

# Google Gemini on EPA WIFIA's Violation of Anti-Deficiency Act if Predictable Funding Losses are Excluded from Loan Commitment Apportionment

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InRecap questions and comments in red – Google Gemini responses in black

Is intentionally inadequate apportionment a violation of the Anti-Deficiency Act?

Yes, **intentionally inadequate apportionment** is a violation of the [Antideficiency Act \(ADA\)](#). According to **31 U.S.C. § 1512**, the Office of Management and Budget (OMB) is required to apportion funds to "prevent obligation or expenditure at a rate that would indicate a necessity for a deficiency or supplemental appropriation".

## Key Violations Related to Apportionment

- **Excessive Obligations:** The most common violation occurs when an agency makes an obligation or expenditure that exceeds the amount available in an apportionment (**31 U.S.C. § 1517(a)**).
- **Creating "Coercive Deficiencies":** The ADA was specifically designed to prevent "coercive deficiencies," where agencies spend funds so quickly—or are given so little initially—that Congress is forced to provide more money to keep the agency running.
- **Intentional Mismanagement:** While the Act primarily prohibits exceeding limits, GAO has noted that apportionments are legally binding. Intentionally providing an inadequate apportionment to force a specific outcome (like an agency shutdown or a request for more funds) undermines congressional authority and the legal mandate to prevent deficiencies.

## Consequences of Violations

If an official knowingly and willfully violates the ADA, they can face:

- **Administrative Discipline:** Including suspension without pay or removal from office.

- **Criminal Penalties:** A fine of up to **\$5,000**, imprisonment for up to **two years**, or both (**31 U.S.C. § 1350**).

How does this apply to apportionment for credit subsidy estimates when a federal loan program executes a loan commitment?

In federal loan programs, an **intentionally inadequate apportionment** for credit subsidy estimates can trigger a violation of the **Antideficiency Act (ADA)** during the loan commitment phase by forcing a "coercive deficiency" or by leading to an unauthorized obligation of funds.

### **Application to Credit Subsidy Estimates**

Under the [Federal Credit Reform Act of 1990 \(FCRA\)](#), the "cost" of a federal loan—the **credit subsidy**—must be estimated and budget authority must be available before a loan commitment is made.

- **Binding Limit:** The **apportionment** of the credit subsidy is a legally binding limit. If an agency executes a loan commitment that requires more subsidy budget authority than has been apportioned, it violates **31 U.S.C. § 1517(a)**.
- **Preventing "Coercive Deficiencies":** Apportionment is designed to prevent agencies from spending their budget so quickly that they run out of money mid-year, effectively forcing Congress to provide more funds to meet legal obligations. An intentionally inadequate apportionment would fail this statutory requirement to manage funds over the full period of availability.
- **Loan Commitments as Obligations:** When an agency executes a **loan commitment**, it creates a legal obligation for the government to provide the loan. If the credit subsidy for that commitment exceeds the apportioned amount, the official authorizing the commitment has committed an ADA violation.

### **Specific Risks in Loan Programs**

- **Incorrect Subsidy Models:** If an agency or OMB intentionally uses an outdated or flawed model to provide an "inadequate" apportionment that does not cover the true projected cost of the loans being committed, they may be creating a situation where the agency is operating without sufficient legal authority.

- **Modifications:** Agencies cannot modify existing loans in a way that increases the subsidy cost unless they have sufficient budget authority and a corresponding apportionment to cover that increase.
- **Mandatory Reporting:** Any obligation of credit subsidy in excess of the amount apportioned must be reported to the President and Congress, even if the "insufficiency" was caused by the apportionment process itself.

Are you analyzing a specific **loan program** or a **proposed modification** to an existing credit subsidy estimate?

This question is specifically in regard to the Wifia loan program. It appears the high level of mandatory spending at that program, due to interest rate re-estimates, was the result of predictable borrower behavior -- e.g., only drawing a commitment when 'in-the-money', pressuring for resets, using short-term finance for construction advances instead of the WIFIA loan, etc.

Yet to date credit subsidy estimates at the time of loan commitment execution and apportionment only consider credit losses and ignore predictable borrower behavior. There was an incentive to do this -- predictable funding losses could then be characterized as 'unpredictable' interest rate re-estimates and covered with mandatory (vs. discretionary) appropriations, making the Program look much more cost-effective.

In the context of the **WIFIA loan program**, your description highlights a sophisticated tension between the [Federal Credit Reform Act \(FCRA\)](#) and the [Antideficiency Act \(ADA\)](#).

If an agency **intentionally excludes** predictable borrower behaviors—such as adverse selection (only drawing when "in-the-money") or systematic interest rate resets—from its initial credit subsidy estimates, this could be viewed as an attempt to circumvent the ADA's "coercive deficiency" prohibition.

## Legal and Budgetary Framework

- **The Incentive:** By ignoring predictable behavior that reduces government revenue (like [one-time interest rate resets](#)), the program's initial "cost" appears lower. This allows a smaller **discretionary appropriation** to support a larger volume of loans.

- **Mandatory Re-estimates:** Under FCRA, any subsequent losses due to interest rate changes are covered by **permanent indefinite (mandatory) appropriations**. If these "losses" were actually predictable based on program design and borrower behavior, characterizing them as "unpredictable" interest rate fluctuations shifts the true cost from the discretionary budget to the mandatory budget without prior congressional approval of those specific costs.
- **ADA Implications:** The ADA prohibits agencies from making an apportionment at a rate that would necessitate a supplemental appropriation (**31 U.S.C. § 1512**). If the subsidy model is **intentionally designed to be inadequate** to cover predictable costs, it risks creating a "coercive deficiency" where Congress is later forced to provide mandatory funds to honor the legal loan commitments already executed by the agency.

## Specific Borrower Behaviors at Issue

- **Adverse Selection in Draws:** Borrowers often use [short-term financing for construction](#) and only draw on the WIFIA loan if the locked-in federal rate remains lower than market rates at project completion.
- **Interest Rate Resets:** WIFIA allows a one-time reset if rates drop before funds are drawn. This flexibility has already resulted in over **\$2 billion in mandatory spending**.
- **Exclusion from Apportionment:** If OMB and EPA exclude these features from the "subsidy cost" at the time of [loan commitment](#), they are technically obligating the government to potential losses that have not been fully "priced" into the discretionary appropriation.

## Accountability

While GAO has noted that [underestimating credit subsidy costs](#) is a persistent issue in federal credit programs, proving an **ADA violation** requires showing that the apportionment was "knowingly and willfully" inadequate to force a deficiency. If the exclusion is deemed a matter of "accounting policy" rather than "intentional mismanagement," it is often handled as a budgetary dispute between CBO and OMB rather than a criminal ADA matter.

- CBO Says Fair Value Accounting Would Greatly Increase Cost ...

Re "knowingly and willfully" standard, it could be argued that complex borrower behavior was not predictable during the first years of the Program's operations, and that there was no factual basis for assuming funding losses.

But now that the Program has been in operation for seven years, and has data for 140 loan commitments, almost all with the same type of Aa3/AA- water agency, wouldn't continued exclusion of this predictable cost at apportionment be a violation?

The argument that seven years of data transforms "unpredictable" behavior into a "predictable cost" is the central legal pivot for a potential **Antideficiency Act (ADA)** violation. While there is no published GAO legal opinion specifically finding WIFIA in violation on these grounds yet, the following principles apply to your scenario:

## 1. The "Predictable" vs. "Unpredictable" Threshold

The ADA (**31 U.S.C. § 1512**) requires that apportionments be made to prevent the "necessity for a deficiency or supplemental appropriation".

- **Initial Defense:** In a program's early years, agencies often argue that borrower behavior—such as the [one-time interest rate reset](#)—is a "contingent liability" that cannot be precisely modeled.
- **The Seven-Year Shift:** Once a program has a significant track record (e.g., 140 loan commitments), GAO has historically argued that "persistent underestimation" of costs in the presence of historical data may indicate an [intentional effort to circumvent discretionary budget caps](#).

## 2. Systematic Use of Mandatory Re-estimates

Under the [Federal Credit Reform Act \(FCRA\)](#), interest rate re-estimates are covered by **permanent indefinite (mandatory) authority**.

- **The Violation Argument:** If the EPA and OMB **knowingly** exclude a cost they *know* will occur—like the \$2 billion in mandatory spending WIFIA has already generated—they are effectively using the mandatory re-estimate process to "supplement" an intentionally low discretionary appropriation.
- **Coercive Deficiency:** This creates a "coercive deficiency" because the government is legally bound by the [loan commitment](#) to provide a lower rate

later, forcing a draw on the Treasury that was never fully "priced" at the time of apportionment.

### 3. Evidentiary Standard for "Knowing and Willful"

To trigger **criminal penalties** (fine up to \$5,000 or 2 years imprisonment), it must be proven the officials **knew** the model was inadequate and **willfully** used it to bypass budget limits.

- **Administrative vs. Criminal:** Most such cases result in administrative discipline and a required [report to the President and Congress](#) rather than criminal prosecution, as agencies often cite "technical modeling disagreements" with the [OMB Credit Subsidy Calculator](#) as a defense.

### 4. Current Scrutiny

WIFIA's high level of **mandatory spending** (roughly 9% of its total portfolio) is now a known quantity within the administration. Continued exclusion of these factors from the initial [credit subsidy estimates](#) makes it increasingly difficult for officials to claim the costs are "unforeseen" or "unpredictable".

Focus on Wifia resets – a reset is a re-execution of a loan commitment, presumably requiring a new apportionment. Under the circumstances of a reset (e.g. a sophisticated borrower requesting a reset a low point in the interest rate cycle), wouldn't ignoring the increased likelihood of eventual funding losses be even less defensible?

In the case of **WIFIA resets**, the argument for an Antideficiency Act (ADA) violation becomes significantly stronger because the agency is making a specific, affirmative decision to re-obligate funds under conditions where a loss is not just possible, but highly probable.

### 1. Resets as a Re-execution of Commitment

A WIFIA "reset" is technically a **modification** of a federal credit instrument. Under the [Federal Credit Reform Act \(FCRA\)](#), any modification that increases the cost of a loan must be covered by new budget authority and a [new apportionment](#) before it is executed.

- **The Intentionality Argument:** At the moment of a reset, the borrower is intentionally selecting a "low point" in the interest rate cycle to reduce their payments. By definition, this increases the **subsidy cost** to the government.
- **Defensibility:** Ignoring this cost at the point of reset is less defensible than at the initial closing because the "risk" has already materialized. The agency is knowingly locking in a lower return on a loan asset than originally planned, effectively [spending more than was initially authorized](#) for that specific transaction.

## 2. Circumventing Discretionary Controls

WIFIA has saved borrowers over **\$1.5 billion** through just seven resets.

- **Mandatory Spending as a "Safety Valve":** If EPA and OMB treat the cost of these resets as "unpredictable interest rate re-estimates" (covered by **mandatory funding**), they are using a loophole to avoid using the **discretionary appropriations** that Congress provided to "buy" the credit subsidy.
- **Coercive Deficiency:** By executing a reset without first ensuring that the *discretionary* subsidy budget can cover the new, higher cost, the agency is forcing the Treasury to provide the difference through mandatory re-estimates. This is a hallmark of a [coercive deficiency](#), which the ADA was enacted to prevent.

## 3. Sophisticated Borrower Behavior

Your point regarding "sophisticated borrowers" (typically AA/Aa-rated water agencies) is critical.

- **Predictability:** These borrowers have financial advisors who monitor the [Treasury SLGS rates](#) daily to time their resets.
- **Legal Liability:** For an ADA violation to be "knowing and willful," the official must understand the consequences of their action. Given that the [OMB Technical Appendices](#) now clearly show over **\$2 billion** in mandatory spending for these "re-estimates," it is difficult for OMB or EPA to argue that these costs remain "unpredictable" or "unforeseeable".

## Summary of the Potential Violation

If the EPA executes a reset—which is a [new legal commitment](#)—and OMB provides an apportionment of \$0 (assuming the cost is "unpredictable" and will be handled by a later mandatory re-estimate), they are likely violating **31 U.S.C. § 1517**. They are obligating the government to a cost for which they have not secured a proper apportionment from the discretionary funds intended for that purpose.

How could a credit subsidy apportionment reflect expected funding loss -- e.g., based on past results, using 9% of loan amount since that is historical level of mandatory appropriations. How would the amount be categorized -- e.g., equivalent to committing to a sub-UST loan?

To reflect an **expected funding loss** (such as the 9% historical level of mandatory spending you noted) in a credit subsidy apportionment, the agency would need to adjust the cash flow assumptions that feed into the **OMB Credit Subsidy Calculator (CSC)**.

### How the Apportionment Reflects Expected Loss

Instead of treating borrower behaviors as "unpredictable" events to be fixed later by mandatory re-estimates, the agency would incorporate them as **baseline cash flow assumptions**:

- **Adjusting Interest Inflows:** The model would assume that for a given percentage of the portfolio, the interest rate will be **reset** to a lower rate at a specific point in the loan's life.
- **Probability Weighting:** The agency could assign a **probability of exercise** for the reset option (e.g., a 90% likelihood if market rates drop below the original locked rate).
- **Draw Timing:** The model would reflect that borrowers delay draws until "in-the-money," further reducing the Net Present Value (NPV) of expected repayments.

### Categorization of the Amount

This expected loss would be categorized as part of the **Direct Loan Subsidy Cost**.

- **Sub-UST Loan Equivalence:** Economically, this is equivalent to committing to a **sub-UST (United States Treasury) loan**. While the law requires WIFIA rates to be "equal to or greater than" the yield on comparable Treasuries at the time of

execution, providing a **free reset option** creates a "one-way" interest rate risk. The government essentially provides a loan that *starts* at the Treasury rate but can only go *down*, never up, resulting in a net return lower than the Treasury's cost of funds.

- **Discretionary vs. Mandatory:** By including this in the apportionment, the 9% cost would be charged against **discretionary budget authority** at the time the loan commitment is made. Currently, by *ignoring* it, this cost is categorized as a **mandatory re-estimate** later, which bypasses the discretionary caps set by Congress.

## The Impact on Program Appearance

Categorizing the 9% as an upfront discretionary cost would fundamentally change the program's perceived "cost-effectiveness":

1. **Lower Leverage:** Instead of a \$1 million appropriation supporting \$100 million in loans (a 1% subsidy), it would only support roughly \$11 million (a 9% subsidy).
2. **True Transparency:** The "cost to the government" would match the actual taxpayer outlay, rather than hiding it in off-budget mandatory accounts.

Could WIFIA and/or OMB start doing estimates on this basis immediately -- that is, no laws or rules would need to be changed in order to adjust estimates to include this factor?

Yes, WIFIA and OMB have the administrative authority to adjust credit subsidy estimates

**immediately** without changing any laws or formal rules.

Under the [Federal Credit Reform Act \(FCRA\)](#), the **subsidy cost** is defined as the present value of estimated cash flows, adjusted for "expected deviations from the contract terms" (**31 U.S.C. § 661a**). Predictable borrower behavior—like interest rate resets—is legally a "deviation" that should be priced at the outset.

## Administrative Mechanisms for Immediate Adjustment

- **Updating Cash Flow Assumptions:** The [OMB Credit Subsidy Calculator \(CSC\)](#) relies on cash flow spreadsheets provided by the agency. EPA and OMB could immediately update these spreadsheets to include a "probability of reset" and "expected draw timing" based on the last seven years of program data.

- **Revising OMB Circular A-11:** OMB regularly publishes technical updates to [Circular A-11](#), which provides the legally binding guidance for these calculations. They could clarify that "unpredictable" interest rate re-estimates exclude behaviors that are statistically predictable for a specific portfolio.
- **Administrative Approval:** The [WIFIA interest rate reset](#) is not a statutory requirement; it is an administrative flexibility offered by the EPA. Because it is a "bureaucratic practice," OMB could require that the cost of this feature be "scored" and apportioned against discretionary funds at the moment of commitment rather than being deferred to mandatory accounts.

## Barriers to Immediate Change

While no law *prevents* this change, several internal factors discourage it:

- **Political Capital:** Including a 9% "funding loss" assumption would immediately reduce the program's perceived leverage (e.g., a \$50M appropriation might only support \$500M in loans instead of \$5B).
- **Standardization:** OMB typically prefers uniform rules across all federal credit programs. Changing the rules for WIFIA might create pressure to apply similar "behavioral modeling" to other programs (like student loans or TIFIA), which could have massive budgetary implications.
- **Historical Precedent:** Since interest rate re-estimates have historically been a [minor bookkeeping item](#), shifting them to a discretionary "appropriated reserve" model would be a major shift in federal budgeting policy.

In short, the **legal authority exists today** to end the practice of "intentionally inadequate" apportionments by simply updating the program's [financial assumptions](#) to reflect reality.