Biden’s climate fight now has a Fed problem

Democrats are scrambling to prevent a conflict between their goals of fighting climate change and shoring up big banks.

By JASPER GOODMAN
POLITICO

President Joe Biden’s clean energy plan is facing an unexpected threat: banking regulators.

Biden is trying to funnel federal money to clean energy projects using billions of dollars in tax credits. The renewables industry relies heavily on large lenders to finance those developments: Banks and other backers invested $19 billion last year in projects like solar and wind power in return for the credits and other benefits.

But now impending rules to make large banks less risky would also make it a lot more expensive for them to make those investments.

The proposed bank rules are setting up a collision between the effort to transition away from fossil fuels and the push to ensure banks don’t tank the global financial system. The renewables industry is warning the change could undo gains made by the president’s signature climate law, the Inflation Reduction Act.

The outcry shows how competing priorities can force tough choices in Washington. It could help Wall Street in broader efforts to water down banking regulations that have been in the works since the 2008 global financial crisis. At the same time, it’s forcing Democrats to scramble to prevent a conflict between their goals of fighting climate change and shoring up big banks.

“The implication is a massive reduction in the amount of capital that’s available to decarbonize our energy system and make investments in cheaper energy assets,” Rep. Sean Casten (D-Ill.) said in an interview.

The banking agencies issuing the rules — the Federal Reserve, the FDIC and the Office of the Comptroller of the Currency — declined to comment. The Fed’s Vice Chair for Supervision, Michael Barr, who was appointed by Biden and spearheaded the tougher rules, acknowledged the concerns in a speech at the American Bankers Association Annual Convention in Nashville, Tenn., this month.

“We welcome all comments that provide the agencies with additional data and perspectives to help ensure the rules accurately reflect risk,” he said.

Banking regulators have extended the comment period on the proposed new capital rules to give the public more time to weigh in on the plan, which is expected to be finalized next year. The rules would not fully take effect until 2028.

The clash centers around certain types of investments banks make in clean energy projects. Laws like the Inflation Reduction Act incentivize clean energy primarily by offering tax breaks to developers. But because renewable energy developers often don't have enough tax liability to fully use the subsidies they qualify for, they rely on partnerships with banks in which investors provide financing for project costs in exchange for tax credits and other benefits.

The banking rules are part of a broader effort to enact an international agreement hammered out in Basel, Switzerland, in the wake of the 2008 financial crisis to minimize the risk of bank collapses. They would increase the amount of capital that large banks are required to hold to offset potential losses from investments. They would quadruple the capital requirement for investments in exchange for the renewable energy tax credits, decreasing the financial benefit banks would see when they invest.

"It is a big concern," said David Burton, a partner at the law firm Norton Rose Fulbright who specializes in tax equity transactions. "Congress made a decision to address climate change through the tax code. And this would really, really undermine it."

Some big banks have started to warn developers that they would dramatically reduce their exposure to the tax credits if the capital hike takes effect. Bank Policy Institute president Greg Baer, whose trade group represents the largest U.S. banks, told House Financial Services Committee lawmakers last month that his members "would absolutely exit this market" if the rule took effect.

The warnings have the renewables industry on high alert. The American Council on Renewable Energy told the White House in a letter that the proposed rules "threaten to derail the clean energy transition." More than 40 renewable energy companies and trade groups signed the letter, including the American Clean Power Association and the Solar Energy Industries Association.

It's drawing the attention of Democrats on Capitol Hill, who are also speaking out.

"When you start with a draft out of Switzerland and you don't perfectly tailor it for the United States, that might be because you started from a draft in Switzerland," Rep. Brad Sherman (D-Calif.) said in an interview. "I hope to see that change, absolutely."

Financial watchdogs are keeping a close eye on whether it triggers a broader rollback of the rules.

"These tax equity financing deals are not a reason to call for lower capital requirements for the big banks," said Alexa Philo, a senior policy analyst at Americans for Financial Reform. "This space is dominated by the megabanks, such as JPMorgan and Bank of America, and these deals are usually highly extractive."

“Again the megabanks are using others to advocate for policies that will ultimately help their own bottom line,” she added.

The solution could be an exemption for the clean energy tax credits, banks and clean energy advocates say. They argue the credits deserve a carve-out because they are safer than other private equity investments that are subject to the same increased capital requirement.

“There’s been no one on any side of this issue that has made an argument that the assets are risky,” said Casten, who co-chairs the Congressional Sustainable Investment Caucus.