Regulatory Impact Statement

Student Support Package for Budget 2011

Agency Disclosure Statement

This Regulatory Impact Statement has been prepared by the Ministry of Education.

It provides an analysis of options to increase the value of the Student Loan Scheme (the Scheme) to the Government by ensuring study funded through loans contributes to tertiary education priorities, and by improving borrowers' repayment rates.

Changes to the following have been analysed:

- the student loan repayment threshold
- the definition of income
- lending for older borrowers
- lending for borrowers with overdue repayments
- the repayment holiday for overseas-based borrowers
- part-time, full-year students' eligibility for course-related costs
- [2]
- increasing repayment responsibility
- the exemption for the family of 'protected persons'.

The rigour of the analysis is constrained by the difficulties estimating the potential impact of some proposals on affected borrowers and the potential costs and savings generated by some proposals. Analysis and consultation on the proposals outlined in this Regulatory Impact Statement has been constrained due to the tight timeframes and the budget-sensitive nature of the proposals.

None of the options considered in this Regulatory Impact Statement are likely to have an impact on business costs, impair private property rights or override common law principles. [3]

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Status quo

The Scheme was established in 1992 as part of wider tertiary education reforms. Private contributions to tertiary education were introduced to make the expansion of tertiary participation affordable for Government, and the Scheme was introduced to ensure that finance was not a barrier to participation.

Interest-free student loans were introduced in 2006. They have provided an incentive for a higher number of students to borrow, and decreased incentives to repay loans. The uptake of loans increased dramatically following the introduction of interest-free student loans – from 56% in 2006 to 71% in 2009. The repayment rate[1] has decreased from 9.5% in 2005 to 7.3% in 2010.

Since 2006 students have borrowed a total of $13.9 billion and repaid $6.4 billion. The difference between new lending and repayments is currently $770 million and this is forecast to rise to $1.1 billion by 2030 if current settings remain the same.

New Zealand-based borrowers generally have high repayment compliance. Systems make it easier for borrowers in New Zealand to repay – mostly via deductions from their earnings. Inland Revenue can more readily keep in contact with New Zealand-based borrowers. As well, New Zealand-based borrowers face no interest charges, so once they leave study their loans cannot increase, as long as they do not incur penalties.

By contrast, overseas-based borrowers have interest added to their loans, and in many cases take a repayment holiday of up to three years. In addition, many overseas-based borrowers either do not inform Inland Revenue when they go overseas, or do not maintain contact with Inland Revenue, so there is a higher risk of an overseas-based borrower falling behind on repayments and incurring penalties.

Problem definition

This Regulatory Impact Statement (RIS) addresses several problems within the Scheme with the aim to increase repayments, reduce borrowing, ensure value-for-money lending, and widen the expectation of repayment.

The proposals outlined below aim to contain government expenditure and improve the performance of the Scheme, while maintaining the interest-free student loan policy. The options in the RIS aim to facilitate greater personal responsibility from borrowers for their student loan debt. They also seek to address the increasing cost of the Scheme and thereby achieve a fairer distribution of benefits and costs between current and future taxpayers.

There are constraints on the analysis in this RIS. First, the current Government indicated that currently, it does not want to reverse the interest-free student loan policy. This is a significant constraint on the options available to contain government expenditure and improve the performance of the Scheme. Second, due to system constraints there are difficulties in estimating the potential savings and the number of people who may be affected by some proposals. Third, consultation on the options outlined in this RIS has been limited at this stage due to the budget-sensitive nature of the proposals. Key agencies involved with the Scheme – Inland Revenue, the Ministry of Social Development and the Treasury – have been consulted on the proposals and this RIS. There have also been considerable time constraints around this RIS which may have led to gaps in some analysis.

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1 Calculated as total repayments divided by the opening student loan balance.

Objectives

The objective of the proposals in this paper is to modify the Scheme to contain the Government's tertiary education expenditure and improve its performance, while maintaining the interest-free policy. The proposals address several problems within the Scheme with the aim to increase repayments, reduce borrowing, ensure value-for-money lending, and widen the expectation of repayment.

The two policy levers available to the Government to achieve this are:

- restrict access to the Student Loan Scheme;
- introduce new methods to encourage or require repayment.

Any modifications to the Scheme need to take into account the intention of student loans, which is to remove financial barriers to accessing tertiary education. Any changes would also need to be considered in the context of the Government's goals for tertiary education, particularly participation and achievement for priority groups.[2]

Specific mechanisms for restricting access to loans, and increasing repayment rates, and options within each, are discussed below, and are summarised in a table in the conclusion section below.

Regulatory impact analysis

<u>Broadening the definition of income</u>

[2]

[2] Young people aged under 25, Māori students, Pasifika students.

Option 3 – Adding back business and investment losses

This option involves business and investment losses no longer being off-set against a borrower's income when assessing income for student loan repayment. Currently, losses are added back to a borrower's income, meaning that these borrowers may have little or no repayment obligation.

Those who would be affected by the inclusion of losses can be broadly split into two groups, those with business losses and those with investment losses.

Within the business losses group will be people who are setting up businesses and using their income stream to fund the growth of the business. Requiring student loan repayments from these borrowers reduces the money they have available to grow their business and may reduce entrepreneurship. However, this group will also include people who are for example earning salary or wages from a job and setting up or running a separate business, but not using their salary or wage income to fund the growth of their business. Government should not provide subsidies for business decisions through decreasing a borrower's repayment obligation.

Those with investment losses have made a decision to invest their income, which is no different to any other consumption decision. Government should not be foregoing student loan repayments in order to subsidise the spending or investment decisions of student loan borrowers.

Approximately 10,300 borrowers would have a higher repayment obligation under this option. Approximately 2,500 of these borrowers would not have had a repayment obligation and would become liable to make repayments.

Restricting further student loans for those with overdue repayments

Ensuring that lending is good value, widening expectations of repayment and increasing repayments, reduction in borrowing

Once a student loan borrower's income exceeds the annual income threshold (currently set at $19,084), they must start repaying their loan. A penalty is charged to loan accounts when a borrower underpays and becomes in default. These borrowers are currently able to take out further student loans. Inland Revenue estimates that in 2009, approximately 1,864 borrowers took out new student loans while having overdue repayments on previous loans. The number of borrowers in this situation has increased every year, and doubled between 2008 and 2009.

Between 1998 and February 2010, approximately 4,600 borrowers took out a new student loan while having overdue repayments of over $500 on a previous loan. An additional 1,100 borrowers had overdue repayments of less than $500. These overdue repayments totalled approximately $19.4 million. The new loans totalled approximately $27 million for the first year of new study, but the total lending could be higher if borrowers are engaged in courses of study across several years. Borrowers with overdue repayments are most likely to be people who have previously studied for a qualification and are returning to undertake further study after a period in the workforce.[3]

Restricting loans for those with overdue repayments would signal that repayment obligations need to be met, and that there are consequences for non-compliance. This would improve the value of the loan scheme through increased repayments and would also focus on deliberate non-compliance by borrowers, rather than on borrowers who cannot meet their repayment obligations due to their financial situation.

Option 1 - Status quo

This option would retain the status quo, with student loan borrowers who have overdue loan repayments remaining eligible to take out further student loans. Changing the status quo would be likely to have a disproportionate impact on key target groups, such as Māori and Pasifika as well as beneficiaries.

Option 2 – Threshold for overdue repayments

Two options were explored for a threshold for overdue repayments: $500 or more, and $2,500 or more. $2,500 is the average amount for repayments overdue. Data show that of those studying in 2009, 4,773 were in arrears of $500 or more, and 1,479 were in arrears of $2,500 or more.

The following groups are the most likely to have overdue repayments, and therefore would be the most affected by any change:

- Māori
- Pasifika
- people in their 30s
- those at wānanga or private training establishments (PTEs)
- those studying qualifications at certificate and diploma level
- beneficiaries (about 50% of those in arrears are beneficiaries and around 60% of them were studying at certificate and diploma level).

A threshold of $500 or more would capture a larger number of borrowers with overdue repayments.

Option 3 - Ineligible one year after being in default

This option would remove loan eligibility for borrowers who have been in default for one or more years on overdue repayments of $500 or more, from the time they were declared to be in default by Inland Revenue.

In 2009, of the 4,800 in-study borrowers who were in default with overdue repayments of $500 or more, around 3,800 (80%) would have been ineligible for student loans if this option had applied. This means that around 1,000 (20%) would have remained eligible because they were in default for less than a year.

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3 Some reasons why people may be in arrears include: intentional non-repayment; people or employers not using the correct student loan tax code; errors in deduction calculations; non-wage sources of income, or other income not taxed at source; borrower did not meet repayment obligations while overseas.

A one year time limit would mean that borrowers notified by Inland Revenue that they are in default would become ineligible to borrow if they have not reduced their default below $500 within one year. Due to the time it takes between under-payment and being classified as in default, this option would provide close to a two year period between under-payment and no longer being able to borrow.

This option offers some protection for people who have only recently been in default, and (when system time-lags are included) it provides time for people to pay overdue amounts.

Option 4 - Ineligible two years after being in default

This option would remove loan eligibility for borrowers who have been in default on overdue repayments of $500 or more for two or more years, from the time they were declared to be in default by Inland Revenue.

Of the 4,800 in-study borrowers in 2009 who had overdue repayments of $500 or more, 2,900 (60%) would have been ineligible for student loans if this option had been fully implemented in 2009.

Further, 1,900 (40%) of in-study borrowers were in default within the last two years and would mostly be exempt from ineligibility under this option.

A two year limit would allow borrowers in default a two year limit for repayment to avoid losing loan eligibility. Considering the time since the default is incurred, this would allow almost three years from the time a person underpays their student loan obligation until they would lose their loan eligibility. This long delay between being in default and losing eligibility is likely to be too long to be effective.

Older borrowers

Ensuring that lending is good value, reduction in borrowing

The cost to the Crown per student is significantly higher for older borrowers than for other groups, since older people are likely to repay under the income-contingent loan scheme at a slower rate and for less time than younger borrowers. Research predicts that, over the next 20 years, an increasing number of older people will remain in the workforce beyond 65. However, the return to the country of the investment in a person's education is much less if after tertiary education, the person has only a few years in the workforce, or if they are not active in the workforce.

[3]

Restricting borrowing for older borrowers would affect those who seek to borrow as well as current borrowers. Any restrictions that were applied immediately would affect current borrowers more, and may prevent them from finishing their study due to unaffordability. This risk can be mitigated by introducing grandparenting for those older borrowers who are currently studying. Time-limiting the grandparenting, and restricting it to those already studying, would allow older borrowers who may have been affected by the change to continue to borrow to allow them to finish their study, but would prevent them continuing to borrow for additional qualifications.

Option1 - Status quo

Retaining the status quo recognises that tertiary education has other benefits for older people, for example, it can equip them to undertake valuable voluntary work in the community and also to contribute towards the learning of others. It also recognises that, with the aging of the baby boom generation, an increasing number of older people are likely to remain in the workforce after the age of 65.

However, older people are not a priority group in the Tertiary Education Strategy and the costs to government of the Scheme are significantly higher for older borrowers than for other groups, since older people are likely to repay at a slower rate under the income-contingent loan scheme than other borrowers. However, older borrowers make up a smaller proportion overall of all borrowers. This option would not change current costs.

Option 2 - Restrict eligibility to the student loan scheme for people aged 65 and over to fees only

This option reduces the risks around lower returns and non-repayment of student loans, while still providing opportunities (through tuition subsidies[4] and fee support) for older people to up-skill to improve their economic position.

This option would provide minimal savings. In 2009, eligibility to the living costs component of the loan was removed for those who receive social security benefits (including New Zealand Superannuation). Based on 2009 borrowing, if student loan support to those aged 65 and over was restricted to fees only, then the number of students affected (which includes those already in the system) would be approximately 800 per year.

Borrowers aged over 65 borrowed approximately $3.6 million for livings costs and course-related costs in 2009. Based on 2009 borrowing, and incorporating the expected impact of the Budget 2010 changes, savings from reduced lending by removing eligibility to living costs and course-related costs to those aged 65 and over is estimated to be between $1 to $3 million per annum.

Option 3 - Remove eligibility to the student loan scheme for people aged 65 and over

This option proposes that when people reach age 65 they would not be eligible for student loans. Those over 65 would still be eligible to participate as domestic students, paying domestic fees, but without the ability to access the Scheme to fund their study.

This option addresses the risks around lower returns and non-repayment of student loans, while still providing opportunities (through tuition subsidies) for older people to up-skill to improve their economic position.

If the age limit were set at 65, then the number of students affected (which includes those already in the system) would be approximately 800 per year. Borrowers aged over 65 borrowed $6.9 million across all three fee components in 2009. Based on 2009 borrowing, savings from reduced lending by removing eligibility to those aged 65 and over is estimated to be between $4 to $6 million per annum.

This would be a significant shift in student support policy. The principle of open eligibility for loans has been regarded as one of the key features of the student support system.

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4 Tuition subsidies are Government's contribution to the direct costs of teaching, learning, and other costs driven by learner numbers.

Option 4 - Restrict borrowing for people aged 55 and over to fees only

This option proposes restricting student loan eligibility to fees only for people aged 55 years and over. Based on 2009 borrowing, if student loan support to those aged 55 and over was restricted to fees only, then the number of students affected (which includes those already in the system) would be approximately 3,200 per year. Those borrowers already committed to a course of study would be most adversely affected by these changes.

In 2009, borrowers aged over 55 borrowed $11.1 million for living costs and course-related costs and $14.6 million for fees. Based on 2009 borrowing, savings from reduced lending by removing eligibility to living costs and course-related costs for those aged 55 and over is estimated to be between $8 and $11 million per annum.

This option proposes only restricting lending for living costs and course-related costs. The Government will still provide significant support (through tuition subsidies and fee support) for people aged 55 and over to up-skill to improve their economic position.

Option 5 - Restrict borrowing for people aged 40 and over to fees only

This option proposes restricting student loan eligibility to fees only for people aged 40 years and over. Applicants must be below 40 at the point of application in order to be eligible for course-related costs and living costs.

This option would generate the most significant savings. Based on 2009 borrowing, if student loan support to those aged 40 and over was restricted to fees only, then the number of students affected (which includes those already in the system) would be approximately 17,000 a year.

In 2009, borrowers aged over 40 borrowed $38.8 million for livings costs and course-related costs and $83.6 million for fees. Based on 2009 borrowing, savings from reduced lending by removing eligibility to living costs and course-related costs to those aged 40 and over is estimated to be approximately $40 million per annum.

Repayment holiday

Widening expectations of repayment, increasing repayments

Since 2007, an automatic repayment holiday has been available to overseas-based borrowers, giving them a three-year break from repayments. Overseas-based borrowers are charged interest on their loans, to recognise the cost to the Crown of lending. Approximately 50% of New Zealanders under the age of 30 who go overseas return within two years, and 70% return within three years. The underlying policy behind the current three-year repayment holiday is to prevent overseas-based borrowers' loan balances increasing due to the imposition of penalties on missed payments while they are overseas, and this being perceived as a barrier to them returning to New Zealand and re-entering the workforce and repaying their loan. The three-year length of the repayment holiday recognises that the majority of overseas-based borrowers return home during this period and become compliant.

About 8% of overseas-based borrowers make voluntary repayments towards their student loans, while on a repayment holiday. The remainder take advantage of the holiday and make no repayments at all. Once the repayment holiday ends, levels of compliance with making repayments are very low.

There are constraints around the analysis of options regarding repayment holidays. Agencies do not yet hold complete information on the impact of the repayment holiday on overseas-based borrowers, as the first cohort of borrowers who went overseas following the introduction of this policy are only now due to make their first repayment. Those who have already come off repayment holidays are those who were already overseas at the time the holiday was introduced, and in many cases were already non-compliant prior to the introduction of the holiday. Therefore, no clear indication exists of the impact a reduced repayment holiday may have on repayment rates and the behaviour of borrowers regarding leaving New Zealand. To mitigate this, this proposal could be revisited once we have evidence about how the repayment holiday has worked.

Option 1 - Status quo

Generally, borrowers who spend some time as an overseas-based borrower become compliant upon their return to New Zealand. Migration statistics show that 50% of New Zealanders under the age of 30 years return from overseas within two years, and about 70% return within three years. These figures suggest that the current three-year repayment holiday enables most borrowers to return without being characterised as non-compliant.

About 92% of borrowers living overseas take advantage of the three-year repayment holiday and make no repayments to their student loan. 27,000 borrowers came off their repayment holiday in 2010. The vast majority of those borrowers who remain overseas-based (73% or almost 20,000) have not started to make repayments as required.

Option 2 - Reduce the three-year repayment holiday to one year

Moving to a one-year repayment holiday would create a repayment obligation of between $1,000 and $3,000 for borrowers in their second year away. Under this option, those who do not comply would face a greater loan balance than they would have if the repayment holiday had been left at three years. This can be expected to have a negative impact at the margin on borrowers' decisions regarding whether to return to New Zealand.

Changing the length of the repayment holiday from three years to one is estimated to have a one-off impact on student loan debt of $68m in the year of introduction, and an estimated ongoing increase in debt of $12m.

Option 3 - Reduce the three-year repayment holiday to two years

Moving to a two-year repayment holiday would create a repayment obligation of between $1,000 and $3,000 for overseas-based borrowers in their third year away respectively. This would apply to approximately 50% of overseas-based borrowers. If the 73% non-compliance ratio holds at the two-year mark, then the number of overseas-based borrowers in default could be expected to rise from 21% to 36.5%.

Around half of those who are overseas at the end of year two return to New Zealand around the end of year three. As with the one-year repayment holiday option, those who do not comply would face a greater loan balance than they would have if the repayment holiday had been left at three years. This can be expected to have a negative impact at the margin on borrowers' decisions regarding whether to return to New Zealand.

Changing the length of the repayment holiday from three years to two is estimated to have a one-off impact on student loan debt of $28m in the year of introduction, and an estimated ongoing increase in debt of $3m.

Option 4 - Introduce an application process for the repayment holiday

Inland Revenue finds it very difficult to maintain up-to-date contact details for overseas-based borrowers. Borrowers are currently obliged by both the student loan legislation and contract to advise Inland Revenue before they go overseas and to provide contact details. However, no practical sanction exists for non-compliance with this obligation. Historically, only 16.5% of borrowers adhere to this obligation. The lack of contact details makes it difficult for Inland Revenue to advise overseas-based borrowers of their obligations, or of any changes to the operation of the Student Loan Scheme.

The following two options have been considered to address this problem:

- All borrowers would continue to be entitled to a repayment holiday, but those who do not complete an application for it would be subject to a one-off penalty of $250. If the $250 penalty remains unpaid at the end of a 12-month period, this amount would be added back to the loan balance.
- Requiring all borrowers to apply for a repayment holiday prior to departing New Zealand and, if they do not apply, they would not be entitled to a repayment holiday.

An application process provides Inland Revenue with an opportunity to obtain up-to-date borrower contact details, and rewards compliant borrowers. Better contact details would enable Inland Revenue to inform borrowers of their repayment obligations and other information regarding their student loan.

A new process including a sanction for non-compliance should increase the number of borrowers who provide contact details. However, overseas based borrowers are generally non-compliant, so a significant proportion of borrowers are likely to not complete a new application process. If they do not complete the application for the repayment holiday, there is also a strong likelihood that they would not make the repayments which would arise in the absence of a repayment holiday. The missed payments would attract interest and penalties, and add to the balance of the loan. The value of the Government's student loan debt will also be increased by these unpaid amounts, interest, and penalties.

To be effective, the fixed penalty for failing to notify Inland Revenue of a move overseas would need to be heavily promoted to borrowers before they left New Zealand.

Applying a penalty of $250 provides consistency with an alternative rationale for the proposal, which is simply as a penalty levied by Inland Revenue for failure to comply with a "tax" obligation. Penalties of $250 are levied for non-compliance with various other tax obligations, such as failure to provide a tax return (on incomes above $100,000 per annum); an employer failing to file a monthly PAYE return; and failing to file a GST return.

Increasing repayment responsibility

Ensuring that lending is good value, increasing repayments

The long-term cost of the Scheme needs to be controlled. Current projections indicate that, by 2029/30, new lending could rise to as much as $2.7 billion per year, compared to $1.5 billion in 2009/10.

One of the main contributing factors for the rapid growth is the interest-free student loan policy. It provides little incentive for borrowers to repay their student loan early, when they are also liable for other personal loans and mortgages that are interest-bearing.

More emphasis on self-management by borrowers could reduce repayment times and decrease the student loan book balance. **[2]**

[2]

[2]

Option 3 - Require every new borrower to name a contact person

Inland Revenue's recent collection campaign experience with Australia-based borrowers showed that, when family members were made aware of a borrower's default, some remedied the default themselves and others contacted the borrower and put pressure on them to repay.

This option would involve all borrowers being obliged to name a contact person when they apply for their loan. This requirement would place no additional costs on borrowers and would provide another avenue through which Inland Revenue can contact borrowers to advise them of any issues with their loan. This option would be much easier for borrowers to comply with, as opposed to the guarantor option. The contact person would bear no responsibility for the loan, and as such, may be more inclined to agree to be a contact person.

Student Loan Repayment Threshold

Widening expectations of repayment, increasing repayments

The amount that Scheme borrowers must repay in any year depends on a borrower's income. If a borrower earns over a set threshold, currently $19,084 per year, they must make student loan repayments. Borrowers who earn above the repayment threshold are subject to a repayment rate of 10 cents in the dollar.

Until the 2005/06 tax year, the student loan repayment threshold was set relative to the Domestic Purposes Benefit rate for a sole parent with two children. In the following years, the threshold was inflation-adjusted based on the movement in the Consumer Price Index. In 2009, the Government suspended the inflation-adjustment of the repayment threshold for the 2010/11 tax year. In December 2010, the Government also suspended the inflation-adjustment of the repayment threshold for the 2011/12 tax year. Government needs to determine when to lift the suspension. We have identified three potential options for updating the repayment threshold:

- maintaining the status quo
- maintaining the threshold without CPI adjustment until 1 April 2015
- maintaining the threshold until the operating balance returns to surplus, including the cost of adjusting the student loan repayment threshold for CPI.

Demographic data on borrowers under the threshold, shows that all three options are more likely to impact on priority groups that have been identified in the Tertiary Education Strategy 2010–2015 than on other groups. The demographic profile of those currently under the threshold includes a disproportionate number of Māori, Pasifika and those under 25 years old. Although we do not know exactly how many of these borrowers will come over the threshold under each option, we can say that there will be a disproportionate impact on those groups compared to other groups. The options are graduated, so the impact will be smallest under the status quo (up to $38.17 per annum) and highest under option 3 (up to $38.17 per annum in 2012 increasing to $192.70 per annum in 2016).

Option 1 - Status quo

Maintaining the status quo (suspending the threshold until 31 March 2012 and inflation adjusting thereafter) will result in increased student loan repayments of approximately $7.6 million for the 2011/12 year, increasing to $10.6 million by 2014/15.

The proportion of borrowers with repayment obligations would gradually increase. This option would capture an increasing number of low income workers over time, potentially increasing hardship.

The New Zealand repayment threshold of $19,084 is already low compared with other countries with income contingent student loan schemes, for example Australia and the UK, and is significantly below the income of a borrower working full-time for the minimum wage.[5]

Borrowers currently under the repayment threshold (excluding current students) reflect a range of individual circumstances, including:

- unemployment, sickness, and invalid's benefit recipients; and other beneficiaries
- superannuitants
- low-income workers working part-time or part-year
- parents caring for children.

[2]

Under the Student Loan Scheme Act 1992, where a repayment deduction is required to be made from a benefit, the Commissioner of Inland Revenue must determine the repayment deduction amount in consultation with the Chief Executive of the Ministry of Social Development. Currently this agreed amount is zero, and the Ministry of Social Development's current payment systems do not deduct a student loan obligation from a borrower's benefit.

The size of the group earning under the repayment threshold, coupled with the large number of overseas-based borrowers, means that currently over 50% of all borrowers have no repayment obligation.

Option 2 - Maintain the threshold without CPI adjustment until 1 April 2015

Maintaining the threshold without CPI adjustment until 1 April 2015 would result in increased student loan repayments of approximately $12 million for the 2011/12 year, increasing to $16 million by 2014/15.

This option would be administratively simple (unless repayments from beneficiaries were required). It is less likely than option 3 to be perceived as increasing borrowers' obligations and increasing hardship for low-income earners.

The bulk of the savings from this option is generated by borrowers already over the repayment threshold. The impact of inflation will mean that even though the nominal amount of repayments will stay the same for each particular income level, inflationary effects on income will mean that most borrowers will be making higher repayments in real terms. This

5 A worker working 40 hours a week for a full year at the minimum wage of $12.75 an hour has an annual pre-tax income of $26,520.

fiscal drag will widen the base of borrowers who have a compulsory obligation, and increase the obligation amount for those currently with an obligation.

However, this option would capture an increasing number of low income workers over time, potentially increasing hardship. The Commissioner for Revenue has a number of measures under the Student Loan Scheme Act 1992 to ensure that very low income-earners do not suffer serious hardship as a result of a student loan repayment obligation. For example, the Commissioner can refrain from collecting small amounts of student loan penalties for overdue repayments.

Option 3 - Maintain the threshold until the operating balance returns to surplus, including the cost of adjusting the student loan repayment threshold for CPI

Maintaining the threshold at $19,084 until the operating balance returns to surplus involves holding the threshold until the point that, after the CPI adjustment is made, that adjustment won't put the operating balance back into deficit.

On pre-February 22 2011 predictions, maintaining the threshold without CPI adjustment until the operating deficit returns to surplus will result in increased student loan repayments of approximately $16 million for the 2011/12 year, increasing to $21 million by 2014/15. As with option 2, the bulk of the savings from this option is generated by borrowers already over the repayment threshold. However, there is a risk these numbers would change if the operating deficit returns to surplus quicker or slower than predicted.

This option would be administratively simple (unless repayments from beneficiaries were required). Compared with option 2, this option would capture an increasing number[6] of low income workers, potentially increasing hardship.

As noted above, the Commissioner for Revenue has a number of measures under the Act to ensure that very low income-earners do not suffer serious hardship as a result of a student loan repayment obligation.

Overseas-based borrowers

Increasing repayments

The level of overseas-based borrower default on student loan repayments continues to grow. As these borrowers are not within New Zealand jurisdiction, Inland Revenue has few measures to enforce payment from non-compliant overseas-based borrowers. Further, the non-compliance sends the wrong message to compliant New Zealand-based and overseas-based borrowers.

Option 1 – **[2]**

[2]

Option 2 – **[2]**

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6 The actual number affected cannot be estimated as student loan repayments are moving to a pay period system from 1 April 2012. Inland Revenue cannot access pay period data yet and any estimate of borrowers moving over the threshold would be skewed by those who have an obligation under the new pay period system and not because of the threshold freeze.

[2]
Removing the course-related cost component for part-time full-year students

Ensuring that lending is good value, reduction in borrowing

Full-time students and part-time full-year students, are able to borrow up to $1,000 for course-related costs each year to help cover expenses related to their studies such as equipment, textbooks and travel. Part-time, full-year students are those who study for a minimum of 32 weeks, and have a course load of less than 0.8 EFTS. The number of part-time, full-year borrowers increased significantly between 2002 (14,300 borrowers) and 2009 (27,800 borrowers).

Option 1 – Status quo

In 2009, the 24,200 borrowers who studied part-time full-year, made up 12% of total borrowers. Of these 24,200 students, 56% drew down course-related costs of $23.6 million in 2009. On average, every part-time full-year student borrowed $979 from the $1000 maximum course-related cost entitlement loan component.

Option 2 – Remove eligibility to course-related costs

This option would remove eligibility to the course-related cost component of the Scheme for part-time full-year study. Part-time students would only be eligible for the compulsory fees component of the Student Loan Scheme. This would affect approximately 28,000 borrowers annually.

Those most affected by the changes would be:

- older borrowers – older borrowers make up a higher proportion of part-time full-year students who borrow course-related costs
- Māori borrowers – the proportion of Māori studying part-time full-year who borrowed course-relates costs is higher than the overall proportion of Māori who borrowed course-related costs (32% versus 23%)
- female borrowers – the proportion of females studying part-time full-year who borrowed course-related costs is higher than the overall proportion of females who borrowed course-relates costs (68% versus 59%).

This option would recognise that part-time students have more of an opportunity than full-time students to undertake part-time or full-time work to meet the costs of their text books and other non-compulsory study costs. This is consistent with the reason why students cannot borrow for living costs if they are studying part-time. A risk exists that this option may lead to or increase financial difficulty for some part-time, full-year students who have a sizeable study load that just falls short of the 0.8 EFTS.

Ongoing exemption for the family of ‘protected persons’

Ensuring that lending is good value

In Budget 2010, Government agreed to introduce a two-year stand-down for eligibility for student loans for new permanent residents and Australian citizens, to apply from 1 January 2011.

The stand-down signals the Government’s expectation that new residents demonstrate their commitment to working and living in New Zealand before they can receive the benefits of the Student Loan Scheme. Importantly, it aligns student loan eligibility with eligibility for benefits and student allowances, in order to reduce the potential for misuse of student loans as income support for new migrants who cannot receive other forms of income support.

Option 1 - Status quo

The current two-year stand-down for student loans and allowances provides an exemption for ‘protected persons’ under the Immigration Act 2009, who are people considered at risk of torture, death or cruelty if deported, and for refugees and their sponsored family members. It does not include an exemption for the sponsored family members of ‘protected persons’. This creates an inconsistency in respect of student loans and allowances between the sponsored family members of protected persons and sponsored family members of people with refugee status, who are granted residence in New Zealand.

Option 2 - Exempting the families of ‘protected persons’

This option would exempt the sponsored family members of ‘protected persons’ from the two-year stand-down for student loan and allowance eligibility. This would make student support consistent with other Government policies to support this group. The change would enable the family members of people who were at risk of torture or human rights abuses overseas to study soon on their arrival in New Zealand, if needed. The Department of Labour estimates that fewer than ten people per year will be eligible for this exemption.

Consultation

The Ministry of Education, the Inland Revenue Department and SudyLink developed these proposals. The Ministry of Social Development, the Treasury, Te Puni Kōkiri and the Ministry of Pacific Island Affairs were all consulted on these proposals. We did not consult with sector groups due to the budget-sensitive nature of the proposals.

[2]

The Treasury supports the overall direction of the proposals. However, it does not support changes to the repayment holiday length as it believes that a change will not produce any significant change in behaviour. However, Treasury does support the application process for the repayment holiday, recognising this will improve the collection of contact details for overseas-based borrowers.

The Ministry of Pacific Island Affairs is concerned that the proposed changes are likely to have significant impacts on low income earners, including Pacific people. It would like to see further analysis outlining how the proposals will affect priority groups, such as Pacific learners.

[3]

Conclusions and recommendations

Proposal	Part of problem addressed	Options	Option being progressed	Borrowers affected	Impact on affected borrowers of option being progressed
Student Loan Repayment Threshold	Widening expectations of repayment Increasing repayments	Option 1 - Status quo Option 2 - Maintain the threshold without CPI adjustment until 1 April 2015 Option 3 - Maintain the threshold until the operating balance returns to surplus, including the cost of adjusting the student loan repayment threshold for CPI	Maintain the threshold without CPI adjustment until 1 April 2015. Repayments not collected from beneficiaries.	Low-income earners with a student loan.	Increases the repayment obligations of all NZ-based borrowers (220,000 people) by approximately $31.20 per year in 2012, rising to approximately $154.20 per year in 2015.
Broadening the definition of income	Widening expectations of repayment Increasing repayments	Option 1 - Status quo. Option 2 - Broadening the definition of income Option 3 - Adding back business and investment losses	Business and investment losses added back. Officials to investigate further broadening the definition of income.	Borrowers who have business and investment losses.	Approximately 10,300 borrowers will have a higher repayment obligation. Approximately 2,500 of these borrowers would not have had a repayment obligation and now will become liable to make repayments.
Restricting further student loans for those with overdue repayments	Ensuring that lending is good value Widening expectations of repayment and increasing repayments Reduction in borrowing	Option 1 - Status quo Option 2 – Threshold for overdue repayments Option 2 - Ineligible one year after being in default Option 3 - Ineligible two years after being in default	Restrict loan eligibility for borrowers have been in default for one or more years on overdue repayments of $500 or more from the time they were declared to be in default by Inland Revenue.	Borrowers with overdue repayments.	Borrowers with overdue repayments will be ineligible for further loans.
Older borrowers	Ensuring that lending is good value Reduction in borrowing	Option1 - Status quo Option 2 - Restrict eligibility to the student loan scheme for people aged 65 and over to fees only Option 3 - Remove eligibility to the student loan scheme for people aged 65 and over Option 4 - Restrict borrowing for people aged 55 and over to fees only Option 5 - Restrict borrowing for people aged 40 and over to fees only	Restrict borrowing for people aged 55 and over to fees only	Those aged 55 and over, those nearing this age and planning to study.	Those over 55 will be ineligible for living and course-related costs.

Proposal	Part of problem addressed	Options	Option being progressed	Borrowers affected	Impact on affected borrowers of option being progressed
Repayment holiday	Widening expectations of repayment Increasing repayments	Option 1 - Status quo Option 2 - Reduce the three-year repayment holiday to one year Option 3 - Reduce the three-year repayment holiday to two years Option 4 - Introduce an application process for the repayment holiday	One-year repayment holiday with an application process. A condition of successful application is either providing, or reconfirming a New Zealand contact.	Overseas-based borrowers and those borrowers intending to travel overseas.	Non-compliant borrowers will face a greater loan balance. All borrowers lose two years of repayment holiday.
Increasing repayment responsibility	Ensuring that lending is good value Increasing repayments	Option 1 - Voluntary payments on behalf of borrowers [2] Option 3 - Require every new borrower to name a contact person	Encouraging voluntary payments. Requiring every new borrower to name a contact person.	Potentially, all borrowers.	No additional costs for borrowers.
Overseas-based borrowers	Increasing repayments	[2]	[2]	Borrowers with outstanding repayments.	None as yet – officials to scope options.
Removing the course related cost component for part-time full-year students	Ensuring that lending is good value Reduction in borrowing	Option 1 – Status quo Option 2 - Remove eligibility to course-related costs	Remove eligibility to course-related costs for part-time, full-year students	Borrowers studying part-time, full-year.	Will remove eligibility for approximately 28,000 borrowers annually.
Ongoing exemption for the family of 'protected persons'	Ensuring that lending is good value	Option 1 - Status quo Option 2 - Exempting the families of 'protected persons'	Extend exemption from two-year stand-down for new permanent residents to include sponsored family members of 'protected persons'.	Anyone sponsored into NZ by a family member under the "protection" status.	Will extend the exemption to families of protected person (likely to be one or two people per year). This ensures consistency with other government policy and with the Immigration Act 2005.

Implementation

Implementation of these changes will largely require changes to computer systems, administrative procedures and communication/information to borrowers. Inland Revenue and StudyLink will implement the proposals and deal with all the system changes needed.

If the repayment threshold is to be inflation-adjusted from 1 April 2012, regulations will need to be made by the end of December 2011. System changes in relation to inflation adjusting the threshold occur as part of business as usual at Inland Revenue. If the threshold is not adjusted, no changes are required and no implementation issues arise.

Legislative amendment is required for to broaden the definition of income; the reduction of the repayment holiday and application requirement; and the information matching aspect of the contact person and not re-lending to debtors proposals. These proposals will be included in a Student Loan Scheme Amendment Bill in late 2011.

[2]

Within broadening the definition of income, the proposal to add-back business and investment losses has minimal implementation issues. This change can be implemented in existing Inland Revenue systems with minimal changes and at a cost that will be absorbed by Inland Revenue. This will be implemented for the tax year commencing 1 April 2012. **[2]**

Implementing the proposal to reduce the repayment holiday to a maximum of one year for all borrowers from 1 April 2012 will necessitate communications with some borrowers who are overseas as at that date. These borrowers may have expected to receive a longer repayment holiday. While borrowers are legally obliged to provide their contact details, it is expected that Inland Revenue will not be able to contact a number of these borrowers, resulting in them facing assessments that they are not aware of. In cases where borrowers have met their obligations to keep their contact details updated and incur penalties because Inland Revenue was still not able to contact them, there are relief provisions in the legislation which may apply. The changes will be administered in existing Inland Revenue systems. The transitional arrangements (reducing the holiday of borrowers already overseas) add a degree of complexity, but it is anticipated that this can be managed.

The requirement to apply for a repayment holiday will apply from 1 April 2012, and will initially be a phone based application process. It will subsequently become part of the online services provided as part of Student Loan Re-design, however the delivery date will need to be prioritised against other deliverables for this project.

The requirement for new borrowers to name a contact person will apply for loan applications from 1 January 2013. The process will therefore need to be in place by 1 October 2012.

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Monitoring, evaluation and review

The three agencies involved with the Scheme (Inland Revenue, StudyLink and the Ministry of Education) will monitor and review these proposals. The Scheme Governance Group will monitor the overall performance of the Scheme changes and their affect on the Scheme and borrowers and will report to Ministers on the outcomes of the initiatives.