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Update on the sale of student loans

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The first loans which were introduced in 1990 were known as 'mortgage –style' loans, these loans were superseded in September 1998 by income-contingent loans.

The entire mortgage-style loan book has been sold off to private investors as a result of three separate sales which took place between 1998 and 2013.

In the Budget 2007 the Government announced plans to sell off more of the loan book and the *Sale of Student Loans Act 2008* put in place provisions to allow the sale of income-contingent student loans issued between 1998 and 2012. The Act applied to England and Wales.

In December 2013 the Government announced its intention to sell off some of the English income-contingent loan book. Subsequently George Osborne stated that the removal of the cap on student numbers in 2015 would be funded by the sale of more student debt to private companies. In the event the expected sale did not occur due to the market conditions at the time and the policy stalled.

However, a sale remained Government policy and was referred to in the Autumn Statement 2014, the Budget 2015 and in the March 2016 Budget.

Finally in February 2017 it was announced that a sale would go ahead and **the first sale of Plan 1 income contingent loans was completed in December 2017**. The sale covered loans issued by English local authorities that entered repayment between 2002 and 2006. **The sale achieved £1.7 billion from 1.2 million loans with a face value of £3.5 billion held by over 400,000 borrowers**. This represented a write off of 51 per cent of the face value of the loans.

A **second sale** of a tranche of Plan 1 loans that entered repayment between 2007 and 2009 was completed in December 2018. The sale was of loans with a **total face value of around £3.9bn and achieved £1.9bn**.

Issues around the sales concerned the value for money of sales and the impact on borrowers. A report by the National Audit Office in July 2018 concluded that the first sale achieved value for money, however other commentators have said that the sales show that the government "prefers cash today over a larger sum of cash tomorrow".

1. Overview: Sale of the student loan book

There are two types of student loans. The first loans that were introduced in 1990 were referred to as '**mortgage –style' loans**,[1] these loans were superseded in September 1998 by **income-contingent loans**.[2]

The entire mortgage-style loan book has been sold off to private investors as a result of three separate sales which took place between 1998 and 2013.

It has long been the Government's intention to sell off further parts of the student loan book. The Labour Government first announced plans for a sale of income -contingent loans in 2007.

The current Government is planning to sell off all pre-2012 income-contingent loans in a series of four sales. The first sale was completed in December 2017.

The history of the sale of student loans is discussed in more detail in the library briefing CBP 1079 *Student Loan Statistics*, 2 December 2016 p15-18.

1.1 Reason for the sale of loans

The Government categorises the student loan book as an asset and, as such, it is able to sell that asset to raise money.

The Business, Innovation and Skills Committee conducted and inquiry into student loans in 2014, their report, *Student Loans*,[3] looked into past sales of the loan book and stated that the primary objective of sales had been to bring in money for the Government.[4] The report also said that the sales reduced public sector debt:

> The sale of the remaining mortgage style student loan book represents good value for money, helping to reduce public sector net debt by £160 million. The private sector is well placed to maximise returns from the book which has a deteriorating value. [5]

Information on the benefit of the last sale was given in answer to a PQ on 22 February 2017:

> **Students: Loans**: Written question - 65007
>
> **Asked by Steve McCabe**: 22 February 2017

"These student loans could be sold precisely because they have achieved their original policy objective of supporting students to access higher education. "

Source: Government response to Treasury Committee 7th report, *Student Loans*, 11 May 2018

1 These loans became repayable from the April after the student finished higher education when their gross income exceeded the threshold of 85% of national average earnings. If their income stayed above the threshold then repayments were made over 5 years in 60 equal monthly instalments hence 'mortgage-style'.

2 Repayments for these loans are 9% of income above the repayment threshold, rather than a set amount each month. Any balance remaining is written off after the end of the loan period (currently 30 years)

3 Business, Innovation and Skills Committee, Student Loans, 22 July 2014, HC 558 2014-15

4 *Ibid* p14

5 *Ibid*

> To ask the Secretary of State for Education, what the potential (a) short-term and (b) long-term benefits are of selling the student loan book for (i) the taxpayer, (ii) students with outstanding loans and (iii) current and future students.
>
> **Answered by: Joseph Johnson**: 27 February 2017
>
> The proposed sale of the student loan book, set out in Written Statement HCWS458, gives the Government the capacity to invest in other policies with greater economic or social returns and reduces fiscal pressures.
>
> The position of students and graduates, including those with loans in scope of the sale, will not be affected by the sale.

In 2013 the then Chancellor of the Exchequer George Osborne said that the finance raised by selling some of the student loan book would pay for an expansion in student numbers when the cap on student numbers was removed in September 2015.

1.2 Management of the sale

The Department for Education sets student loan policies and oversees the administration and collection of student loans by the Student Loans Company and HM Revenue & Customs. HM Treasury identified the assets as available for sale and UK Government Investments (UKGI), a company wholly owned by HM Treasury, managed the sale and acted as the Department's transaction adviser.[6] Details of the management of the sale are given in Part Three of a report by the National Audit Office, *The Sale of Student Loans*, 20 July 2018.

6 National Audit Office, *The Sale of Student Loans*, 20 July 2018, HC 1385 p5

2. History of the sale of student loans

There have been three sales of the old pre-1998 mortgage style loans taken out between 1990 and 1998, all these loans have now been sold.

The sales took place in 1998, 1999 and 2013. On 25 November 2013 the Government announced that the final sale of outstanding student loans, owed by around a quarter of a million borrowers, had been completed – the sale had been made to Erudio Student Loans for £160 million.[7]

Borrowers' terms and conditions did not change as a result of any of these sales.

2.1 Sale of income contingent loans

Plans to sell off more of the loan book were announced in the **Budget 2007** and subsequently the *Sale of Student Loans Act 2008* put in place provisions to allow the sale of income contingent student loans issued between 1998 and 2012. The Explanatory Notes to the Act gave further detail on the policy.

Budget 2007

Plans for loan sell offs totalling £6 billion over the period 2008-11 were announced in Budget 2007.[8] More detail is given in the Library Research Paper *Sale of Student Loans Bill*. These plans were made before the financial crisis. The Labour Government said in late June 2009 that market conditions did not allow sales to make a good return for the taxpayer and that they would look for sale opportunities when market conditions improved.[9] In 2011 the Coalition Government announced in the Higher Education White Paper that:[10]

> We want to find a solution that will manage all current and future ICR [income contingent repayment] loans on an ongoing basis (unlike the one-off sales of the late 1990s).

Autumn Statement 2013: removal of the cap on student numbers

The intention to sell off income-contingent loans was re-iterated in the 2013 Spending Round. More detail was given in the Autumn Statement 2013. Sales of pre-2012 income-contingent loans were expected to start before the end of financial year 2015-16. These would be in a number of tranches and the estimated that gross proceeds were expected to be in the range of £10-15 billion, with a central estimate of £12 billion.

7 GOV.UK, *Sale of mortgage style student loan book completed*, 25 November 2013
8 *Budget 2007*, HM Treasury
9 HC Deb 30 June 2009 c147W
10 *Higher Education. Students at the heart of the system*, BIS June 2011 (Cm 8122)

The proceeds of the sale were said to more than cover the costs of removing the cap on student numbers from 2015-16 which was announced at the same time. The central estimates of the cash proceeds from the loan sales over five years were above the Government's estimate of the cash cost of removing the cap over the period 2013 to 2018. Thus if sales went as planned they would cover these costs, albeit for a limited time.

The Institute for Fiscal Studies made the following comments after the Autumn Statement:[11]

> …in his speech the Chancellor claimed that the additional cost of student loans arising from lifting the cap on the number of students in higher education would be "financed by selling the old student loan book". This may work in the near-term fiscal numbers, but economically it makes little sense. Selling the loan book will be broadly fiscally neutral in the long run, bringing in more money now at the expense of less money later on. Lifting the cap on numbers will cost money every year.

A report by the Business, Innovation and Skills Select Committee expressed concern about the amount which the loan sales might raise and the link between these proceeds and the expansion of student numbers:[12]

> The Government appears to have committed itself to the sale of the income contingent loans before it has fully assessed the financial viability of such a move. Demand for these assets is untested and without the introduction of a synthetic hedge would only realise around £2 billion of the £12 billion return expected by Government. While demand would increase with the introduction of a synthetic hedge, this would come with an additional long-term cost to Government, which has yet to be quantified.
>
> […]
>
> Given that the Chancellor of the Exchequer has linked the removal of the student numbers cap to the sale of the income-contingent loan-book, we seek clarification from the Department whether the removal of the cap is dependent on the sale of the loan book.
>
> If the policy is not dependent on the sale, the Government must set out in its response where it will raise the £5.55 billion between now and 2018–19 required to remove the cap without putting an additional burden on the taxpayer

2014 the policy stalls

In July 2014 the then Secretary of State was reported to have ruled out any sale of these loans (in this Parliament) because recent evidence suggested that there was "no longer any public benefit" to the sales.[13]

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11 *Autumn Statement 2013: Introductory Remarks*, IFS

12 *Student Loans*, Business, Innovation and Skills Select Committee, third report of 2014/15

13 *Student loans sell-off abandonment raises tension in cabinet*, The Guardian 20 July 2014

The coalition Government subsequently said that the expansion of student numbers had been agreed with the Treasury and "student numbers are not contingent on the sale"[14] The Government's response to the Business, Innovation and Skills Committee report on student loans reiterated this. It also added that the £5.5 billion additional loan outlays (up to 2018-19) needed for the expansion was "fully funded".[15]

The longer term fiscal impact of loan sales will be neutral if they are sold at a 'fair' price. The main effect is on timing with sales realising the value of repayments sooner rather than later.

In their long-term fiscal projections the Office for Budget Responsibility (OBR) said that so long as these loans are sold at a 'fair' value the expected return (on these assets) to the Government at the point of sale would be zero. In other words, the sale price is equal to the present value of the lost future repayments. Selling loans at a fair price would only affect the *flow* of receipts not their present value.[16]

Budget 2015

In the Summer Budget 2015 the Government stated its intention to sell the first tranche of income contingent loans by the end of 2015/16. The Spending Review and Autumn Statement 2015 put this back to 2016/17.[17]

Autumn Statement 2016

In the Autumn Statement 2016 the Government said that it intended to launch the first sale in early 2017 "subject to market conditions"[18]. The OBR's Economic and Fiscal Outlook, published alongside the Autumn Statement, said that they continued to expect that around £12 billion would be raised from the sales.

Budget 2018

In Budget 2018 the Government announced that it planned to extend loan sales by an extra year. This would take the loan sales programme to 2022-23 and increase the expected total proceeds from £12 billion to £15 billion.[19]

14 PQ HL1512 [on Higher and further education: Admissions], 11 August 2014
15 *Student Loans: Government Response to the Committee's Third Report of Session 2014-15*, BIS Select Committee second special report of session 2014-15
16 *Fiscal Sustainability Report – July 2014*, OBR p88
17 Spending Review and Autumn Statement 2015, p.74
18 *Autumn Statement 2016*, HM Treasury. para 1.66
19 *Budget 2018*, HM Treasury. para 1.57

3. February 2017 Statement: Sale of Plan 1 loans

On **6 February 2017** the Government announced in a written statement, Government Assets Sale, that it planned to sell off **pre-2012 (plan 1) loans**, specifically those issued between **2002 and 2006**:

> The Government's intention to launch this sale at this time, subject to market conditions, was set out in last year's Autumn Statement. The decision to launch this process is consistent with the Government's fiscal policy and approach to asset sales. The position of all graduates, including those whose loans are part of a sale, would also not change as a result of the sale.
>
> This Government is committed to cutting the deficit, reducing debt, and living within our means as a country. The Government's policy is to sell assets where it is value for money to do so and where there is no policy reason to continue to own them. Selling assets gives headroom for the government to invest in other policies with greater economic or social returns and reduces fiscal pressures.
>
> The Government's policies towards student finance and higher education are not being altered by this sale. Under the current system of student support (the framework for which has been in place since 2012) we will continue to offer financial support so people who have the qualifications and want to pursue higher education are able to do so, with no limit on their numbers. This is part of making sure our economy works for everyone.
>
> Students are protected by statute and completely unaffected. A sale would not alter the mechanisms and terms of repayment and sold loans would continue to be serviced by Her Majesty's Revenue and Customs (HMRC) and the Student Loans Company (SLC) on the same basis as equivalent unsold loans. These protections mean that purchasers would have no right to change any of the current loan arrangements or to directly contact borrowers.
>
> The Government has launched the first sale process on the basis there is a good prospect of achieving value for money, but will only proceed with the sale subject to market conditions and a final value for money assessment. The assessment of value for money is in accordance with the HMT Green Book framework and includes a comparison of the value of retaining the student loan book and receiving payments over time (the retention value) and receiving cash now (the proceeds of the sale).
>
> This sale will comprise the future repayments on the outstanding balances on a selection of loans, with a total face value of around £4bn. The retention value to Government is lower and is calculated using standard Treasury Green Book methodology developed for asset sales, and also accounts for Government subsidy of the student loan system. The loans which are being sold have already been in repayment for over ten years, and therefore much of the original value of the loans has already been paid back to Government.
>
> The sale process is expected to take several months. Selling the loan book involves securitising the remaining future repayments on the loans and selling securities representing the rights to these

> to a range of purchasers. The House will be informed if and when a sale is completed.

3.1 December 2017 first sale income-contingent loans completed

On 6 December 2017 the Government announced that it had completed the sale of part of the student loan book, for a tranche of loans issued by English local authorities that entered repayment status between 2002 and 2006. The sold loans were transferred to **Income Contingent Student Loans 1(2002 – 2006) Plc**, who will retain ownership of the loans for the duration.

The sale achieved **£1.7 billion** from 1.2 million loans with a face value of **£3.5 billion** held by over **400,000 borrowers**.

Soon after the sale the Government published a formal report[20]. The report set out the rationale for the sale, the objectives of the sale and the approach to the sale including the sale structure and arrangements for servicing the loans. The report also contained a value for money assessment which explained how the three key tests of value for money set out in the HM Treasury Green Book (efficient market, efficient pricing and comparison of sale price and retention value) had been met.

3.2 Cost of the sale

The cost of the sale was around **£16 million** – this was stated in an answer to a PQ on 12 March 2018:

> The advisory and transaction costs were circa £16 million from 2013/14 to the closing of the first sale in December 2017. The costs of servicing the sold loans are being charged to investors on a cost recovery basis, uprated annually in line with the retail price index. [HC Deb 12 March 2018]

A detailed breakdown of the cost was given in a PQs on 27 March 2018:

> **Students: Loans**: Written question - 134033
>
> **Peter Dowd** on: 22 March 2018
>
> To ask the Secretary of State for Education, pursuant to the Answer of 12 March 2018 to Question 131183, if he will provide a breakdown of the advisory and transaction costs in the sale of the student loan book.
>
> **Mr Sam Gyimah** on: 27 March 2018
>
> The advisory and transaction costs from 2013/14 to the closing of the sale in December 2017 are broken down in the attached table.
>
> The cost against the proceeds of the sale (£1.7 billion) is less than 1 per cent and the preparation and execution spanned five years.
>
> Advisory_and_Transaction_Costs_2013/14_to_Dec2017 (Word Document, 12.51 KB)

[20] Sale of Pre-2012 (Plan 1) Income Contingent Student Loans

3.3 Impact of sale on borrowers

The Student Loans Company website has a page ICR Debt Sale which contains information for borrowers on the effect of the sale and includes the following:

> **What this means for you**
>
> The sale means an independent Investment Company called; Income Contingent Student Loans 1(2002-2006) Plc will own your loan(s) on behalf of a number of investors.
>
> The UK Government has confirmed that:
>
> - The individual and overall repayments you make will not change as a result of the sale.
> - The way you repay your loan(s) will not change as a result of the sale.
> - The way the interest rate is calculated will not change as a result of the sale.
> - The terms and conditions of your loan(s) will not change as a result of the sale

The National Audit Office report, *The Sale of Student Loans*, 20 July 2018, made the following comment on the impact of the sale on borrowers:

> The Department is only selling the rights to the future cash flows from the loans and so borrowers will experience no change in either repayment terms or collection processes. They will have no contact with investors, and investors will pay a fee to the Department for performing the Master Servicer function. The Department distributes this fee to those performing the function. This means there is no additional privatisation benefit from the sale, as the new owners cannot invest in the asset to, for example, make collecting repayments more efficient and improve returns.[21]

[21] National Audit Office, *The Sale of Student Loans*, 20 July 2018 HC 1385, p16

4. Second sale of Plan1 loans

On 10 October 2018,[22] the Government announced the intention to proceed with the second sale of a tranche of Plan 1 loans which **entered repayment between 2007 and 2009.** These loans had a **total face value of around £3.9bn.** The sale has now been completed. These loans were transferred to Income Contingent Student Loans 2(2007 – 2009) Plc, who will retain ownership for the life time of the loans. As with the previous sale neither the investors nor Income Contingent Student Loans 2(2007 – 2009) Plc will have any rights to change the terms of the loan, including the amount repaid or when it is repaid.

A written statement[23] on 4 December 2018 said that the tranche which had a was sold for **£1.9bn** and that the sale achieved good value for money:

> This sale is good for the taxpayer. It releases money that is tied up and serving no policy purpose, to invest in other policy priorities now, whilst keeping within the spending limits we need to strengthen public finances. The sold loans have already been in repayment for over nine years, and therefore a portion of the original value has already been paid back to Government. The Government does not expect all of the remaining loans to be paid off in full and the sale guarantees money upfront today rather than waiting for fluctuating and uncertain payments over a long period of time. This sale also transfers risk to the private sector. Repayment income from student loans fluctuates with economic performance, as do tax receipts and managed expenditure like benefits. Selling the loans reduces the Government's exposure to this fluctuation. The Government is committed to reducing public sector net debt in order to enhance the UK's economic resilience, improve fiscal sustainability and lessen the debt interest burden on future generations. This sale makes a significant contribution to that objective.
>
> Government does not sell at any price. Throughout the process, Government's decision on whether to proceed remained subject to market conditions and a final value for money assessment. This looked at whether we were selling to an efficient market, that can price the asset efficiently, and at a price that was worth more to Government than retaining the loans. The Government's retention value takes into account predicted repayments, the effect of inflation, the riskiness of the asset and the opportunity cost of having money tied up in the asset.
>
> I can confirm that the price offered in aggregate across the book was above the Government's retention value range. I will shortly be laying before Parliament a report on the sale in accordance with Section 4 of the Sale of Student Loans Act 2008. This will provide more detail on the sale arrangements, and the extent to which they give good value as well as covering the sale's different fiscal impacts.

"Through the sale, the government has exchanged a stream of uncertain future cash flows spread over thirty years for a certain lump sum now"

Minister of State for Universities, Chris Skidmore, [HC Deb 11 December 2018]

22 HCWS979, Government Asset Sale, 10 October 2018
23 HCWS1137 Government asset sale update, 4 December 2018

A report on the sale arrangements and the extent to which they gave good value will be presented to parliament within three months of the date of the transfer arrangements.

5. Concerns with sales

5.1 Achieving value of money

The sale of the student loan book was delayed over concerns that the sale would not achieve value for money. The following PQ after the announcement of the sale suggested that the Government would only sell when conditions would secure value for money:

> **Students: Loans**:Written question - 65006
>
> **Asked by Steve McCabe**: 22 February 2017
>
> To ask the Secretary of State for Education, what estimate her Department has made of the effect of the vote to leave the EU on the value of the student loan book; and whether that estimate affected her decision to sell it.
>
> **Answered by: Joseph Johnson**: 27 February 2017
>
> The decision to start the sale process for the student loan book (set out in Written Statement HCWS458) was based on a robust and comprehensive assessment of the market which showed that it has a good prospect of achieving value for money.
>
> An in-depth market testing exercise suggested there was strong interest in this type of long-term, inflation-linked asset. Conditions in the equity and debt markets remain strong.
>
> The Government will continue to monitor market conditions carefully to ensure we get a fair price and secure value for money for taxpayers.

"If the rate of losses on these sales is maintained, billions of pounds of student loan losses will be crystallised without having any impact on the deficit. Its inclusion would increase the deficit as forecast by the Office for Budget Responsibility (OBR) by 13 per cent, from £45.5 billion to £51 billion"

Source: Treasury Select Committee report, *Student Loans*, February 2018 para 29

The sale of the first tranche of income contingent loans on 6 December 2017 achieved proceeds of £1.7 billion, on loans with a face value of £3.5 billion. This represented a 51 per cent reduction or write down on the face value of the loans upon sale to the market. These loans were already written down from the £3.5 billion to £2.6 billion in the Government's accounts to reflect the fact that not all would be repaid. The value of the sales was also below this lower figure of £2.6 billion. The difference between the value in the accounts and the proceeds from the sale was therefore £0.9 billion and recorded in the Department for Education's accounts as a 'loss'.[24]

£3.5 billion face value of loans sold

£2.6 billion carrying value in accounts

£1.7 billion proceeds from sale of these loans

However, the Government assessment of value for money does not compare the sale value with the figure given in the accounts, but a different value calculated using a higher discount rate.

The Government report on this sale concluded that the value achieved in the sale was above their 'retention value' and hence represented value for money. The retention value is calculated by discounting future loan repayments by the Social Time Preference Rate. The actual rate used for this sale is thought to be in the range of RPI +2.5-3.0%.[25] This is considerably higher than the rate used to calculate the 'carrying' or 'book value' of loans for Government accounts of RPI +0.7%. The lower

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24 *DfE consolidated annual report and accounts 2017 to 2018*, DfE. note 11.3
25 Critical Education Securitisation structure & loan sale value for money, Andrew McGettigan 2 January 2018

rate is meant to reflect the cost of capital (borrowing) to the Government, while the higher rate, used for these sales:[26]

> …must consider the effect of inflation, the riskiness of assets and the opportunity cost of having money tied up in an asset. The opportunity cost reflects the fact the Government must make choices between different alternatives for the use of this money, and these choices are made within a fixed spending and investment envelope.

Repayments for the loans that were sold will be spread out over the next two decades. This means that the higher discount rate 'writes down' the retention value of this asset to a large extent and, according to the Government, to a value below what was achieved in the sale.

£3.5 billion of loans were sold for **£1.7billion**. Despite this the Government said the sale represented value for money as it achieved more than their 'retention value'.

Source: Government report, Sale of Pre-2012 (Plan 1) Income Contingent Student Loans

In their latest Economic and Fiscal Outlook[27] the Office for Budget Responsibility (OBR) said that the amount raised in the first sale was around £0.7 billion less than they had assumed in earlier forecasts. They suggested this was because the initial tranche of loans that were sold were older than typical loans. This would normally make them 'lower quality' as the 'higher quality' loans are repaid more quickly and therefore the average quality falls over time. The OBR also said the 'novel nature' of the sale might have resulted in a lower price. Their forecasts now include a higher value of receipts from loan sales up to 2021-22 loan sale to meet the Government's commitment to £12 billion in sales in total.

An article in the *Financial Times* discussed the sale and raised the issue of value for money:

> The UK government has completed its biggest ever privatisation of student loans, raising £1.7bn in a process that raises questions over the valuation of tens of billions of outstanding graduate debt.
>
> The sale, which is designed to help reduce the government debt and generate value for the taxpayer, was carried out through the securitisation market, where loans are packaged together and sold on as bonds to investors.
>
> As the FT reported last week, the deal crystallises an accounting loss of close to £800m for the government. The loans are part of around £43bn of face value pre-2012 student loans on the books of the Department of Education, which were valued at around £30bn as of the end of March this year.
>
> The securitisation exceeded a different "green book" valuation which is designed to ensure the government does not sell assets too cheaply, and was a requirement for the sale to complete. The details of that calculation have not been made public.
>
> The sale marks the "creation of an efficient market for the securities", according to a statement marking the release. While there is a deep market for student loan securitisation in the US, the UK market has until now been extremely small.
>
> Securitisation allows the issuer to sell tranches of debt of varying degrees of risk. All four of the tranches in the student loans deal

26 Sale of Pre-2012 (Plan 1) Income Contingent Student Loans (para 36)
27 Para 4.164

> were oversubscribed, with the riskiest class of bonds bringing in the strongest demand.
>
> The 411,000 loans in the deal, which became eligible for repayment from 2002-2006 and are dependent on graduates earning above a certain threshold, had a face value of £3.7bn in 2015-2016, though only £3.54bn were transferred because of rules requiring the government to retain 5 per cent of the deal.
>
> Half of the borrowers entering repayment between 2002 and 2006 have already paid off their student loans by last year, meaning that the credit quality of the remaining graduates may be lower than those for more recently graduated groups of borrowers.
>
> Barclays, Credit Suisse, JPMorgan and Lloyds were on the deal.[28]

In a PQ 20 March 2018 the Minster explained how the Government assessed the value for money of the sale:

> **Students: Loans**: Written question - 133546
>
> **Angela Rayner** on: 20 March 2018
>
> To ask the Secretary of State for Education, with reference to the written statement of 6 December 2017 on Government Asset Sake, HCWS317, what assessment he has made of the net fiscal effect of the sale of the student loan book after accounting for reduced income arising from lost repayments.
>
> **Mr Sam Gyimah** on: 26 March 2018
>
> The government only sells assets when it can secure value for money for taxpayers from doing so. In assessing the value for money of the sale, the government took into account repayments foregone on the loans sold. In executing the sale, we achieved a price that exceeded the retention value of the loans sold, calculated in line with standard HM Treasury green book methodology.
>
> Selling financial assets, like student loans, where there is no policy reason to retain them, where value for money can be secured and where borrowers are not impacted is sound asset management. The sale ensures government resources are being put to best use and is an important part of our plan to repair public finances.
>
> Pursuant to Section 4 of the Sale of Student Loans Act 2008, a report on the sale arrangements was deposited in the House libraries on 7 December 2017 (deposit reference DEP2017-0778): https://www.parliament.uk/depositedpapers.

5.2 Administrative issues following previous sales

In 2013 Erudio Student Loans bought a tranche of the student loan book. Subsequently students began complaining about the handling of their loans by Erudio – this was discussed in an article in the *Guardian*, "Student loans firm Erudio leaves graduates fuming over latest error", 8 April 2016 and in the *Independent*, Erudio student loans: time to complain to the ombudsman?, 30 April 2014.

28 "UK raises £1.7bn via student loan-backed securitisation", *Financial Times*, 6 December 2017

Students complained about administrative issues with the company's handling of repayments and in particular with arrangements for deferral of payments.

6. Analysis of the sales

A number or bodies have issued reports analysing the sales and making recommendations.

Treasury Committee

The Treasury Select Committee looked at the value for money of these sales in a report *Student Loans* para 33-42.[29]The report questioned the value of the sale and made the following recommendations:

> 39. The Government is better able to manage an exposure to macroeconomic risks—such as low overall wage growth and low rates of employment—than the private sector. As a result, private sector investors require a large risk margin when taking on student loan assets from Government. The risk margin on the first student loans sale was, in aggregate, 51 per cent of the sale price.
>
> 40. **Exchanging student loans for cash does not improve the Government's financial position, it merely exchanges one asset for another. Despite this, the sale does reduce Public Sector Net Debt. Such a fiscal illusion does little to improve the Government's financial position and may in fact cost the taxpayer money**.
>
> 41. Such a high risk margin—and the fact that selling off the loans does not improve the Government's fiscal position—suggests **the Government may be better off keeping student loans on its own balance sheet, rather than shifting the risks to the private sector and paying a large premium for doing so**.
>
> 42. Whether the sale of student loans passes the Treasury's value for money test is **heavily dependent on the discount rate used to calculate the future value of student loan repayments**. As with all discount rates, there is a large margin for error. The Government has chosen a different discount rate for the purposes of the sale—a rate which places a lower value on the future repayments of the loans—than that which is used in the Department for Education Accounts. As part of its major review, the Government should consider using the same discount rate as that used in the Department for Education Accounts, as audited by the National Audit Office. (p11)

Office for Budget Responsibility

In a paper on the accounting treatment of loans the Office for Budget Responsibility made similar points to the Treasury Select Committee about the incentive for the Government to sell off loans simply because of the way they are treated in public accounts:[30]

> 3.18 For a given cohort of loans, once the write-offs have been completed the cumulative impact on PSNB [deficit] will equal the net cash position. And so, while the fiscal illusion from the capitalised interest persists for three decades, it does eventually unwind. But this is not the case if the loans are sold before the write-offs occur. **This generates a permanent illusion, as a**

[29] Treasury Committee, *Student Loans*, 6 February 2018, HC 478
[30] Office for Budget Responsibility, *Working paper No.12 Student loans and fiscal illusions*, July 2018

result of which a government can avoid ever having to recognise the cost of write-offs in the deficit.

3.19 When the government sells a tranche of student loans, it receives cash upfront in return for surrendering income streams that extend over a period of years. The cash-based PSND [national debt], with its distinction between liquid and illiquid financial assets, will be reduced at the point of sale, but will then increase relative to the path it would have taken due to the future income foregone. Whether PSND ultimately ends up higher or lower as a result of the sale will depend on the cash raised, the income foregone and the debt interest consequences. …

3.20 The PSNB [deficit] treatment of student loan sales generates a more serious fiscal illusion, so long as they take place at what is judged to be a market price. If this is the case, the inevitable (and perhaps large) discount to the nominal value is recorded as a holding loss that does not affect the deficit. This means that the deficit will be flattered by the build-up of never-to-be paid interest on the loans that are sold, but will never be hit by the write-offs that follow. As well as creating a perverse incentive for the government to sell loans, this breaks the rule that accruals adjustments should only change the timing of cash payments, not their overall value.

3.21 Student loan sales take place at steep discounts to the nominal value, largely reflecting the expectation of low recovery rates on the loans, but also relative costs of capital between the private sector buyers and the public sector seller and an additional risk premium. The expected recovery rate diminishes as the loan book matures and higher earners repay their loans. In December 2017, the Government sold a tranche of Plan 1 English student loans and achieved a price of 49 per cent of the nominal value of the loans. As the sale means that no write-offs will ever be recorded in respect of these loans, it cements a fiscal illusion in the National Accounts.

…

3.23 We estimate that the Government's plan to sell £12 billion of Plan 1 loans up to 2021-22 will ultimately deprive it of £23.0 billion of repayments over the lifetime of these loans. Including the interest saved by no longer having to finance the loans that are sold, but also the much larger loss of interest that could have been saved thanks to the income stream foregone, **we estimate that the government will lose an undiscounted £28.1 billion overall on the sales over the period until the loans would have been written off**. The TSC has noted that the value-for-money case for selling such large future income flows at a steep discount is flattered by the use of a higher discount rate than is used to value them in DfE's accounts (i.e. the rate specified in the Treasury's Green Book guidance on project appraisal). While loans may have "achieved their original policy objective" as the Government states, it is not immediately obvious why selling them at such a loss is of net benefit to the taxpayer.

House of Lords Economic Affairs Committee

A report by the House of Lords Economic Affairs Committee in June 2018 suggested that the priority of the sales was the reduction of the national debt rather than achieving value for money:

369.Why was the Government prepared to make a sale at such a large loss? **It prefers cash today over a larger sum of cash tomorrow. This preference is a result of another of the Government's targets: to reduce the national debt**. The present Government is aiming to see the national debt (referred to as 'public sector net debt') falling as a percentage of GDP by 2020/21.

370.When student loans are issued, the value of the loan is added to the national debt. When repayments on the loans are made, the national debt is reduced accordingly. If the loans are sold, the value of the sale is taken off the national debt. As repayments of the loans takes place over 30 years, the national debt is reduced much more quickly by selling the loans, even at a substantial loss.

371.For the Government to sell assets such as student loans, the sale must pass HM Treasury's value for money test. The test is skewed to reflect the Government's preference for cash today: a sale can pass this test despite it taking place at a price far below the value the Government itself places on the asset.[31]

National Audit Office

In July 2018 the National Audit Office published an investigation into the recent sale to assess whether value of money was achieved. The report, *The sale of student loans*,[32] stated that the sale had showed up limitations around how the Government assessed value for money and costs with regard to student loans, but concluded that **the sale had achieved value for money**:

20. The sale of student loans was conducted under government's policy to sell assets where there is no policy reason for continued public ownership. In this context UKGI prepared well for the sale, creating a structure which encouraged investor interest and maintained competitive tension during the process. The value of the loans is subject to a high level of uncertainty, but UKGI's estimates of what investors would pay were reasonable, and **the sale achieved prices at the upper end of these estimates. In terms of the preparation, process and proceeds of the transaction itself UKGI has achieved value for money**.

21. But the sale of student loans also shows limitations in the way that government assesses value for money and measures for the costs of student loans over time. The Department uses one set of assumptions for the cost of student loans when they are added to government's balance sheet, and HM Treasury uses another set of assumptions in support of its decision to sell them. This offers two different ways of calculating the subsidy to, and value of, its rapidly growing student loan portfolio. The two approaches give different answers which risks government: not knowing with enough certainty the cost to the taxpayer of student loans when they are issued; and of selling assets too cheaply relative to their long-term value despite achieving its objective of reducing public sector net debt.

31 House of Lords Economic Affairs Committee, *Treating Students Fairly: The Economics of Post-School Education*, 11 June 2018, HL Paper 139

32 National Audit Office, *The Sale of Student Loans*, 20 July 2018, HC 1385

Public Accounts Committee

In November 2018 the Public Accounts Committee issued a report, Sale of student loans,[33] the report was critical of the sales:

> **The Treasury and the Department for Education have not made clear how this transaction decreases the long-term risk to the public finances**. This first sale is part of a series designed to de-risk public finances and reduce public debt without affecting borrowers, however there does not seem to be a long-term strategy. The government's current plan is simply to achieve sale proceeds of around £12 billion by 2022 for loans issued before 2012—this focusses only on debt reduction. In the first sale, it achieved this debt reduction by selling the rights to an estimated £3.3 billion of future repayments for a £1.7 billion lump sum now. But it is an example of selling off assets for short-term capital gain, without demonstrating how the deal is in the best long-term interests of the taxpayer given the scale of future repayments that has been sacrificed. Government's own analysis suggests that, had it not sold the loans, it would have recouped the £1.7 billion in only eight years, and a further £1.6 billion over the next 25 years. Of all the student loans government has issued, the ones before 2012 are more likely to be repaid, and therefore represented a lower risk to public finances.

"The government's objective to reduce 'public sector net debt', as with previous asset sales, runs the risk of being prepared to sell at any price"

Public Accounts Committee, *Sale of student loans*, 22 November 2018

The report also contained the following conclusions:

- The uncertainty over future repayments undermines the government's ability to accurately value the loan book
- In deciding whether to sell, Treasury does not take sufficient account of a range of valuations, instead relying on a conservative 'retention value
- We are concerned about the lack of transparency to the public and Parliament surrounding this sale.

33 Public Accounts Committee, *Sale of student loans*, 22 November 2018, HC 1527

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