National Audit Office

Report
by the Comptroller
and Auditor General

HM Treasury, Department for Business, Energy & Industrial Strategy, British Business Bank plc

Investigation into the Bounce Back Loan Scheme

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Investigation into the Bounce Back Loan Scheme

Report by the Comptroller and Auditor General

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Comptroller and Auditor General
National Audit Office

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This investigation looks at government's Bounce Back Loan Scheme (the Scheme). It describes the Scheme's purpose and how it functions; performance to date; and how government manages the associated value-for-money risks.

Investigations

We conduct investigations to establish the underlying facts in circumstances where concerns have been raised with us, or in response to intelligence that we have gathered through our wider work.

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Contents

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This report can be found on the National Audit Office website at www.nao.org.uk

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What this investigation is about

1 This investigation is one of a series of National Audit Office (NAO) reports considering government's response to the COVID-19 pandemic. In our first report we summarised government's main actions in England across five areas: health and social care; emergency responses; support for individuals; support to businesses; and other support schemes, including international aid.[1] This investigation focuses on the Bounce Back Loan Scheme (the Scheme), one specific measure government took to support businesses.

2 On 27 April 2020, the Chancellor of the Exchequer (the Chancellor) announced the Scheme to provide a "simple, quick, easy solution for those in need of smaller loans", aimed at the smaller end of small- and medium-sized enterprises (SMEs). The Scheme provides registered and unregistered businesses with loans of up to £50,000, or a maximum of 25% of annual turnover, to maintain their financial health during the pandemic. The Scheme complements two others launched earlier: first, the Coronavirus Business Interruption Loan Scheme (CBILS), followed by the Coronavirus Large Business Interruption Loan Scheme (CLBILS), both support SMEs and large businesses to access loans, overdrafts and other types of finance.

3 The Chancellor initiated the Scheme after businesses criticised CBILS for the strict eligibility criteria, which created a backlog of applications for the smaller end of the SME market. The Scheme's design focused on decreasing the time between application and payment of loans, which was a concern for businesses. The Scheme achieved this by removing administrative complexities inherent in a loan application process. It reduced the complexity, in part, by removing credit and affordability checks required under the Consumer Credit Act.

1 Comptroller and Auditor General, *Overview of the UK government's response to the COVID-19 pandemic*, Session 2019–2021, HC 366, National Audit Office, May 2020.

4 The Scheme launched on 4 May and will be open until 30 November, with government retaining the right to extend the Scheme. The loans are provided by commercial lenders (for example, banks, building societies and peer-to-peer lenders) directly to businesses, who are expected to repay the debt in full. Failure to do so may have a negative impact on their credit score and may affect their ability to borrow in the future. Government provides lenders a 100% guarantee against the loans (both capital and interest). This means if the borrower does not repay the loan, government will step in and repay the lender. The loans have a fixed interest rate of 2.5% and a maximum length of ten years; in the first year of the loan there are no capital repayments due, and government pays the interest – making it interest-free for the borrower. HM Treasury data shows that as of 6 September, the Scheme delivered more than 1.2 million loans to businesses, totalling £36.9 billion.

5 HM Treasury developed the Scheme with the Department for Business, Energy & Industrial Strategy (the Department) and the British Business Bank (the Bank). HM Treasury, in conjunction with the Department, identified the need and set the Scheme policy and overarching terms, such as the interest rate and 100% guarantee. HM Treasury is also involved in Scheme implementation and monitoring. The Bank, established to help finance markets work better for small businesses across the UK, was involved in the Scheme's design and is responsible for its implementation. It delivers the loans under the Scheme via a network of accredited lenders and it is responsible for the Scheme's ongoing administration, in consultation with HM Treasury and the Department. The Bank is fully owned by the Department, which has a wider policy responsibility for business and enterprise.

6 The Department's accounting officer (AO) sought a Ministerial Direction before the Scheme's launch. A ministerial direction is requested when an AO, usually a permanent secretary, believes that a spending proposal breaches any of the following criteria: regularity; propriety; value for money; or feasibility. Based on the AO's assessment there was a strong case for government intervention; however, the level of risk and uncertainty associated with the Scheme meant a direction was necessary on all four criteria. On 1 May, the Secretary of State for Business, following approval from the Chancellor, directed the AO to proceed with the Scheme. The Bank, which administers the Scheme on behalf of the Department, raised similar concerns in a Reservation Notice to the Department's AO and received a written direction to proceed with the Scheme on 3 May.

Scope of the report

7 The report focuses on this Scheme as it is government's largest and most risky business loan support scheme. It provides a factual overview of the government's actions and covers:

- how the Scheme was developed, what it aims to achieve and how it is managed (Part One);
- the Scheme details and how it performed to date (Part Two); and
- the main Scheme risks (Part Three).

8 The report does not assess the value for money of the Scheme, as loan repayments will not start until May 2021 and there is not yet enough information on the Scheme's costs and benefits. The report only focuses on the Scheme; other business loan support schemes such as CBILS and CLBILS are featured only for comparative purposes and to provide context. The report does not assess the impact of changes to consumer protection legislation under the Consumer Credit Act which reduce administrative complexities.

9 On 24 September, the Chancellor announced changes to the Scheme. The changes relate primarily to loan duration and how borrowers can repay. According to HM Treasury's 'Winter Economy Plan', the Scheme will now offer borrowers "more time" and "more flexibility" for loan repayments under its 'Pay as you Grow' option. At the time of writing this report, limited details of the changes were available. We have reflected the high-level announcement in our descriptions of the Scheme (paragraph 1.5 and Figures 1 and 3), but the effect of the changes has not been considered further in the report.

10 Both HM Treasury and the Bank collect Scheme performance data. These two datasets differ in the type of data and from when this was first collected. Our report draws on both datasets: HM Treasury's for aggregate Scheme performance up to 6 September; and the Bank's for more detailed analysis of individual loans up to 7 September. As a result, not all figures in our report reconcile owing to the difference in the timing and content of the two datasets. More information on the limitations of these data can be found in our methodology appendix.

Summary

Key findings

Scheme performance

11 **The Department and the Bank expect the Scheme to have lent between £38 billion to £48 billion by 4 November 2020, substantially more than it initially expected.** The three business loan support schemes have provided around £55.3 billion in loans between March and September. This is close to the total lent to small- and medium-sized enterprises (SMEs) in all of 2019 (£57 billion). HM Treasury data shows that at 6 September, the Scheme had approved more than 1.2 million loans to businesses, totalling £36.9 billion. By 10 May, the end of the first week of operation, 268,000 loans totalling £8.4 billion were approved, increasing to £21.3 billion and 699,000 loans by the end of the first month. When launched, the Department and the Bank expected Scheme take-up of between £18 billion and £26 billion (paragraphs 2.2 to 2.4, and Figures 7 and 8).

12 **As of 7 September, around 90% of the loans under the Scheme went to very small (micro) businesses located across the UK.** Micro businesses (turnover below £632,000) received £29.4 billion from 1,039,000 loans. Sole traders, a legal form that small businesses can take, received £6.4 billion from 297,000 loans, representing 18% of the total support by value. Most of those receiving support were also private limited companies (75% of the total support by value). The geographic distribution of the loans across the UK is in line with the overall distribution of business. A split by industry shows that real estate, professional services and support activities received the largest amount of support from the Scheme – £8.5 billion from 283,000 loans (paragraphs 2.7 to 2.10 and Figures 10, 11, 12 and 13).

13 **Based on HM Treasury data, lenders approve loans for existing business customers within 24 to 72 hours but approval times for new customers take substantially longer.** Lenders are expected to approve and make payment of loans within 24 hours, or in some cases 48 hours if further anti-fraud checks are required. The approval time applies only to existing business customers. Neither HM Treasury nor the Bank monitor lenders' approval time for existing personal customers or new customers. Feedback from lenders during the design process indicated that applications by existing personal customers would take between two and four days to complete if applicants were able to provide the necessary information. Recent feedback from two large lenders indicates that existing personal customer processing times may take longer than anticipated at launch and new customers may take between four and 12 weeks to process. This is because of the volume of applications, and COVID-19-related operational constraints. The volume of lending under the schemes exceeded the average monthly lending activity in pre-COVID-19 times (paragraphs 1.8 and 2.5).

Scheme set-up and administration

14 **The Scheme was launched within two weeks of the Chancellor of the Exchequer (the Chancellor) proposing it to the Department and the Bank, but without detailed objectives.** The Chancellor proposed the Scheme on 21 April, and it was launched 4 May. The Scheme was launched quickly to address businesses and trade bodies' concerns that some of the smallest businesses had acute cash flow issues and were struggling to access finance. According to a survey conducted by the Association of Chartered Certified Accountants in mid-April, one-third of businesses would probably not be able to access enough cash to last more than two weeks of lockdown. Owing to the pace of the Scheme's launch, HM Treasury did not produce a business case; the Scheme also lacked clear objectives beyond the aim of fast financial support for smaller SMEs, which makes measuring the Scheme's success a challenge (paragraphs 1.2 to 1.4, 1.11 and Figures 5 and 6).

15 **The Scheme has less strict eligibility criteria than CBILS and CLBILS, to improve quick access to finance for smaller SMEs. This increases credit and fraud related risks.** The Scheme facilitates faster lending, removing credit and affordability checks by banks and allowing businesses to self-certify their application documents. The application process requires businesses to confirm they are impacted by COVID-19 and are able to repay the loan. Lenders are required to conduct anti-fraud, anti-money laundering and 'know your customer' checks on loan applications. The Bank takes assurance from lender accreditation due diligence and post-accreditation audits that lenders comply with the Scheme rules. To help lenders mitigate fraud risks, the Bank established fraud prevention forums with a wide group of stakeholders to share best practice and aid implementation of additional fraud measures (paragraphs 1.6 and 1.7 and Figures 1, 2 and 4).

16 The Bank was able to have a reporting system in place at launch and it took about a month to fully operationalise it. The reporting system (the portal) allows the Bank to collect the data needed to administer guarantees in the event of borrower default. It was not designed to monitor risks or prevent fraud in real-time, with lenders performing checks. While the portal was in place at Scheme launch, automatic reporting was not; this meant lenders had to manually upload data on individual applications, which was a slow process owing to their volume. In order to assist with Scheme monitoring, HM Treasury put in place a database collecting daily reports directly from lenders, but at an aggregate level only. The Bank implemented automated reporting by mid-June, which allowed lenders to provide data in bulk. However, the information held on the Bank's and HM Treasury's systems do not reconcile owing to the time and type of data collected (paragraphs 1.12 to 1.14).

17 The Bank was not able to prevent duplicate applications across lenders for the first month of the Scheme. The Bank highlighted in its Reservation Notice that there was not enough time to agree with lenders a methodology to prevent duplicative applications before launch. The Bank worked with lenders and counter-fraud groups to develop this methodology and it was implemented on 2 June, almost one month after the Scheme's launch. The Bank and the Department identified, based on a fraud organisation's estimate, that up to 2.3% of approved applications were duplicates before the solution went live (paragraphs 1.13 and 3.3 to 3.6).

18 The Bank's preliminary assessment of the administrative costs of the three COVID-19 business loan support schemes is £75 million by the end of 2024-25. The assessment suggests a cost of £20 million for the year ending 2020-21. This includes the Bank's own delivery costs, mainly staff, as well as external advisers and outsourced operations, such as reconciling interest payments. The cost does not include the Department and HM Treasury's costs. The Bank explained to us that many costs, like the outsourced operations or the portal, are interlinked and allocation between the schemes is difficult. Based on the Bank's current cost allocation between the schemes, it estimates the Scheme's cost to total £9 million by the end of 2020-21 and £32 million by the end of 2024-25. The Bank's estimates are highly likely to change as the level and scope of activities are uncertain and will only become clearer after May 2021 when borrowers start repaying loans (paragraphs 2.13 and 2.14).

19 The Department estimates that offering the loans interest-free for the first year will cost around £1 billion. Under the Scheme terms, government pays the borrower's interest costs for the first 12 months directly to the lender. This payment is a grant and excludes any capital repayments. After the first year, borrowers will need to make repayments (capital and interest) up to the end of the loan, in line with their arrangement with their lender. As of September 2020, the Bank estimates the cost of covering borrowers' first years' interest to be £1,068 million; this will rise as more loans are issued (paragraph 2.15).

Value-for-money risks

20 Credit risk: The Scheme has a low level of credit and customer checks, increasing the likelihood of some businesses not being able to repay loans and therefore leading to taxpayer losses. A credit risk is the risk that an eligible borrower does not repay a loan. The Scheme relies on businesses self-certifying application details with limited verification and no credit checks performed by lenders for existing customers. New customers or existing personal account customers may generate additional credit and customer checks depending on the lender's business processes. The lower level of customer checks increases the speed of delivery. According to the Department, "the fact that businesses that were unviable before COVID-19 may be able to access the Scheme owing to the absence of external credit checks, [...], creates significant risks around value for money, propriety and potentially regularity ..." (paragraphs 1.6, 1.7, and 3.2, and Figure 2).

21 Fraud risk: Government recognises that the decision to provide funds quickly leaves taxpayers exposed to a significant residual fraud risk, even after lenders have implemented mitigation strategies. Fraud results from dishonesty which can be a false representation or a failure to disclose information with the intention to cause financial gain or loss such as applications by ineligible businesses. The Bank assessed the Scheme risks before launch, and instructed PricewaterhouseCoopers LLP to conduct a risk review. The review found that, while some risks can be mitigated, there remains a "very high" level of residual fraud risk. Based on feedback from lenders, the adviser summarised the residual external fraud risk causes as: self-certification; multiple applications; lack of legitimate business; impersonation; and organised crime. The nature of the Scheme places the main responsibility for managing fraud risk on the lenders as part of the loan approval process. To support lenders in managing fraud-related risks, the Bank established fraud prevention forums with the lenders and a wider group of stakeholders, to share best practice and aid implementation of additional fraud measures. From October 2020, the Bank, alongside the Department and lenders, will utilise the reporting portal (paragraph 16) to provide a monthly fraud report. This will provide details on: prevented loss; detected loss; errors; and recoveries. The Cabinet Office's Government Counter Fraud Function believes fraud losses are likely to be significantly above the general estimates of public sector fraud levels of 0.5% to 5%. The fraud risks were also highlighted in, and contributed to, the Bank's Reservation Notice and the Department's request for a ministerial direction (paragraphs 1.7, 3.3 to 3.6 and Figure 4).

22 As a result of credit and fraud risks, the Department and the Bank's preliminary central estimate is that 35% to 60% of borrowers may default on the loans but the estimate is highly uncertain. Government's default estimates at Scheme launch ranged between 30% and 75%. The latest estimates, including those including those by the Bank and the Office for Budget Responsibility, have widened to between 15% and 80% depending on the UK's economic performance. According to the Bank, credit and fraud risks are interrelated and therefore it did not assess them separately. The Department's 2019-20 annual report and accounts highlights likely total credit and fraud losses of between 35% and 60%, based on historic losses observed in prior programmes which most closely resemble the Scheme. Assuming the Scheme lends £43 billion, this would imply a potential cost to government of £15 billion to £26 billion. However, actual losses may differ from those forecast and indications of the extent of credit losses and fraudulent applications will not become apparent until borrowers are due to start repaying their loans. Loan repayments begin from 4 May 2021 as government is paying interest on all loans for the first 12 months (paragraph 3.7 and Figure 16).

23 Recovery process: Loans are likely to be written off more quickly than for other COVID-19 related business loan support schemes, but HM Treasury has not finalised yet how lenders should collect overdue loan repayments. Lenders are required to pursue "appropriate recovery processes" in line with their existing standards under the terms of the guarantee agreement. The Scheme terms give lenders a 12-month time limit after they have issued a formal demand on the borrower to pursue outstanding amounts. However, claiming on the government guarantee is not conditional on having completed the recoveries process – lenders are able to make a claim on the government guarantee "within a reasonable time period" following the first formal demand date, or sooner, if lenders believe "no further payment is likely". Government provides a 100% guarantee to lenders owing to the absence of credit checks, but this reduces the lenders' incentives to recover money from borrowers. Moreover, the Scheme does not include actions to recover outstanding debt after the 12-month time limit, for example by requiring lenders to continue recovery processes in exchange for a fee. The recovery process has been agreed with lenders on a principles-level and HM Treasury expects to agree specific operational details by winter 2020-21 (paragraphs 1.15, 1.16, 3.8 and 3.9).

24 Crowding out: The five largest UK lenders provided the largest share of loans under the Scheme, increasing their foothold in the SME lending market; this risks having a negative impact on competition. The Bank's data shows that the five largest UK lenders (Barclays, HSBC, Lloyds/Bank of Scotland, NatWest/RBS and Santander) provided £31.3 billion of loans under the Scheme, while the remaining 18 lenders were responsible for £3.9 billion. The five largest UK lenders are responsible for 89% of the value of the loans distributed. The Bank of England estimates the total SME debt to be £167 billion, with the big banks accounting for 65% of this lending. The Bank and the Department raised concerns that the Scheme's terms are making it uncompetitive for smaller lenders to compete with incumbents, which in turn has a negative impact on competition in the SME lending sector. One of the Bank's key objectives is to help create a more diverse finance market for smaller businesses, with a greater choice of options and providers. The Bank is seeking to mitigate this risk by broadening the number of lenders under the Scheme. The Scheme had seven accredited lenders at launch and had 23 by 18 September 2020 (paragraphs 2.11, 3.10 to 3.12 and Figure 14).

Concluding remarks

25 Once government decided to support small businesses facing cash flow problems owing to the pandemic, it moved very quickly to set up a scheme. It prioritised one aspect of value for money – payment speed – over almost all others and has been prepared to tolerate a potentially very high level of losses as a result. These losses can stem from businesses wanting to pay back loans but finding themselves unable to, through to organised criminals taking out loans with no intention of ever paying them back. The Scheme achieved its initial objective of quickly supporting small businesses, but a lack of more detailed Scheme-specific objectives will make it difficult to measure its ultimate success. Systems and processes have evolved since the Scheme launch but much hard work remains over the coming months and years to ensure that the risks to value for money are minimised. This work must include implementing a robust debt collection plan with lenders and fraud investigation arrangements. Government should also take this opportunity to consider now the controls it would put in place to protect against fraudulent abuse for any future schemes.

Part One

Introduction to the Bounce Back Loan Scheme

1.1 This part provides a description of the key terms of the Bounce Back Loan Scheme (the Scheme) in the context of the other COVID-19 loan schemes. It provides an overview of the roles and responsibilities of the parties involved in the Scheme, and a timeline of the main events.

Business loan support schemes

1.2 On 11 March 2020, the Chancellor of the Exchequer (the Chancellor) announced the Coronavirus Business Interruption Loan Scheme (CBILS) in response to the economic challenges businesses faced as a result of the COVID-19 outbreak. CBILS launched on 23 March, offering financial support to small- and medium-sized enterprises (SMEs) across the UK that were losing revenue and seeing their cashflow disrupted. On 20 April, the Coronavirus Large Business Interruption Loan Scheme (CLBILS) was launched, targeting large businesses with turnover beyond the £45 million CBILS threshold (**Figure 1** on pages 14 and 15).

1.3 After CBILS's launch, businesses and trade bodies raised concerns that some of the smallest businesses had acute cash flow issues and were still struggling to access finance. A survey conducted by the Association of Chartered Certified Accountants and the Corporate Finance Network of 9,000 accountants in mid-April revealed that one-third of businesses "will probably not be able to access the cash they need to last more than two weeks of lockdown". Through CBILS, access to loans below £25,000 was particularly difficult owing to consumer protection legislation. The Consumer Credit Act demands that lenders conduct client and affordability checks for borrowers who are not legal entities; considering the economic uncertainty owing to the pandemic, it is challenging to assess whether loans are affordable.

1.4 As a result, on 27 April, the Chancellor announced the Scheme. The Scheme aims to complement the existing business loan support schemes, CBILS and CLBILS, enabling more businesses, especially sole traders, to access support. Figure 1 provides a comparison of the key terms of the three schemes.

Figure 1
COVID-19 business loan support schemes

A comparison of the key terms of the three business loan support schemes

	Bounce Back Loan Scheme	Coronavirus Business Interruption Loan Scheme	Coronavirus Large Business Interruption Loan Scheme
Launch date	4 May 2020	23 March 2020	20 April 2020
Eligibility	No business size restrictions. Must not be in a restricted sector. Businesses self-certify that they were not a 'business in difficulty' on 31 Dec 2019; not bankrupt; in liquidation; or in a similar situation. Applicant must be carrying on business on 1 March 2020.	Maximum turnover £45 million. Must not be in a restricted sector. Must have a borrowing proposal that the lender would consider viable under normal circumstances.	Minimum turnover £45 million. Must not be in a restricted sector. Must have a borrowing proposal that the lender would consider viable under normal circumstances.
Use of proceeds	Businesses self-certify that they will use the loan only to provide economic benefit to the business, and not for personal purposes.	Lenders check that the loan is for a suitable business purpose.	Applicants provide a 'borrowing proposal' for which lenders believe the finance will enable the business to trade out of any short-to medium-term difficulty. Companies borrowing more than £50 million will be subject to further restrictions on dividend payments, senior pay and share buy-backs.
Support offered per company	Up to 25% of turnover or a maximum loan of £50,000 (minimum of £2,000).	£50,001 to £5 million.	Up to £200 million.
Interest rate	2.5% fixed per annum.[1] Government pays first year of interest.[1]	Interest rate varies by lender. Government pays first year of interest and fees.	Interest rate varies by lender.
Repayment period	Six years, starting after the first year; option to extend to 10 years.[1]	Up to six years.	Up to three years.
Finance Type	Term loans.	Term loans, overdrafts, invoice finance, and asset finance.	Term loans, overdrafts, invoice finance, and asset finance.
Early repayment	Free of charge.	Varies by lender.	Varies by lender.
Government guarantee	100%	80%	80%

Figure 1 *continued*
COVID-19 business loan support schemes

Notes

1 On 24 September, the Chancellor of the Exchequer announced changes to the Bounce Back Loan Scheme terms, including the end date of the Scheme. Changes also include flexibility for the borrowers in difficulty to take payment holidays, temporarily pay only the interest on the loans, or extend the repayment period.

2 Restricted sectors are banks, building societies, insurance companies, public-sector organisations and state-funded primary and secondary schools. Lenders may apply additional business sector restrictions if part of their overall business strategy.

3 Companies can only access one of these schemes.

4 This table is a summary of the scheme terms. Full details can be found here:

https://www.british-business-bank.co.uk/ourpartners/coronavirus-business-interruption-loan-schemes/bounce-back-loans/

https://www.british-business-bank.co.uk/ourpartners/coronavirus-business-interruption-loan-scheme-cbils-2/

https://www.british-business-bank.co.uk/ourpartners/coronavirus-business-interruption-loan-schemes/clbils/

Source: British Business Bank

1.5 On 24 September, the Chancellor launched the 'Winter Economy Plan', which included an extension of the Scheme's end date and term changes. The Scheme will offer borrowers "more time" and "more flexibility" for loan repayments under its 'Pay as you Grow' option. According to HM Treasury, all borrowers under the Scheme will be allowed to extend the term of the loan to 10 years, temporarily move to interest-only payments for a limited time, and take repayment holidays. The objective of these changes is to reduce the size of the regular repayments by extending the repayment time. Applications under the Scheme have been extended from 4 November to 30 November.

1.6 The Scheme has less strict eligibility criteria than CBILS and CLBILS, to improve access to finance for small businesses. The Scheme facilitates faster lending by removing credit and affordability checks required under the Consumer Credit Act and allowing businesses to self-certify their application documents. As part of an application, businesses are required to confirm they have been impacted by COVID-19 and that they are able to repay the loan. Lenders are not required to verify the self-certified details of applicants. As lenders are not allowed to assess whether customers are able to repay the loans, government provides a 100% guarantee to the lenders: if the borrower defaults on the loan, the lender can recover the funds from government through the guarantee.

1.7 The Scheme allows lenders to verify application details as they "see fit" but there are no requirements to do so. Lenders may cancel loans if they have found applicants breach Scheme eligibility criteria; if such a cancellation occurs, government will not be obliged to make any payments to the lender in respect of the guarantee. Lenders are required to conduct anti-fraud, anti-money laundering and 'know your customer' checks on all loan applications. The British Business Bank's (the Bank's) accreditation process for lenders and post-accreditation audits gives it assurance that lenders have the appropriate controls in place to complete these checks (see **Figure 2**). To support lenders to manage fraud-related risks, the Bank established fraud prevention forums with a wide group of stakeholders, to share best practice and aid implementation of additional fraud measures.

Figure 2

Approval checks conducted by lenders on the COVID-19 business loan support schemes

The Bounce Back Loan Scheme removed some approval checks to facilitate faster lending

Type of checks	Bounce Back Loan Scheme	Coronavirus Business Interruption Loan Scheme	Coronavirus Large Business Interruption Loan Scheme
Anti-fraud	✔	✔	✔
Anti-money laundering	✔	✔	✔
Know-your-customer (ID verification)	✔	✔	✔
Business viability	✗	✔	✔
Loan affordability	✗	✔	✔
Supporting documentation	✗	✔	✔
Self-certification	✔	✗	✗

Note

1 Lenders also conduct transaction monitoring, as usual, for all schemes.

Source: HM Treasury

1.8 Lenders are expected to approve and make payment of loans within 24 hours, or in some cases 48 hours if further fraud checks are required. The Chancellor highlighted speed of delivery as a key requirement of the Scheme when it was announced to ensure that small firms who need vital cash injections can keep operating. The approval time only applies to existing business customers. Under the terms of the Scheme there is no designated timeline for existing personal or new customers and lenders will follow their standard business procedures, which may include additional credit and fraud checks.

1.9 Internationally, governments have introduced and extended measures to incentivise commercial banks to expand their lending to SMEs. The table overleaf provides a summary overview of key terms of schemes in Germany and Switzerland. We chose Germany and Switzerland as comparators because the Chancellor used these as exemplar schemes. These schemes support small SMEs with simplified application procedures without credit checks and provide a 100% guarantee to lenders. However, unlike the UK, the schemes do not rely fully on self-certification, and require banks to check application details. The schemes are also more restrictive in the way loans can be used (**Figure 3** overleaf).

Roles and responsibilities

1.10 Officials from HM Treasury, the Department for Business, Energy & Industrial Strategy (the Department) and the Bank worked together to design and get the Scheme up and running. The Bank delivers the Scheme through private sector lenders. The roles and responsibilities of the key parties involved in the Scheme are described in **Figure 4** on page 19.

Scheme objectives

1.11 HM Treasury did not develop a business case for the Scheme, which means, at its launch the Scheme lacked clear objectives beyond the aim of fast financial support for smaller SMEs. In order to allow effective appraisal, planning, monitoring and evaluation, the Bank developed objectives after the Scheme launch, in consultation with HM Treasury and the Department. The Bank combined the objectives for the three COVID-19 debt programmes because of the similarity of the objectives to provide financial support in the form of loans. The Bank felt it was not "proportionate [...] to produce a unique set of objectives for each product" owing to the likely evolution of the three programmes, together with the uncertain economic outlook. HM Treasury, the Department and the Bank agreed the objectives on 15 July. The Department and the Bank told us that they are in the process of developing metrics for measuring the performance of the individual loan support schemes (**Figure 5** on page 20).

Figure 3

International comparisons of business loan support schemes

International comparators are similar to UK's Bounce Back Loan Scheme but contain more detailed application checks and are more restrictive in the use of proceeds

	Germany	Switzerland	United Kingdom
Name of scheme	KFW-Schnellkredit 2020[1]	COVID-19 Kredit[1]	Bounce Back Loan Scheme
Target companies	Businesses with more than 10 employees and which have been incorporated before 1 Jan 2019. Aims to support businesses impacted by COVID-19 but not a legal requirement.	Small- and medium-sized businesses (SMEs) domiciled in Switzerland which are financially sound but have been impacted by COVID-19.	No business size restrictions. Business has been carrying on business on 1 March 2020. Businesses impacted by COVID-19.
Scheme details	Up to 25% of turnover up to €800,000 (€500,000 for SMEs with up to 50 employees). 3% interest on loans. Up to 10-year term including a two-year grace period.	Up to 25% of turnover up to CHF500,000. 0% interest on loans. Up to five-year term.	Up to 25% of turnover or a maximum loan of £50,000 (minimum of £2,000). 2.5% fixed per annum (government pays first year of interest fees).[3] Six years, starting after the first year; option to extend to 10 years.[3]
Government guarantee	100%	100%	100%
Start date	15 March 2020	25 March 2020	4 May 2020
End date	31 December 2020	31 July 2020	30 November 2020[3]
Use of proceeds	Investments (except for financial investments). Operating expenses (including interest payments and repayments). But no debt refinancing, limitation on dividends and payments to board members and chief executive officer.	Operating expenses. But no debt refinancing, investments and limitation on dividends.	Businesses self-certify that they will use the loan only to provide economic benefit to the business, but loan contract contains no specific restrictions.
Application checks	Banks check application details (turnover, number of employees, profit in 2019 or 2017–2019 in total) and anti-fraud checks. They do not conduct credit checks but check for negative entries on the applicant's credit record.	Banks use automated systems to check application details (for example, turnover) and anti-fraud checks but do not conduct credit checks. Multiple applications are checked centrally.	Banks carry out know-your-customer, anti-fraud and anti-money laundering checks but do not conduct credit checks for approval purposes.

Notes

1 KFW-Schnellkredit is based on KfW's website information (https://www.kfw.de/PDF/Download-Center/F%C3%B6rderprogramme-(Inlandsf%C3%B6rderung)/PDF-Dokumente/6000004525_M_078.pdf and https://www.kfw.de/PDF/Download-Center/F%C3%B6rderprogramme-(Inlandsf%C3%B6rderung)/PDF-Dokumente/6000004524_F_078_ergaenzende_angaben_schnellkredit.pdf).

2 COVID-19 Kredit is based on the Swiss Ministry of Finance's website (https://www.admin.ch/opc/de/official-compilation/2020/1077.pdf and https://www.efd.admin.ch/efd/de/home/covid19-ueberbrueckungshilfe/faq.html).

3 On 24 September, the Chancellor of the Exchequer announced changes to the Bounce Back Loan Scheme terms, including the end date of the Scheme. Changes also include flexibility for the borrowers in difficulty to take payment holidays, temporarily pay only the interest on the loans or extend the repayment period.

Source: National Audit Office analysis

Figure 4
Roles and responsibilities for delivering the Bounce Back Loan Scheme (the Scheme)

The government utilises arm's-length bodies and private organisations to deliver the Scheme

Stakeholder	Description
HM Treasury	HM Treasury initiated the Scheme and, in conjunction with the Department for Business, Energy & Industrial Strategy (the Department) and the British Business Bank (the Bank), set the policy and designed the Scheme. HM Treasury collects and publishes Scheme data. It also leads the discussion with lenders on finalising the operational guidance in relation to the debt recovery process under the Scheme.
Department for Business, Energy & Industrial Strategy	The Department is the Bank's sole shareholder and has a wider policy remit for business and enterprise. As sole shareholder, its accounting officer is ultimately responsible for the three COVID-19-related business support schemes and issued the Written Direction to the Bank to pursue the Scheme.[1]
British Business Bank	The Bank is the Department's delivery partner for the loan schemes (via lenders). The Bank helped design the Scheme and is responsible for its administration and implementation, in consultation with HM Treasury and the Department. The Bank delivers the loans via a network of accredited lenders.
Lenders	Accredited lenders review applications and provide loans to borrowers. Lenders are responsible for conducting the required anti-fraud, anti-money laundering and 'know your customer' checks prior to loan approval.
Other organisations involved in fraud-related checks	The Bank coordinates with lenders and fraud-related organisations to mitigate fraud, including: • **Cabinet Office** – Leads the Government Counter Fraud Function and works closely with the Bank and lenders to tackle fraud. • **National Crime Agency** – Investigates and prosecutes the most serious fraud cases such as those involving serious or organised crime and terrorist groups. • **National Investigation Service (NATIS)** – NATIS is a law enforcement body specialising in financial crime and fraud, mostly at a local authority level. NATIS will investigate and prosecute medium/high severity fraud cases, supported by the Crown Prosecution Service. • **Insolvency Service** – Investigates and prosecutes breaches of company legislation and other criminal offences on the Department's behalf. • **Companies House** – The UK's registrar of companies; can share company data to enable better identification of fraudulent applications. • **UK Finance** – A trade association for the banking and finance industry. • **Counter-Fraud organisations** – There are several nationally recognised organisations that allow lenders to check loan applications for fraud. Under the terms of the Scheme, each lender must use a reputable counter-fraud organisation to screen for fraud at the application stage.

Note

1 The three COVID-19-related business support schemes are: the Coronavirus Business Interruption Loan Scheme, the Coronavirus Large Business Interruption Loan Scheme and the Bounce Back Loan Scheme.

Source: Department for Business, Energy & Industrial Strategy

Figure 5
Objectives for the three COVID-19 business loan support schemes

The loan guarantee schemes have seven overarching objectives, split into short-, medium-, and long-term[1]

	Objective
Short term (COVID-19 restrictions place significant limits on business operations)	**1** Guarantee schemes complement other government support and initiatives. **2** Unlock finance at scale and pace such that businesses disrupted by COVID-19 still have access to finance.
Medium term (COVID-19 restrictions lifted)	**3** Businesses receive the maximum opportunity to maintain liquidity until lockdown measures are lifted (given what was known about the pandemic at the scheme launch date). **4** Scheme design should incentivise appropriate risk-taking by lenders.[2]
Long term (over the life of the loan)[3]	**5** Debt structure should take account of long-term business survival. **6** Debt structure should allow firms with long-term growth potential to continue to grow. **7** Long-term economic benefits realised from 5) and 6) exhibit value for money against any government-incurred losses.

Notes

1 The three COVID-19-related business support schemes are: the Coronavirus Business Interruption Loan Scheme, the Coronavirus Large Business Interruption Loan Scheme and the Bounce Back Loan Scheme.

2 'Appropriate' will vary across the three business loan support schemes.

3 The long-term objectives are subject to subsequent or further rounds of government support initiatives and policy direction.

Source: British Business Bank

Scheme launch and subsequent events

1.12 The Chancellor launched the Scheme on 4 May, within two weeks of proposing it to the Department and the Bank. The Bank was able to move quickly because it amended the reporting system (the portal) of an existing programme (Enterprise Finance Guarantee scheme) to support the Scheme.[2] In its Reservation Notice, the Bank raised concerns around the "compressed timetable" which has created "huge operational challenges for delivery partners".[3] The Bank explained that given the pace at which decisions were being made, it would not be feasible to put in place "robust controls and governance" to ensure public funds are used appropriately. The Department recognised the restrictions and limitations imposed on the Bank in its Ministerial Direction to proceed with the Scheme on 3 May. The Department recognised the restrictions and limitations imposed on the Bank in its Ministerial Direction to proceed with the Scheme on 3 May (**Figure 6** on pages 22 and 23).

2 Government-backed debt finance for viable smaller businesses lacking security, launched in 2009. At the March Budget 2020 it was announced that this programme would be suspended and replaced by the Coronavirus Business Interruption Loan Scheme.

3 The Bank's Reservation Notice is similar to an accounting officer's request for a ministerial direction. It is a statement from the Bank to the Department to outline any concerns it has with a specific policy. In this case, the relevant grounds were: propriety; value for money; and feasibility.

1.13 The Reservation Notice highlights, given the speed of delivery, that it was not possible to agree with lenders a methodology to prevent duplicative applications at launch, and incorporate this in the Scheme legal agreement. The structure of the Scheme means that lenders initially had no way of identifying multiple applications made across lenders.[4] While lenders were not required to identify duplicate applications under the Scheme terms, the Bank worked with lenders and counter-fraud groups to develop this methodology and it was implemented on 2 June. Prior to this, the Bank and the Department identified, based on a fraud organisation's estimate, that up to 2.3% of approved applications were duplicates.

1.14 The Bank's reporting portal (paragraph 1.12) was designed to allow the Bank to collect loan-level data to administer guarantees in the event of borrower default. While the portal was in place at Scheme launch, it could not consolidate the activities of lenders on a daily basis, such as the number of borrowers and the borrower information. This is because automated reporting was not yet available, requiring lenders to upload data on individual loans manually, rather than in bulk. Manually uploading the data was a slow process owing to the volume of applications. In order to assist with Scheme monitoring HM Treasury put in place a database collecting daily reports directly from lenders, and both HM Treasury and the Bank monitored the activity levels. The Bank finalised the amendments to the existing system by mid-June, while HM Treasury continues to collect data and monitors the overall lending activities of lenders. The information held on the Bank's and HM Treasury systems does not reconcile (see Appendix One for further information).

1.15 The Scheme is underpinned by a legal agreement between the Bank and the lenders setting out the contractual terms and conditions, and a lenders' manual which provides operational guidance on administering the Scheme. According to the Bank it followed its standard principles-led approach, in which the details of a scheme's operational guidance evolve in accordance with the principles laid out in the legal agreement. At Scheme launch there were three areas where operational guidance needed to be agreed with the lenders: how the guarantee would work in practice; the recovery process, if the loans were in default; and how lenders' compliance with the terms of the Scheme might be audited.

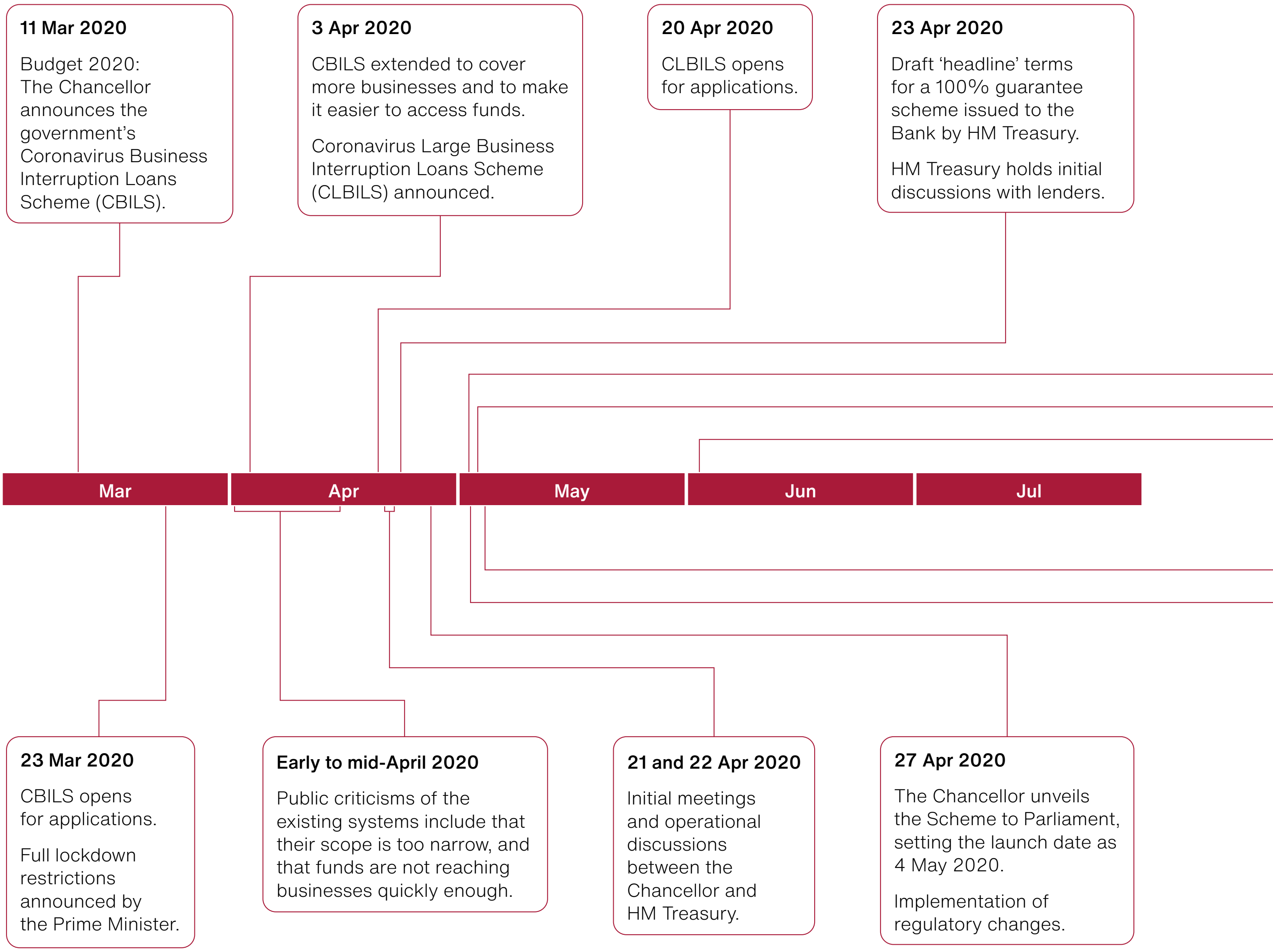
1.16 HM Treasury is leading the work on the recovery process and the Bank on the other two. HM Treasury and the Bank expect to complete the recovery and guarantee work by winter 2020-21 to allow time for lenders to put it into operation and communicate with borrowers ahead of the first repayments on loans, which are due from May 2021. The Bank has completed how lenders are audited and the audits started in September 2020.

4 The Scheme is being delivered by accredited lenders who assess each application independently of one another.

Figure 6

Timeline of events for the Bounce Back Loan Scheme (the Scheme)

The Scheme was launched on 4 May 2020, less than two weeks after the Chancellor of the Exchequer (the Chancellor) proposed it to the Department for Business, Energy & Industrial Strategy (the Department) and the British Business Bank (the Bank)



Source: National Audit Office analysis of HM Treasury, British Business Bank and Department for Business, Energy & Industrial Strategy documents

1 May 2020

The Chancellor provides the Department with final approval to introduce the Scheme.

The Department's accounting officer (AO) writes to the Bank's AO instructing him to continue with preparations.

2 May 2020

The Bank's AO writes to the Secretary of State for Business setting out the Bank Board's reservations.

3 May 2020

The Department's AO issues written direction to the Bank to implement the Scheme, on behalf of the Secretary of State.

4 May 2020

Scheme launched.

Bank of England confirms the Prudential Regulation Authority's regulatory treatment of the Scheme.

The Financial Ombudsman and the Financial Conduct Authority exchange letters outlining the regulatory implications of the Scheme and their respective responses.

The Bank puts portal in place.

2 Jun 2020

The Bank implements a multiple application check.

Aug | Sep | Oct | Nov | Dec | 2021

24 Sep 2020

The Chancellor announces changes to the Scheme. The Scheme's end date for new loan applications is extended from 4 November to 30 November.

30 Nov 2020

The Scheme closes for new applications. Existing applications can be processed up to 31 December 2020.

4 May to 31 Dec 2021

Borrowers commence interest and capital repayments on the loans.

Part Two

Scheme performance

2.1 This Part looks at the performance of the Bounce Back Loan Scheme (the Scheme). This includes: the number and value of loans provided; how they are distributed by business type, size and geographical location; the number of accredited lenders involved; the loan approval processing time; and the Scheme's costs.

2.2 There are three business loan support schemes which have provided a total of 1.3 million loans worth £55.3 billion by 6 September. HM Treasury data shows that the Scheme is the largest of the three, providing £36.9 billion – 67% of the total loans by value (**Figure 7**). The aggregate value of loans provided under the three schemes between March and September is close to the total lending to small- and medium-sized enterprises (SMEs) in 2019, which amounted to £57 billion.[5] The average monthly lending to SMEs in 2019 was £4.5–5 billion.

2.3 The purpose of the Scheme is to provide fast-track financial support for small businesses and in the first week of operation 268,000 loans were approved, totalling £8.4 billion. Within the first month this increased to £21.3 billion (699,000 loans) representing more than 58% of the outstanding amount as of 6 September (**Figure 8** on page 26). The volume of loan approvals has been faster compared to both the Coronavirus Business Interruption Loan Scheme (CBILS) and the Coronavirus Large Business Interruption Loan Scheme (CLBILS), which approved 19,000 and 154 loans respectively in the first month of operation. More than 80% of loan applications have been approved under the Scheme, which is higher than both CBILS and CLBILS (48% and 57% respectively).[6]

2.4 At launch, the Department for Business, Energy & Industrial Strategy (the Department) and the British Business Bank (the Bank) expected the Scheme to support 800,000 to 1,200,000 businesses with between £18 billion and £26 billion loaned. They currently estimate the amount to reach between £38 billion and £48 billion by 4 November.

5 Coronavirus Large Business Interruption Loan Scheme provides lending to businesses with a turnover above £45 million, and therefore may include businesses which are above the size threshold of SME businesses of £500 million.

6 The approval percentage has been calculated by using HM Treasury data on applications received and applications approved. The received application data include all applications approved, in progress, withdrawn, or declined.

Figure 7
Number and value of loans provided by the three COVID-19 business support schemes

The Bounce Back Loan Scheme is the largest of the three COVID-19-related schemes

Business loan support scheme[1]	Total number of loans provided[2]	Total value of loans (£bn)[2]
Coronavirus Business Interruption Loan Scheme	63,647	14.6
Coronavirus Large Business Interruption Loan Scheme	553	3.8
Bounce Back Loan Scheme	1,222,548	36.9
Total	**1,286,748**	**55.3**

Notes

1 The Coronavirus Business Interruption Loan Scheme, Coronavirus Large Business Interruption Loan Scheme and Bounce Back Loan Scheme were launched on 23 March 2020, 20 April 2020 and 4 May 2020 respectively.

2 Figures as at 6 September 2020.

Source: National Audit Office analysis of HM Treasury scheme data

Loan approval processing time

2.5 Under the terms of the agreement with lenders, loan applications should be approved, with the money provided to borrowers, within 24 hours, or in some cases 48 hours.[7] Based on lenders' reports to HM Treasury, the average application time for existing business customers was between 24 and 72 hours. Neither HM Treasury, nor the Bank, monitor lenders' approval time for existing personal customers and new customers. Feedback from lenders during the design process indicated that applications by existing personal customers would take between two and four days to complete if applicants were able to provide the necessary information. Recent feedback from two large lenders indicates that existing personal customer processing times may take longer than anticipated at launch and for new customers it may take between four and 12 weeks. This is because of the volume of applications, and COVID-19 related operational constraints.[8]

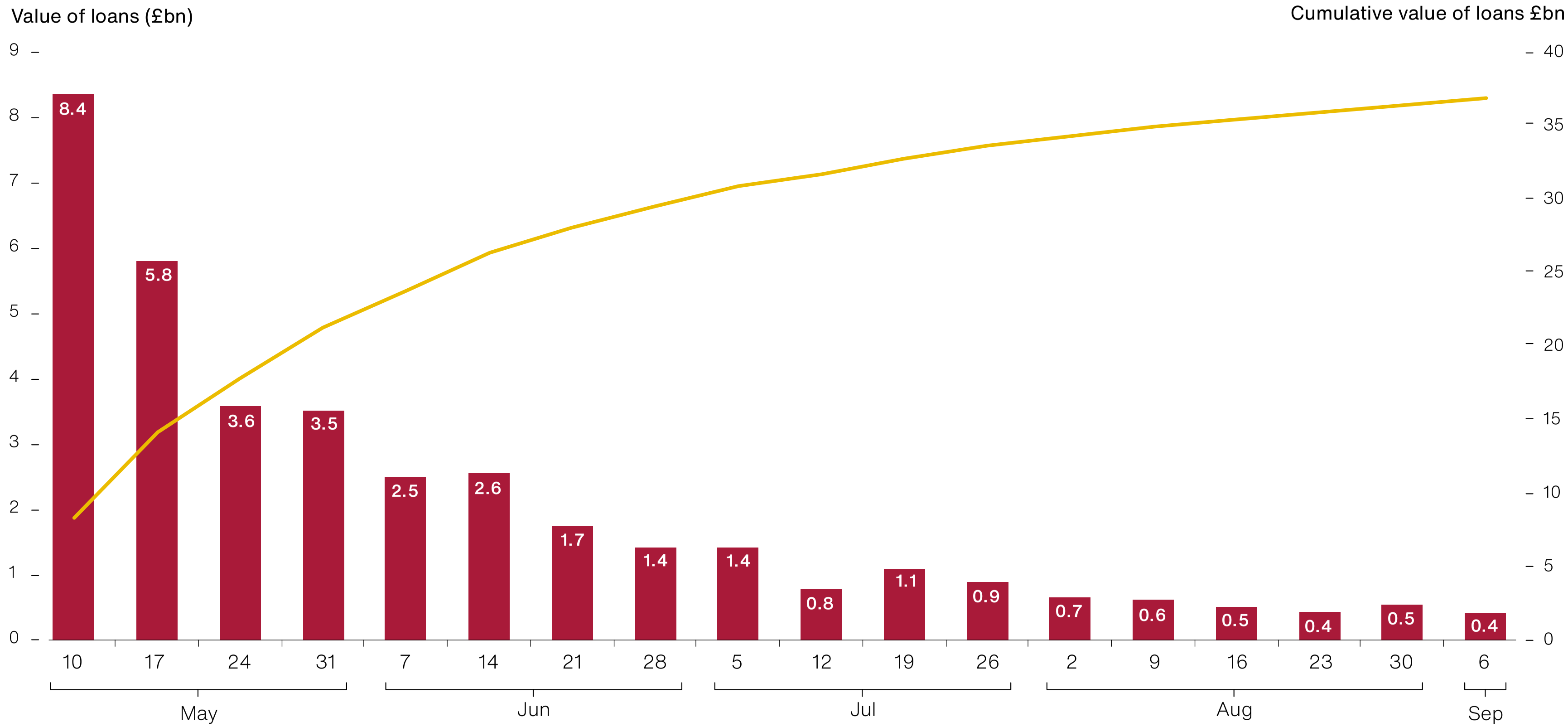
7 If a potential fraud risk is identified with an application, the loan should be approved within 48 hours to allow for additional manual checks to be carried out.

8 We undertook a survey of 15 lenders under the Scheme and received 10 responses (see Appendix One). The responses include four of the five largest UK lenders – of these, three provide loans to new customers although one of them has only accepted applications from a small number of business clients. Based on the other two lenders (representing 36% of all loan applications drawn (by number) under the Scheme), the time required to open a new account ranges between four and 12 weeks.

Figure 8

Value of loans provided per week since the launch of the Bounce Back Loan Scheme (the Scheme)

In the four months since the Scheme's launch, £36.9 billion of loans have been provided to businesses[1]



Notes

1 The Scheme was launched on 4 May 2020.

2. Figures as at 6 September 2020.

Source: National Audit Office analysis of HM Treasury scheme data

Scheme figures

2.6 **Figure 9** overleaf provides a summary of the number and value of bounce back loans. The average loan under the Scheme is £30,343, with 35% of loans by number being at the Scheme's maximum of £50,000.

2.7 Around 90% of loans were provided to micro businesses, defined by Companies House as having an annual turnover below £632,000 (**Figure 10** on page 29), which is in line with the Scheme aim of providing financial support to smaller SMEs. More than 70% of all loans were received by businesses with an annual turnover below £250,000 (£20.7 billion from 850,000 loans).

2.8 Three-quarters of the total support was provided to private limited companies, which received £26.5 billion from 793,000 loans. Sole traders received £6.4 billion from 297,000 loans, representing almost one-fifth of the total support (**Figure 11** on page 30). More than one-third of bounce back loans were received by businesses that have been operating for more than four years.

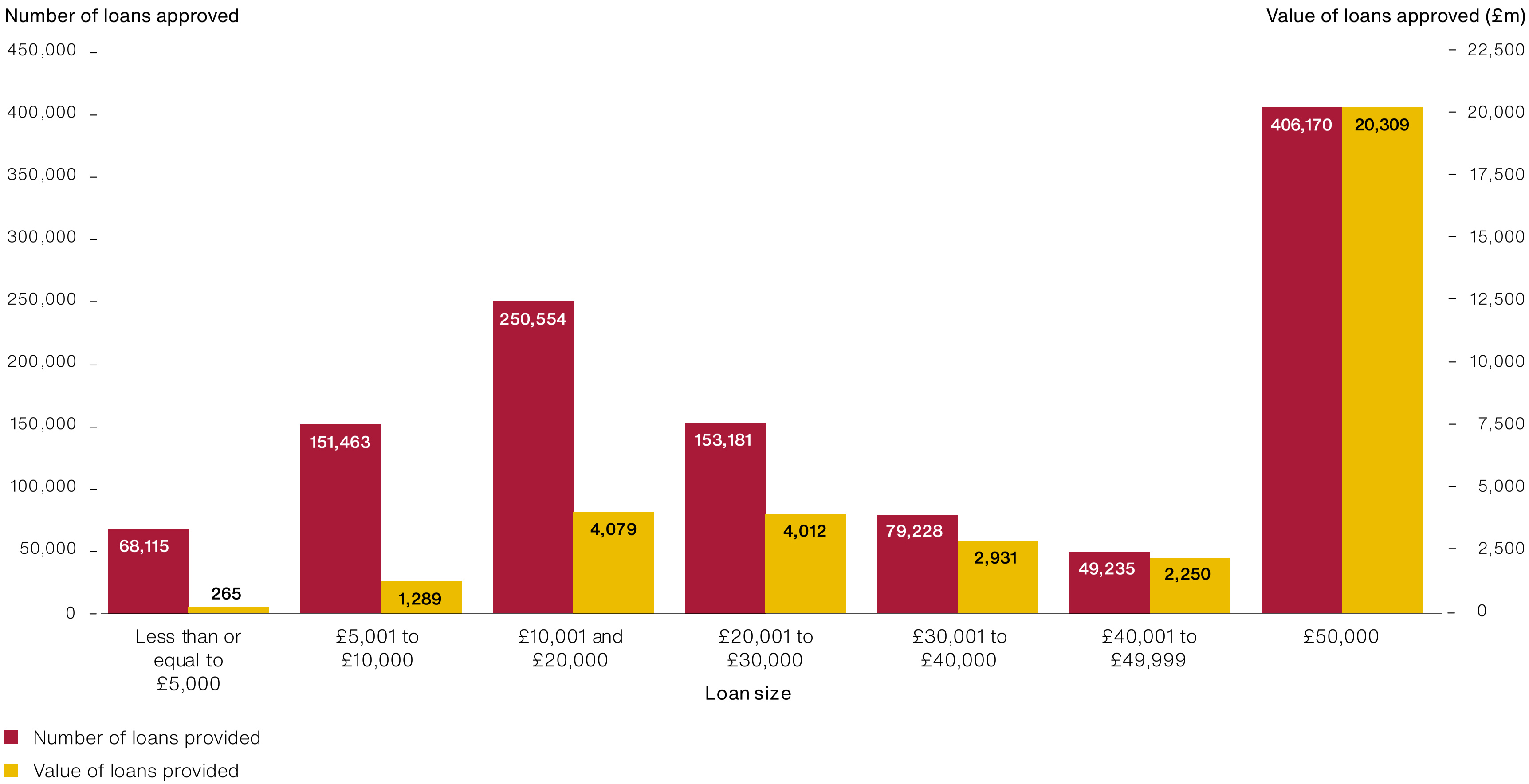
2.9 The geographic distribution of the businesses supported by the Scheme is in line with the overall distribution of businesses in the UK (**Figure 12** on page 31). For example, businesses in London, which represent 19% of the total UK SME population, received 20% of loans (235,000 loans).

2.10 A split by industry sector shows that real estate, professional services and support activities received the largest support by value and number of loans from the Scheme, at £8.5 billion (24% of the total by value) from 283,000 loans. The construction sector received the second highest number of loans, receiving £5.7 billion from 193,000 successful applications. The accommodation, wholesale and retail trade, construction, transport, manufacturing and recreational sectors all have a higher proportion of loans under the Scheme compared with their pre-COVID borrowing levels (**Figure 13** on pages 32 and 33).

Figure 9

Number and value of loans provided by the Bounce Back Loan Scheme (the Scheme), grouped by loan size

Most loans are at the maximum value of £50,000



Notes

1 Loans are capped at 25% of turnover or a maximum of £50,000. The minimum loan value is £2,000.

2 Figures as at 7 September 2020.

Source: British Business Bank data

Figure 10

Total value and number of loans provided by the Bounce Back Loan Scheme (the Scheme), by business size

Micro businesses received the highest number of loans (1,038,662) at a value of £29.4 billion

Business size	Total value of loans provided (£m)	Total number of loans provided
Micro[1]	29,437	1,038,662
Small	5,471	113,849
Medium	107	2,575
Mid-sized	115	2,739
Large	5	121
Total	**35,135**	**1,157,946**

Notes

1 Business sizes are defined by turnover: micro businesses have a turnover below £632,000; small businesses have a turnover between £632,000 and £10.1 million; medium businesses are between £10.2 million and £24.9 million; mid-sized businesses have a turnover between £25 million and £500 million; and large business have a turnover greater than £500 million.

2 The Scheme was launched on 4 May 2020.

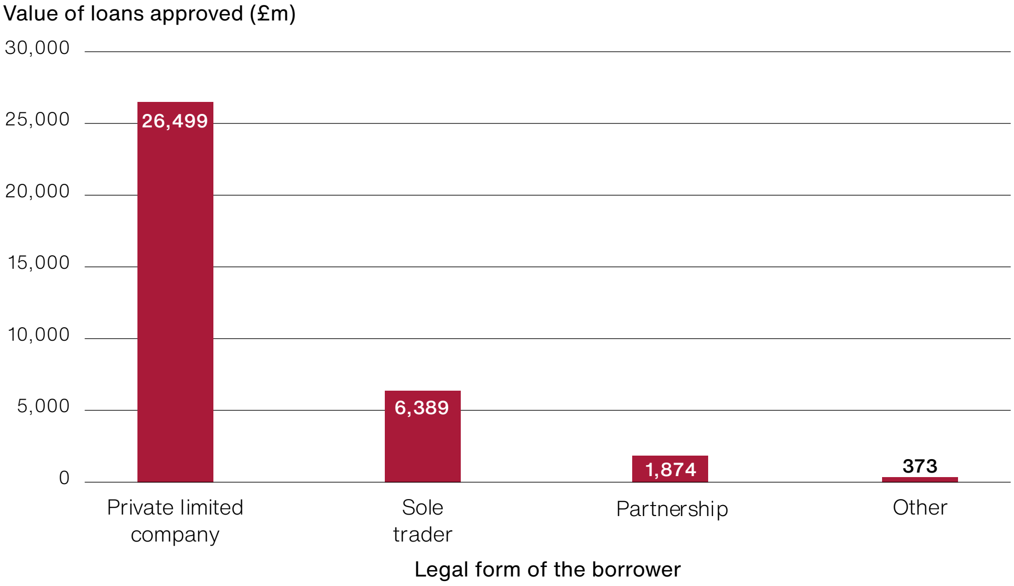
3 Figures as at 7 September 2020.

Source: British Business Bank data

Figure 11

Total value of loans provided by the Bounce Back Loan Scheme (the Scheme), by legal form of the borrower

Private limited companies received the highest value of loans at £26.5 billion



Notes

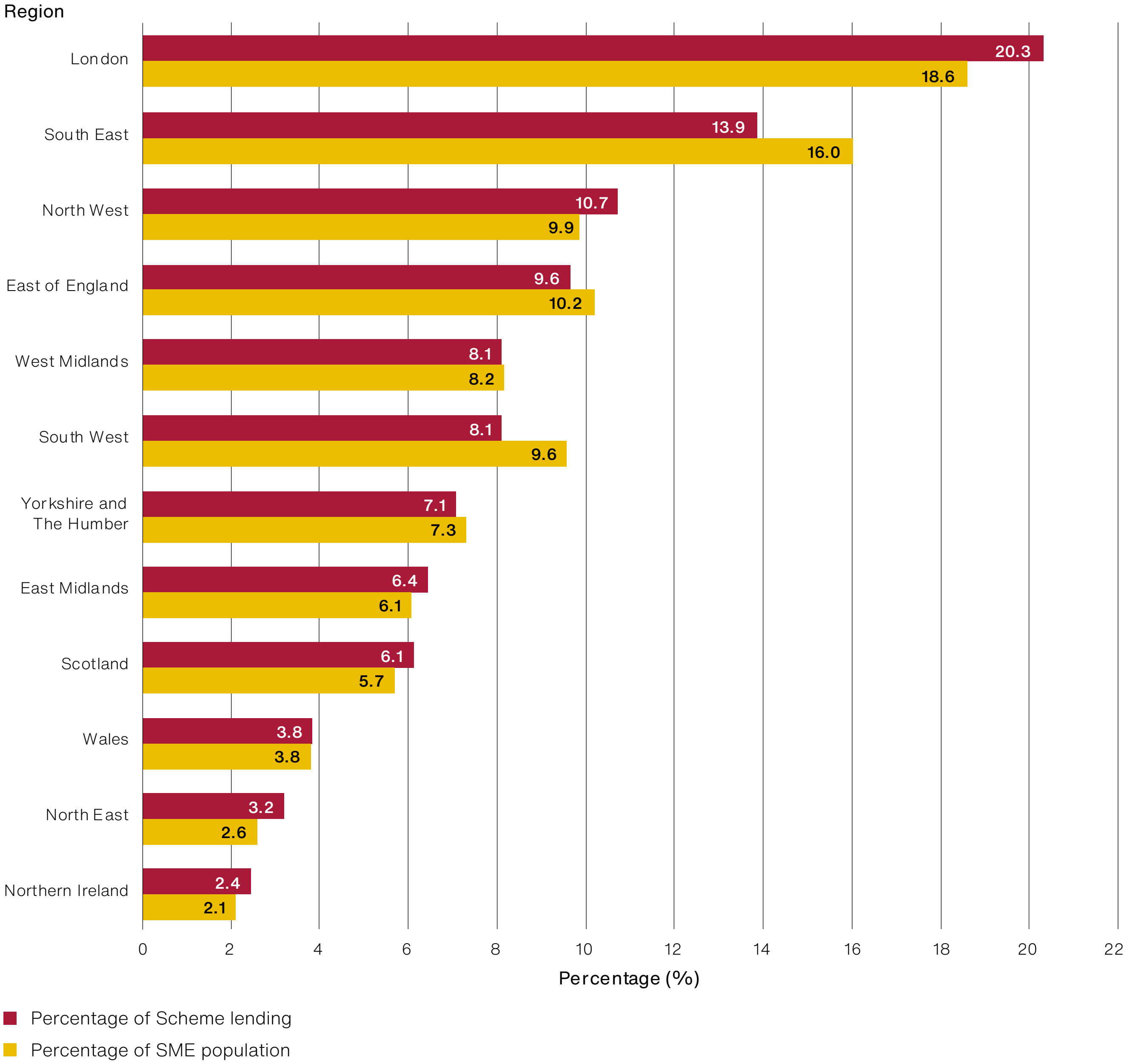
1. The ‘other’ category includes limited liability partnerships (£231 million), public limited companies (£15 million) and those businesses where the legal form could not be identified (£127 million).
2. The Scheme was launched on 4 May 2020.
3. Figures as at 7 September 2020.

Source: British Business Bank data

Figure 12

A comparison of the share of loans provided by the Bounce Back Loan Scheme (the Scheme) against the small- and medium-sized enterprise (SME) population, by region

The regional distribution of loans under the Scheme broadly reflects the population of SMEs across the UK



Notes

1 The percentage of Scheme lending does not sum to 100% because the regional data for some loans were not valid.

2 An SME is defined as any business with fewer than 250 employees.

3 SME population data as at 2019. Scheme data as at 7 September 2020.

Source: National Audit Office analysis of British Business Bank and Department for Business, Energy & Industrial Strategy data

Figure 13

A comparison of small- and medium-sized enterprise (SME) borrowing market share between pre-COVID-19 levels and under the Bounce Back Loan Scheme (the Scheme), by industry sector

The wholesale and retail trade sector's share of borrowing is more than twice as much under the Scheme than prior to the COVID-19 outbreak

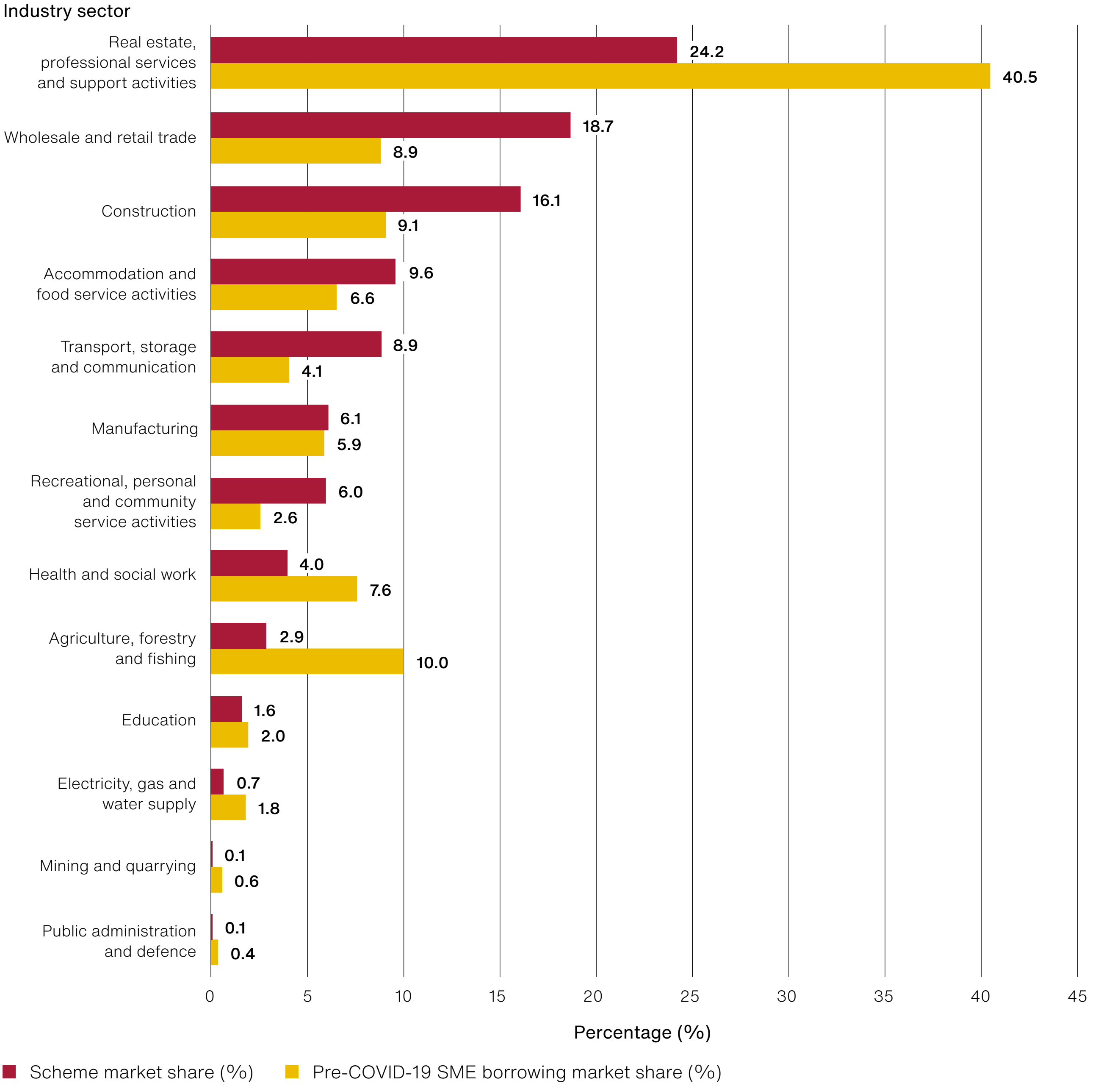


Figure 13 *continued*

A comparison of small- and medium-sized enterprise (SME) borrowing market share between pre-COVID-19 levels and under the Bounce Back Loan Scheme (the Scheme), by industry sector

Notes

1 Scheme data as at 7 September 2020.

2 Pre-COVID-19 borrowing market share is an average of the 12-month period from January 2019.

3 Pre-COIVD-19 borrowing levels are based on Bank of England data which uses the definition of an SME as any business with annual turnover below £25 million.

4 Figures do not sum to 100% as not all industry sectors have been included owing to incomplete information, or a lack of SME lending comparison data.

5 Industry sectors are based on Standard Industry Classification (SIC) codes adapted to bring them in line with the categories used in the Bank of England's Bankstats. As such, the industry sectors and percentages differ slightly to those published by the British Business Bank.

Source: National Audit Office analysis of British Business Bank and Bank of England data

Lenders

2.11 The Scheme was launched with seven accredited lenders, consisting of the five largest UK banks (Barclays, HSBC, Lloyds/Bank of Scotland, NatWest/RBS and Santander) and two other banks (**Figure 14** overleaf).[9] Six of these lenders were ready to accept loan applications at the Scheme launch date; the seventh lender started one day later. The first non-bank was accredited a week after launch (11 May) and began participating in the Scheme from 18 May.[10] By 18 September, 23 lenders had been accredited – seven of these being non-banks.[11]

2.12 Non-banks, such as building societies and peer-to-peer lenders, were responsible for less than 1% of all loans provided under the Scheme (3,000 loans) as of 7 September. In contrast, the UK's five largest banks distributed 89% of loans (1,031,000 loans) (**Figure 15** on page 35).

Scheme costs

2.13 The Bank made a preliminary assessment of the administrative costs for the three business loan support schemes in September 2020. This assessment estimates the three schemes to incur a total cost of £20 million by the end of 2020-21, and £75 million by the end of 2024-25.[12] These costs do not include the Department and HM Treasury's costs. The Bank explained to us that many costs of the three schemes, such as the outsourced operations or the portal, are interlinked and allocation between the schemes is, therefore, difficult. The Bank made a preliminary allocation of the costs using an expected value or volume of work on the three schemes. Based on this allocation, the Bank expects to incur Scheme costs of £9 million by the end of 2020-21, and £32 million by the end of 2024-25: this represent around 40% of the overall estimate of the three COVID-19 business loan support schemes.

9 Largest UK banks as defined by the British Business Bank.

10 Non-banks are institutions that are not registered with the Prudential Regulation Authority.

11 The 23 accredited lenders represent the parent companies only. The total number of lenders, after separating out the individual brands acting on behalf of the parent company, is 28.

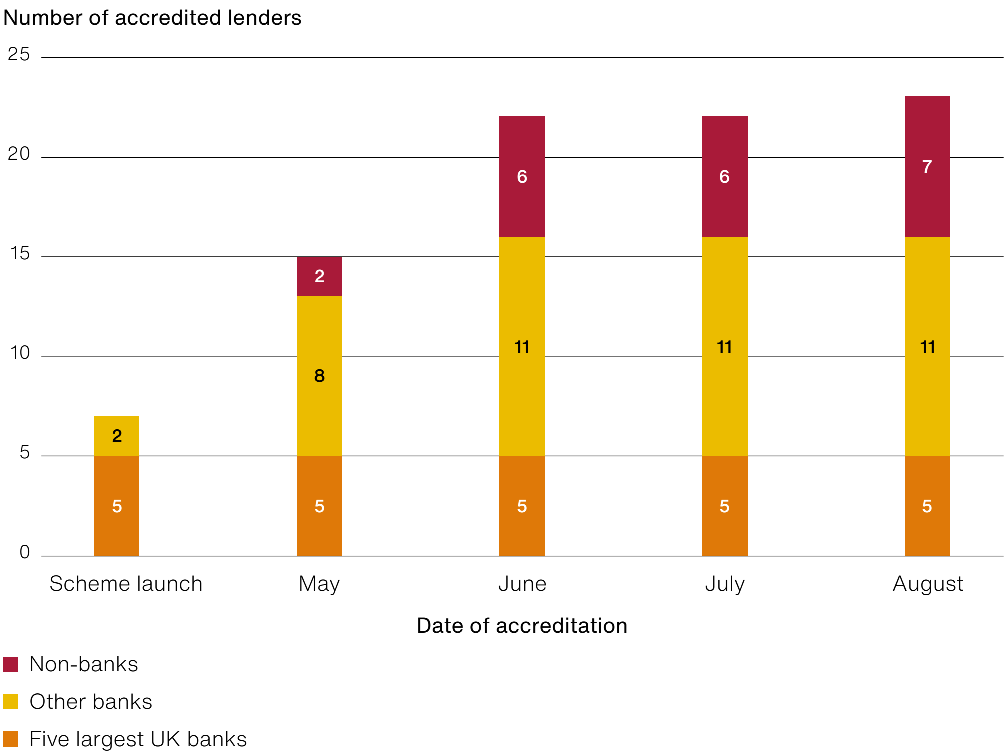
12 The cost estimate has been rounded to the nearest £5 million. The estimate is £74.4 million. The preliminary assessment does not reflect Scheme changes announced by the Chancellor on 24 September.

2.14 The Bank's assessment suggests at least 75% of the administration costs are external. The Bank estimates the two largest items, lender audits and outsourced operations, will cost £55 million by the end of 2024-25.[13] The Bank explained that these estimates are uncertain owing to the difficulty in predicting the volume and scope of work. The volume of work will be affected by the actual levels of credit and fraud losses. The scope of work is affected by the outcome of the recovery process led by HM Treasury.

Figure 14

Cumulative number of lenders accredited under the Bounce Back Loan Scheme (the Scheme)

The Scheme was launched with seven accredited lenders, with a further 16 added over time



Notes

1 The Scheme was launched on 4 May 2020.

2 The five largest UK banks are Barclays, HSBC, Lloyds/Bank of Scotland, NatWest/RBS and Santander.

3 Non-banks are institutions that are not registered with the Prudential Regulation Authority.

4 The accreditation date is the point at which a lender is approved to participate in the Scheme. The point at which a lender starts accepting applications is not always the same as the accreditation date.

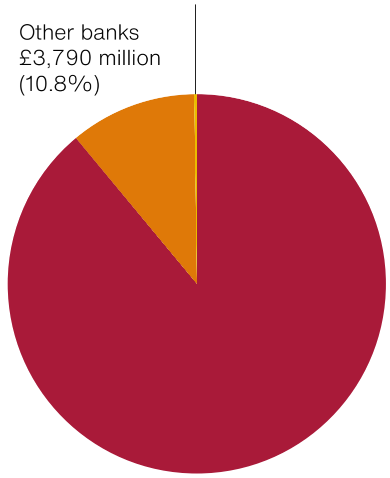
Source: National Audit Office analysis of British Business Bank data

13 The figure £55 million for the three business support schemes is based on three line items in the Bank's forecast. The items relate to lender audits and operation centre activities.

Figure 15

Value of loans provided by the Bounce Back Loan Scheme (the Scheme), by lenders

Nearly 90% of the total value of all bounce back loans have been provided by the five largest UK banks



Notes

1 Figures as at 7 September 2020.

2 The five largest UK banks are Barclays, HSBC, Lloyds/Bank of Scotland, NatWest/RBS and Santander.

3 Non-banks are institutions that are not registered with the Prudential Regulation Authority.

Source: National Audit Office analysis of British Business Bank data

2.15 Under the Scheme the government pays a borrower's first 12 months of loan interest directly to the lender. This payment is a grant, and covers the borrower's interest payments but not capital repayments.[14] After the first year, borrowers are required to make full repayments (capital and interest) up to the end of the six-year term, in line with their arrangement with their lender. The Department and the Bank forecast the cost to total £1,068 million (£847 million in 2020-21 and £221 million in 2021-22); this will rise as more loans are issued.[15]

14 This payment is referred to as a 'Business Interruption Payment'.

15 The Chancellor of the Exchequer announced changes to the Scheme rules on 24 September. Full details of the changes were not available at the publication of this report. The changes allow an increase in the time borrowers have to repay the loan.

Part Three

Value-for-money risks

3.1 Whether the Bounce Back Loan Scheme (the Scheme) represents value for money will depend upon the Scheme delivering its overall objectives, the ultimate costs and how well the risks are managed. The then accounting officer for the Department for Business, Energy & Industrial Strategy (the Department) requested a ministerial direction to proceed with the Scheme. She raised concerns based on value for money, "propriety" that may also impact "regularity", as well as feasibility and concerns on competition.[16] The British Business Bank's (the Bank's) Board also issued a Reservation Notice on propriety, value for money and feasibility. We cannot conclude on value for money at this stage in the Scheme's lifecycle. This part outlines: the main Scheme risks; mitigation strategies, where they exist; and the potential impact to the taxpayer.

Credit and fraud risks

3.2 A credit risk is the risk that a borrower does not repay a loan. The Scheme relies on businesses self-certifying application details. Lenders are required to perform limited verification and no credit or affordability checks. The Bank and the Department were concerned that the lower level of credit checks may result in lenders making loans to businesses which are unable to repay, leading to the loss of taxpayer money; but HM Treasury felt on balance it was necessary to increase delivery speed. According to the Department, "the fact that businesses that were unviable before COVID-19 may be able to access the Scheme owing to the absence of external credit checks [...] creates significant risks around value for money, propriety and potentially regularity,...". The Bank agreed with the Department's view.

16 HM Treasury's *Managing Public Money* states that accounting officers should seek a direction on Regularity: "if a proposal is outside the legal powers, parliamentary authority, or Treasury delegations; or incompatible with the agreed spending budgets" and on Propriety if "a proposal would breach parliamentary control procedures or expectations".

3.3 Fraud is dishonesty which can be a false representation, a failure to disclose information that is legally required, or the abuse of position, with the intention to cause financial gain or loss.[17] HM Treasury, the Department and the Bank recognise that, in the interests of speed, the decision to allow limited customer verification and a lower level of credit checks leaves taxpayers exposed to a significant fraud risk, even after lenders have implemented mitigation strategies.

3.4 The Bank assessed the fraud risks early and instructed a third-party, PricewaterhouseCoopers LLP (PwC), to conduct a risk review. The review aimed to support the Bank in understanding and articulating the potential fraud risks that may crystallise, based on the views of the lenders participating in the Scheme. The review found that, while some risks in the Scheme can be mitigated, there remains a "very high" level of residual fraud risk as defined by the Cabinet Office's Government Counter Fraud Function risk assessment methodology. Based on feedback from the lenders, PwC summarised the main residual external fraud risks coming from self-certification, multiple applications, lack of legitimate business, impersonation and organised crime. The fraud risks were also highlighted in, and contributed to, the Bank's Reservation Notice and the Department's request for a ministerial direction (see paragraph 1.12).

3.5 The nature of the Scheme places the main responsibility for managing fraud risk on the lenders as part of the loan approval process. Subject to lenders meeting the Scheme rules, including limited fraud checks, they are entitled to the government guarantee. The guarantee agreement sets minimum fraud standards. The lenders are obliged to ensure that applicants pass anti-fraud, anti-money laundering and 'know your customer' checks, but they are not allowed to apply a credit check for loan approval purposes. They can only refuse an eligible application based on fraudulent self-certification if it can be identified from the information in the application. Lenders may conduct additional checks for new customers or existing customers requiring a new bank account.

17 As set out in the Fraud Act 2006.

3.6 The Bank has been working with lenders to improve checks and has established fraud prevention forums with a wide group of stakeholders to share best practice and aid implementation of additional fraud measures. However, it is reliant on lenders' goodwill to manage the risks, given that these additional checks are over and above what is required in the Scheme agreement. The Bank, through its coordination function, alongside the Department works with lenders to utilise the portal for fraud loss measurement and reporting. At the end of September, the Department put in place a service level agreement with the National Investigation Service (NATIS) to support it identifying and responding to fraud within the COVID-19 loan schemes. Under the agreement, NATIS will help identify suspicious activities as well as investigate priority fraud cases, exercising law enforcement capabilities. From October 2020, lenders will produce a monthly fraud report. Although this is not active fraud prevention, given it is conducted once the lenders upload the details into the portal, it is aimed at identifying and minimising potential losses. However, the Bank is currently unable to estimate the overall level of fraud. Based on the Cabinet Office's Government Counter Fraud Function, fraud losses are likely to be significantly above the general estimates of public sector fraud levels of 0.5% to 5%.

Total potential impact of credit and fraud risks

3.7 There is a high degree of uncertainty in estimates of the Scheme's expected losses (**Figure 16**). According to the Bank, credit and fraud risks are interrelated and therefore are not separately identifiable. In the Department's advice leading up to the Ministerial Direction, it estimated potential losses to range between 30% and 75% and did not rule out actual losses being "even higher". In its annual report and accounts, published in September 2020, the Department estimated that 35% to 60% of borrowers could default on the loans as a result of credit and fraud risk. This was based on historic losses in prior programmes which most closely resemble the Scheme. Assuming the Department's expected default rates, and Scheme size estimate of £43 billion, implies a potential cost to the government owing to credit and fraud losses of between £15 billion and £26 billion.[18] However, actual losses could differ from those forecast. The full extent of credit losses and fraudulent applications will not become apparent until after borrowers are due to start repaying loans (from 4 May 2021) – government is paying interest on all loans for the first 12 months.[19]

18 £43 billion is based on the rounded mid-point value of the estimated Scheme lending of £37.7 billion and £48.7 billion.

19 The estimates of credit and fraud losses have been made before 24 September 2020 and, as such, do not reflect changes to the Scheme announced by the Chancellor of the Exchequer.

Figure 16

Estimated credit and fraud loss rates on the Bounce Back Loan Scheme (the Scheme)

Expected loss estimates under the Scheme range from 15% to 80%

	Estimated credit and fraud loss rate (%)			
	At scheme launch		Most recent estimate	
	Minimum	Maximum	Minimum	Maximum
HM Treasury	40	40	N/A	N/A
Department for Business, Energy & Industrial Strategy[1]	30	75	35	60
British Business Bank[2]	30	50	35	80
Office for Budget Responsibility[3]	N/A	N/A	15	60

Notes

1 The Department for Business, Energy & Industrial Strategy's (the Department's) latest expectation is based on the British Business Bank's (the Bank's) data and is published in the Department's 2020 annual report and accounts.

2 As of 9 September, the Bank's base scenario is 35%–60%, with a current central estimated loss rate of 45%: pandemic as expected, mitigation effect, loan scheme design, and wider measures as expected. The downside scenario is 60%–80%: pandemic longer than expected, mitigation effect smaller than expected.

3 The Office for Budget Responsibility (OBR) assumes a base case of 30%, and upside and downside scenarios of 15% and 60% depending on the UK's economic performance. These estimates were published in July.

4 The Scheme was launched on 4 May 2020.

5 The estimates of credit and fraud losses have been made before 24 September 2020 and, as such, do not reflect changes to the Scheme announced by the Chancellor of the Exchequer.

Source: British Business Bank, the Department for Business, Energy & Industrial Strategy, HM Treasury, and the Office for Budget Responsibility

Post publication this page was found to contain an error which has been corrected (Please find Published Correction Slip)

Recovery process

3.8 In the event a borrower does not repay the loan (a default), the Bank expects lenders to pursue "appropriate recovery processes", in line with their existing standards. The recovery process for loans in default is less onerous than in the other COVID-19-related business loan support schemes; unlike the other schemes, the Scheme has not been designed with an open-ended recovery timescale. Lenders are given a 12-month time limit after they have issued a formal demand on the borrower to pursue outstanding amounts. However, claiming on the government guarantee is not conditional on having completed the recoveries process; lenders are able to make a claim on the government guarantee "within a reasonable time period" following the first formal demand date, and may claim if they believe "no further payment is likely". Any outstanding debt collected by the lender after the guarantee has been claimed would be paid back to the government. The Scheme does not include actions to recover outstanding debt after the 12-month time limit, for example by requiring lenders to continue recovery processes in exchange for a fee. According to the Department, "the Chancellor has given a firm steer against this" because, as HM Treasury explained, he believes 12 months is an appropriate time frame to pursue a loan of this nature.

'Moral hazard'

3.9 Borrowers may have limited incentives to pay back the loans, and with a 100% guarantee, lenders have limited incentives to seek a full recovery. The Scheme's loan terms do not require the borrower to provide any security, such as personal guarantees or assets. This risk is further increased by the approach to recovery of any outstanding debt and government providing lenders a 100% guarantee against the outstanding payments under the Scheme (both capital and interest). This is a higher guarantee level than the other COVID-19-related business loan support schemes which are typically 80% (Figure 1, page 14). To overcome this the Bank has asked lenders to stress to borrowers that non-repayment of loans may affect a business's future credit rating, and thus its ability to borrow.

Wider value-for-money risks

Crowding out

3.10 The Bank's data shows that the five largest UK lenders (Barclays, HSBC, Lloyds/Bank of Scotland, NatWest/RBS and Santander) approved £31.3 billion through 1,031,000 loans, while the remaining 18 lenders were responsible for approving £3.9 billion through 127,000 loans. Thus, the largest UK lenders are responsible for 89% of the value of the loans distributed. This is market-distorting. Bank of England data estimate the total small- and medium-sized enterprise (SME) debt to be £167 billion, with the big banks accounting for 65% of the lending. The Bank and the Department raised concerns that the Scheme's terms are making it uncompetitive for smaller lenders to compete with incumbents which, in turn, has a negative impact on competition in the SME lending sector. Although HM Treasury recognised this concern, it believed it to be a commercial decision for individual lenders. One of the Bank's key objectives is to help create a more diverse finance market for smaller businesses, with a greater choice of options and providers.[20] The Bank has sought to mitigate this risk by broadening the number of lenders under the Scheme – see Figure 14 on page 34.

3.11 Government fixed the loan interest rates at 2.5% in order to provide a "reasonable return" for lenders while remaining attractive to borrowers, but policy-makers recognised that this rate would mean that there would be limited economic incentive for challenger banks and other lenders to participate in the Scheme. Based on HM Treasury's assessment of an average loan size of £15,000 and an interest rate of 2.5%, it would allow lenders to make an expected return lower than the UK banking sector average of 0.7%. However, the current average loan size is approximately £30,000, and these loans are risk-free for the lender as they are government-guaranteed, and so the expected returns may differ.

3.12 The Bank accredited most lenders under the Scheme using an 'accelerated lender accreditation process'. The Bank applied this process to lenders which were already accredited under the Coronavirus Business Interruption Loan Scheme (CBILS). The process involved checks against their fraud processes, operational capacity and plans for recoveries. There were only three new lenders and they were subject to the Bank's standard accreditation process. In turn, the Bank has put in place an audit plan to ensure lenders' compliance with the Scheme.

20 Comptroller and Auditor General, *British Business Bank*, Session 2019-20, HC 21, National Audit Office, February 2020.

'Deadweight loss'

3.13 The Scheme offers a 100% guarantee to lenders whereas CBILS only offers 80% (Figure 1). Scheme rules allow borrowers to use the loans to pay down existing borrowing – so they may choose to repay a higher-interest loan, which will reduce the potential profits of that lender, while de-risking its balance sheet slightly. If a loan has been extended to a borrower under CBILS and subsequently been refinanced with a Scheme loan, it means that government needlessly assumes the higher guarantee when the risk could reasonably be borne by the lender. The benefit of this is that the borrower will be making lower interest payments. The Bank and the Department raised a concern about deadweight loss when seeking the Ministerial Direction. As of August 2020, around 5,000 loans worth £183.9 million have been used to refinance loans which had already been awarded under CBILS. According to HM Treasury, this may be an underestimate as a number of lenders have been unable to provide details on refinancing.

Appendix One

Our investigative approach

Scope

1 We investigated the Bounce Back Loan Scheme (the Scheme). The report covers:

- how the Scheme was developed, what it aims to achieve and how it is managed (Part One);
- the Scheme details and how it performed to date (Part Two); and
- the main Scheme risks (Part Three).

2 The investigation is non-evaluative. We have not assessed the value for money of the Scheme.

Methods

3 In examining these issues, we drew on a variety of evidence sources. We:

- reviewed key documents in relation to the design, implementation and performance of the scheme by HM Treasury, Department for Business, Energy & Industrial Strategy (the Department) and the British Business Bank (the Bank);
- reviewed key documents in relation to the Scheme and agreements with lenders;
- undertook a survey of 15 lenders under the Scheme. The survey covered application processing times, number of new customer loans, use of proceeds and wider lender feedback. Of these, we received 10 responses. The responses include four of the five largest UK lenders;
- reviewed key documents in relation to similar international schemes;
- held interviews with HM Treasury, the Department and the Bank; and
- drew on discussions with external parties such as the Financial Conduct Authority, the Financial Ombudsman Service and other industry and customer representative groups.

Quantitative analysis

4 We analysed Scheme performance data provided by both HM Treasury and the Bank. HM Treasury collects aggregate performance data from the start of the Scheme. The Bank gathers data from the point by which its collection system (the portal) allowed automated input by the lender (mid-June). The Bank collects the data to administer the guarantees. These two datasets differ for two reasons:

- what data are collected – HM Treasury collects summary-level data of loan application and loan applicants, whereas the Bank has data on a loan-by-loan basis; and
- when the data are collected – HM Treasury collects the data on a daily basis from lenders. The Bank data allow automated input directly by lenders. As this was only in place by mid-June, it meant that lenders have to retroactively update the portal with lending activity as well as gathering information on new lending.

5 As a result, not all figures in our report reconcile. HM Treasury data used in our report have a cut-off date of 6 September; on this date 1,222,548 loans have been approved with an aggregate value of £36.9 billion. These data were used in Figure 7 and 8 when illustrating the overall loan issuance over time, as well as the approval rates. The Bank data have a cut-off date of 7 September; on this date 1,157,946 loans have been issued to borrowers with an aggregate value of £35.1 billion.

6 We have not audited the underlying loan-level data owing to confidentiality issues. The data contain sensitive personal and commercial details. We relied on the summary data provided by HM Treasury and the Bank. HM Treasury and the Bank, in turn, rely on the information provided by the lenders.

7 The Bank's preliminary cost assessment is based on a summary spreadsheet of the anticipated annual cost out to 2024-25, supplied to us on 23 September. The Bank made this assessment in September 2020. The assessment is based on the Bank's estimates of all COVID-19 business loan support schemes. The Bank allocated the total costs to the relevant scheme, expense category and year. The allocation methods vary depending on the cost items and mainly use volume, value, or number of schemes. We have not audited the underlying operational expenditure data. We have verified the calculations in the spreadsheet and conducted limited checks on the allocation of the cost between the schemes.

Appendix Two

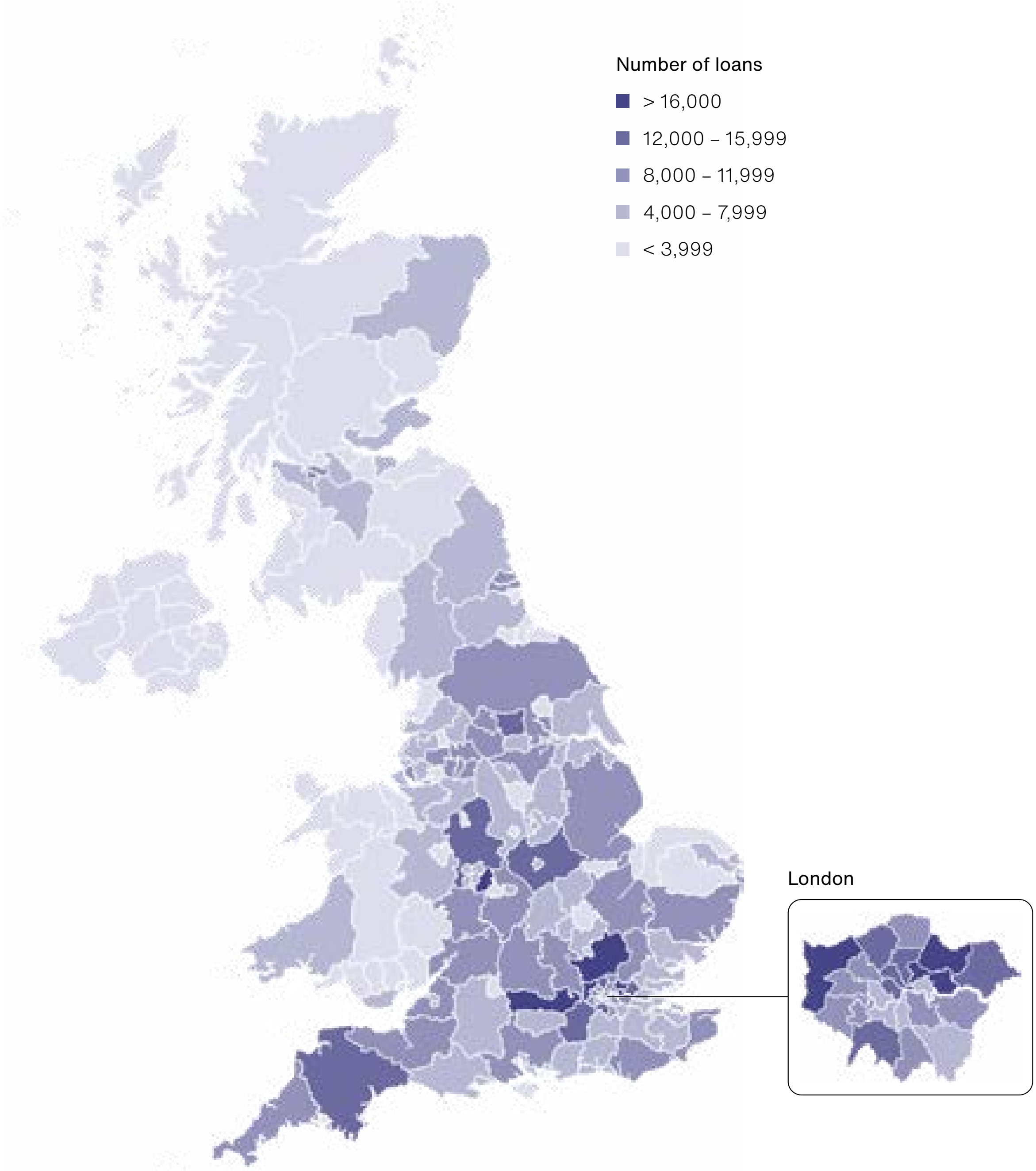
Regional distribution of loans

1 **Figure 17** on pages 46 and 47.

Figure 17

Breakdown of the number and value of loans provided under the Bounce Back Loan Scheme (the Scheme), by region

Under the Scheme, businesses across the UK received loans



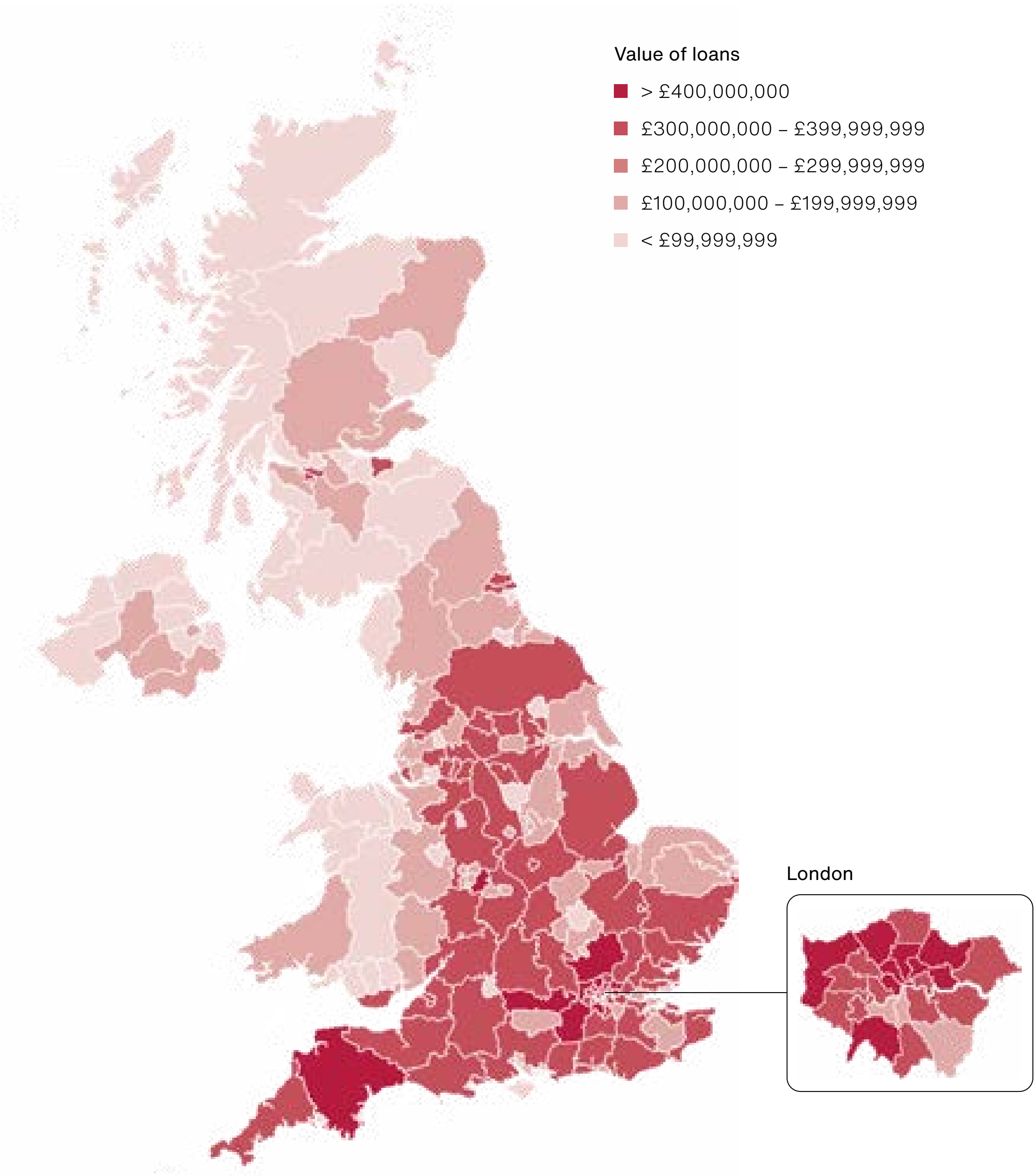
Notes

1 Data exclude 1,551 loans with a total value of £47,999,023 as the location information was not provided by the applicant.

2 Regions are based on Level 3 Nomenclature of Territorial Units for Statistics (NUTS) codes of the UK.

3 Data as at 7 September 2020.

Source: National Audit Office Analysis of British Business Bank data


Value of loans
> £400,000,000
£300,000,000 – £399,999,999
£200,000,000 – £299,999,999
£100,000,000 – £199,999,999
< £99,999,999
London

CORRECTION SLIP

Title: Investigation into the Bounce Back Loan Scheme

Session: 2019–2021

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Correction One:

Paragraph 2.8 (page 27) of the report was produced in error, ‘more than’ should have been deleted.

The paragraph currently reads:

2.8 ~~More than~~ three-quarters of the total support was provided to private limited companies, which received £26.5 billion from 793,000 loans. Sole traders received £6.4 billion from 297,000 loans, representing almost one-fifth of the total support (**Figure 11** on page 30). More than one-third of bounce back loans were received by businesses that have been operating for more than four years

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BACK

Correction Two:

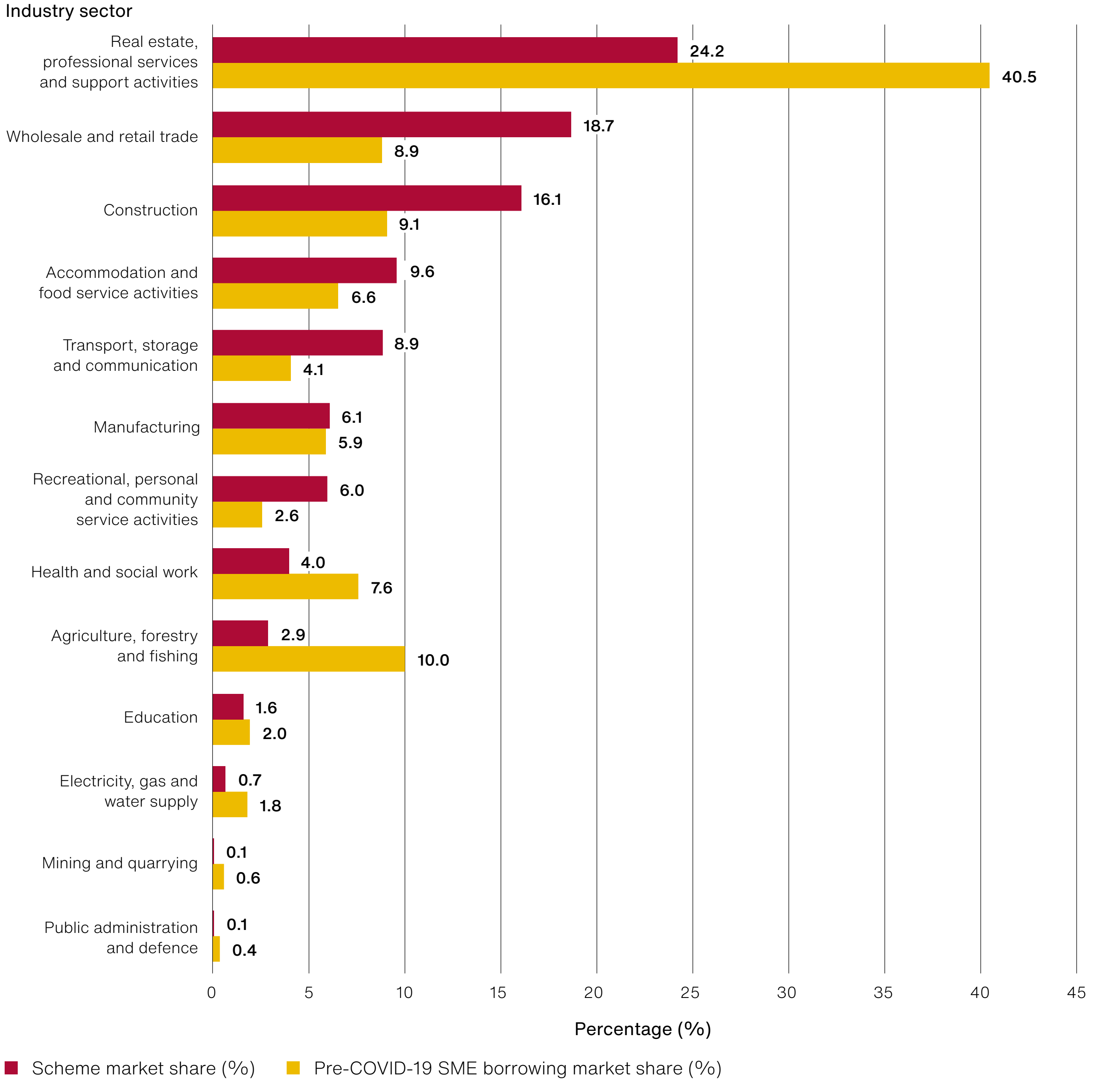
Figure 13 (page 32) an error was produced in the subtitle, ‘almost’ should have read ‘more than’.

The figure currently reads:

Figure 13

A comparison of small- and medium-sized enterprise (SME) borrowing market share between pre-COVID-19 levels and under the Bounce Back Loan Scheme (the Scheme), by industry sector

The wholesale and retail trade sector’s share of borrowing is ~~almost~~ twice as much under the Scheme than prior to the COVID-19 outbreak



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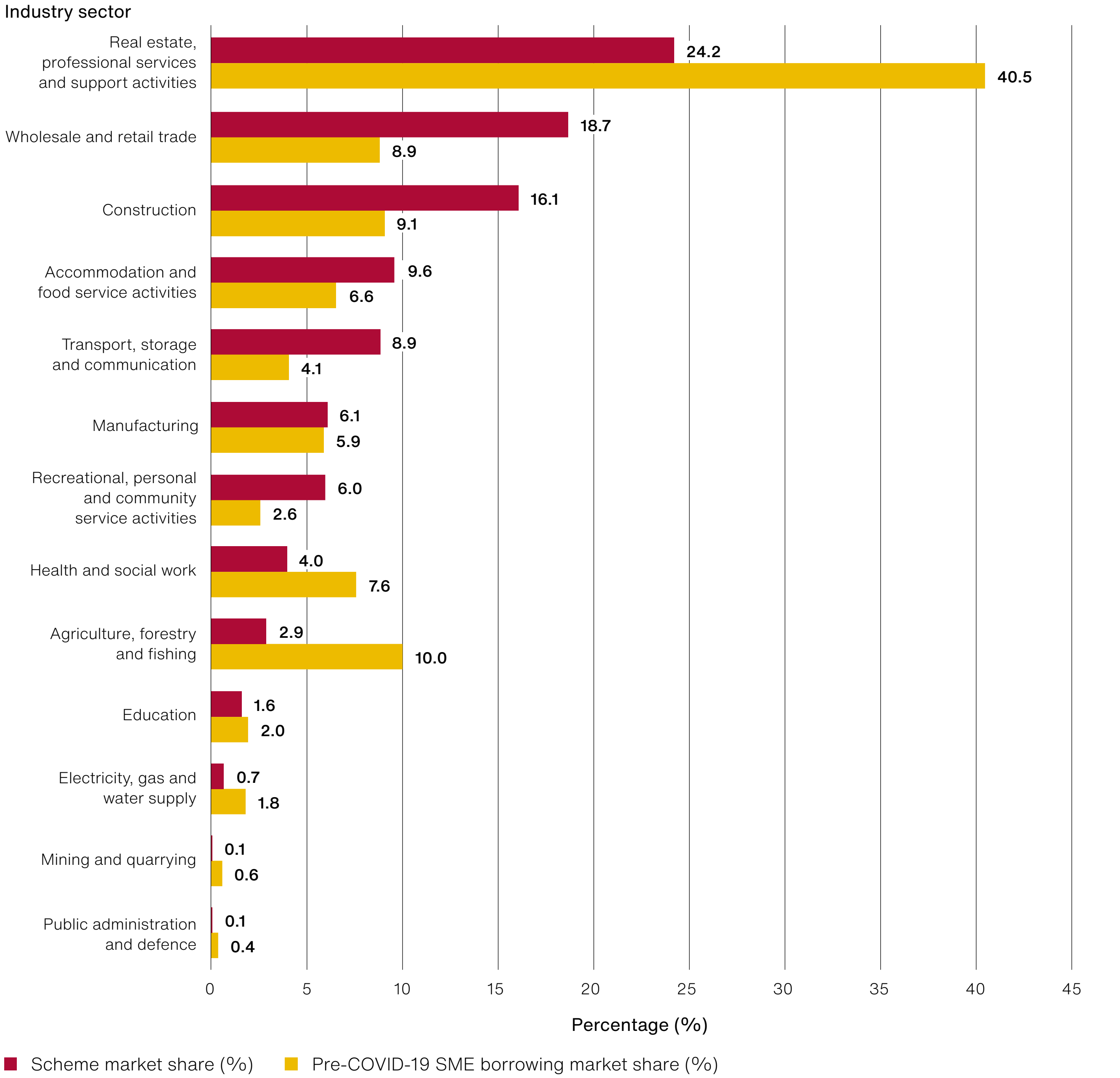

BACK

Correction Three:

Figure 16 (page 39) an error was produced in the subtitle, 30% should have read 15%, a new sentence was added at the end of note 3 and note 5 should have been deleted.

The figure currently reads:

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Estimated credit and fraud loss rates on the Bounce Back Loan Scheme (the Scheme)

Expected loss estimates under the Scheme range from ~~30~~% to 80%

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	At scheme launch		Most recent estimate	
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3 The Office for Budget Responsibility (OBR) assumes a base case of 30%, and upside and downside scenarios of 15% and 60% depending on the UK's economic performance.

4 The Scheme was launched on 4 May 2020.

5 ~~The most recent estimates vary by date: the Department's estimate was published in September, the Bank's was produced in June and the OBR's was published in July.~~

6 The estimates of credit and fraud losses have been made before 24 September 2020 and, as such, do not reflect changes to the Scheme announced by the Chancellor of the Exchequer.

Source: British Business Bank, the Department for Business, Energy & Industrial Strategy, HM Treasury, and the Office for Budget Responsibility

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BACK

Date of correction: 12 October 2020

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