Introduction & General Points

When the new student loan iteration was introduced for 2012 new starters, the Coalition government declared that the repayment threshold would be set at £21,000 in 2016 and rise annually in line with average earnings thereafter.

The relevant regulations were never 'made' and the new Conservative government has now expressed its preference for freezing the threshold for five years from 2016 (Option 1).

The second Option presented would see no change for existing borrowers, but instead new starters in 2016/17 would face a freeze to the threshold for five years once their repayments first fall due.

Both options put out for consultation are misguided and regressive: the proposed changes will fall disproportionately on middle and lower earners. Moreover, when Option 2 is combined with proposed changes to student support from 2016/17, the government will have effectively created a tax on social mobility. This is at odds with its public statements from the new government.

In the case of Option 1, it is also unfair as it represents a retrospective price hike for borrowers who have already taken out loans. As others such as the Sutton Trust and Money Saving Expert have also stated in response: retrospective changes to repayments terms are by definition unfair and risk undermining confidence in the student finance system given the much larger graduating debts that are now proposed.

With both Options, the Consultation document outlines future, possibly regular reviews after the freeze ends. Such a suggestion makes a nonsense of recent market reforms (whatever their merits) premised on rational consumers making judgements about quality and price.

Prospective students will now find it impossible to assess what the likely cost associated with study will be. It is basic microeconomics: the headline tuition fee is not a price and cannot signal as such given the nature of income contingent repayment loans. A graduate could currently look at likely career options and base any cost-benefit analysis on information about typical salary

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1 There have been amendments to loan thresholds for existing borrowers previously, but these have previously not disadvantaged borrowers, such as the change to ‘pre-2012’ loans: the relevant threshold is now uprated inline with Retail Price Index.
paths and the details of the student loan repayment scheme. That possibility is undercut by regular reviews of the repayment threshold and other administrative details of the loan scheme.²

Reviews and revisions displace any approximation of price and instead signal uncertain costs, thus undercutting any vestige of normal consumer practice.

Goodwill is perhaps more fundamental to a well-functioning higher education system than the fiscal headlines. The measures outlined in the Consultation risk creating a precedent for future governments to treat graduates as an indentured group from whom more cash can be extracted if and when needed with the loosest of fiscal justifications.

The two Options not only undermine confidence in English HE, but confidence in political processes as well. As the submission from Money Saving Expert states:

> The Government used Parliament as a vehicle to tell students about the raising of the threshold. Commitments of this stature create a bond of trust between the Government and students. This change is not what the Government told students, so it breaches this trust and is wrong.

That is, it breaches trust placed in parliament and ministers.

It is not just that intentions expressed in 2010 that are being revised (§19 Consultation); the Conservative Minister then responsible for higher education stated in April this year, immediately prior to the General Election, that there would be no changes for borrowers.³

I put the following question to Greg Clark via Times Higher Education's 'election panel':

> Will the Department for Business, Innovation and Skills have to change the terms for existing borrowers of student loans to balance its budget after 2015? Does your party commit to protecting borrowers’ conditions?

The reply from the Minister was:

> The strength of our system is that it is robustly sustainable – as the OECD has confirmed – without any changes in terms being needed.

'Robustly sustainable' in April, but three months later in July we learn that the current scheme is 'unsustainable' without changes to the repayment threshold (§39 Consultation). But loans have not

² There is insufficient detail on these proposed reviews. Will they only consider where to set the repayment threshold? Or also consider the interest rate taper, repayment period and repayment rate?
³ http://andrewmcgettigan.org/2015/04/24/robustly-sustainable/
become unaffordable overnight - the major revisions to value occurred in 2013/14 when Project Hero was replaced.

We have not had an explanation of what might have changed since April, nor what level of public contribution to undergraduate study is deemed to be 'sustainable' or otherwise. This is not acceptable: the fiscal arguments presented in the Consultation are vague and carry little weight.

As I will outline below, the demand set out in the Consultation document in paragraph 10 is contradictory:

> As we enable more students to study, we must reflect the challenge faced by the Government, to put debt on a declining path as part of fiscal consolidation plans. (my emphasis)

More students borrowing money to finance their study and living costs can only put *upwards* pressure on public debt. This upwards pressure is much greater than the additional repayments that would be generated by a threshold freeze over the course of this parliament.

A tiny percentage of public debt would be repaid by those facing the freeze; the loss of goodwill in the system overall is a far greater risk than the minimal gains achieved over the course of this parliament.

In sum, government must resist the temptation to exploit graduates and instead fix terms for each cohort of borrowers. Neither Option 1 nor Option 2 as outlined in consultation document are acceptable insofar as they open the possibility of regular reviews to terms and conditions.

The tax revenue benefits of higher education are recognised by the government and are more than sufficient to secure the affordability of current support for higher education. The government should avoid policies which are likely to undermine participation, particularly when they are driven by the short-term presentational demands of national accounting and budgeting.

Given the level of graduating debt, it is now rational for individuals to avoid exposure over 35 years to repeated reviews by future governments with who knows what fiscal mandates. This cannot be good for HE and the economy.
Consultation Questions

Q1: Please could you provide your views, stating reasons and providing supporting evidence, on;

a. Keeping the threshold of £21,000 the same for all post-2012 borrowers until April 2021

Unfair impact on middle and lower earners

This is an unfair proposal that places unanticipated, additional repayments on middle and lower earners.

The impact analysis in the Consultation document provides four case studies for typical borrowers. Two of those have starting salaries of £21,000 and £30,000 respectively. Each sees pay rise subsequently in line with average earnings. They would both pay an additional £6,100 in net present value terms.

First, the discount rate used for these calculations is the government's financial reporting and budgeting rate, which at RPI + 2.2 is higher than the assumed growth in average earnings in the standard loan models. Since the latter, average earnings growth, would be a more likely discount rate for individuals, the level of additional payments faced by these hypothetical individuals is understated in NPV terms.

Second, even with higher discount rate, the additional payments would add a significant percentage to the estimated costs of a degree: between 20 and 33 percentage for lower lifetimes earning deciles. This is a very significant price increase for roughly half of the projected graduate population.

Third, the other two case studies (illustrating graduates with higher lifetime earnings) show either a very small increase or decrease in repayments. This is highlights that this proposal is a regressive move.

Although income contingent repayment loans have 'tax-like' features, the relevant one here is that the highest earners stop making contributions because they clear their accounts.

This point is particularly important for assessing the likely impact of future reviews.
Will any review look at the repayment threshold only? If so, it is likely to be repeatedly returning to middle and lower earners for more and more repayments.

**Informed consumers need to be able to assess price**

A well-functioning market requires that consumers make assessments about the quality of goods and prices.

The headline undergraduate tuition fee is not a *price* owing to the income contingent loans that 90 per cent plus of eligible students use to cover their fees. These loans are subsidised by public finances. The fee cannot therefore signal as prices do in well-functioning markets with regards to quality.

Threatening to tinker with loan repayment terms after agreement has been entered disrupts further this signalling mechanism, which the government might hope to use to have universities align tuition fees with their cost base.

Making changes after students and graduates have assumed new liabilities risks introducing a wholly new signal into the equation - that the loan scheme is unreliable and untrustworthy. Potential 'customers' may respond by avoiding English HE and its loans.

**Fiscal mandate and sustainability**

If no changes are made to the current policy, raising the threshold by earnings from April 2017 for all borrowers, as originally set out in 2010, there will be no impact on borrowers. This does not contribute to debt reduction and is *unaffordable in the long term.* (my emphasis)

Consultation document, §39

The affordability of student loans (with lifetimes longer than 30 years) is not determined by the short-term impact on public sector net debt. Unfortunately, the fiscal mandate adopted by the government is governed by short-term targets. This presentational decision treats student loans in skewed manner, meaning that long-term economic sense is distorted by accounting and budgeting conventions.

This government and the previous one were fond of quoting the OECD in support of the recent changes to student finance in England; a habit repeated in the Consultation document at paragraph 16:

The OECD has said that the UK is the first European country to have found a sustainable approach to higher education funding.
The OECD has *not* conducted any official study of English higher education since the latest reforms were introduced. *Its published official comments only relate to the pre-2012 regime.*

The government should instead attend to the following statement from the OECD, made in the 2010 edition of *Education at a Glance*:

… public investments in education, particularly at the tertiary level, are rational even in the face of running a deficit in public finances. Issuing government bonds to finance these investments will yield significant returns and improve public finances in the longer term.

The thrust of this message was recognised by Greg Clark in January 2015.

The [2012] reforms have made it possible—without them it would not have been possible—to abolish the cap on student numbers. That is overwhelmingly in our national interests, as I think most Members would acknowledge. The earning power of graduates means that it is not just the graduates themselves who gain—the Exchequer gains hundreds of thousands of pounds over a graduate’s lifetime of employment. That is many times more than even the most conservative estimate of the so-called RAB charge. (Hansard, 8 January 2015, col. 446)

The then Minister is here rebutting the charge that the financing scheme is unsustainable (or unaffordable) and he does so with reference to the increased tax contribution made by graduates, a contribution entirely separate to student loan repayments and one which will manifest itself over the next three decades, not this or the next parliament. HE is affordable so long as these increased tax revenues materialise.

It is an unfortunate decision of the Consultation document to conflate sustainability with 'putting debt on a declining path'; with the latter glossed as 'public sector net debt to be falling as a percentage of GDP in every year of the Parliament.' (§10 Consultation)

If we do adopt such a blinkered view of economic health, and the overriding policy aim is to have debt falling in such fashion, then it is hard to see why the government has committed to the 2016/17 changes to student support and the uncapping of student numbers. (It is precisely the 'human capital style' arguments repeated by Greg Clark above which justify the latter measures. The logic of this argument for expansion should override the false economies offered by the Options in this Consultation.)

As the following tables show, abolishing maintenance grants and replacing them with higher loans leads to higher Public Sector Net Cash Requirement in each year of this parliament. PSNCR is the driver of Public Sector Net Debt.

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*4 Andreas Schleicher has commented on the post-2012 scheme, but in a personal capacity.*
In Academic Year 2013/14, £1.6bn was awarded in Maintenance Grants.\(^5\) Government projects that figure to grow to £2.5bn by Financial Year 2020/21 owing to the uncapping of student numbers.\(^6\) These grants will be replaced by larger maintenance loans meaning that the net cash requirement is larger, hence PSND grows. Additional maintenance loans are projected to move past £3 billion in 2020/21 - and additional £0.5bn of upwards pressure on public debt.

**Summer 2015 Budget**

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<td>i Sale of shares in Royal Mail</td>
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<td>iii Higher education: additional maintenance loans for students</td>
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<td>-1,535</td>
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<td>iv Contribution to the Asian Infrastructure Investment Bank(^3)</td>
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<td>vi Sale of land around Kings Cross(^1)</td>
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**TOTAL POLICY DECISIONS**

\[+3,735 + 5,100 + 4,185 + 3,115 + 2,680 - 3,265\]

\(^1\) Costings reflect the OBR’s latest economic and fiscal determinants, and are presented on a UK basis.  
\(^2\) Contribution will be made in USD and therefore the amount in GBP will be subject to exchange rate fluctuations.  
\(^3\) This transaction forms part of the £3 billion departmental savings identified in 2015-16 – see also table 2.1. It relates to the sale of shares held by the Department for Transport in property around Kings Cross, valued in the department’s 2013-14 accounts at £345 million. The OBR has forecast receipts from this sale in the region of £360 million, taking into account wider market information. The Department for Transport will publish further details on the sale, which will be a full commercial process, in due course.

In addition, the uncapping of numbers means that additional tuition fee loans will be issued. OBR figures show the resulting net increases in loan cash outlay. This can be seen by comparing its July Economic & Fiscal Outlook to that from March.

\(^5\) The figures covers ‘applicants and students domiciled in England taking a designated Higher Education (HE) course at a University, Further Education (FE) College or Alternative Provider in the UK, as well as applicants and students domiciled in the EU (outside UK) taking a designated course in England’ (SLC First Statistical Release November 2014).

\(^6\) George Osborne, Chancellor’s speech accompanying Summer Budget 2015.
Tabulating that change in net cash outlay:

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<td>11.2</td>
<td>12.9</td>
<td>14.7</td>
<td>16.4</td>
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</tr>
<tr>
<td>Mar-15</td>
<td>11.2</td>
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<td>2.7</td>
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The maintenance grant saving of £2.5bn by 2020/21 is set to be a good £1 billion short of the additional loan outlay (maintenance and tuition fee) that year.
The chart provided in the Consultation document shows additional contributions contributing perhaps £200m in that year, and less than £1 billion over the whole five-year period.

Consultation Document, page 17

In sum, higher education is a long-term factor in economic growth and policy decisions should reflect that. Affordability is not determined by short-term accounting and budgetary impacts and certainly not the presentational targets of the fiscal mandate.

Setting that aside, the idea that freezing repayment thresholds will have a significant effect on PSND pathways offers a weak argument when considered alongside the changes to student support proposed for 2016/17.

What the scale of these numbers do reveal is that any retrospective freeze justified on such grounds would only be the overture to a series of reviews, each one likely to worsen the conditions for borrowers. This precedent sets the justificatory bar too low.

The conception of ‘affordability’ offered in the Consultation cannot be taken seriously as grounds for retrospective price hikes.

Any discussion of sustainability needs to be conducted through an analysis of long-run economic benefit, not short-term impacts on the headline fiscal statistics.
b. For borrowers starting in September 2016 (and subsequent intakes), from April 2020 keeping the threshold at the same level as existing borrowers for a further five years.

This proposal does not represent a regressive retrospective price hike like Option 1.

But it has major failings.

First, it suggests future regular reviews. Borrowers terms need to be fixed if they are to approximate rational consumers.

I am regularly asked whether university is 'worth it'. Despite my criticisms of recent policy, I have always answered in the affirmative. I am not sure now whether it would be responsible to advise students to study full-time away from home in London.

It is now in the interests of students to minimise their exposure to the student loan debt as the cost implications are unpredictable. Note that it is the high commencing debt and real interest rates faced by graduates under the new loan iteration that makes a freeze and the threat of subsequent reviews such a problem.

Second, even without subsequent reviews, the freeze to the repayment threshold is compounded by the abolition of maintenance grants from 2016/17. As I will outline in response to Q3, this means that the government has devised a tax on social mobility: those coming from poorer backgrounds but ending up as higher earners pay a premium of several thousand as compared to their wealthy student peers (because they start with higher graduating debt).

The government appears to have run no independent assessment of how threatened reviews compounds the separate changes to student support to be introduced in 2016/17. This is remiss.

c. Allowing the threshold to rise by earnings.

This is the only acceptable option.

Option 2 could be redeemed if the policy to abolish maintenance grants were rescinded and the suggestion of threshold reviews were dropped.

In truth, the government needs to instigate a review of student support which is now woefully inadequate for full-time study (especially in London).
If it is keen to find savings, then it should review how to encourage part-time study.

**Q2: What risks and impacts do you think that holding the threshold at the same level for five years would have for;**

**a. Current students/ borrowers?**

Regarding Option1, the Consultation document states

> It will still ensure that higher education is free at the point of use, and that repayments are affordable for all graduates. (§21)

*We know very little about the disposable income of recent graduates.*

Former students leave university with credit card debt, overdrafts, commercial loans and even payday loans. These have much more onerous repayment terms than SLC debt and we simply do not know what the impact of additional SLC payments would be on graduates servicing these different debts or, for example, on their ability to participate in pension schemes or save for mortgage deposits.

Any problems are likely to be particularly acute in London owing to high accommodation and transport costs.

The government ought to commission research here as the potential issues will be exacerbated for a mooted postgraduate loan scheme that would see repayments made *concurrently with undergraduate loans*. Anyone taking out both UG & PG loans would see a marginal take of 50% on earnings over the threshold (20% income tax; 12% NI; 18% student loan repayments).\(^7\)

As argued above the change is also regressive, since the highest earners stop contributing.

The loss of trust and goodwill here towards politicians and higher education can probably not be quantified, but an estimated 2 million borrowers could be hit by this measure. How they will respond at the 2020 election?^2

**b. Prospective students/ new borrowers?**

Option 2 compounds the problems associated with maintenance support changes proposed for 2016/17. Together these two measures create *a tax on social mobility*. Students from poorer

\(^7\) This would climb to 70% and over for the higher tax thresholds!
backgrounds who become higher earners face a very poor deal: up to an extra £999 per year in return for additional repayments of perhaps £13 000 (NPV).

c. Employers of borrowers with loans?
d. The Student Loans Company (SLC) and HM Revenue and Customs (HMRC)?
The administrative burden of an additional loan plan would be negligible.

e. Learning providers?
N/A. This is primarily an issue between government (lender) and student/graduate (borrower), though if HEI's are seen to support the freeze then they too could lose goodwill.

f. The Tax-payer?
Government revenues benefit from higher education. Any increased taxpayer burden that can attributed to mistakes in modelling and erroneous projections ought to be picked up from general revenues rather than passed to graduates with lower lifetime earnings.

Q3: Can you identify any equality issues introduced by these possible changes?

Unfair Deal, Sutton Trust Research Brief, September 2015 identifies that more of the additional costs will fall on women than men.

While the overall average extra repayments are £2,800, there are differences between men and women, with men’s at £2,300 and women’s £3,300. This is because women’s earnings tend to be lower and they are more likely to be repaying across the 30 year repayment period. After the freeze period, there is to be a review to see what follows; if the threshold freeze were extended, the extra repayments would be greater.

But in relation to Option2, the proposed freeze would, in conjunction with other changes to student support from 2016/17, create a tax on social mobility.

The abolition of maintenance grants and their replacement by loans means that students from poorer backgrounds will leave university with much higher graduating debts than their peers.
For example, a new starter in 2016/17 coming from a household with income less than £25,000 and studying for three years, full-time, away from home in London would graduate with an additional £13,000 of debt compared to their peers from wealthier homes.

With no threshold freeze, this additional debt would only translate into significantly higher loan repayments for higher earners.

In their report on the proposed changes, Institute for Fiscal Studies wrote:

We estimate that 65% of students who would have been entitled to a full maintenance grant are likely to experience no change in how much they can expect to repay (as they would not have paid back their old lower loan in full, let alone their new higher loan). Of the remaining 35% of those students, the average student will be repaying their loan for an extra four years, contributing an extra £9,000 towards their degree.8

(IFS, p. 17)

Again, this figure of £9,000 is in NPV terms using the government's financial budgeting and reporting discount rate, which may diverge significantly from the discount rate an individual

8 IFS, Analysis of the Higher Education Funding Reforms Announced in Summer Budget 2015, p. 17.
might use to value future repayments. It is also likely to understate the value of the additional repayments made.

The IFS posted an additional chart to accompany the report on social media.

**IFS, Analysis of the Higher Education Funding Reforms Announced in Summer Budget 2015**

As can be seen from this chart, replacing grants with loans generates additional repayments only from deciles 7-10. Poorer students who become high-earning graduates pay so much more in repayments, that extra £9000, that they drag up significantly the average contribution from those deciles.

I asked Dr Jack Britton from the IFS to conduct some additional analysis on the impact of the repayment threshold freeze (Option 2) on those socially mobile graduates. When you add in the effects of the proposed repayment threshold freeze the results are that the extra £9 000 contribution rises to an extra £13 000 on average.

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9 [http://andrewmcgettigan.org/2015/07/22/ifs-provide-revised-figures-for-he-financial-changes/]
In addition, the chart above indicates clearly the relative impact of the freeze - hitting borrowers hardest in the deciles from 3 to 7 and, in the very highest deciles, affecting those graduates who came from poorer backgrounds with larger graduating debts.

Overall, the average students eligible for a full grant make £3000 in additional contributions owing to the move from grants to loans: this rises £7000 with the repayment freeze. But this mean effect is skewed by the most socially mobile.

This appears to offer a very poor deal: an extra £999 per year at most, but repayments three to four times higher in NPV terms.

While the additional cash while borrowing will be welcome, it comes at a high cost when the two policies (abolition of grant and freeze) are combined.

**Q4: Do you think the Government could mitigate the impact of the proposed changes for borrowers?**

If so, what do you consider those actions might be? (Please indicate all that you consider to be relevant)

If the government is serious about social mobility, it should abandon Option 1 and Option 2 and commit to an extensive review of student support, particularly in light of the large rises in student rents over the last decade.

As someone who has taught HE in London for the last decade, I am most concerned excessive paid work in term time by students striving to meet the real costs of living. This causes stress and affects final degree classifications.