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CLINCH RIVER: ANOTHER OFF-BUDGET MISTAKE

It seems that Congress never learns. Just as the Senate is wrestling with the fallout from the \$2.25 billion bond default by the Washington Public Power Supply System (WPPSS), it is giving consideration to an ill-conceived plan to float \$1 billion in federally guaranteed bonds to finish the controversial Clinch River Breeder Reactor. The reactor's supporters also want an additional \$1.5 billion in direct appropriations for the project. Like WPPSS, the Clinch River plan would use "off-budget" financing to mask a \$1 billion increase in the federal deficit. In short, it is another expensive fiasco in the making.

Last December funding for the Clinch River Reactor was defeated by the House, and it squeaked through the Senate by just one vote. Congress eventually agreed to continue funding only if the Department of Energy (DOE) would "vigorously explore" ways of including private sector finance "that would reduce federal budget requirements."

The new DOE proposal, backed by Clinch River supporters, finesses this requirement with a package that includes private sector financing in name only. Although investors supposedly would provide 40 percent of the \$2.5 billion needed to complete the \$3.6 billion reactor (current DOE cost estimates), this turns out to mean a \$675 million short-term loan from private sources, to be retired in 1990 (with accrued interest) by \$1.04 billion in federally guaranteed bonds, together with just \$150 million in equity shares and \$175 million from the utilities. The remaining \$1.5 billion would be provided by the taxpayer through a one-time congressional obligation vote. The taxpayer also would be responsible for any further cost overrun, and for redeeming the guaranteed bonds if project revenues fall below expectations.

The plan has many of the inherent weaknesses of the original WPPSS package--and is as bad a deal for the American taxpayer as it would be lucrative for the bondholders and investors. According to Congressional Budget Office Director Rudolph Penner, the tax advantages available "imply that the after-tax rate of return earned by the equity investors would be about 37 percent, while the after-tax rate of return for bondholders would be 7.5 percent." Moreover, the bondholders will enjoy a federal guarantee, so they need care little whether the reactor produces any revenues at all. Not only that, CBO calculates that this private "cost-sharing" plan would actually cost the Treasury nearly \$250 million more than financing the reactor with an on-budget appropriation.

So who benefits? Certainly the bondholders. The investment brokers are also likely to do very nicely out of the \$1 billion bond offering--as they did with the WPPSS issue. Merrill Lynch, for instance, made \$22.5 million in commissions--the largest in the firm's history--by underwriting

\$750 million in WPPSS bonds. And the contractors can take cheer that future work would be assured, virtually free of congressional oversight or real cost constraints.

The taxpayer, on the other hand, has little to be happy about. Not only will he end up paying more, thanks to the financing package, but he can take little comfort in the "considerable confidence" expressed by Energy Secretary Donald Hodel regarding the estimated completion costs. When the reactor was first authorized in 1971, the cost was put at \$400 million (over half to be provided by the utilities). A year later this was revised upwards to \$700 million. The most recent estimate by DOE is \$3.6 billion. But the ink was hardly dry on that figure before it was revealed that an internal departmental study had predicted a further overrun of \$300 million, and a delay in the completion date of 1½ years.

The plan also shifts the enterprise off-budget, and it ends congressional oversight by substituting a one-time obligation of \$1.5 billion in place of the annual Clinch River appropriation. When projects are moved off-budget in this way, the taxpayer loses the power to have the management and finances scrutinized by his representatives. Yet the enterprises are not subject to marketplace constraints either. They move to a twilight zone where management is insulated from those who must foot the bill for any mistakes. WPPSS is a classic example of what can happen.

Removing projects from the glare of the federal budget process makes good sense to politicians, however. It means that new debt can be created without expanding the official federal budget deficit. Yet there is only one practical difference between issuing \$1 billion in federally guaranteed Clinch River bonds and openly appropriating the money and adding it to the federal deficit--it costs more.

Proponents of the Clinch River project maintain that the technology has enormous commercial value, yet they can only interest the private sector by giving away the store. They say the construction costs are now firm--but estimates have jumped nearly ten-fold in 12 years. They contend that revenues from the project will cover the cost of financing bonds--just as Congress assumed in the case of WPPSS--yet the economics of breeder-generated electricity is, to say the least, uncertain. And when finally pressed for reasons why Congress should borrow and spend at least \$2.5 billion, they say that it makes sense because the taxpayers have already sunk \$1.5 billion into the project.

It is time for the American public to cut its losses. The breeder reactor might well be the energy technology of the future--so might solar power or some yet unimagined system. That does not mean the federal government should risk billions of dollars on the Clinch River project. It is the epitome of crude industrial policy for Congress to pick an energy "winner" and then bribe a reluctant private sector to invest in it. The marketplace will channel finance into the right technology--at the right time--given the state of available estimates on comparative costs, demand and risk. When government tries to outguess the market, and ignore its signals, the result is WPPSS.

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For further information:

Testimony of Rudolph Penner, Subcommittee on Energy Conservation and Power, House Committee on Energy and Commerce, September 20, 1983.

"The Clinch River Folly," Heritage Backgrounder No. 231, December 3, 1982.

"Clinch River Reactor: A Dying Nuclear Dream," Congressional Quarterly, May 21, 1983, p. 995.