



CHAPTERSIX

Student Loan Scheme Financial Statements

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for the Year Ended 30 June 2008

6.0 Financial statements for the year ended 30 June 2008

The financial statements for the Student Loan Scheme comprise schedules of revenue and expenditure, assets and cash flows relating to student loans. The Ministry of Social Development (MSD) and the Inland Revenue Department (IRD) administer student loans on an agency basis within policy parameters set by the Ministry of Education (MOE), on behalf of the Crown.

The financial information represents extracts from the financial statements of Crown activities carried out by the entities administering student loans to provide an overview of the Student Loan Scheme.

The schedule of assets shows a total asset value as at 30 June 2008 of \$6,741 million (\$6,011 million at 30 June 2007).

6.1 Schedule of revenue and expenditure for the year ended 30 June 2008

Table 22 Schedule of revenue and expenditure for the year ended 30 June 2008

Actual 2007 \$ million		Actual 2008 \$ million	Main Estimates 2008 \$ million	Supp. Estimates 2008 \$ million
Revenue				
359.5	Interest unwind	407.3	400.9	414.2
91.3	Interest income	-	-	-
8.7	Administration fees - MSD	8.6	9.4	8.7
459.5	Total revenue	415.9	410.3	422.9
Expenditure				
151.1	Impairment	(230.6)	19.6	260.0
487.5	Fair value write-down on new borrowings	486.7	495.4	486.7
638.6	Total expenditure	256.1	515.0	746.7
(179.1)	Net surplus/(deficit)	159.8	(104.7)	(323.8)

- The accompanying accounting policies and notes on pages 52 to 54 form part of these financial statements.
- Budget figures represent the combined total for the applicable agencies.
- For a full understanding of the Crown's financial position and the results of its operations for the year, reference should be made to the consolidated audited Financial Statements of the Government, for the year ended 30 June 2008.
- Details of the consolidated movements schedule for the year ended June 2008 are shown in Note 1 on page 53.

6.2 Schedule of assets as at 30 June 2008

Table 23 Schedule of assets as at 30 June 2008

Actual 2007 \$ million		Actual 2008 \$ million	Main Estimates 2008 \$ million	Supp. Estimates 2008 \$ million
Current assets				
1,129	Student loans	630	871	1,109
1,129	Total current assets	630	871	1,109
Non-current assets				
4,882	Student loans	6,111	5,381	5,169
4,882	Total non-current assets	6,111	5,381	5,169
6,011	Total assets	6,741	6,252	6,278

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- Details of the consolidated movements schedule for the year ended June 2008 are shown in Note 1 on page 53.

6.3 Schedule of cash flows for the year ended 30 June 2008

Table 24 Schedule of cash flows for the year ended 30 June 2008

Actual 2007 \$ million		Actual 2008 \$ million	Main Estimates 2008 \$ million	Supp. Estimates 2008 \$ million
Cash flows – operating activities				
<i>Cash was provided from:</i>				
37.5	Interest repayments received	-	-	-
37.5	Net cash inflow from operating activities	-	-	-
Cash flows – investing activities				
<i>Cash was provided from:</i>				
517.9	Capital repayments received	628.9	621.3	610.9
<i>Cash disbursed for:</i>				
(1,175.9)	New borrowings	(1,200.5)	(1,268.4)	(1,216.2)
(658.0)	Net cash outflow from investing activities	(571.6)	(647.1)	(605.3)
(620.5)	Net cash outflow	(571.6)	(647.1)	(605.3)

- The accompanying accounting policies and notes on pages 52 to 54 form part of these financial statements.
- Budget figures represent the combined total for the applicable agencies.
- For a full understanding of the Crown's financial position and the results of its operations for the year, reference should be made to the consolidated audited Financial Statements of the Government, for the year ended 30 June 2008.
- Details of the consolidated movements schedule for the year ended June 2008 are shown in Note 1 on page 53.

6.4 Statement of accounting policies for the year ended 30 June 2008

Reporting entity

The scheme is a Crown activity which forms part of the consolidated Financial Statements of the Government. The scheme has dimensions of revenue, expenditure, assets and cash flows within the overall Financial Statements of the Government.

Statutory authority

The Student Loan Scheme is administered jointly by the Ministry of Education, Inland Revenue and the Ministry of Social Development, under the Student Loan Scheme Act 1992. Also relevant to the administration of the scheme are the Credit Contracts and Consumer Finance Act 2003 and the Education Act 1989.

Budget figures

The budget figures are those presented in the Budget Night Estimates (Main Estimates) and those amended by the Supplementary Estimates (Supp. Estimates) and any transfer made by Order in Council under section 26A of the Public Finance Act 1989. The budget figures provided are extracted from the details of the Estimates of Appropriation for Inland Revenue and the Ministry of Social Development, as applicable. The totals shown are the combined totals for the applicable agencies.

Financial instruments

Student loans are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are recognised initially at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method, plus or minus any impairment movement. Fair value on initial recognition is determined by projecting forward the expected repayments required under the scheme and discounting them back at an appropriate discount rate. The difference between the amount lent and fair value is expensed on initial recognition.

The subsequent measurement at amortised cost is determined using the effective interest rate calculated at initial recognition.

The effective interest rate discounts estimated future cash flows through the expected life of the loan to the net carrying amount of the loan, excluding future credit losses. Interest is recognised on the loan evenly in proportion to the amount outstanding over the period to repayment.

Allowances for impairment are recognised when there is objective evidence that the loan is impaired. Impairment movements are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the loan, and that the event (or events) has an impact on the estimated future cash flows of the student loan book that can be reliably measured.

The measurement of impaired value can result in an increase or decrease in the carrying value of the student loan book.

Interest

Interest is calculated on the nominal student loan account balances on a daily basis at a rate determined by the government, currently 6.7 percent per annum. Interest is charged to both New Zealand-based borrowers and overseas-based borrowers, however, there is a concurrent write-off by Inland Revenue for New Zealand-based borrowers under the interest-free policy.

Credit risk

For the Student Loan Scheme, credit risk is the risk that borrowers will default on their obligation to repay their loans or die before their loan is repaid, causing the scheme to incur a loss.

The Student Loan Scheme policy does not require borrowers to provide any collateral or security to support advances made. As the total sum advanced is widely dispersed over a large number of borrowers, the Student Loan Scheme does not have any material individual concentrations of credit risk.

The credit risk is reduced by the collection of compulsory repayments through the tax system.

Interest rate risk

Interest rate risk is the risk that the value of financial instruments will fluctuate due to changes in interest rates. Changes could impact on the return on loans advanced. The interest rate and the interest write-off provisions attached to student loans are set by the government.

Changes in accounting policies

There have been no changes in the student loan accounting policies applicable to the preparation of financial statements of Crown activities administered by the Ministry of Social Development and Inland Revenue for Crown consolidation, from those used in the previous year. All accounting policies have been applied on a basis consistent with the previous year.

6.5 Notes to the financial schedules for the year ended 30 June 2008

Note 1: Consolidated movements schedule for the year ended 30 June 2008

Table 25 Consolidated movements schedule for the year ended 30 June 2008

Consolidated Actual 2007 \$ million		Consolidated Actual 2008 \$ million	Inland Revenue 2008 \$ million	Ministry of Social Development 2008 \$ million
9,412.7	Nominal loan balance ⁴⁹	9,573.2	8,552.6	1,020.6
(3,401.7)	Adjustment due to initial fair value recognition and impairment	(2,831.9)	(2,512.3)	(319.6)
6,011.0	Total student loans	6,741.3	6,040.3	701.0
5,569.2	Student loans opening balance	6,011.0	5,429.2	581.8
-	Borrowings transferred from Ministry of Social Development to Inland Revenue	-	1,118.6	(1,118.6)
-	Fair value write-down on borrowings transferred	-	(454.6)	454.6
1,175.9	Amount borrowed in current year	1,200.5	-	1,200.5
(487.5)	Fair value write-down on new borrowings	(486.7)	-	(486.7)
8.7	Administration fees on loans made in current year	8.6	-	8.6
(555.4)	Repayments made in current year	(628.9)	(550.0)	(78.9)
450.8	Interest on impaired student loans	407.3	361.2	46.1
0.4	Small balance write-offs	(1.1)	(1.1)	-
-	Impairment losses reversed	230.6	137.0	93.6
(151.1)	Impairment	-	-	-
6,011.0	Student loans closing balance	6,741.3	6,040.3	701.0

⁴⁹ The nominal loan balance for 2008 excludes accrued interest whereas in the prior year the nominal balance included accrued interest of \$493 million. Accrued interest is written off each year when certain criteria are met.

Note 2: Recognition

Student loan nominal value

The nominal balance is the total obligations that borrowers have including loan principal, interest and penalties. The change in nominal value from year to year reflects the net growth of the portfolio through new lending less repayments and other adjustments such as write-offs due to deaths and bankruptcies. The nominal balance is the basis for other values such as the carrying value and fair value.

In the current year there has been a change to the way the nominal balance has been stated. Previously, accrued interest (some due to be written off under the interest-free policy) has been included in the total. From 2008 onwards this accrued interest is excluded.

Student loan carrying value

Student loans are initially recognised at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method less any impairment loss.

Fair value on initial recognition of student loans is determined by projecting forward expected repayments required under the scheme and discounting them back at an appropriate discount rate. The subsequent measurement at amortised cost is determined using the effective interest rate calculated at initial recognition. This rate is used to spread the interest income across the life of the loan and determines the loan's carrying value at each reporting date.

The valuation model has been adapted to reflect current student loan policy. The carrying value is also sensitive to changes in a number of underlying assumptions, including future income levels, repayment behaviour and macroeconomic factors such as inflation. The significant assumptions are shown below.

Table 26 Significant assumptions at 30 June

	2008	2007
Carrying value		
Effective interest rate ⁵⁰	8.44%	7.12%
Interest rate applied to loans for overseas borrowers	6.7%-6.8%	6.7%-7.2%
Consumers price index	2.5%-4.0%	2.4%-2.6%
Future salary inflation	3.5%-4.7%	3.4%-3.6%
Fair value		
Fair value (\$000)	5,521	5,443
Discount rate	9.19%	8.17%
Impact on fair value of a 1% increase in discount rate (\$000)	(321,000)	(232,000)
Impact on fair value of a 1% decrease in discount rate (\$000)	366,000	258,000

Source: Inland Revenue.

The data for the valuation of student loans has been integrated from files provided by Inland Revenue, the Ministry of Social Development and the Ministry of Education. The current data is up to 31 March 2007 and contains information on borrowings,

repayments, income, educational factors, and socio-economic factors, amongst others, and has been analysed and incorporated into the valuation model. The integrated data has been supplemented by less detailed, but more recent, data to value student loans at balance date.

Given the lead time required to compile and analyse the detailed integrated data and its availability for use in the valuation model, it is expected that there will always be a 15-month lag between the integrated dataset and the valuation reported in the annual financial statements.

Student loan fair value

Fair value is the amount for which the loan book could be exchanged between knowledgeable, willing parties in an arm's-length transaction as at 30 June 2008. It is determined by discounting the estimated cash flows at an appropriate discount rate. The estimated fair value of the student loan debt at 30 June 2008 has been determined to be \$5,521 million (\$5,443 million at 30 June 2007).

Fair values will differ from carrying values due to changes in market interest rates, as the carrying value is not adjusted for such changes whereas the fair value was calculated using a discount rate that was current at 30 June 2008. At that date, the fair value was calculated on a discount rate of 9.19 percent, whereas, a weighted average discount rate of 6.56 percent was used for the carrying value. The difference between fair value and carrying value does not represent an impairment of the asset.

Note 3: Reconciliation of impairment allowance account

Table 27 Reconciliation of impairment allowance account at 30 June

Impairment allowance account	2008 \$ million	2007 \$ million
Balance at beginning of year	533	382
Impairment losses recognised on receivables	-	151
Impairment losses reversed	(230)	-
Balance at end of year	303	533

Source: Inland Revenue.

50 This is the weighted average of effective interest rates that apply to the cohorts of borrowers who borrow for the first time in each financial year.