows = inflows
- Negative subsidy or Subsidy Income, outflows < inflows

Source: GAO. | GAO-22-105280

Before a federal agency enters into a direct loan or loan guarantee that would be afforded special budgetary treatment under FCRA, Congress must appropriate the subsidy cost or provide other authority.[6] Since the subsidy cost of a direct loan is the amount of the loan less estimated repayments or fees, it will generally be less than the full amount of the loan. As a result, an agency can issue a larger amount of loans with any given appropriation than it could if the loans were recorded on a cash basis. Figure 3 below shows a simplified example of how an interest-free loan would be recorded on a net present value basis compared to a cash basis in the federal budget.

Figure 3: Comparison of the Cost of a Hypothetical Loan under a Cash and Net Present Value Basis



Source: GAO and Funtap/stock.adobe.com. | GAO-22-105280

[6]2 U.S.C. § 661c(b).

Data for Figure 3: Comparison of the Cost of a Hypothetical Loan under a Cash and Net Present Value Basis

Cash Basis (Teal):

Total amount of loan recorded as $500 in the federal budget the year the loan is made. Repayments occur in future years and are recorded in the years the repayments are made.

Net Present Value Basis (Purple):

Total amount of loan is reflected at $55 the year the loan is made.

Subsidy cost of loan estimated at $55

- Total value of the loan = $500 (in blue)
  - Term = 5 years
    - Discount rate = 4 percent
    - Annual Repayments = $100
      - **Present value of the loan = $445** (in green)
- **$500** (in blue) **-** **$445** (in green) = $55 subsidy cost

Budgeting on a net present value basis appears less costly in the first year than scoring loans on a cash basis. However, the cost will be the same over time given the time value of money associated with the repayments.

	Cash Basis	Net present value basis
Budget Year	$500	$55
Repayment Year 1	-$100	NA
Repayment Year 2	-$100	NA
Repayment Year 3	-$100	NA
Repayment Year 4	-$100	NA
Repayment Year 5	-$100	NA

Source: GAO and Funtap/stock.adobe.com. | GAO-22-105280

Note: This figure is an estimate calculated based on a scenario where the government gives an interest-free $500 loan that is repaid $100 per year over 5 years. The scenario assumes that the loan recipient repays the loan as required with no default and the discount rate is 4 percent. The subsidy cost, rather than the cash basis, is reflected in the budget for loans eligible for special budgetary treatment under FCRA. The subsidy cost is generally what the agency estimates will not be repaid by borrowers. The portion of the loan that the agency predicts will be repaid by borrowers is financed by borrowing from the Department of the Treasury (Treasury) and is not considered a cost to the government as it will be returned in future years. Therefore, it is not recorded in the budget the year the loan is made. The various credit programs across the federal government can have different assumptions than this example, resulting in higher or lower subsidy cost, neutral subsidy, or negative subsidy. The discount rate reflects the concept that $1 received in the future is less than $1 received today because the dollar received today can be invested and grow with interest over that year. In other words, there are interest costs associated with borrowing money to finance direct loans that will be repaid in the future. In calculating present value under FCRA, prevailing interest rates on Treasury securities of similar maturity provide the basis for converting future amounts into their “money now” equivalents.

OMB’s Policies for Determining Whether Federal Loan Program Applications Would Potentially Fund Federal Activities Are Not Transparent

OMB Staff Reported Considering Several Factors to Determine Whether a Loan Would Fund Federal Activities

According to OMB staff, their classification of a borrower as federal or non-federal depends on whether a loan is sought for a federal or non-federal activity, rather than solely on whether the direct recipient of the loan is a federal or non-federal entity. In other words, the fact that a loan applicant is not a federal entity does not automatically mean that the proposed project will be considered non-federal for the purposes of FCRA.

OMB staff consider multiple factors to determine the extent to which a project may be considered federal in nature. These factors include: the structure of the project, the financing of the project, and the project liabilities.

- **Structure of the Project.** OMB staff stated that if the federal government is the primary recipient of a completed project or if it receives the majority of a benefit from a project completed by a non-federal borrower, OMB may determine the loan would not qualify for FCRA’s special budgetary treatment. For example, according to OMB staff, if a loan to a non-federal entity resulted in a structure that predominantly benefited a federal agency, OMB may determine the project to be federal. Likewise, OMB staff stated that if a loan applicant was seeking financing for capital improvements to a federal asset, OMB may conclude that this project should be considered federal, even if the loan applicant is not a federal entity. This is because the loan would be akin to financing a federal activity that would be recorded on a cash basis.

- **Financing of the Project.** OMB also assesses the resources available to a borrower for repayment and how dependent a project may be on federal support. OMB staff stated that as part of credit program implementation, agencies are asked why a given objective cannot be achieved without federal support, what existing private sources of credit are available to support the project's objective, and what other federal credit or noncredit programs exist to support the objective.
- **Project Liabilities.** OMB staff stated that, in some cases, former or current federal involvement in projects may confer a significant level of control and future responsibility, or liability, to the federal government. OMB staff stated that in these cases, future activity completed by a non-federal borrower on an asset would still be considered a federal project.

OMB staff reported that they developed these criteria based on the principles outlined in the 1967 *Report of the President's Commission on Budget Concepts*.[7] OMB staff stated that OMB applies concepts from the report to determine if an activity is federal in nature, and thereby ineligible for special budgetary treatment under FCRA. If an activity is determined to be federal in nature then an agency must seek appropriations to pay for the full value of the activity and record its full liability for the activity consistent with the recording statute.[8]

[7]President's Commission on Budget Concepts, *Report of the President's Commission on Budget Concepts* (Washington, D.C. Oct. 10, 1967).

[8]31 U.S.C. § 1501.

Report of the President's Commission on Budget Concepts

The 1967 Report presented recommendations to make the federal budget a more understandable and useful public policy and financial planning instrument. It set forth the basic accounting rules generally followed in the modern budget process and remains an authoritative statement on federal budgetary accounting concepts and principles. The Report acknowledged and provided examples of why it is difficult to draw a boundary line between what entities may be considered federal and non-federal. When faced with a project or asset where this federal designation is unclear, the 1967 Report recommended ''a comprehensive budget, with very few exclusions'' and stated that ''borderline agencies and transactions should be included in the budget unless there are exceptionally persuasive reasons for exclusion.'' For example, based on the Report's recommendation to the President, transactions of federal trust funds should be included in the budget, but privately owned government-sponsored activities should not be included, although case-by-case situations can be taken into consideration.

Source: GAO analysis of President's Commission on Budget Concepts Report. | GAO-22-10528

OMB staff also told us the criteria are consistent with the views as expressed in the Congressional Budget Office's (CBO) *How CBO Determines Whether to Classify an Activity as Governmental When Estimating Its Budgetary Effects*.[9]

How CBO Determines Whether to Classify an Activity as Governmental When Estimating Its Budgetary Effects

CBO's 2017 report on how it estimates budgetary effects of legislation provides criteria for identifying cash flows of governmental activities. According to the report, if a non-federal entity (1) carries out activities that require it to exercise the sovereign power of the federal government; (2) is performing an activity that will serve a specific governmental purpose; or (3) is directed, controlled, or owned by the government, the non-federal entity may be performing a governmental activity. The CBO report explains that the extent to which an activity would meet these criteria will affect the decision about whether its cash flows should be considered federal and included in its budget estimates. Analyzing and applying these criteria involve some judgment on a case-by-case basis to determine if the cash flows of a non-federal entity should be deemed federal in nature.

Source: GAO analysis of CBO report. | GAO-22-105280

OMB Has Not Issued Government-Wide Criteria for Determining Federal Participation in Applicant Activities

According to OMB staff, OMB has not published government-wide criteria for evaluating potential federal involvement in a project seeking a federal

[9]CBO, *How CBO Determines Whether to Classify an Activity as Governmental When Estimating Its Budgetary Effects* (Washington, D.C.: June 20, 2017).

loan to determine if it is eligible for the special budgetary treatment under FCRA. However, the Environmental Protection Agency's (EPA) fiscal year 2020 appropriation for the Water Infrastructure Finance and Innovation Act (WIFIA) program required EPA, OMB, and the Department of the Treasury (Treasury) to jointly develop and publish criteria in the *Federal Register* for limiting federal participation in projects receiving WIFIA loans and loan guarantees.[10] Furthermore, the appropriation specified the criteria must be consistent with the requirements for the budgetary treatment provided for in section 504 of FCRA.[11] EPA, OMB, and Treasury published these criteria on June 30, 2020.[12] While the criteria were developed specifically for the WIFIA program, OMB staff told us the concepts in the criteria are a distillation of the long-held practices and considerations used by OMB. These concepts are generally applicable to all federal lending programs.

The WIFIA notice in the *Federal Register* also outlines two initial federal asset screening questions specifically tailored to the program (see figure 4). The screening questions and criteria help EPA and OMB identify whether there is any potential federal participation in a proposed WIFIA project, evaluate the extent of this participation, and determine whether the level of participation makes the project federal in nature. For example, one question asks if the project is in whole or in part currently authorized by Congress for the U.S. Army Corps of Engineers (Corps) or the Department of the Interior's Bureau of Reclamation to construct. If so, OMB staff stated that many factors must be considered by staff evaluating the proposed projects. These factors include the extent to which the Corps may dictate parameters of the project and the potential

[10]Further Consolidated Appropriations Act, 2020, Pub. L. No. 116-94, div. D, tit. II, 133 Stat. 2534, 2721-22 (2019); see also Water Infrastructure Finance and Innovation Act of 2014, Pub. L. No. 113-121, tit. V, subtit. C, 128 Stat. 1193, 1332-1345 (2014) (codified as amended at 33 U.S.C. §§ 3901-3914).

[11]Additionally, the criteria were to be based on the recommendations contained in the 1967 Report of the President's Commission on Budget Concepts. The appropriation provision also provided that EPA could not issue a Notice of Funding Availability for applications for WIFIA financing in fiscal year 2020 until the criteria were published. It further provided that a project could not be financed unless EPA and OMB certified that it complied with the criteria.

[12]*Water Infrastructure Finance and Innovation Act Program (WIFIA) Criteria Pursuant to the Further Consolidated Appropriations Act, 2020,* 85 Fed. Reg. 39189 (June 30, 2020).

future liability of the government to determine if the project is federal in nature.[13]

[13]The WIFIA criteria state that while a project authorized by an Act of Congress to be built by the Corps or Bureau of Reclamation is ineligible for WIFIA financing, a project that may connect to, or be tangentially related to, such a project may be eligible depending on the factual circumstances.

Figure 4: Federal Register Notice with Criteria for Considering Federal Participation in Potential Water Infrastructure Finance and Innovation Act (WIFIA) Projects

Federal Register / Vol. 85, No. 126 / Tuesday, June 30, 2020 / Notices

IV. Initial Federal Asset Screening Questions

A. Is the project, in whole or in part, a project currently authorized by Congress for the Army Corps of Engineers or Bureau of Reclamation to construct? [3]

B. Is the project, in whole or in part, a local cost share requirement for an of Army Corps of Engineers or Bureau Reclamation project? [4]

V. Federal Asset Screening Criteria

Structure of the Project

1. To what degree does the Federal Government comprise the WIFIA project's user base?

2. Does the project involve the use of the Federal Government's sovereign power (excluding, *e.g.,* National Environmental Policy Act (NEPA) review)?

3. Does the WIFIA project require the construction or acquisition of an asset for the special purpose of or use by the Federal Government?

4. To what degree does the Federal Government direct the contracting process for the WIFIA project?

5. Is there a specific authority provided to the WIFIA project by an Act of Congress without which the WIFIA project could not proceed?

6. What is the Federal Government's role in the governance of the project? In other words, what is the role of the Federal Government in selecting management or overseeing the project (including, but not limited to, approval of contract scope and step-in rights, or as a member of a board of directors), both during construction as well as in terms of operations and ongoing maintenance?

7. Is this project part of a larger Federally authorized project (not limited to but consistent with the initial screening criteria) and if so, does the project under consideration for a loan or loan guarantee constitute a useful segment—either a planning segment or a useful asset—as defined in the Capital Programming Guide (supplement to OMB Circular A–11)?

Financing of the Project

8. Does the Federal Government provide resources for the WIFIA Federal loan repayment?

9. Will the WIFIA project meet the nonsubordination requirement provided in 33 U.S.C. 3908(b)(6)?

10. Does the WIFIA project depend on the Federal Government making other in-kind contributions (land, real estate, right-of-way, etc.)?

11. Is non-Federal financing available for the project?

12. If the project is required to obtain an investment-grade rating opinion letter, per 33 U.S.C. 3901(4) and 3908(a)(3), to what extent does the rating opinion letter consider Federal support as a credit enhancement?

Project Liabilities

13. To what degree will the Federal Government bear funding liabilities associated with the WIFIA project not otherwise appropriated by Congress or captured in the loan subsidy?

14. Is the risk to the Federal Government low relative to the private sector for the financing of the WIFIA project?

15. To what degree does the Federal Government own or is the Federal Government contractually obligated to complete, maintain, or repair damage to the WIFIA project?

16. Is the Federal Government liable for unforeseen costs (*e.g.,* environmental impacts, damage from natural disasters, or cost overruns) either before, during, or after completion of the WIFIA project?

[3] A project authorized by an Act of Congress to be built by the Army Corps of Engineers or Bureau of Reclamation is ineligible for WIFIA financing. However, a project that may connect to, or be tangentially related to, such a project, may be eligible depending on the factual circumstances (*e.g.,* a project to upgrade a water distribution system that is connected to an Army Corps of Engineers- or Bureau of Reclamation-constructed water source may be eligible for WIFIA financing in some circumstances). Furthermore, a project at a local municipal facility might not be deemed ineligible simply because it was originally built by the Army Corps of Engineers or Bureau of Reclamation. Such questions will need to be resolved on a case-by-case basis.

[4] WIFIA authorizes loans to support local cost-sharing requirements. *See* 33 U.S.C. 3908(b)(8) ("The proceeds of a secured loan under this section may be used to pay any non-Federal share of project costs required if the loan is repayable from non-Federal funds."). However, such a loan that would finance a project that is in whole, or in part, a project authorized by Congress for the Army Corps of Engineers or the Bureau of Reclamation to construct would not meet the Federal asset screening process. Project applicants are encouraged to review all applicable statutory requirements before seeking WIFIA financing.

Source: 85 Fed. Reg. 39189, 39190 (June 30, 2020). | GAO-22-105280

OMB publishes government-wide guidance for implementing FCRA, but these documents do not specify criteria for distinguishing between federal and non-federal activity:

- **OMB Circular No. A-11** provides detailed instructions for calculating subsidy cost estimates and budget formulation reporting requirements.[14]
- **OMB Circular No. A-129** prescribes policies and procedures for justifying, designing, and managing federal credit programs.[15]

FCRA and OMB Circular A-129 assign responsibility to OMB to work with agencies to design and implement federal loan programs. For example:

- FCRA states that OMB is responsible for coordinating the estimates of costs of direct loans and loan guarantees and shall consult with agencies that administer such programs.[16]
- OMB Circular A-129 states that OMB is responsible for (1) working with agencies to identify and implement common policies, processes, or other resources to increase efficiency of credit program portfolio management functions; and (2) providing training to credit agencies.[17]
- Further, Circular A-129 states it is the explicit role of OMB to review legislation to establish new credit programs and to monitor agency conformance with FCRA.[18]

OMB staff told us that they have not published government-wide criteria for determining whether an activity is federal or non-federal for the purposes of applying FCRA because such criteria are infrequently needed. OMB staff also told us that they review draft regulations for new credit programs. As part of this review, they seek to ensure that the programs will not finance federal projects or activities.

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[14]See Office of Management and Budget, *Preparation, Submission, and Execution of the Budget*, Circular No. A-11, pt. 6, § 185 (Washington, D.C.: August 2021).

[15]See Office of Management and Budget, *Policies for Federal Credit Programs and Non-Tax Receivables*, Circular No. A-129 (Washington, D.C.: January 2013).

[16]2 U.S.C. § 661b(a).

[17]OMB Circular No. A-129, pt. I, A.

[18]OMB Circular No. A-129, pt. I, A.

OMB staff also told us that they use the apportionment process to review federal loans to ensure the loans are not funding federal activities.[19] Apportionment is an administrative process through which OMB distributes amounts available for obligation to federal agencies.[20] It is intended to prevent agencies from obligating or expending in excess of their available appropriation. Agencies that obligate or expend in excess of their apportionment violate the Antideficiency Act, and are required to report the violation.[21] For federal loans, OMB staff told us that their review and acceptance of loan subsidy cost estimates is reflected in their documentation of the apportionment. OMB staff also told us that in some select cases, OMB documents each loan by year along with the subsidy cost estimate and recipient in the apportionment.

However, since not every loan government-wide is documented in this way, OMB may be unaware of every case that could have benefitted from clearer guidance and criteria. For example, U.S. Department of Agriculture (USDA) officials told us that the USDA Rural Electric, Rural Telecommunications, and Rural Water and Waste Disposal Direct Loan Programs all receive apportionments based on subsidy cost estimates agreed upon by OMB and the agency program at the beginning of each year (i.e., they receive the special budgetary treatment under FCRA). USDA officials told us that within these programs, OMB only reviewed loans that were significant outliers in terms of loan size or default risk. In cases where OMB does not review all individual loans, OMB cannot be sure if or how loans have been reviewed to assess whether they may fund federal activities.

In another case, EPA approved a WIFIA loan to fund a climate resilience project in the Fargo-Moorhead metropolitan area in North Dakota and Minnesota in a manner officials said is consistent with all applicable FCRA and budgetary scoring requirements for federal WIFIA loans in place at the time. EPA approved the loan prior to the implementation of the criteria published in the *Federal Register* to help EPA and OMB determine federal participation in projects under WIFIA. The climate resilience project EPA funded through the WIFIA program is part of a

[19]FCRA subjects financing accounts to apportionment, and the Antideficiency Act subjects program accounts to apportionment. 2 U.S.C. § 661d(c) (citing to apportionment provisions in subchapter II of chapter 15 of title 31 of the United States Code); 31 U.S.C. §§ 1511, 1512.

[20]31 U.S.C. § 1512.

[21]31 U.S.C. § 1517(b).

public-private partnership project for recurring flood waters diversion that involves the Corps. EPA officials told us that if the criteria had been in place during the letter of interest review of the Fargo-Moorhead project, the project would have been deemed ineligible to receive the special budgetary treatment under FCRA. As a result, EPA officials stated EPA would not have proceeded, based solely on the restrictions imposed by the June 30, 2020, *Federal Register* publication. This is because financing the project on a cash basis would have required a higher level of appropriations than the net present value basis allowable for loans receiving special budgetary treatment under FCRA.

Following the publication of the *Federal Register* notice, EPA officials are aware of the criteria OMB applies to assess whether a prospective borrower's activity is federal or non-federal in nature for the WIFIA program.[22] However, officials from other agencies we interviewed were unaware of the criteria and assessment that OMB conducts. For example, a USDA official told us that it was their understanding at the time we met with them that it was possible they could issue a loan to a non-federal entity to repair or enhance infrastructure that was built by a federal entity. Depending on the specific circumstances, the loan may not qualify as a non-federal project under OMB's criteria.

Without published criteria to consider when evaluating federal credit applications, agencies may extend the special budgetary treatment provided under FCRA to projects that would not otherwise be eligible. This could result in the inconsistent treatment of federal loans across the federal government. In turn, this could make it harder for policymakers to assess and compare the cost of federal programs.

[22]Since fiscal year 2020 when the criteria were put in place, Congress has included language in WIFIA appropriations requiring EPA to use its direct loan and loan guarantee authority in accordance with the criteria published in the *Federal Register* on June 30, 2020. Projects may not be financed unless EPA and OMB certify in advance that the project complies with the criteria. See Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, div. G, tit. II, 134 Stat.1182, 1514 (2020); Consolidated Appropriations Act, 2022, Pub. L. No. 117-103, div. G, tit. II, H.R. 2471—339-340 (2022). Similarly, language included in the Corps' WIFIA appropriations for fiscal year 2021 and 2022 also required the Corps to use its direct loan and loan guarantee authority in accordance with this criteria and prohibited the financing of a project unless the Secretary of the Army and OMB certify that the project complies with the criteria. Pub. L. No. 116-260, div. D, tit. I, 134 Stat. at 1355-56 (2020); Pub. L. No. 117-103, div. D, tit. I, H.R. 2471—167 (2022).

Process for Screening Federal Loan Applications for Potential Federal Activity Varies between Selected Programs

Only One Case Study Program Expressly Identifies Federal Activity in Loan Applications and Is Aware of the OMB Criteria

Of the six case study programs we analyzed, only the WIFIA program has a review process with the express purpose of identifying whether a loan would potentially fund a federal activity. As described above, this process was developed in response to a provision in EPA's fiscal year 2020 WIFIA appropriation. The appropriation required EPA, OMB, and Treasury to jointly develop and publish criteria in the *Federal Register* limiting federal participation in WIFIA projects consistent with the requirements for the budgetary treatment provided for in section 504 of FCRA, among other things.

The *Federal Register* notice invites prospective WIFIA borrowers to submit a letter of interest to demonstrate their projects' eligibility, financial creditworthiness, engineering feasibility, and alignment with the WIFIA selection criteria. The *Federal Register* notice encourages prospective WIFIA program borrowers to evaluate the screening questions and criteria in the notice and provide sufficient information in their letter of interest to address any federal asset questions or concerns. EPA uses the information provided in the letter of interest to evaluate and select projects. OMB staff then evaluate each selected project to determine whether they consider a proposed project to be federal or non-federal in nature and by extension whether or not it is eligible for the special budgetary treatment under FCRA. Answering "yes" to the questions from the *Federal Register* notice does not disqualify a prospective borrower from receiving a loan. Rather, the questions prompt EPA and OMB to further investigate the prospective borrower and the proposed project.

At the time of our review, EPA had applied the criteria for 2 fiscal years. EPA officials told us that:

- in fiscal year 2020, they received 70 letters of interest and one was denied; and

- in fiscal year 2021, they received 45 letters of interest; none were denied but one was partially denied and one required more information before proceeding.[23]

EPA officials told us that the only criterion that has caused projects to be partially or fully denied is the first screening criterion, which asks whether the project in whole or in part is currently authorized by Congress to be constructed by the Corps or the Bureau of Reclamation. The applicant that was fully denied was not a federal entity. However, since the project intended to modify a congressionally authorized structure built by the Bureau of Reclamation, the application was not deemed to pass the criterion.

OMB staff reported that while the facts and circumstances of each proposed loan need to be considered, their understanding is that once authorized, a Corps project, for example, generally confers a significant level of control and future responsibility to the Corps. In such circumstances, this would make the project federal in nature. However, Corps officials stated that non-federal project sponsors generally own the underlying real estate. These sponsors are responsible for the operation, maintenance, repair, rehabilitation, and replacement of the project. Corps officials also noted that, by law, any alteration of a structure or its use is subject to the Corps' approval.[24] This ensures that any proposed improvement or change will not impair the usefulness of the structure.

Outside of officials at EPA who manage WIFIA, none of the agency officials we spoke with were aware that OMB considers all of the principles outlined in the *Federal Register* notice to be applicable to their loan programs. However, these officials did not believe applying these criteria would have affected loans that have been approved within the last 5 years. For example, the evaluation of federal activity is irrelevant for interstate highway projects within the Transportation Infrastructure

[23]In the case of the partial denial, the overall project presented as a single application was deemed ineligible, but some subprojects were considered eligible for funding under the criteria.

[24]Section 14 of the Rivers and Harbors Act, as amended, prohibits anyone from injuring, obstructing, or otherwise impairing the usefulness of a structure built for, among other things, the preservation or improvement of navigable waters by the United States. The provision also provides the Corps with authority to grant permission for any proposed use or alteration of the public work upon a determination that the proposed change will not be injurious to the public interest or impair the usefulness of the public work. 33 U.S.C. § 408.

Finance and Innovation Act program. The states own and operate the interstate highway within their boundaries.

Other Case Study Programs Use Screening Criteria Focused on the Type of Borrower and Sources of Funding

Selected programs other than the EPA WIFIA program, did not have processes specifically intended to identify federal activities nor to deny loan applications that would fund them. We found the selected programs, other than WIFIA, use internal processes to evaluate the eligibility of loan applications based on the type of borrower or source of funding, which may preclude funding federal activities as a secondary effect.

For example, according to USDA, its Telecommunications Infrastructure Loans Program provides loans to state and local governmental entities, federally recognized tribes, nonprofits, or for-profit businesses in rural areas and towns with a population of 5,000 or less. USDA officials told us that these criteria effectively eliminate the chance of a federal borrower being eligible for the program.

Another way that case study programs screen for federal participation in projects applying for loans is by evaluating the overall sources of financing for a project. Ensuring a borrower can finance a project with some non-federal sources helps reduce the amount of fiscal risk to the federal government. For example, DOT officials told us that as part of their loan evaluation, they ensured the 2016 Railroad Rehabilitation and Improvement Financing loan provided to Amtrak was fully repayable by Northeast Corridor revenues.[25] DOT officials assessed Amtrak's available revenues and did not consider any federal assistance as a repayment source for the loan.

Conclusions

FCRA was enacted, in part, to improve the accuracy of the cost of federal credit programs reflected in the federal budget and permit better cost comparisons both among credit programs and between credit and noncredit programs. OMB is responsible for identifying and implementing

[25]The Northeast Corridor connects eight states, stretching from Washington, D.C. to Boston. Amtrak owns and operates 80 percent of the mainline Northeast Corridor. It carries more than 2,200 daily trains, including Amtrak, commuter, and freight trains.

common policies, processes, or other resources for federal credit programs to enable these goals. However, it has not published government-wide criteria determining federal versus non-federal activity for the purposes of FCRA. Publishing criteria government-wide to help agencies distinguish between federal and non-federal activity for the purposes of determining if a project is eligible for special budgetary treatment under FCRA would help ensure that this distinction is made consistently across government and assist policymakers when assessing the cost of federal programs.

Recommendation for Executive Action

The Director of OMB should publish government-wide criteria outlining factors that agencies should consider when evaluating federal involvement in a potential project to help determine whether the project is eligible for the special budgetary treatment under FCRA. (Recommendation 1)

Agency Comments

We provided a draft of this report to the Department of Defense (DOD), DOT, EPA, USDA, and OMB for review and comment. DOD, DOT, EPA, and OMB provided technical comments, which we incorporated as appropriate. OMB neither agreed nor disagreed with our recommendation. USDA responded that the agency had no comments on the report.

We are sending copies of this report to the appropriate congressional committees, the Secretaries of Agriculture, Defense, and Transportation; the Administrator of EPA; and the Director of OMB. In addition, the report will be available at no charge on the GAO website at http://www.gao.gov.

If you or your staff members have any questions regarding this report, please contact me at (202) 512-6806 or arkinj@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix I.

Sincerely,

Jeff Arkin
Director, Strategic Issues

Appendix I: GAO Contacts and Staff Acknowledgments

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Staff Acknowledgments

In addition to the contact name above, the following staff members made key contributions to this report: Thomas McCabe (Assistant Director), Katherine D. Morris (Analyst-in-Charge), Michael Bechetti, Marcia Carlsen, Caitlin Cusati, Susan J. Irving, Karin Fangman, Charlie McKiver, Amalia Konstas, and Kari Terrio.

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