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Mr. Eric Solomon
Assistant Secretary for Tax Policy
Department of the Treasury
1500 Pennsylvania Ave., NW, Room 3120
Washington, D.C. 20220

Dear Mr. Solomon:

I write to request that the Treasury Department conduct a thorough review of the financial and environmental risks associated with the use of tax-exempt financing for coal-fired power plants. Recent research shows that the risks make them poor candidates for federal support and problematic for investors.

Your testimony to Congress last October and a recent GAO study have both cited cost concerns about the growth in the use of tax-exempt financing instruments. Though the energy sector constitutes a relatively small percentage of the tax-exempt program, they are clearly among the most costly on a project-by-project basis and fast becoming more expensive.

Attached you will find a copy of a report recently prepared by Synapse Energy of Cambridge, Massachusetts. It highlights the skyrocketing increase of construction costs for new coal plants with no relief in sight. Regulatory uncertainty over CO2 emissions further clouds the investment horizon. Plants constructed under current rules will incur new financial obligations to curb greenhouse gases. Other recent reports on the price of coal suggest a new higher price floor is altering cost assumptions for coal plants.

The Basics:

- The current climate for construction of coal-fired power plants has significant and unprecedented financial and environmental risks.

- Faced with these risks, USDA's Rural Utility Services (RUS) has instituted an effective *moratorium* on new coal plant loans through at least 2009. RUS chief, James M. Andrew has said: "Since there is no clear consensus on what emission standards will be enacted and associated costs, ***attempting to make decisions on loans absent a factual base is speculative, at best."*** (emphasis added)

- The United States Department of Energy has 'restructured' its commitment to a major clean coal demonstration project citing rising costs.

- Cancellations and postponements of proposed plants across the country are now commonplace.

- Investment banks have already enacted a program of enhanced due diligence called the Carbon Principles to monitor new coal plant financings. However, their new enhanced diligence program currently excludes public power sponsors that use the tax-exempt markets, thereby greatly limiting the effectiveness of the Carbon Principles in analyzing public power projects that rely on tax-exempt financing.

- The assumptions used to support the sale of tax-exempt bonds for coal-fired plants are the same speculative ones that have caused RUS to enact a moratorium, DOE to rethink its support for the Future Gen project, and investment banks to adopt enhanced diligence.

- Speculative assumptions should not be the basis for statements made in official bond documents.

- There has been no effective policy response to the use of tax-exempt financing for coal-fire plants despite obvious risk to investors and taxpayers.

Despite the risks, several high profile coal-fired power plants are moving forward with tax-exempt support. Perhaps the most notable are the AMP-Ohio and Prairie State projects in the Midwest. They are proceeding based on the assumption that ratepayers will simply pay any price increases without question. This problematic assumption could prove disruptive to municipal systems, bond markets, and the federal government.

A recent article in the New York Times raises the specter of obsolete coal plants, not unlike the history of nuclear plant failures. Also likely is that near and long term cost increases unacknowledged by project proponents will place pressure on plant costs and begin to undermine the payment of debt service obligations. At minimum, premature refinancing and other forms of disruptive debt restructuring are increasingly likely over the life of these bonds given the current economic climate.

In February, investment banks, JP Morgan Chase, Citigroup and Morgan Stanley, initiated an enhanced due diligence review based on new carbon principles. The principles were presented as a *first step* in assessing the environmental risk posed by coal-fired plants in private sector transactions. The principles currently exempt municipal electric systems and other public power providers.

Local and state officials and credit underwriters planning some tax-exempt projects are pushing forward despite warning signs. Plants are being advanced through the development process based on outdated assumptions and a suspension of disbelief that the risks will be managed or wished-away. Normal due diligence should have sent up red flags, but so far, haven't. I agree with RUS's position cited above – there exists no factual support for the current economic assumptions.

I firmly believe that an immediate review and timely action by the Treasury Department might spare the nation's taxpayers a series of expensive losses.

Thank you for the opportunity to express my concerns. I look forward to your response.

Very truly yours,

William C. Thompson, Jr.

Attachment