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Treasury Committee

Student Loans: Government and Office for National Statistics responses to the Committee's Seventh Report

Fourth Special Report of Session 2017–19

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The Treasury Committee

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Fourth Special Report

On 18 February the Treasury Committee published its Seventh Report of session 2017–19, *Student Loans* (HC 478). The Government's response was received on DATE, and is published as Appendix A to this report. The Office for National Statistics's response was received on DATE, and is published as Appendix B to this report.

Appendix A: Government Response

The Treasury Select Committee published the report of its inquiry into Student Loans on 6th February 2018. This document sets out the Government's response to the Committee's report. In some cases, these responses reflect the fact that the Government is currently conducting a major review of post-18 education and funding that is due to report in early 2019.

Introduction

The Government welcomes the Committee's report on student loans.

We have a world-class higher education system, and the Higher Education and Research Act 2017 has set the foundation for further improvements to the system. We have: established the Office for Students to act as a new register of providers and ensure minimum standards; created the Director for Fair Access and Participation to drive social mobility; and enacted the Teaching Excellence and Student Outcomes Framework (TEF) to hold universities to account for the teaching and outcomes they deliver for students. We are also encouraging further diversity within the system, with new providers and shorter degrees delivered at a lower cost to students.

More specifically, evidence clearly shows that the current student finance system has delivered benefits in key areas. The Government has been able to lift the cap on the number of student places, so that universities can expand and widen access. The system is delivering improved outcomes for disadvantaged students; there is a record entry rate for 18 year olds going to university for full-time study, including those from disadvantaged backgrounds. Students on the lowest incomes who have started their courses this academic year (2017/18) have access to the highest ever amounts of support for living costs. The Government has also improved the terms on which it provides financial support to students by increasing the earnings threshold above which graduates are required to make repayments on their loans from £21,000 to £25,000 from 6th April 2018, and rising by average earnings thereafter.

While the current student finance system has enabled significant improvements, the Government agrees that further work needs to take place to build on these important achievements and ensure a joined-up system that works for everyone. The Government has therefore announced a major review across post-18 education and funding to look at how we can ensure that the education system for those aged 18 years and over is accessible to all, is supported by a funding system that provides value for money and works for students and taxpayers, incentivises choice and competition across the sector, and encourages the development of the skills that we need as a country.

The overall review is being led by the Department for Education (DfE) and will report to the Secretary of State for Education, the Chancellor of the Exchequer, and the Prime Minister. An independent panel, led by Philip Augar and comprising five experts from across the tertiary education sector, has been appointed to provide input into the review. The panel will be informed by an extensive programme of engagement with stakeholders and experts, including students and recent graduates.

The panel will publish its report at an interim stage, before the Government concludes the overall review in early 2019.

Responses to individual recommendations

Public finances and the design of the system

1. *Due to the National Accounts accounting rules, there is no impact on the deficit when student loans are issued. As such, shifting the vast majority of all higher education spending into loans that are written off in 30 years has shifted nearly all higher education spending out of the deficit. Policy decisions taken today will have no impact on the public finances for the next 30 years. Based on the current RAB charge, £6–7 billion of annual write-offs are missing from the deficit. This figure is approximately equivalent to excluding the entire NHS capital budget from the deficit.* (Paragraph 27)

2. *The National Accounts accounting rules stipulate that if student loans are sold off at a loss before they are written off after 30 years, there is no impact on the deficit whatsoever. The policy of selling off student loans prior to their write-off allows the Government to spend billions of pounds of public money without any negative impact on its deficit target at all, creating a huge incentive for the Government to finance higher education through loans that can be sold off.* (Paragraph 28)

3. *The Government concluded its first sale of income contingent student loans in December 2017, when it sold £3.5 billion of loans, writing off £1.8 billion (51 per cent) of those loans in the process. The Government plans to sell off £12 billion of loans over the next five years. If the rate of losses on these sales is maintained, billions of pounds of student loan losses will be crystallised without having any impact on the deficit. Its inclusion would increase the deficit as forecast by the Office for Budget Responsibility (OBR) by 13 per cent, from £45.5 billion to £51 billion.* (Paragraph 29)

4. *Political control over increasing Government expenditure is exerted through analysis of Public Sector Net Borrowing (the deficit) which the Government sets as its fiscal target. The OBR assesses whether the Government will meet this target and subsequently the majority of political debate on public spending is focused on it. As the writing off of student loans will have no impact on the deficit for the next 30 years, the large and increasing level of money spent on higher education makes no difference to whether the Government is meeting its target, and therefore escapes scrutiny. There is no effective control over the increasing fiscal cost of the student loan regime.* ***Better oversight could be achieved through linking the Government's fiscal borrowing target to the Public Sector Net Cash Requirement, (how much money the Government actually needs to borrow).*** (Paragraph 30)

In accounting for student loans, the Government follows international accounting and reporting standards.

The treatment of student loans in the National Accounts follows rules set out by the European System of National and Regional Accounts 2010, which is enshrined in European legislation. These are in turn based on the UN's System of National Accounts 2008. These rules set out that loans should be represented at their face value and only show write-offs when they occur.

Student loans accounting is further set out in the annual report and accounts of the Department for Education, and in the Whole of Government Accounts. These are prepared in line with International Financial Reporting Standards (IFRS), and show the carrying value of student loans (the face value less the impairment).

The value of the impairment is set out as the Resource Accounting and Budgeting (RAB) Charge in the Department for Education's budgets. HM Treasury also sets a target impairment, which is designed to ensure that the Department has an increased incentive to manage the loan book effectively and that the impact of any changes which affect the impairment can be reflected in budgets subject to agreement with HM Treasury.

Together, these provide transparent and complementary information on the student loan system and are all used to inform policy decisions. The Government follows the international standards determined for each set of accounts – it would not be appropriate to be selective about the standards to follow.

The systems outlined above provide oversight on the fiscal and budgeting impacts of student loans. The government has fiscal targets on debt and student loans have an immediate impact on Public Sector Net Debt (PSND) at issue, meaning that policy decisions taken today have an impact on public finances.

Public Sector Net Borrowing (PSNB) is used as a key fiscal measure as opposed to Public Sector Net Cash Requirement (PSNCR) because PSNB, as an accrued measure, aligns more closely with economic activity than PSNCR and also captures longer-term effects than pure cash transactions, such as depreciation. PSND is a cash measure used for control alongside PSNB. PSNCR also does not align closely with what the Government needs to borrow via gilts.

It is the Government's policy (as outlined in the Green Book) to take opportunities to reduce PSND by selling public assets it no longer has a reason to hold in a way that represents value for money for the taxpayer. These student loans could be sold precisely because they have achieved their original policy objective of supporting students to access higher education. The benefit to PSND is equivalent to the proceeds received. The amount that would have been written off as a cost in PSNB remains as debt in the PSND measure.

5. *The Government is not responsible for the international accounting rules that allow the fiscal illusions within student loans to exist. However, the National Accounts accounting rules regarding financial transactions were not intended to be used for loans that, as the Government readily promotes, are designed to not be paid back in full. Loans that are intended to be written off are, in substance, a partially repayable grant rather than a loan.* ***The ONS should re-examine its classification of student loans as financial assets—which they are in legal form—and consider whether a portion of the loan should, in substance, be classed as a grant.*** (Paragraph 31)

The ONS will provide a separate response to this recommendation from the Committee.

6. *The Resource Accounting and Budgeting (RAB) charge is one of the most important numbers in the student loan debate. It presents, as a single figure, how much student debt the Government expects it will have to write off.* ***Despite this, the 2016–17 Department for Education Annual report and accounts did not specify the RAB charge. The Committee recommends that it should be published prominently in the Department for Education's Annual report and accounts, and should be publicly updated alongside any changes to the student loan repayment framework.*** (Paragraph 32)

DfE makes public the RAB charge each year, as used in its accounts. The 2016/17 RAB charge was published in response to a written parliamentary question from Lord Hunt of Kings Heath on July 20 last year. Following the announcement of the increase in the repayment threshold in 2018–19, an updated RAB charge estimate was published on 23 October 2017 in response to a written parliamentary question from Angela Rayner.

From this year, DfE will start publishing a regular statistical publication containing its student loan forecasts, including the RAB charge. The first publication is planned for June 2018, and it will be updated annually. We do not plan to publish updated forecasts between publications unless it is deemed necessary due to exceptional circumstances, for example if there was a substantial change to the student loan repayment framework, in which case they would be published in an ad hoc statistical release.

Work is currently underway to complete the Department for Education's annual report and accounts for 2017–18, including its disclosure requirements. How the RAB will be presented is under review.

7. *The Government is better able to manage an exposure to macroeconomic risks— such as low overall wage growth and low rates of employment—than the private sector. As a result, private sector investors require a large risk margin when taking on student loan assets from Government. The risk margin on the first student loans sale was, in aggregate, 51 per cent of the sale price.* (Paragraph 39)

The loans sell at a discount to face value because a certain lump sum today is worth more than a risky flow of repayment income over many years in to the future (the face value represents the current outstanding balances of the loans). A number of factors contribute to this discount and risk margin is only one of these. Firstly, The Government issues student loans to enable anyone who is eligible for support and able to gain a place to study, and therefore does not expect them all to be repaid in full. This accounts for much of the discount to face value on sale. Secondly, as the loans mature, a higher proportion of the loans left will not be repaid in full, which is reflected in a larger discount to face value. Thirdly, and more generally, the Government forecasts future repayments and discounts these to determine their present value. The discount rate used to determine the value of retaining the loans takes account of the risks the Government is exposed to as a holder of the asset and the opportunity cost of having money tied up in the asset. The "risk margin" properly refers only to the portion of the discount rate which reflects the risk of the return varying from what is forecast.

The Government holds assets to achieve policy objectives, and in making investments it does not aim to achieve diversified returns. Once these policy objectives have been achieved, as is the case once student loans are issued, it considers whether it would be better value for money to retain or sell them. The market as a whole has a much larger and more diversified balance sheet than Government and hence is likely to have a greater risk appetite. Repayments of student loans are linked to earnings, RPI and the Bank of England Base Rate (for pre 2012 loans). Selling the loans reduces the Government's exposure to fluctuations in these. The private sector will place value on the opportunity the asset presents to diversify their portfolios and / or hedge liabilities with similar features.

8. *Exchanging student loans for cash does not improve the Government's financial position, it merely exchanges one asset for another. Despite this, the sale does reduce Public Sector Net Debt. Such a fiscal illusion does little to improve the Government's financial position and may in fact cost the taxpayer money.* (Paragraph 40)

The Government aims to maintain credible public finances. Its policy is to reduce debt by selling public assets it no longer has a reason to hold, in a way that represents taxpayer value. Each sale is intended to have the assets declassified with substantially all the risk and rewards transferred to investors.

Through each sale, the Government will exchange an illiquid asset for a liquid one. The Government also exchanges the uncertainty of future repayments for the certainty of sale proceeds that can be reinvested in policies where market failures or gaps exist, or used to reduce debt. The Government appraises value for money on a consistent basis, following Green Book principles for all investment and asset management decisions, irrespective of the fiscal position.

9. *Such a high risk margin—and the fact that selling off the loans does not improve the Government's fiscal position—suggests the Government may be better off keeping student loans on its own balance sheet, rather than shifting the risks to the private sector and paying a large premium for doing so.* (Paragraph 41)

The Government is not better placed to carry this type of risk than investors, and the sale of student loans has a significant fiscal benefit in reducing PSND – exchanging an illiquid asset for a liquid one, and uncertainty of future repayments for the certainty of sale proceeds. The Government's policy is to take the opportunity to reduce debt by selling public assets it no longer has a reason to hold, in a way that represents taxpayer value.

10. *Whether the sale of student loans passes the Treasury's value for money test is heavily dependent on the discount rate used to calculate the future value of student loan repayments. As with all discount rates, there is a large margin for error. The Government has chosen a different discount rate for the purposes of the sale—a rate which places a lower value on the future repayments of the loans—than that which is used in the Department for Education Accounts. As part of its major review, the Government should consider using the same discount rate as that used in the Department for Education Accounts, as audited by the National Audit Office.* (Paragraph 42)

HM Treasury's value for money test

On 7th December 2017, the Department laid a report in the library of the House which set out the detail of the sale arrangements to give Parliament information about the extent to which the arrangements represented good value, reflecting any guidance given by the Treasury about assessing value for money, as is required by Section 4 of the Sale of Student Loans Act 2008.

When considering whether the sale arrangements delivered good value for the taxpayer, the Government followed the guidance set out in HM Treasury's Green Book for assessing public spending decisions and the supplementary guidance "Value for money and the valuation of public sector assets". HM Treasury also provided a framework for applying this guidance to assess whether a sale of student loans represented value for money for the taxpayer.

This framework set out three key tests to ensure the sale represented value for money:

- That an efficient market exists for this asset.
- That the sale is structured and executed in such a way as to promote efficient pricing.
- That the sale value exceeds the Government Retention Value (calculated using HM Treasury Green Book principles).

These tests were met for the first sale and the detail is set out in that report. Further, the NAO is currently undertaking a value for money study on the first sale and expects to report to the Public Accounts Committee before summer recess.

Accounting vs retention value

The accounting value and retention value of the loans are different because they serve different purposes. The accounting value is equal to the fair value of the asset and this is calculated in line with the relevant accounting standards, and is consistent with the way the Government prepares its accounts across departments, and is audited by the NAO. It is not based on—and is not intended to represent—market value. By contrast, the retention value takes into account the risks that the Government is exposed to as a holder of the loans and the opportunity cost of having money tied up in the loans. As the accounting value does not need to reflect these factors, it uses a discount rate (as per the FReM) which is lower than the discount rate used to compute the retention value. The retention value is determined using HM Treasury's Green Book approach to setting discount rates for asset sales. This is the approach that the Government uses for all investment and asset management decisions to ensure there is a fair comparison across a whole range of future spending and investment options.

11. ***It is undisputed that writing off a significant proportion of student loan debt is a deliberate design feature of the student loan system, making a student loan unlike any other form of loan or debt. In the absence of an effective explanation of the student loan framework—including the terms and conditions students are accepting—it is inevitable that the public will see write-offs as emblematic of a failing system. The criticism of retrospective changes which increase the burden on graduates as "unfair", levelled by MoneySavingExpert and the National Union of Students, is justified. The Government should cease this practice.*** (Paragraph 49)

Prospective students have access to a wide range of information across a range of platforms before they submit their loan application. Full terms and conditions are set out at the last stage of the student loan application process, and it is made clear that these may be amended in the future. Students must sign a declaration confirming that they have read and understood the terms and conditions before they are able to submit a loan application. The Student Loans Company (SLC) works continually to improve the information that it provides to students and their parents on all aspects of student loan repayment.

The key terms and conditions of student loan repayment are set out in the Education (Student Loans) (Repayment) Regulations 2009. This means that any changes to these terms and conditions are subject to Parliamentary scrutiny. It is important that, subject to this Parliamentary scrutiny, the Government retains the power to adjust the terms and conditions of student loan repayment after loans have been taken out. This is because if this Government or a future Government decides to make changes to the terms and conditions of student loans, in many circumstances it may be more equitable to apply these changes to all student loan borrowers rather than solely to new student loan borrowers. Changes to terms and conditions can benefit borrowers; for example, the increase in the repayment threshold from £21,000 in 2017–18 to £25,000 in 2018–19 will benefit borrowers by up to £360 in 2018–19 in terms of reduced repayments.

12. *The then Universities Minister Jo Johnson stated that the higher education funding system "is delivering [its] core policy objectives", one of which is to "fairly share costs between the general taxpayer and the individual student". The fairness of the funding split is subjective; the Government should instead aim to achieve a split that is economically optimal. It is not clear how large a range of funding splits the Government would consider optimal, given that the split has swung by 10–12 percentage points since the new repayment threshold has been introduced.* ***The Government should define what it considers to be an optimal split to give greater certainty for future public spending.*** (Paragraph 50)

Our higher education sector plays a significant role in delivering key benefits for the UK economy and society as a whole, as well as conveying a considerable private benefit to students.

The review of post-18 education and funding will consider how to ensure the system provides value for money and works for students and taxpayers. In particular, the review will look at how students and graduates contribute to the cost of their studies, including the level, terms and duration of their contribution. The review's recommendations will be guided by the need to maintain the principle that students should contribute to the cost of their studies while ensuring that payments are progressive and income contingent.

13. *The Committee welcomes the Government's planned major review of student financing and university funding. It is, however, regrettable that Jo Johnson effectively ruled out "radical change to the core architecture [of the student loan system]" in his oral evidence. The Committee hopes that Sam Gyimah, the new Minister for Higher Education, will approach the review with an open mind.* ***The review must be objective, widely framed, and empowered to bring about any changes deemed necessary, be they radical or otherwise.*** (Paragraph 51)

An independent panel, led by Philip Augar and comprising five experts from across the tertiary education sector, has been appointed to provide input into the review. The panel will be informed by an extensive programme of engagement with stakeholders and experts, including students and recent graduates.

The scope of the review is wide-ranging and intended to ensure a joined-up system that works for everyone. The review will look at how we can ensure that the education system for those aged 18 and over is:

- accessible to all;
- supported by a funding system that provides value for money and works for students and taxpayers;
- incentivises choice and competition across the sector; and
- encourages the development of the skills that we need as a country.

It is for the independent panel to consider the issues raised within the terms of reference in their report to Government. The Government cannot prejudge the findings of the panel or outcomes of the review.

14. *In his evidence to the Committee, Lord Willetts argued for a five-year review in which the parameters of the student loan system are openly considered. There is merit in this proposal—which the Committee assumes would mean changes are made only after such reviews—not least for greater transparency.* ***As part of its major review, the Government should analyse the benefits and drawbacks associated with introducing a pre-defined periodic review of student loan terms, and should ensure it takes account of the thoughts of students when considering the merit of this proposal.*** (Paragraph 52)

The terms of reference of the review cover all post-18 education and training. It is now for the independent panel to consider the issues raised within the terms of reference in their report to Government. The Government cannot prejudge the findings of the panel or outcomes of the review.

The recommendations of the Committee will be passed to the panel to consider alongside other evidence.

15. *The Committee sees no justification for using RPI to calculate student loan interest rates. RPI is no longer a National Statistic and has been widely discredited. In its Autumn Budget the Government acknowledged that the use of RPI was unfair for business rates, and the Committee is unconvinced by the case put forward for its use by the then Minister, in line with the Committee's report on the Autumn Budget.* ***The Government should abandon the use of RPI in favour of CPI to calculate student loan interest rates.*** (Paragraph 64)

The ONS currently publish several measures of inflation. RPI has always been used for calculating interest on student loans, providing consistency over time. RPI is also the measure used for the Government's index-linked gilt issuance.

The flaws in the RPI measure of inflation are well understood, and the ONS have delivered a substantial programme of work to improve the way they measure inflation over the last two years.

The review of post-18 education and funding will look at how students and graduates contribute to the cost of their studies, including the level, terms and duration of their contribution. It is now for the independent panel to consider the issues raised within the terms of reference in their report to Government. The Government cannot prejudge the findings of the panel or outcomes of the review.

16. *The Committee recognises the importance of preventing student loans being taken out to be invested, and it is right that the interest rate should seek to prevent this. However, given that tuition fee loans—which make up significantly more than half of an average student's stock of debt on graduation—are paid by the Student Loans Company directly to the university, there is little justification for applying high interest rates to the tuition fee element of student loans while students are studying.* ***Applying an interest rate above the level of inflation to tuition fee loans whilst the student is still at university is perceived to be a punitive measure and should be reconsidered.*** (Paragraph 65)

17. *The Government has justified the existing level and structure of interest rates on student loans on the grounds that it is progressive. In reality, the student loan system has complex redistributive effects that are not strictly progressive. High-flying lawyers will generally pay less than teachers; but both will pay more than a graduate who does not receive a pay premium from their time in higher education.* ***As part of its major review, the Government should re-examine the repayment system to address this anomaly so that the highest earning graduates are those that make the highest contribution.*** (Paragraph 66)

18. *The Committee is therefore unconvinced that the interest rates currently charged on student loans can be justified on redistributive grounds. Nor has any other persuasive explanation been provided for why student loan interest rates should exceed those prevailing in the market, the Government's own cost of borrowing, and the rate of inflation.* (Paragraph 67)

The interest rate on student loans needs to be considered together with the other aspects of the student finance system as a coherent whole.

We disagree with the Committee's view that student loan interest rates exceed those prevailing on the market. Section 22 of the Teaching and Higher Education Act 1998 states that the rates of interest charged on student loans must be either: (i) lower than those prevailing on the market; or (ii) no higher than those prevailing on the market, where the other terms on which such loans are provided are more favourable to borrowers than those prevailing on the market. DfE regularly monitors the interest rates on student loans against the interest rates prevailing on the market. It should be noted that Government-issued student loans have much more favourable terms than commercial loans. Loans are available to all eligible students, regardless of their previous financial history. Repayments are calculated based on income, not on the amount borrowed. Borrowers earning less than the repayment threshold (£25,000 in the 2018–19 financial year) repay nothing at all, and loans are written off after 30 years with no detriment to the borrower. DfE is not aware of any commercial loans that offer this level of borrower protection, which means that it is difficult to identify exact comparators on the market. The most appropriate comparators that DfE has identified for undergraduate student loans are the reference rates published by the Bank of England (data series CFMBJ77 and CFMBJ94 – effective interest rates for new and existing unsecured personal loans). Both rates are currently above the maximum interest rate charged on student loans.

Under the current student finance system, the main purpose of charging an interest rate of RPI+3% during study is to increase the contribution that higher-earning graduates make to the student finance system. In practice, charging an interest rate of RPI+3% during study only increases the lifetime payments of those who go on to be high earners and pay back all, or very nearly all, of their student loans. The vast majority of those who do not fully pay back their loans will see this part of their borrowing written off. Reducing the in-study interest rate would, therefore, benefit only high earning graduates, and even then only years in the future when they are close to repaying their loans in full. This is a key reason why the Government decided to increase the repayment threshold to £25,000 instead of lowering in-study interest rates; it was a more progressive change because it benefited lower and middle earning graduates.

When the current student finance system was introduced, the Government decided that post-study interest rates should be variable based on income. This was intended to address the shortcoming of the pre-2012 student finance system, as identified in the Browne Review, that no graduate paid a real rate of interest and so everyone, even the highest earners, benefited from the same level of Government subsidy. Without the income-based variable interest rate, the highest earners would pay off their loans more quickly and so make a lower contribution to the student finance system than those on lower incomes who make lower repayments and so are spending longer in repayment with interest being charged. The income-based variable interest rate system therefore makes the system more progressive, as higher earners contribute more to the sustainability of the higher education system than under a system without income-based variable rates. The Government recognises the point made by the Committee that a graduate who experiences rapid pay growth in the early stages of their career and continues to be a high earner may pay back less overall than graduates who do not experience such rapid pay growth in the early stages of their careers. However, this will be a feature of any loan system where repayments are linked to income and where a real rate of interest is charged to higher earners, and any move to lower the interest rate would see a reduction in the total contribution from the highest earners.

The review of post-18 education and funding will look at how we can ensure our post-18 education system is joined up and works for everyone. It will consider how to ensure the system provides value for money and works for students and taxpayers: in particular, how students and graduates contribute to the cost of their studies, including the level, terms and duration of their contribution, while maintaining the link that those who benefit from post-18 education contribute to its costs.

19. *It is incumbent on the Government to ensure that the student loan system is well explained so that prospective students and their families are able to make well informed decisions.* ***The Government must take steps to ensure that the student loan system—and particularly the interest rate—is well explained to those that it affects.*** (Paragraph 68)

The SLC uses customer research and insight to test student finance information, including that on interest rates. Information, advice and guidance is prepared using plain English, and delivered on the channels and in the formats that students, prospective students and their parents prefer. SLC regularly reviews and updates these materials and is continually looking for ways to improve them. A recent example is the new parents' guide published on .GOV.UK, which was co-written by the SLC and the Government Digital Service to advise parents on the income they need to submit as part of the student application process.

In addition to student finance guides published by Student Finance England (SFE) on .GOV.UK for students, prospective students and their parents, the "SFE Student Finance Zone" on the studentroom.co.uk website also provides advice for students and prospective students on the student support package and loan repayments.

For each of the past seven years, the Government has also commissioned the "Student Finance Tour", which sees a team of recent graduates deliver presentations to prospective higher education students in years 12 and 13, and their parents, in schools, sixth forms and colleges across England. The presenters provide attendees with clear information on the financial support package available to support higher education study (including an explanation of how interest is applied and how repayments are made).

The terms of reference of the review of post-18 education and funding include consideration of how the Government and institutions communicate with students and graduates around student finance, ensuring this communication is as clear as possible (consistent with the relevant legal requirements) about the nature and terms of student support.

Is there a market in higher education?

20. *In implementing the 2012 reforms, contrary to the recommendations of the Browne Review, the then Coalition Government chose to introduce a cap on tuition fees. The evidence provided to the Committee suggests this was done in the knowledge that it would create a market with no meaningful price competition. Whether price competition in the higher education sector could ever be a realistic, or desirable, prospect—even without a tuition fee cap—is debatable; the incentives for students to choose courses that command smaller tuition fees are weak.* (Paragraph 79)

21. *Nevertheless, the Coalition Government's expectation in advance of the 2012 reforms was that competition from new market entrants—combined with additional obligations for those universities choosing to charge above £6,000—would lead to prevailing tuition fees of around £7,500. It is overwhelmingly clear that this was a naïve assumption. Given that fees are almost universally well in excess of the level the Government intended when introducing the new fee regime,* ***the Government should explain, and explore in its expected review, why the higher rate of fees being charged is desirable.*** *In England, the consequences of reducing the maximum tuition fee to £7,500 or £6,000, as some have advocated, would be that the highest earning graduates pay less, and the level of funding for universities would be reduced, without either a significant increase in subsidy from the taxpayer or, more likely, the reintroduction of caps on student numbers.* (Paragraph 80)

The review will look at how the system can incentivise choice and competition across post-18 education while placing no cap on the number of students who can benefit from it.

The majority of universities charge the maximum possible fees for at least some of their courses. The review will consider value for money for both the student and the taxpayer. It will also consider how best to promote institutional efficiency whilst ensuring that funding arrangements across post-18 education and training are transparent and do not act as barriers to choice or provision.

22. *The current structure of the higher education market creates financial incentives for universities to recruit more students, yet the NAO has found that market incentives*

to achieve such expansion by improving course quality are weak. It is wrong to assume that the competition to recruit more students will be played out through competing on the basis of quality. If pursued recklessly, the aim of attracting ever greater student numbers can be damaging. The fact that university spending on marketing is increasing shows that universities can compete in ways that do not deliver any educational improvements. The market mechanisms the Government has applied to the sector are not, in and of themselves, sufficient to drive meaningful improvements in quality. (Paragraph 84)

23. ***If the Government is committed to creating a higher education market that functions effectively, it must take steps to improve both the quality and dissemination of information.*** *Without adequate information, an efficiently functioning market will struggle to develop. Prospective students face the unenviable task of determining whether to participate in higher education based on increasing quantities of university marketing material coupled with a lack of proven, reliable metrics for judging the quality of courses. It is vitally important that students are able to make informed choices about what and where to study. Such decisions are typically taken at a relatively young age, yet they carry significant long-term implications.* (Paragraph 88)

24. *The Committee notes that the Office for Students will be tasked with developing the Teaching Excellence Framework further by taking it to subject level. This is a sensible step, but the Committee fears the Government's efforts may be wasted if it fails to address the fact that so few students are currently making use of information that is already available.* (Paragraph 89)

The Office for Students (OfS) will be developing a new student information strategy, which will consider how to improve the information available to students. We expect that it will have extensive input from current and prospective students, teachers and advisers. As part of this new strategy, the OfS will launch a revised Unistats website by September 2019. We envisage a much-improved website which will be accessible for all students and we expect the OfS to take the latest research into account. OfS will incorporate Longitudinal Educational Outcomes (LEO) data into Unistats as soon as is possible.

The terms of reference of the review of post-18 education and funding review confirm that it will look at how we can help young people make effective choices between academic, technical and vocational routes after 18, including information on earnings outcomes and the quality of the teaching they receive.

Recommendations will complement ongoing reforms, including the Teaching Excellence and Student Outcomes Framework (TEF), which seeks to drive up the standard of teaching and to give students clear information about where teaching quality is best and where students have achieved the best outcomes. The TEF assesses providers against a set of core and supplementary metrics which measure: how many students do not continue with their studies after starting; how satisfied students are with key aspects of their teaching and learning; grade inflation; and graduates' employment after they leave. Higher education providers will have to comply with the new Transparency Duty, which will be an ongoing condition of registration for all registered providers prescribed by the Secretary of State. This requires providers to publish on their websites, and supply to the OfS, information on the number of applications, offers, and acceptances, and completion and attainment rates, broken down by gender, ethnicity and socioeconomic status.

University finances

25. *Against a backdrop of sustained reductions in public spending, the 2012 reforms saw university funding increase significantly. The sector was spared austerity. The provision of extra resource to universities sought to bring funding up to an appropriate, sustainable level that could ensure the delivery of high quality teaching outcomes. The country's universities are an asset, and are rightly admired internationally; a point that is often forgotten in public discourse.* (Paragraph 98)

26. *The Committee heard that universities are not awash with cash, rather, they are now being funded sustainably, with teaching now typically breaking even. This position must be maintained to ensure that we defend the UK's world-class higher education system.* (Paragraph 99)

We are pleased that the Committee has recognised that the 2012 reforms saw university funding increase significantly. These reforms have helped ensure that universities are sufficiently resourced while allowing expanding student numbers. The Office for Students will have a duty to monitor the financial sustainability of the sector and following the regulatory framework consultation we will be working closely with them on this.

As set out in the terms of reference of the review of post-18 education and funding, the Government is committed to maintaining the financial sustainability of a world-class higher education and research sector.

Issues for students

27. *It is clear that the student loan system is complex, and has become even more so as a result of piecemeal changes to student loan terms.* ***In conducting its major review of university funding and student financing, the Government must be mindful of the risk that additional changes lead only to more confusion. The Government should take this opportunity to simplify the system and significantly improve how it is explained. Prospective students must be able to easily comprehend the system, given the long-lasting financial implications of accessing student finance. It is the Government's responsibility to ensure that a good understanding of the system is commonplace.*** (Paragraph 108)

The terms of reference of the review of post-18 education and funding include ensuring that funding arrangements across post-18 education and training are transparent and do not act as barriers to choice or provision.

The review will also look at how the Government and institutions communicate with students and graduates around student finance, ensuring this communication is as clear as possible (consistent with the relevant legal requirements) about the nature and terms of student support.

28. *Student loan debt is only repaid when earnings surpass a given threshold and is written off after a defined number of years. It should not be thought of as akin to typical debt. In using the terms "loan" and "debt", the Government has made it all too easy for students and their families to think of it in this way. It is easy to imagine how the thought of accruing tens of thousands of pounds in so-called "debt" could serve as a deterrent for young people considering applying to university, and the Committee is concerned by the thought of prospective students choosing not to enter higher education due to misperceptions about*

the nature of student loan debt. ***Loan statements sent by the Student Loans Company are likely to have reinforced this troubling misconception, and must be improved to better convey the true nature of student loan repayments.*** (Paragraph 109)

29. *The Committee welcomed the former Universities Minister's admission that alternative language would be preferable.* ***The Government should introduce new language that better reflects the workings of the student finance system.*** (Paragraph 110)

The Government recognises that some prospective students and their parents are worried about what they see as rising levels of graduate debt. DfE and the SLC are committed to improving understanding of the student loan repayments system and the income-contingent nature of student loan repayments. The Government's response to recommendation 19 above outlines some key steps that SLC and the Government are currently taking to explain the student loan system to those whom it affects.

The review of post-18 education and funding will consider how the Government and institutions communicate with students and graduates around student finance, ensuring this communication is as clear as possible (consistent with the relevant legal requirements) about the nature and terms of student support.

30. *Maintenance loans are equally, if not more, difficult than tuition fees for prospective students to understand.* ***The Government sends mixed messages; former Universities Minister Jo Johnson told the Committee that maintenance loans are not intended to cover a student's living costs in their entirety, but that the Government is not being prescriptive about an expected parental contribution. This may mean that some students who lack access to additional sources of income are priced out of a university education. This is clearly at odds with the Government's stated aim of removing barriers to access—the Government should consider how to address this as part of its major review.*** (Paragraph 118)

The household income assessment for living costs support inevitably involves a degree of complexity. We believe the current income assessment balances the need to assess a student's household income fairly and equitably and to ensure that student support is assessed accurately and paid at the start of each term.

The Government is clear that it does not prescribe exactly how much support parents should provide for a student's living costs while attending university. It has been a long-standing principle of student support in England that living costs support is paid as a contribution towards a student's living costs at university rather than necessarily to cover them in their entirety. This is because survey evidence shows that students' living costs vary widely and it is therefore not realistic to come up with one figure that represents "the cost of attending university".

The review of post-18 education and funding will consider how to provide a system that is accessible to all, and in particular how we can ensure that people from disadvantaged backgrounds have equal opportunities to progress to and succeed in all forms of post-18 education and training.

The review will consider how disadvantaged students and learners receive maintenance support, both from Government and from universities and colleges. It is now for the independent panel to consider the issues raised within the terms of reference in their report to Government. The Government cannot prejudge the findings of the panel or outcomes of the review.

31. *The former Minister's assertion that the Government does not assume parents will contribute to living costs is directly contradicted by official Student Loans Company documentation, which states that depending on their income, parents may have to contribute towards the living costs of their student children. The assumed parental contribution will undoubtedly create financial pressure for households with multiple children at university, and the Committee is unconvinced that the maintenance loan system adequately accounts for this.* ***The fact that parents are expected to contribute to living costs must be made much more explicit. Alternatively, if the Government maintains that it does not expect a parental contribution, Student Loans Company documentation must be corrected, and the Government must explain how university is free at the point of use for students without additional sources of income.*** (Paragraph 119)

While parents may make a contribution towards a student's living costs, the Government does not define a parental contribution, nor can one be implied simply by subtracting a student's actual loan for living costs entitlement from the maximum loan. Students supplement their living costs support through a variety of means, including parental support, their own employment, or savings. The Government does not stipulate how much parents should contribute towards the costs of their children's education and it is not for the Government to regulate family relationships in that respect.

The Government already provides additional help for families with more than one student at university. When assessing a family's income, we take account of the size of the family, and for each additional child in the family reduce the income to be taken into account in the household income assessment by £1,130 per child.

Additional support for students' living costs is available to help middle income families on incomes of above £42,875 with more than one full-time student attending higher education courses during an academic year. Each student in a middle income family with more than one student will receive more loan for living costs per student than a student from a single-student family with the same household income.

Student Finance England publishes guides for students and prospective students on an annual basis and DfE will ensure that these fully reflect Government policy.

32. *It is vital that public debate on the issue of maintenance loans is well informed. It is deeply regrettable that* ***the Government is still yet to publish the 2014–15 Student Income and Expenditure Survey****, which will clearly be highly informative in helping the public understand students' financial circumstances. The value of the survey's findings is no doubt diminishing with the passage of time.* ***The Committee recommends that this information is published urgently. The need for maintenance grants to be reintroduced has also been highlighted to the Committee, and the Government should assess the case for doing so as part of its major review****.* (Paragraph 120)

The 2014–15 Student Income and Expenditure Survey report has now been published and can be found at the following link:

https://www.gov.uk/government/publications/student-income-and-expenditure-survey-2014-to-2015

The dataset will also be published in the UK Data Archive.

As noted above under recommendation 30, the review will consider how disadvantaged students and learners receive maintenance support, both from Government and from universities and colleges.

33. *The Committee agrees that the sharp decline in part-time student numbers—brought about in part by the 2012 reforms—is regrettable. It is clear that the Government failed to anticipate the impact the 2012 reforms would have on part-time students.* ***The Government's major review of student financing and university funding should include a fundamental rethink of its offer to part-time students. It should ensure that part-time study is a credible option as part of lifelong learning and retraining, and that it provides access to higher education for those who are unable to study full-time.*** (Paragraph 122)

We want everyone with the potential to benefit from higher education to be able to do so. Studying part-time and later in life brings enormous benefits for individuals, the economy and employers. We are confident that by making the higher education system more diverse, innovative and responsive, we can open it up to people who need more flexible ways of studying. This is not just about increasing part-time study, but also accelerated courses, online learning and work-based learning (including degree apprenticeships).

The reasons for the decline in part-time numbers since they peaked in 2008 are complex. The decline began before the 2012 fee changes and it is likely that there are a number of factors at play.

The Government offers tuition fee loans for part-time students. In addition to this, maintenance loans for part-time students will be introduced, for the first time, from 2018/19, and we intend to extend these loans to distance learners in 2019/20 subject to robust controls being developed and put in place. This reflects the Government's intention to provide financial support to part-time students similar to the support given to full-time students.

The review of post-18 education and funding will look at the needs of all post-18 students, to ensure a joined-up system that works for everyone. The terms of reference of the review confirm that it will look at how we can encourage learning that is more flexible (for example, part-time, distance learning and commuter study options) and complements ongoing Government work to support people to study at different times in their lives.

34. *The Committee recognises the complexities associated with the task of introducing Sharia compliant loans.* ***The Department for Education should make use of Islamic Finance expertise both within Government and externally to ensure an alternative student finance model is introduced as soon as possible.*** (Paragraph 124)

We are making good progress in preparing for the introduction of an alternative student finance offer. We agree with the Committee's recommendation and have appointed expert specialist advisers, Islamic Finance Council UK, to help us with the early stages of this process, as well as seeking out expertise within Government to address the complexities in this area.

35. *It is concerning that the Student Loans Company's inability to make use of readily available data is leading thousands of graduates to overpay their student loans.* ***The***

Committee notes the Government's commitment to tackling this problem in the 2017 Autumn Budget, but questions whether the April 2019 deadline for completing this work is ambitious enough. *HMRC told the Committee that it could perform the administration of student loans, though it would need additional capacity in order to do so.* ***The Government's major review should consider the case for transferring responsibility for the administration of student loans to HMRC, along with a commensurate increase in resource.*** (Paragraph 126)

As the Committee has acknowledged, in the 2017 Autumn Budget the Government committed to tackling the problem of graduates over-repaying their student loans by introducing More Frequent Data Sharing (MFDS) between SLC and HMRC.

Due to the way in which the student loan repayment system operates, this project must go live at the beginning of a tax year. Both organisations (SLC and HMRC) will need to work together closely to deliver the required solution. It is essential for the success of the project that data is transferred accurately (to ensure that remaining loan balances are calculated correctly) and securely (as the data will include sensitive personal financial information). In addition to this, DfE will need to make changes to secondary legislation in order for MFDS to be implemented successfully. This means that April 2019 is the earliest that MFDS can realistically be delivered.

Under the current system, no borrower need over-repay their loan. SLC tells borrowers up to two years before they are due to finish repaying their loans that they may complete their loan repayments by direct debit, rather than through the tax system. Borrowers who take up the option to repay by direct debit do not over-repay their loans.

In the current student finance system, SLC is responsible for managing the process of issuing all student loans. Once a borrower becomes eligible to start repaying, their loan repayments are processed by HMRC through the UK tax system. The SLC manages direct repayments from borrowers who move overseas. Transferring responsibilities from SLC to HMRC would not alter the need to make data sharing as efficient as possible between the loan issuer and the body responsible for collection, so continuous improvement of this process is our priority.

Conclusion

In responding to the Treasury Select Committee's report on Student Loans, we have been clear that many of the issues raised are areas where future action will be considered by the major review of post-18 education and funding that is due to report in early 2019. In other areas, such as the accounting treatment of student loans, we trust that we have given a full account of the rationale for our approach. We would like to thank the Select Committee for its careful consideration of the range of issues relevant to student finance and for its report and recommendations.

Appendix B: Office for National Statistics Response

I am writing to offer the Office for National Statistics (ONS) response to the Treasury Committee report on Student Loans.[1]

The Committee made one recommendation to ONS:

"*The Government is not responsible for the international accounting rules that allow the fiscal illusions within student loans to exist. However, the National Accounts accounting rules regarding financial transactions were not intended to be used for loans that, as the Government readily promotes, are designed to not be paid back in full. Loans that are intended to be written off are, in substance, a partially repayable grant rather than a loan. The ONS should re-examine its classification of student loans as financial assets—which they are in legal form—and consider whether a portion of the loan should, in substance, be classed as a grant.* (Paragraph 31)"

In our written evidence, submitted to the Committee January 2018, we explained how student loans are currently treated in the National Accounts and public finance statistics, specifically that student loans are treated as any other loan following the approach mandated in the European System of Accounts and System of National Accounts.

However, as you mention in your report, there are certain features of UK student loans that appear to distinguish them from other loans. They have a high level of contingency, both as they are based on a student's subsequent income and as there are a number of scenarios under which the loans, or the portion of the loans not yet repaid, will be written off.

Reflecting further on the contingent nature of student loans and the issues raised by the Committee, we recognise that there is a need to establish whether student loans should be treated as loan assets for government, or whether they should in part, or in total, be viewed as contingent assets. This is not an easy issue to tackle and one which has implications wider than the UK given the use of income contingent repayment student loans in other countries.

We have therefore begun working with Eurostat, the IMF and other countries to discuss the relevant issues and examples with a view to identifying the appropriate statistical treatment, and from there to develop relevant guidance. As part of this dialogue, on 9 March, ONS, Eurostat and statisticians from countries across Europe discussed possible statistical recordings for income contingent loans, using the example of UK student loans as a case study. The discussion was productive and helped not only to frame the statistical discussion but also to identify other countries dealing with the complex issue of income contingent loans.

ONS is continuing to pursue international dialogue on this issue and Eurostat have indicated their support of this agenda by proposing to include statistical guidance on the

1 Treasury Committee, Seventh Report of Session 2017–19, Student Loans, HC 478

recording of income contingent repayment loans in the next edition of their Manual on Government Deficit and Debt, which has an anticipated publication date of late 2018 or early 2019. I hope the Committee will welcome this work.

ONS also noted the following recommendation:

"*The Committee sees no justification for using RPI to calculate student loan interest rates. RPI is no longer a National Statistic and has been widely discredited. In its Autumn Budget the Government acknowledged that the use of RPI was unfair for business rates, and the Committee is unconvinced by the case put forward for its use by the then Minister, in line with the Committee's report on the Autumn Budget. The Government should abandon the use of RPI in favour of CPI to calculate student loan interest rates.* (Paragraph 64)"

As the Committee is aware, ONS has put on record[2] that RPI is a very poor measure of general inflation. There are other, better measures available and any use of RPI over these far superior alternatives should be closely scrutinised.

ONS Update to Treasury Select Committee, Student Loans Report, conclusion in paragraph 28

> *28. The National Accounts accounting rules stipulate that if student loans are sold off at a loss before they are written off after 30 years, there is no impact on the deficit whatsoever. The policy of selling off student loans prior to their write-off allows the Government to spend billions of pounds of public money without any negative impact on its deficit target at all, creating a huge incentive for the Government to finance higher education through loans that can be sold off.*

Under the international National Accounts standards, when loan assets are sold the transaction is a purely financial one (as with sales of equity and bonds) with no impact on the net borrowing of the seller, purchaser or loan holder. The rationale for this treatment is that at the point of sale of the asset there is no change to the liability of the holder and so no debt cancellation crystallises.

As the Committee have highlighted in their report, the National Accounts rules mean that when student loans are sold, as was the case in December 2017, there is no impact on public sector net borrowing (the deficit). There is an impact on public sector net debt, where it is decreased at the point of sale by the amount of the sale value, although it should be remembered that public sector net debt will have been increased by the higher nominal value of the loans at the point of loan issuance. These fiscal impacts reflect the National Accounts accounting treatment for all loans.

As previously communicated to the Committee, ONS has begun work with international agencies and other National Statistical Offices to consider further the most appropriate statistical recording of income-contingent loans, such as UK student loans. It is planned that through this work, initiated by ONS, an appropriate statistical treatment in National Accounts can be agreed internationally. If this treatment were different to that currently applied by ONS to UK student loans then it may not only impact the treatment of the loan

2 ONS Note: Shortcomings of the RPI as a measure of inflation

assets themselves but also the sale of those assets. However, whether there would be an impact and the extent of any such impact depends on the details of any new internationally-agreed treatment.

ONS will be announcing, in the Public Sector Finances release of 24 April 2018, the work it is doing with the international statistical community to consider the statistical accounting of income-contingent loans, such as UK student loans.

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Office for National Statistics
23 April 2018