CONGRESSIONAL BUDGET OFFICE
U.S. Congress
Washington, DC 20515

December 11, 2008

Honorable Barney Frank
Chairman
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

CBO has reviewed H.R. 7321, the Auto Industry Financing and Restructuring Act, as passed by the House of Representatives on December 10, 2008. The legislation would:

- Provide funding sufficient to cover the costs of up to $14.0 billion in bridge loans or commitments for lines of credit to eligible domestic automobile manufacturers, in part by reallocating $7.0 billion in funding previously provided for loans to automobile manufacturers and component suppliers under section 136 of the Energy Independence and Security Act (EISA);

- Authorize the appropriation of funds to replace the sums previously available for section 136 loans;

- Provide a federal insurance backstop for certain long-term financial instruments used in the past by transit agencies, some of which are currently in technical default; and

- Authorize a 2009 cost-of-living adjustment for certain justices and judges of the United States.

CBO estimates that enacting H.R. 7321 would increase net direct spending by $3.9 billion over the 2009-2013 period and $1.7 billion over the 2009-2018 period (see the following table). CBO has not completed an estimate of the bill's potential impact on spending subject to appropriation. Such spending could include at least $7 billion to provide new funding for loans to the automobile industry under section 136 of EISA. H.R. 7321 would not affect federal revenues.

	By Fiscal Year, in Millions of Dollars											
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2009-2013	2009-2018
DIRECT SPENDING												
Spending Under Current Law for Loans to Automobile Manufacturers and Component Suppliers (Section 136 Loans)												
Budget Authority	7,500	0	0	0	0	0	0	0	0	0	7,500	7,500
Estimated Outlays	375	750	1,125	1,500	1,500	1,500	750	0	0	0	5,250	7,500
Proposed Changes:												
Net Cost of Bridge Loans to Automobile Manufacturers from Existing Spending Authority												
Estimated Budget Authority	0	0	0	0	0	0	0	0	0	0	0	0
Estimated Outlays	7,125	-750	-1,125	-1,500	-1,500	-1,500	-750	0	0	0	2,250	0
Cost of Loans to Automobile Manufacturers from New Spending Authority												
Estimated Budget Authority	1,500	0	0	0	0	0	0	0	0	0	1,500	1,500
Estimated Outlays	1,250	150	100	0	0	0	0	0	0	0	1,500	1,500
Insurance for Transit Agencies' Financing Agreements												
Estimated Budget Authority	40	27	13	0	0	0	0	0	0	0	80	80
Estimated Outlays	40	27	13	0	0	0	0	0	0	0	80	80
COLA for Judges												
Estimated Budget Authority	6	8	8	8	8	8	8	8	8	8	38	78
Estimated Outlays	6	8	8	8	8	8	8	8	8	8	38	78
Total Proposed Changes												
Estimated Budget Authority	**1,546**	**35**	**21**	**8**	**8**	**8**	**8**	**8**	**8**	**8**	**1,618**	**1,658**
Estimated Outlays	**8,421**	**-565**	**-1,004**	**-1,492**	**-1,492**	**-1,492**	**-742**	**8**	**8**	**8**	**3,868**	**1,658**
Spending Under H.R. 7321												
Budget Authority	9,046	35	21	8	8	8	8	8	8	8	9,118	9,158
Estimated Outlays	8,796	185	121	8	8	8	8	8	8	8	9,118	9,158
CHANGES IN SPENDING SUBJECT TO APPROPRIATION [a]												
Replenish Funds for Section 136 Loans												
Estimated Authorization Level	7,010	0	0	0	0	0	0	0	0	0	7,010	7,010
Estimated Outlays	10	750	1,125	1,500	1,500	1,500	625	0	0	0	4,885	7,010

Note: COLA = cost-of-living adjustment.

a. CBO has not completed an estimate of all costs subject to appropriation under the legislation.

Bridge Loans to Automobile Manufacturers

H.R. 7321 would provide for up to $14.0 billion in financial assistance to domestic automobile manufacturers. The assistance would take the form of loans bearing an interest rate of 5 percent for the first five years and 9 percent for subsequent years. To help cover the estimated subsidy costs of those “bridge loans,” the act would make available $7.0 billion of federal funds previously appropriated to cover the cost of loans to automobile manufacturers and component suppliers for the manufacture of advanced technology vehicles. It would also appropriate any additional amounts that would be necessary for the cost of the bridge loans. CBO estimates that enacting those provisions would increase net direct spending for financial assistance to those firms by $3.8 billion over the 2009-2013 period and $1.5 billion over the 2009-2018 period.

Under the Federal Credit Reform Act (FCRA), most loans and loan guarantees issued by the federal government are not recorded in the budget on a cash basis. Rather, estimates of the various cash flows (including, for example, disbursement of the loan principal, interest and principal payments received, and recoveries on defaults) are netted and discounted to the year of disbursement so as to show a net cost or savings to the government on a present-value basis; the amount of funding needed is not the total amount of the loan, but rather the net cost, if any, on that present-value basis. The net cost, as a percentage of the loan principal, is called the subsidy rate. For example, if the subsidy rate for a $1 billion loan is 50 percent, its net subsidy cost and the amount of funding necessary would be $500 million.

Under current law, CBO estimates that $7.5 billion would be spent over the next several years for the cost of loans involving the automobile industry, pursuant to the Consolidated Security, Disaster Assistance, and Continuing Appropriations Act (Public Law 110-329); that legislation provided funding of that amount to the Department of Energy (DOE) to cover the subsidy cost of providing up to $25 billion in direct loans to automobile manufacturers and component suppliers pursuant to section 136 of EISA—often labeled “section 136 loans.” H.R. 7321 would reallocate most of the existing funding to the proposed bridge loans; although the pace of spending would change, that reallocation, by itself, would have no net budget impact over 10 years. But CBO estimates that other provisions of the act would raise the total subsidy cost for loans to the domestic automobile industry to $9 billion, thus increasing net direct spending for loans to the automobile industry by $1.5 billion over the 2009-2018 period.

The net estimated cost of H.R. 7321 over 10 years reflects two key provisions of the act:

- First, if the $7.0 billion in existing funding is insufficient to cover the subsidy cost of $14.0 billion in bridge loans, the legislation would appropriate such sums as necessary to fill any shortfall; CBO estimates the cost of that provision to be about $1.0 billion (over and above the existing $7.0 billion).

- The act would provide, out of the indefinite "such sums" appropriation, $500 million in new funding for loans to auto makers under section 136 of EISA.

Under FCRA, the Administration determines the estimated subsidy cost of loans based on the procedures specified in that act. In CBO's judgment, the subsidy cost of the bridge loans authorized in this legislation could fall within a wide range depending on estimates of potential interest income, a significant probability of default (which could be different for different firms), and possible recoveries in the event of default. CBO estimates that the bridge loans would have a weighted average subsidy rate of about 50 percent. At such a subsidy rate, CBO estimates the President's designee, who would be responsible for administering the loan program, would require $7.0 billion in budget authority to support $14.0 billion in bridge loans, the amount of existing funds made available for that purpose. The subsidy rate for those loans is very uncertain, however, and CBO's point estimate of 50 percent represents a weighted average of many possible outcomes, taking into account the possibility that subsidy rates assigned by the Administration could fall within a wide range.

To the extent that the Administration assigns subsidy rates to loans that exceed CBO's current estimate of average subsidy rates, total funding available to the President's designee for bridge loans would exceed the $7.0 billion reallocated from existing funds. Such an outcome would result in greater spending for bridge loans. If, on the other hand, the Administration assigns subsidy rates lower than 50 percent, there would be no corresponding reduction in spending for loans under the bill because any amounts not required for bridge loans would remain available to DOE for section 136 loans. As a result, there is a possibility that the total loan costs resulting from this legislation could exceed the $7.0 billion in existing funds, but no possibility that they could be smaller. Reflecting the significant uncertainty and the possibility that the Administration might assign subsidy rates other than 50 percent, CBO estimates that authorizing the President's designee to spend higher amounts if necessary yields about $1.0 billion in additional spending for bridge loans in 2009.

In addition, section 10(a)(2) of the act would provide DOE with $500 million of new budget authority, pursuant to the "such sums" appropriation, to cover the costs of section 136 loans (for advanced technology vehicles). CBO estimates that enacting this provision would increase net direct spending by $250 million in 2009 and $500 million over the 2009-2013 period.

The estimated budget impact over the first five years is greater, however. Although CBO estimates that allowing the President's designee to access existing appropriations would have no net cost over time, that provision would accelerate outlays relative to current law because we expect that the bridge loans would be fully disbursed in 2009. In contrast, we estimate that section 136 loans will be disbursed gradually over several years. Therefore, redirecting the existing DOE funds to support bridge loans would increase net direct spending in fiscal year 2009 and correspondingly decrease spending over the following six years, CBO estimates. That acceleration of spending would add $7.1 billion in spending in 2009 but would result in no net cost over the 2009-2018 period.

Insurance for Transit Agencies' Financing Agreements

H.R. 7321 would provide a federal insurance backstop for certain long-term financial instruments used in the past by transit agencies, some of which are currently in technical default. In the event of a claim against that insurance, the bill would require that the President's designee recoup those amounts from insured entities over the subsequent three years. CBO estimates that enacting this provision would increase net direct spending by $80 million over the 2009-2018 period.

From the late 1980s until the early 2000s, many transit agencies entered into agreements with investors using complex financial instruments called "Sale In/Lease Out" (SILO) or "Lease In/Lease Out" (LILO). Under those deals, the transit agencies sold newly purchased equipment such as rail cars or buses to investors such as banks that were able to depreciate the assets for tax purposes. The investors then leased the assets back to the transit agencies. Among other things, those agreements required that the agencies acquire insurance to ensure timely lease payments, and most agreements required that the insurer hold a AAA bond rating. Many of the insurers of those agreements have lost their AAA bond rating, placing the agreements in default. According to transit industry groups, transit agencies currently have about $4 billion in exposure from such agreements.

Upon the request of a transit agency that entered into a SILO or LILO transaction, the President's designee would provide insurance for those transactions. By providing such an insurance backstop, the federal government would be acting as a guarantor for the SILO and LILO transactions and would be taking on risks associated with the deals. Based on the market rates currently charged for such insurance coverage, CBO estimates that the likelihood of losses to the government under this program would be small and that any such losses would eventually be recouped by fees assessed on transit agencies that chose to participate in this program. Net costs over the first 10 years would be about $80 million by CBO's estimate.

Cost-of-Living Adjustment for Certain Judges

H.R. 7321 also would provide for a 2009 cost-of-living adjustment (COLA) for judges appointed under Article III of the Constitution and bankruptcy judges. (Article III judges include the Chief Justice and associate justices of the Supreme Court, judges of the circuit and district courts, and judges on the Court of International Trade.) Assuming a COLA of 2.8 percent, CBO estimates that a 2009 COLA would cost about $8 million a year on an annualized basis, for a total of $38 million over the 2009-2013 period and $78 million over the 2009-2018 period.

Intergovernmental and Private-Sector Mandates

H.R. 7321 contains an intergovernmental mandate as defined in the Unfunded Mandates Reform Act (UMRA), but CBO estimates that the mandate would impose no costs on state, local, or tribal governments. By exempting communications between auto manufacturers and interested parties regarding restructuring plans from some state antitrust laws, the bill would preempt state law. That preemption would be a mandate as defined in UMRA, but the bill would impose no duty on states that would result in additional spending.

H.R. 7321 could impose a private-sector mandate, as defined in UMRA, by preventing private entities from seeking damages under certain antitrust laws for negotiations authorized under the bill. The direct cost of the mandate would be the forgone net value of the awards and settlements in such claims. Because the Attorney General and the Federal Trade Commission would retain the authority to enforce antitrust laws, CBO expects the cost of this mandate would likely be small and fall below the annual threshold established in UMRA for private-sector mandates ($136 million in 2008, adjusted annually for inflation).

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contacts are Megan Carroll (for auto loans), Sarah Puro (for transit insurance), and Leigh Angres (for judges' pay).

Sincerely,

Robert A. Sunshine

Robert A. Sunshine
Acting Director

cc: Honorable Spencer Bachus
Ranking Member