

Accounting for Federal Student Loan Costs

Q. The student loan industry is claiming that “cash accounting” shows that guaranteed loans are cheaper than the federal budget indicates. Is that analysis correct?

A. No, it is a distortion. Budget and accounting experts agree that “cash” accounting is not appropriate for a loan program because costs occur sporadically and need to be accounted for over the long term. The correct approach—according to guidance from the commissions and agencies that set accounting rules for the private and public sectors—is to use “present value” accounting methods.

According to the U.S. General Accounting Office (GAO):

“Estimating the costs of federal credit programs, over their lifetime, on a net present value basis when the loans are made is more meaningful because it provides transparency regarding the government’s total estimated subsidy costs rather than recognizing these costs sporadically on a cash basis over several years as payments are made and receipts are collected.”

Prior to budget reforms, “for loan guarantees, since budget authority and costs were recorded only when defaults occurred, no costs were recognized when the guarantees were made, despite the fact that the guarantees were likely to entail future losses related to borrower defaults. **This cash basis distorted costs and did not recognize the economic reality of the transactions.**” [emphasis added]

According to the Federal Accounting Standards Advisory Board:

“Since budgetary resources for direct loan and loan guarantees are provided on a present value basis, financial reporting on the acquisition, use, and status of the resources should be on the same basis. Only by using the same basis can financial information be used to compare the actual results with the budget. Indeed, **distortion would result if present value were not used to report direct loans or loan guarantees** that are budgeted on a present value basis.” [emphasis added]

Q. Some people say that there are hidden costs of direct lending that aren’t captured in the budget figures. Is that true?

A. No, there are no “hidden costs.” According to GAO, auditors determined that the Education Department’s “estimates of the subsidy costs for both FDLP and FFELP were reasonable in the context of the financial statements taken as a whole.” Audit guidelines require agencies to use actual program experience as primary guidance in new and revised estimates of future program performance. If anyone had found any scandalous losses in the direct loan program, it would be reflected in the budget figures. There is nothing to the “hidden costs” claims.

--Robert Shireman