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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Office of the Minister for Tertiary Education, Skills and Employment
Office of the Minister of Revenue

Cabinet

Student support package for Budget 2012

Proposal

1. This paper seeks Cabinet's agreement to changes to the Student Loan Scheme and student allowances for Budget 2012.

Executive summary

2. This student support package enables us to achieve our priorities through Budget 2012, as set out in the accompanying Cabinet paper *Tertiary Education Package for Budget 2012*.
3. The Government has committed to building stronger economic growth as part of our commitment to building a brighter future for New Zealand. Providing quality research-led learning opportunities in core economic professions like biological sciences and engineering makes an important contribution to innovation and stronger growth. Conversely, flat or declining nominal investments and declining real investments in research-led learning would detract from the Government's stronger growth message.
4. New Zealand's tertiary education system has performed well in the face of the global financial crisis, but we face a number of challenges, particularly at higher levels, where our tertiary institutions compete internationally for students and academic staff. Australia, with whom we compete for international students and academic staff, intends to increase funding at the federal level for higher education by 12 percent between 2011/12 and 2014/15.
5. We have made progress in recent Budgets in identifying low priority expenditure in the student support system to reallocate to high priority areas in tertiary education. However, we still have a problem with the balance of our tertiary education expenditure. For example, because we spend double the OECD average proportion of our tertiary education budget on student support, we under-invest in important areas such as engineering and research.
6. We have committed to staying within current funding levels for tertiary education over the next four years. The Budget 2012 student support package is therefore underpinned by the principle that students who can afford to should make a greater contribution to their tertiary education, so that we can continue to strengthen the quality of that education.
7. Funds saved by the student support proposals will allow the Government to invest in:
   a. strengthening tertiary education provision and research at the upper levels of the system
   b. improving vocational and foundation education provision
   c. continuing to contribute to the rebuild needs of Canterbury
   d. progressing the Government's manifesto commitments.

8. The student support system is designed to reduce financial barriers to participation in tertiary education. The Student Loan Scheme provides broad access to upfront finance with repayments to be met from future earnings. Commercial loans are typically unavailable for education, due to the uncertainty about the returns, and students' inability to secure loans. Loans involve a lower level of government subsidy than allowances, so they are a means of managing the trade-offs between access to study and affordability for Government.

9. Student allowances aim to address the financial barriers to study for low-income groups. These barriers may be direct or indirect (for example, the opportunity cost of time in study). Allowances assist people to enter tertiary education who have very little upfront cash or family resources, and who heavily discount the future benefits of qualifications. Student allowances also provide additional living costs support for students with higher financial needs, for example those with dependents.

10. The student support package we are recommending for Budget 2012 will improve the value of student support spending through the following initiatives:

    a. Requiring a greater contribution to tertiary education costs from students who can most afford to pay, and who are more likely to receive higher levels of private return from their study by:

        i. increasing the student loan repayment rate for all New Zealand-based borrowers over the repayment threshold to 11 cents in the dollar OR 12 cents in the dollar from 1 April 2013
        ii. broadening the definition of income for student loan repayment purposes from 1 April 2014
        iii. removing the voluntary repayment bonus from 1 April 2013.

    b. Increasing personal responsibility for debt repayment by:

        iv. implementing an information match between Inland Revenue and the New Zealand Customs Service to identify borrowers in serious default in 2013.[1]

    c. Setting individual borrowing limits by:

        v. introducing an annual 2.0 EFTS borrowing limit from 1 January 2013.

    d. Targeting student allowances to those from low income families and initial qualifications by:

        vi. maintaining the parental income threshold without CPI adjustment until 31 March 2016
        vii. removing eligibility for student allowances for postgraduate study, except Bachelors with Honours, and removing Long Programmes and other related exemptions from 1 January 2013.

11. The initiatives to broaden the definition of income, repeal the voluntary repayment bonus, and extend the alerts from the New Zealand Customs Service to Inland Revenue require legislation. The next available student loan bill is due for introduction in August 2012. This is expected to be enacted in time to implement these initiatives on 1 April 2013 and 1 April 2014.

12. The financial implications of the preferred package for the 2011/12 to 2015/16 financial years are estimated to be: $517.545 million in operating impact, with a debt impact of $387.375 million.

[1] The definition for serious default will be set during the design process. The criteria are likely to include the amount of default, the age of the default and the borrower's risk profile.

13. The major impacts of the package are that it:
    a. reduces the write-down from 44.60 cents in the dollar to 41.92 cents in the dollar (based on preferred package)
    b. increases the repayment obligations of approximately 440,000 New Zealanders to 11 or 12 cents in the dollar
    c. increases repayment obligations for overseas borrowers by introducing an information match between Inland Revenue and the New Zealand Customs Service
    d. removes the eligibility for student allowances of approximately 5,100 postgraduate students in the first year.

Background

14. The Government spends a significant amount of money each year to fund tertiary education. In 2010/11, the Government spent $2,279 million on tuition subsidies, students drew $1,564 million in new student loan lending, and the Government paid $624 million for student allowances. Tuition subsidies, student loans and student allowances combined have represented between 6 percent and 7 percent of core Crown expenditure in each year between 1993/4 and 2010/11.

15. New Zealand spends slightly more on tertiary education than most other OECD countries, as a proportion of GDP, but this has been declining over the past three years. When we exclude the public subsidies to households (which include student loans, scholarships and grants), New Zealand's public expenditure on tertiary education as a percentage of GDP (1.1 percent) is currently similar to the OECD average (1.0 percent).[2]

16. OECD countries spend, on average, 21 percent of their public budgets for tertiary education on financial aid to students (although this calculation includes as financial support to students lending to meet the cost of tuition fees, even if that support is paid directly to providers). New Zealand spends double this proportion.

17. Government introduced broad-based student allowances in 1989 with an objective to increase tertiary participation for those whose income was a barrier to accessing tertiary education. Allowances were introduced in an environment of low participation and in a time of zero, or very low fees. They have an important role in lowering the total cost of tertiary education for students with significant financial barriers to education and those who may heavily discount the future benefits of qualifications.

18. The Student Loan Scheme was established in 1992 as part of wider tertiary education reforms, which moved New Zealand’s tertiary education system from an elite model, where Government subsidised a small number of students at a higher rate, to a model with more open access and where a large number of students are subsidised. Private contributions to tertiary education were increased to make the expansion of tertiary participation affordable for Government, and the Student Loan Scheme was introduced to ensure that finance was not a barrier to participation.

[2] Note that, while New Zealand spends a high proportion of its GDP on tertiary education, the situation is different when we look at actual expenditure per student. Education at a Glance 2011 shows that New Zealand was 20th of 28 OECD countries in the amount spent by tertiary providers per EFTS, on a purchasing power parity basis.

Problem definition

Student allowances

19. Government expenditure on student allowances has increased significantly in recent years – from $385 million in 2007/2008 to $620 million in 2010/11 (a 62 percent increase). The number of students receiving an allowance has also increased, particularly since 2009, due to policy changes and the effects of the recession, including higher tertiary enrolments due to increased unemployment.

20. Policy changes to the parental income threshold mean that the original intent of allowances as a mechanism to support students from low income backgrounds has broadened to include middle income families. Changes to the threshold in Budgets 2004 and 2006 to 2008 mean that the threshold is now 30 percent higher than it would have been had the 1992 threshold been increased annually by CPI alone.

21. In addition, the design of student allowances has not been reviewed since student loans became more subsidised, with interest subsidies and interest-free loans.

22. New Zealand research suggests that the prospect of debt has little impact on the attitudes of young people towards tertiary study, and that financial circumstances are not especially significant in determining the likelihood of participation in study.[3]

23. However, I consider that allowances play an important role, as supplementary support to student loans, for two reasons:

    i. To assist people to enter tertiary education who have very little upfront cash or family resources, and who heavily discount the future benefits of qualifications.
    ii. To provide additional support for students with higher financial needs, for example those with dependents.

Student Loan Scheme

24. The objective of the Student Loan Scheme is to enable a wide range of people to access tertiary education, gaining knowledge and skills that enhance the economic and social wellbeing of New Zealand. However, this needs to be balanced against the affordability of the Scheme for taxpayers in the long term.

25. The Student Loan Scheme is a significant and growing asset on the Crown's accounts. 958,000 people have taken out a student loan since the Scheme began in 1992, borrowing a total of $15,486 million. As at 30 June 2011, the nominal value of loan balances was $12,070 million. The fair value (written down) was $7,221 million.

26. The current value of new lending is 55.40 cents in the dollar (i.e. the Government writes down 44.60 cents). The Budget 2011 policy changes are projected to improve the value of lending to 56.26 cents by 2015. However, the gap between new lending and repayments is forecast to rise from $770 million to $1.1 billion by 2030 if current policy settings remain.

27. The most significant component of the cost of new lending to Government is the time value of money (the value of loans decreases over time as a result of inflation and this cost is not off-set through an interest charge to borrowers). The other components, in order of significance, are borrowers who do not meet their repayment obligations (primarily overseas-based borrowers), borrowers with low life-time earnings who do not have a repayment obligation, and death and bankruptcy.

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[3] Zhang, J. and Kemp. S. (2009) *The relationships between student debt and motivation, happiness, and academic achievement*, New Zealand Journal of Psychology, 38(2), 24-39; Haultain, S., Kemp, S. and Chernyshenko, O.S. (2010) The structure of attitudes to student debt *Journal of Economic Psychology,* 31(3), 322-330; Kemp, S., Horwood, J. and Fergusson, D. (2006) Student loan debt in a New Zealand cohort study *New Zealand Journal of Educational Studies,* 41, 273-291.

28. Recent analysis of the cost of lending shows that reductions in value take three forms:

    i. Borrowers whose labour market returns are insufficient to make progress in repaying their loans.
    ii. Borrowers who go overseas and do not repay.
    iii. Borrowers who would still participate in tertiary education if the government subsidy on student loans was reduced (for example those who are able to self-fund study).

29. The analysis also shows that the Crown's cost of lending is affected by the size of student loans. At the end of February 2012, 6,793 borrowers (1.1 percent of all borrowers) had student loans of $80,000 or more with a median balance of $95,578. 53 percent of these borrowers were based overseas. The loans are of particular concern when borrowers are slow to repay (or never fully repay).

30. The use of loans as a policy lever assumes that increased or more stable earnings should result from study, and that credit market failure is the main reason some people do not invest in study. That is, people understand and are prepared to meet the costs of study, they just do not have the financial means to meet them.

31. Tighter targeting of student allowances to those from low income families means that future policy changes to reduce the cost of the Student Loan Scheme need to retain relatively broad access to student loans.

32. This suggests that loan policy changes need to focus on redistributing costs according to the benefits of study and ability to repay (e.g. through increasing the borrower or student contribution to Student Loan Scheme costs), rather than further options for reducing eligibility for loans.

33. However, in order to reduce the cost of the Scheme, it remains important to reduce lending to those with poor labour market returns and repayment performance, and to ensure that borrowers (particularly overseas-based borrowers) meet their repayment obligations.

Budgets 2010 and 2011

34. The student support package for Budget 2012 builds on the policy changes introduced through Budgets 2010 and 2011. Many of the opportunities for tertiary education savings in the past two Budgets were found in the Student Loan Scheme.

35. The Budget 2010 package aimed to encourage better educational performance from tertiary students and give the Government a better return on its current spending on student support. Initiatives included the introduction of academic performance standards, a two-year stand-down for new permanent residents, a 7 EFTS lifetime limit on borrowing, and a $40 administration fee. All of these initiatives, except the administration fee (2014), took effect in January 2011.

36. Budget 2010 also introduced a 92 week limit for student allowances study at secondary schools and amended the Student Allowances Regulations to exclude eligibility for recipients of New Zealand Superannuation and Veterans Pension.

37. The Budget 2011 package aimed to improve the Government's spend on student support by reducing lending to borrowers who are less likely to repay and increasing personal responsibility for debt repayment. Initiatives included not relending to borrowers who have $500 or more in default (from February 2013), tightening the repayment holiday provisions (from April 2012), and restricting lending to those over the age of 55 to tuition fees only (from January 2013).

Budget 2012 package

38. The proposed Budget 2012 package aims to improve the value of student support spending through the following initiatives:

> *Requiring a greater contribution to tertiary education costs from students who can most afford to pay, and who are more likely to receive higher levels of private return from their study* by:
>
> - increasing the repayment rate to 11 cents in the dollar for all New Zealand-based borrowers over the repayment threshold
>   OR
> - increasing the repayment rate to 12 cents in the dollar for all New Zealand-based borrowers over the repayment threshold
> - broadening the definition of income for student loan repayment purposes
> - repealing the voluntary repayment bonus.

> *Increasing personal responsibility for debt repayment by:*
>
> - implementing an information-matching agreement between Inland Revenue and the New Zealand Customs Service to identify borrowers in serious default.

> *Setting individual borrowing limits by:*
>
> - introducing an annual 2.0 EFTS borrowing limit.

> *Targeting student allowances to those with from low income families and in initial qualifications by:*
>
> - maintaining the parental income threshold without CPI adjustment until 31 March 2016
> - removing eligibility for student allowances for postgraduate study except Bachelors with Honours, and removing Long Programmes and most other exemptions.

39. The broader tertiary education package for Budget 2012 includes an initiative to address large loans and poor employment outcomes associated with aviation training. This initiative has student support implications, which are addressed in the companion paper.

Increasing the borrower contribution

40. Requiring a greater contribution to tertiary education costs from students or borrowers who can most afford to pay, and who are more likely to receive higher levels of private return from their study may ensure a fairer distribution of costs between students and the Government. This contribution may occur prior to study, in study or post study (for example initiatives to increase the repayment rate).

41. Increasing the student contribution may ensure that students are committed to study, which may encourage them to make study choices more likely to be linked to labour market returns.

42. Initiatives that increase the borrower or student contribution to Scheme costs for those with the ability to pay have a lower impact on access to tertiary education than initiatives that directly reduce or remove eligibility.

43. The initiatives which we propose below focus on borrowers who remain in New Zealand after study, but complement the work we are doing to increase compliance and repayment by borrowers who go overseas.

Increasing the repayment rate for New Zealand-based borrowers

44. New Zealand-based borrowers have a repayment obligation of 10 cents for every dollar of income over the repayment threshold, which is currently set at $19,084. The current 10 cent rate has not changed since the beginning of the Scheme, despite the introduction of the interest-free policy which has resulted in decreased voluntary student loan repayments.

45. Increasing the post-study contribution from borrowers through a repayment rate increase will help the Government to reduce the cost of the Scheme at a time of significant fiscal pressure. As the increase is post-study, it is likely to have minimal impact on access to tertiary education, particularly when compared to initiatives to limit eligibility.

46. The income-contingent design of the Scheme ensures that those who gain a higher private benefit from their study have a higher repayment obligation (with hardship provisions for those who are not able to repay). Increasing the repayment rate reaches those who have gained private benefit from their study (i.e. an earnings premium).

47. We propose two options to increase the repayment rate for New Zealand-based borrowers from 1 April 2013:

    I. Increasing the repayment rate to 11 cents in the dollar for New Zealand-based borrowers with income over the repayment threshold, OR

    II. Increasing the repayment rate to 12 cents in the dollar for New Zealand-based borrowers with income over the repayment threshold.

48. Increasing the repayment rate to 11 cents in the dollar will generate $220 million in savings over a five-year period and, together with other changes, would reduce the cost of lending to Government by approximately 2 cents in the dollar in the 2014-2015 financial year.

49. Increasing the repayment rate to 12 cents in the dollar will generate $420 million in savings over a five-year period and, together with other changes, would reduce the cost of lending to Government by approximately 4 cents in the dollar in the 2014-2015 financial year.

50. The repayment rate change also brings forward the repayment of interest-free debt. The median repayment time for those who left study in 2006 and remained in New Zealand is 5.2 years. The median repayment time for all borrowers would decrease by approximately 0.4 years under the 12 cents option[4].

51. The impact of the proposals on a range of income brackets is provided in Table 1. The current repayment threshold is $19,084. Table 1 shows that, under the 11 cents option,

[4] The impact on the median repayment time can only be modelled on all borrowers (including domestic and overseas-based borrowers). This calculation includes the impact of removing the voluntary repayment bonus.

the weekly repayment obligation for a borrower earning the average income five years post study ($38,720) would increase by $3.78 a week, an annual increase of $196.56.

Table 1: Impact of the proposals on weekly repayment obligations

Gross annual income	Current repayment obligation per week	Weekly repayment obligation at 11 cents in the dollar	Increase per week	Weekly repayment obligation at 12 cents in the dollar	Increase per week
$25,000	$11.38	$12.51	$1.13	$13.65	$2.27
$38,720[5]	$37.76	$41.54	$3.78	$45.31	$7.55
$48,000	$55.60	$61.16	$5.56	$66.72	$11.12
$70,000	$97.91	$107.70	$9.79	$117.49	$19.58

52. Increasing the repayment rate increases effective marginal tax rates[6] (EMTR) by 1-2 percentage points for borrowers over the repayment threshold. This increase in EMTRs is not thought to have a significant impact on work incentives. Increases in EMTRs due to the abatement of Working for Families tax credits or an increase in income tax rates reduce after-tax incomes permanently. In contrast, an increase in the repayment rate is a temporary reduction in after-tax income and brings forward the repayment of interest-free debt.

53. This initiative will not impact on beneficiaries, as they are exempt from student loan repayments (CAB Min (11) 14/10 refers).

54. Inland Revenue would only recommend increasing the repayment rate if the only objective were to increase repayments (regardless of how the additional repayments are distributed across borrowers) and reduce the fiscal cost of the scheme. The current domestic repayment mechanism through the tax system is very efficient. Increasing the rate of repayment increases repayments with minimum impact on borrower behaviour.

55. The repayment rate can be increased through regulations made under the Student Loan Scheme Act 2011.

56. Inland Revenue advise that an increase in the repayment rate for all New Zealand-based borrowers can be implemented from 1 April 2013.

Widening the definition of income for student loan repayments

57. In 2011, Cabinet made an in-principle decision to broaden the definition of income for student loan repayment purposes to better align with that used for Working for Families purposes (CAB Min (11) 14/10 refers).

58. In addition to excluding losses from the calculation of net income, as agreed in Budget 2011 (CAB Min (11) 14/10 refers), we recommend broadening the definition of income for student loan repayments to include the following types of income from 1 April 2014:

    i. attributed company income

[5] Average income five years post study (2005 cohort)

[6] An EMTR is the marginal tax rate that a taxpayer pays on any additional dollar of income, when the effect of other social policies such as Working for Families, student loan repayments and the ACC Earner Levy are taken into account.

ii. attributed trust income
iii. major fringe benefits received by shareholder-employees in closely held companies
iv. unlocked portfolio investment entity income
v. tax-exempt salary and wages and certain overseas pensions
vi. main income equalisation scheme deposits
vii. 50 percent of non-taxable private pensions and annuities
viii. distributions from superannuation schemes that relate to contributions made by a person’s employer within the last two years, when the person has not retired
ix. distributions from a retirement savings scheme when the person has retired early
x. distributions from trusts, not being beneficiary income, where the recipient is not the settler of the trust.

59. Broadening the definition of income ensures there is better consistency across other social assistance programmes, such as the Working for Families Tax Credit and the parental income test for student allowances. This initiative will increase the rate of repayment and improves fairness by ensuring that a borrower’s repayment obligation accurately reflects their ability to repay.

60. This initiative is expected to generate at least $1m ongoing annual savings for Government, with a $4m one-off improvement in the value of the student loan book.

61. The additional types of income proposed for inclusion are not currently declared by borrowers for the purposes of repaying their loan, making an accurate estimate of the additional savings difficult. $1m is the projected minimum annual savings, with higher savings expected from this policy.

62. Broadening the definition of income will require changes to the Student Loan Scheme Act.

63. Inland Revenue advise that this initiative can be implemented from 1 April 2014.

Repealing the voluntary repayment bonus

64. The voluntary repayment bonus is a 2008 National Party manifesto commitment that provides a 10 percent bonus for borrowers who make voluntary repayments of $500 or more above their repayment obligation. Cabinet agreed to implement the policy in 2009 [SOC Min (09) 3/2 refers].

65. The policy aimed to encourage borrowers to repay their loans more quickly, particularly New Zealand-based borrowers who have interest-free loans. Faster repayment would lower the cost to the Government of the Student Loan Scheme.

66. However, take-up of the policy has largely been by individuals in circumstances that result in a cost to the Government. Our preliminary assessment is that the level of savings from the voluntary repayment bonus is lower than originally estimated, and the bonus may not be providing good value to the Government.

67. [11]

Our evidence shows that borrowers have benefitted from an estimated $1.8 million of bonuses on loans that may not need to have been borrowed (from approximately $13 million of annual bonus payments).

68. Since the introduction of the bonus, Government has introduced several other interventions to incentivise or increase repayments. These are more certain to improve the value of the Scheme than the voluntary repayment bonus. These include an initiative to increase repayments from overseas-based borrowers using commercial debt collection methods, and policy changes to tighten the repayment regime.

69. Repealing the voluntary repayment bonus may be perceived as inconsistent with the objective of incentivising quicker repayments of student loans. However, we consider that it is timely for the voluntary repayment bonus to be reconsidered, due to the lower than expected return, tighter fiscal conditions, significant administrative costs of the bonus, and the fact that a number of other interventions provide the same signal to borrowers for greater financial return. We note that Australia has recently reduced its voluntary repayment bonus, which was introduced around the same time, from 10 percent to 5 percent.

70. Repealing the bonus will require legislative change. We are considering a Student Loan Scheme Amendment Bill as part of Budget night legislation to achieve this. The bonus would be repealed effective 1 April 2013.

Increasing personal responsibility for debt repayment

71. Forty-eight percent of overseas-based borrowers (about 47,000 borrowers) have overdue repayments amounting to $315 million. The amount in default for overseas-based borrowers is growing rapidly and increased by 58 percent ($115.4 million) in the past year. This is largely due to many borrowers coming off the three year repayment holiday and not meeting their repayment obligations as well as the continued impact of penalties on borrowers who have not paid for some time.

72. The high level of default is primarily due to a significant portion of borrowers not meeting their obligations of keeping Inland Revenue up-to-date with their contact details and making payments.

73. Recent initiatives to address non-compliance of overseas-based borrowers have focused on tracing borrowers, increased enforcement, improved communication and making loan payments easier. Initial activity focused on 1,000 borrowers in Australia. In late 2011, Inland Revenue began scaling up activity in Australia to further borrowers and extended it to the United Kingdom for a three-year period. The initiative will be fully resourced by mid-May 2012. To complement the increase in contact with borrowers, Inland Revenue has also started legal action in Australia against long-term non-compliant borrowers. To date, the initiative is returning over $10 for every $1 invested.

74. To complement the ongoing work to improve repayment rates from overseas-based borrowers, we recommend that a new data match is implemented between Customs and Inland Revenue for borrowers in default. The new data match would operate in the same manner and use the same systems as the existing child support match. Any debt recovery action following a successful match would be undertaken through the scaled up overseas-based borrower compliance initiative.

75. Inland Revenue has analysed the border movements of overseas-based borrowers over the last four years in order to gauge the likely results of a new match. It expects approximately 20,000 overseas-based borrowers to cross the border, of whom an estimated 10 percent would have amounts in default.

76. Implementing the data match will require changes to the Student Loan Scheme Act.

77. It is not possible to model the revenue impact of the data match. However, Inland Revenue will absorb the cost to deliver this initiative.

Setting individual borrowing limits

78. Setting limits on student loans can be expected to make effective use of taxpayer money by:

    i. reducing the costs of the scheme, and thereby reallocating resources to higher priority areas
    ii. improving the efficiency of the scheme by discouraging students from borrowing money that they do not immediately need, or borrowing for non-educational purposes
    iii. ensuring a better return on the Crown's and borrowers' investment in tertiary education, by encouraging borrowers to make wise study choices and take the most direct route through their studies (avoiding churn at lower levels).

79. We recommend limiting the amount of loan-supported study that a student can undertake in a year to 2 EFTS from 1 January 2013, subject to the results of sector consultation underway in May 2012.

80. This initiative is expected to have a debt impact of $0.221 million over a four year period. It is estimated that approximately 28 students per year will have reduced borrowing as a result of this initiative.

81. Limiting annual borrowing to 2 EFTS may reduce student loan debt for borrowers that results from 'backtracking' or undertaking large amounts of study without a clear study plan in mind. It may also reduce, but not eliminate, the potential for borrowing for non-educational purposes. Students borrowing for more than 2 EFTS are likely either to be misusing the scheme or making uninformed study decisions then withdrawing from courses or finding the workload unmanageable.

82. This initiative is a National Party manifesto commitment. As per the manifesto commitment, officials are consulting on where the EFTS cap should be placed. Officials will report back on the outcomes of the consultation after the deadline for Budget 2012 decisions. If further changes to appropriations are needed as a result of the consultation findings, we will propose these changes in June 2012. However, decisions are needed now in order to implement this initiative in 2013.

83. Setting an individual borrowing limit does not require legislative or regulatory change, as the Cabinet minutes of the decision provide authority for changes to student loan eligibility and contracts.

Targeting student allowances to those from low income families and initial qualifications

Removing eligibility for postgraduate study, Long Programmes and other exemptions

84. Focusing allowances on the initial years of study rather than postgraduate study would begin to update allowance policy settings to reflect the wide availability of interest-free student loans. This approach is supported by evidence that suggests that a student's first year in tertiary education is the most important for ensuring they complete their studies.[7]

85. We propose removing allowance access for postgraduate study (level 8 and above) and Long Programmes[8] from 1 January 2013, to acknowledge the higher private returns from such study. Due to variation between providers, we are proposing that all bachelors degrees with honours be considered as undergraduate study, and therefore retain eligibility for student allowances, providing a student has not exceeded the 200 week limit.

86. Among young domestic graduates last enrolled in tertiary education in 2003, median annual earnings three years after completing their studies were 16 percent higher for those with a master's degree compared with those with a bachelor's degree, and 46 percent higher for those with a doctorate —more than twice the national median income.

87. Removing postgraduate eligibility from 1 January 2013 would affect approximately 5,100 students in the first year. Student loans would be available to provide living cost support for most of these students.

88. In addition, students with low incomes who undertake postgraduate study may be eligible for the Accommodation Supplement, depending on their individual circumstances. In many cases, the Accommodation Supplement plus the amount which can be borrowed through the Student Loan Scheme for living costs is close to or greater than the amount of student allowance previously received. The total amount of financial support available to most students will therefore not significantly reduce.

89. However, some students with dependants will experience a greater drop in total support than students with no dependants. Students in this situation are less likely to have the flexibility to respond to the changes as quickly as other students. We therefore propose grandparenting for allowance recipients with dependants for up to one year.

90. Specifically, we propose that students with a spouse, partner or supported child who have an allowance approved in 2012, and are continuing to study the same qualification in 2013, be grandparented until 31 December 2013, as long as they retain eligibility in all other respects.

[7] Jacques van der Meer, Austina Clark and Chikako van Koten *Establishing Baseline Data: using International Data to Learn More About Completion Factors at One New Zealand University.* Journal of Institutional Research, 2008. Jacques van der Meer *I don't even know what her name is: Considering the challenge of interaction during the first year.* Studies in Learning, Evaluation Innovation and Development, 2009.

[8] Long Programmes are approved programmes of study usually culminating in postgraduate study, which exceed 200 weeks, for example Bachelor of Laws, followed by Professional Legal Studies, and then Master of Laws.

91. We also propose that where grandparented allowance recipients cease to meet the criteria for having a spouse, partner of supported child at any time, they will lose eligibility for that student allowance.

92. [8]

93. An exemption currently allows students to exceed the 200 week limit when special circumstances exist. This may mean that students would be eligible for a special circumstances exemption after 200 weeks as a result of the proposed policy change. We propose narrowing this exemption to exclude student allowance policy changes.

94. Further exemptions to the 200 week limit currently exist that are inconsistent with the proposed new focus of allowances. We propose removing these exemptions from 1 January 2013. However, if a student has had an exemption approved prior to this date (including approval for a recognised Long Programme), we consider they should retain this exemption for the approved period.

95. These proposals will require changes to the Student Allowance Regulations 1998.

Maintaining the parental income threshold without CPI adjustment

96. Targeting student allowances to students from low income families signals the Government's expectation that those who will benefit economically from tertiary education and can afford to meet a greater proportion of costs should do so.

97. On 27 February 2012, Cabinet confirmed the Cabinet Business Committee's decision to maintain the student allowance parental income threshold without CPI adjustment from 1 April 2012 (CAB Min (12) 6/1).

98. We intend that this decision apply for the four-year Budget period, meaning that there would be no CPI adjustment to the threshold before 31 March 2016. We seek agreement to this. Student allowance rates will continue to be adjusted for CPI annually, in line with benefits.

99. The student allowance proposals in this paper would generate a total of $46 million in savings over four years, after student loan and Accommodation Supplement flow-ons have been taken into consideration. Removing eligibility for postgraduate study, Long Programmes is estimated to increase Accommodation Supplement costs by approximately $7 million per year.

Overall impact of the package

100. The major impacts of the package are that it:

a) reduces the write-down from 44.60 cents in the dollar to 41.92 cents in the dollar (based on preferred package)

b) increases the repayment obligations of approximately 440,000 New Zealanders to 11 or 12 cents in the dollar

c) increases repayment obligations for overseas borrowers by introducing an information match between Inland Revenue and the New Zealand Customs Service

d) removes eligibility to student allowances for approximately 5,100 postgraduate students in the first year.

Financial implications

101. The tables below set out current estimates of the financial implications of the changes to student support. These estimates incorporate the administration costs of the initiatives.

102. These estimates will be refined to reflect interactions between the policies before the Budget financial recommendations are finalised.

Table 4: Operating impact of the student support package *(preferred package)*

	Operating impact ($ million)					
Proposals	**2011/12**	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**Five year total**
Setting a 2 EFTS annual student loan borrowing limit	-	0.170	(0.032)	(0.030)	(0.030)	**0.078**
Increasing the repayment rate from 10 cents in the dollar to 12 cents in the dollar	(235.103)	(53.644)	(51.891)	(43.471)	(35.184)	**(419.293)**
Broadening the definition of income	(4.081)	(0.857)	(0.691)	(0.837)	(1.053)	**(7.519)**
Repealing the voluntary repayment bonus	(1.097)	(8.185)	(10.251)	(11.881)	(13.175)	**(44.589)**
Removing eligibility for postgraduate study except Bachelors with Honours	-	(2.453)	(8.459)	(10.765)	(11.309)	**(32.986)**
No CPI adjustment to the current parental thresholds for four years	(0.574)	(1.569)	(2.692)	(3.797)	(4.604)	**(13.236)**
Total student support package	**(240.855)**	**(66.538)**	**(74.016)**	**(70.781)**	**(65.355)**	**(517.545)**

Table 5: Debt impact of the student support package *(preferred package)*

	Debt impact ($ million)					
Proposals	**2011/12**	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**Five year total**
Setting a 2 EFTS annual student loan borrowing limit	-	(0.044)	(0.061)	(0.059)	(0.057)	**(0.221)**
Increasing the repayment rate from 10 cents in the dollar to 12 cents in the dollar	-	(36.052)	(158.616)	(166.510)	(152.070)	**(513.248)**
Broadening the definition of income	-	-	(0.227)	(0.917)	(1.000)	**(2.144)**
Repealing the voluntary repayment bonus	-	17.467	12.379	8.475	1.193	**39.514**
Removing eligibility for postgraduate study except Bachelors with Honours	-	11.821	22.049	19.862	18.551	**72.283**
No CPI adjustment to the current parental thresholds for four years	-	2.283	3.636	4.915	5.607	**16.441**
Total student support package	**-**	**(4.525)**	**(120.840)**	**(134.234)**	**(127.776)**	**(387.375)**

Alternative package

103. The operating and debt impact of the alternative package is provided below. This includes the proposal to increase the repayment rate to 11 cents in the dollar.

Table 6: Operating impact of the alternative student support package (repayment rate at 11 cents in the dollar)

	Operating impact ($ million)					
	2011/12	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**Total**
Increasing the student loan repayment rate to 11 cents in the dollar	(124.696)	(28.370)	(27.629)	(23.442)	(19.233)	**(223.370)**
Total student support package	(127.624)	(40.790)	(49.252)	(50.203)	(48.808)	**(316.677)**
Reduced savings from alternative package	**113.231**	**25.748**	**24.764**	**20.578**	**16.547**	**200.868**

Table 7: Debt impact of the alternative student support package (repayment rate at 11 cents in the dollar)

	Debt impact ($ million)					
	2011/12	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**Total**
Increasing the student loan repayment rate to 11 cents in the dollar	-	(18.197)	(80.224)	(85.222)	(79.491)	**(263.134)**
Total debt impact	-	13.418	(42.326)	(52.828)	(55.083)	**(136.819)**
Reduced savings from alternative package	**-**	**17.855**	**78.392**	**81.288**	**72.579**	**250.114**

Administrative implications

104. The proposals will have administrative implications for both the Ministry of Social Development and Inland Revenue. The Ministry of Social Development will absorb the cost of maintaining the parental income threshold without CPI adjustment for four years. Removing student allowances eligibility for postgraduate study and removing most exemptions will have Ministry of Education administration and IT costs of $1.402 million over four years.

105. Inland Revenue will fund the operating and capital costs associated with delivering the data-matching initiative with the New Zealand Customs Service. Applying a repayment rate change from 1 April 2013 requires significant Inland Revenue resources. These require major reprioritisation, and may require increased funding.

106. Due to the combination of existing operating pressures and administrative costs arising from other initiatives progressed in 2010, 2011 and 2012 Budget initiatives, Inland Revenue is unable to absorb the costs associated with widening the definition of income and is seeking an appropriation increase to cover the increase in operating costs.

Inland Revenue comment

107. If the voluntary repayment bonus is not repealed, then the repayment rate change could only be applied from 1 April 2013 by deferring components of the Student Loan work programme until 1 April 2014.

108. Resources from other government priorities within Inland Revenue's change portfolio would then need to be diverted to implement the deferred components. Diverting these resources would necessitate ceasing work on either the Child Support Amendment Bill,

the Returns Filing for Individuals proposals (included in the Taxation (Annual Rates, Returns Filing and Remedial Matters) Bill currently being considered by the Finance and Expenditure Committee) or reducing resources in the e-services project area.

109. [6]

StudyLink comment

110. StudyLink has advised that the timeframes are very tight to implement both the package in this paper, and the Student Loan pilot training fee borrowing limit proposal in the related tertiary budget package. Work will commence, including the commitment of resources, prior to the decisions being confirmed by Cabinet. [6]

111. The estimated administration costs provided by Studylink to implement the proposals are incorporated in the operating impact in Table 4 above.

Consultation

112. The Ministry of Social Development, the Treasury, Inland Revenue and the Department of Prime Minister and Cabinet have been consulted in the development of this paper. The Ministry of Justice has been consulted on the student allowances proposals only. The New Zealand Customs Service and the Office of the Privacy Commissioner have been consulted on the information matching proposal only.

Treasury comment

113. Please refer to the Treasury comment in the accompanying paper *Tertiary Education Package for Budget 2012.*

Human Rights implications

114. The proposal to limit eligibility for student allowances for postgraduate study includes a proposal to provide up to one year of further assistance to students who have dependants and are continuing their existing study.

115. [8]

Legislative implications

116. Amendments to the Student Loan Scheme Act 2011 will be required to broaden the definition of income for student loan repayment purposes, to ensure that borrowers may no longer receive a voluntary repayment bonus, and to implement a new information match between the New Zealand Customs Service and Inland Revenue for borrowers in serious default. These amendments can be included either in Budget night legislative changes, or in the next planned Student Loan Scheme amendment bill, scheduled for introduction in August 2012 which would be enacted in time for a 1 April 2013 or 1 April 2014 application date.

117. The information match between the New Zealand Customs Service and Inland Revenue will also require consequential amendments to the Tax Administration Act 1994, the Customs and Excise Act 1996, and the Privacy Act 1993.

118. An increase to the repayment rate can occur by way of regulation made under the Student Loan Scheme Act 2011.

119. Changes will be required to the Student Allowances Regulations 1998 to give effect to the student allowance proposals.

Regulatory Impact Analysis

120. A regulatory impact analysis has been prepared for all proposals and this is included as Appendix 2. The Ministry of Education has reviewed the regulatory impact statement and associated supporting material, and considers that the information and analysis summarised in it meets the quality assurance criteria.

121. We have considered the analysis and advice of the Ministry of Education, as summarised in the attached regulatory impact statement, and we are satisfied that, aside from the risks, uncertainties and caveats already noted in this Cabinet paper or in the Regulatory Impact Statement, the regulatory proposals recommended in this paper are consistent with our commitments in the government statement “Better Regulation, Less Regulation.”

Gender Implications

122. None anticipated.

Publicity

123. A communications plan will be developed in consultation with agencies and Minister’s offices prior to Budget 2012 announcements.

Recommendations

We recommend that Cabinet:

1. **note** that a package of changes to the Student Loan Scheme and student allowances has been developed as part of Budget 2012 to improve the value of student support spending by:
    i. requiring a greater contribution to tertiary education costs from students who can most afford to pay, and who are more likely to receive higher levels of private return from their study
    ii. increasing personal responsibility for debt repayment

iii. setting individual borrowing limits
iv. targeting student allowances to those from low income families and initial qualifications

2. **note** that this student support package enables us to achieve our tertiary education priorities through Budget 2012, as set out in the accompanying Cabinet paper Tertiary Education package for Budget 2012

Changes to the Student Loan Scheme

3. **note** that consultation will take place in April and May 2012 on the National Party manifesto commitment to set a borrowing limit of between 2 and 2.5 EFTS

4. **agree,** subject to the results of consultation, that a borrowing limit of 2.0 EFTS per loan account (a manifesto commitment) apply for study starting on or after 1 January 2013

5. **note** that the Minister for Tertiary Education, Skills and Employment will report back on results of the consultation in May 2012

6. **agree** to

   EITHER

   6.1 increase the repayment rate for New Zealand-based borrowers to 11 cents in the dollar from 1 April 2013

   OR [7]

   6.2 increase the repayment rate for New Zealand-based borrowers to 12 cents in the dollar from 1 April 2013

7. **note** that, in 2011, Cabinet agreed to broaden the definition of income for student loan repayment purposes to better align with that used for Working for Families purposes (Cab Min (11) 14/10 refers)

8. **agree** to broaden the definition of income for student loan repayments to include the following types of income from 1 April 2014:

   i. attributed company income
   ii. attributed trust income
   iii. major fringe benefits received by shareholder-employees in closely held companies
   iv. unlocked portfolio investment entity income
   v. tax-exempt salary and wages and certain overseas pensions
   vi. main income equalisation scheme deposits
   vii. 50 percent of non-taxable private pensions and annuities
   viii. distributions from superannuation schemes that relate to contributions made by a person's employer within the last two years, when the person has not retired (excluding KiwiSaver and locked-in superannuation schemes)
   ix. distributions from a retirement savings scheme when the person has retired early
   x. distributions from trusts, not being beneficiary income, where the recipient is not the settler of the trust

9. **agree** to implement a new information matching agreement between the New Zealand Customs Service and Inland Revenue for borrowers in serious default from the date of enactment (expected in early 2013)

10. **agree** to repeal the voluntary repayment bonus from 1 April 2013

Changes to the student allowances scheme

11. **agree** to remove student allowance eligibility for all level 8 and above postgraduate certificates and diplomas, Masters degrees and doctorates for study starting on or after 1 January 2013 *(Treasury supported)*

12. **agree** that, due to variation within and between providers, all bachelor degrees with honours retain eligibility for student allowances, providing a student has not exceeded 200 weeks of allowance support

13. **note** that, depending on a student's individual circumstances, the amount they can borrow for living costs through the Student Loan Scheme for postgraduate study may be less than the amount they were previously receiving through the combined student allowance and accommodation benefit

14. **note** that we recommend a transition arrangement for allowance recipients with a spouse, partner and/or supported child who lose allowance eligibility due to undertaking postgraduate study, and continue to study, as these students are less likely to have the flexibility to respond to the changes as quickly as other students and will experience a greater drop in support

15. **agree** to grandparent allowance recipients who have a spouse, partner and/or supported child, have an allowance approved in 2012, and are continuing to study the same qualification, until 31 December 2013; as long as they retain eligibility in all other respects

16. **agree** that, where grandparented allowance recipients cease to meet the criteria for having a dependent spouse and/or children at any time, they will lose eligibility for that student allowance

17. [8]

18. **agree** to remove the Long Programme exemption that allows students who are studying mainly postgraduate qualifications to exceed the 200 week limit to complete their study, effective for study starting on or after 1 January 2013

19. **note** that an exemption allows students to exceed 200 weeks when special circumstances exist, which may mean that students who were affected by the proposed changes would be eligible for a special circumstances exemption

20. **agree** to narrow the definition of the special circumstances exemption in Regulation 20 (7) of the Student Allowance Regulations 1998 as it relates to tertiary study, to exclude student allowance policy changes

21. **note** that exemptions to the 200 week tertiary limit which are also inconsistent with the proposed new focus of allowances on initial years of study and those who most need additional support, exist for:

    i. any particular case or class of case
    ii. courses in the national interest (currently teaching qualifications)

22. **agree** to remove the exemptions in recommendation 21 (i) to (ii) from the Student Allowance Regulations 1998, effective for study starting on or after 1 January 2013

23. **agree** that, for any exemption (as set out in recommendation 21) or Long Programme approved prior to 1 January 2013, a student will retain that exemption for the period approved

24. **note** that students who undertake postgraduate study may be eligible for the Accommodation Supplement available to people on low incomes, depending on their individual circumstances, potentially increasing Accommodation Supplement costs by an estimated $7 million per year

25. **agree** that these increased Accommodation Supplement expenditure in Vote Social Development be met from Budget 2012 student support savings

26. **note** that, on 27 February 2012, Cabinet confirmed the Cabinet Business Committee's decision to maintain the student allowance parental income threshold without CPI adjustment from 1 April 2012 (CAB Min (12) 6/1)

27. **agree** that this decision should apply for the four-year Budget period, meaning there will be no CPI adjustment before 31 March 2016

28. **note** that maximum student allowance weekly rates will continue to be adjusted for CPI, in line with benefits

Legislative implications

29. **authorise** the Minister for Tertiary Education, Skills and Employment and the Minister of Revenue to take any technical policy decisions needed in the drafting process of the necessary legislation or relevant regulations to give effect to the student loan proposals in this paper

30. **authorise** the Minister for Tertiary Education, Skills and Employment and the Minister for Social Development to take any technical policy decisions needed in the drafting process of the necessary legislation or relevant regulations to give effect to the student allowance proposals in this paper

31. **invite** the Minister of Revenue to issue drafting instructions to the Parliamentary Counsel Office for a Student Loan Scheme Amendment Bill or Bills to give effect to the student loan proposals in this paper

32. **invite** the Minister for Social Development to instruct the Parliamentary Counsel Office to draft amendments to the Student Allowances Regulations (1998) to give effect to the changes to student allowances proposed in this report

Financial implications

33. **note** that the financial implications of this package for the 2011/12 to 2015/16 financial years are: $517.545 million in operating impact, with a debt impact of $387.375 million

34. **note** that the operating impact includes administration and IT costs for Inland Revenue of $0.5 million and the Ministry of Social Development of $1.402 million

35. **note** that changes to appropriations, including Ministry of Social Development and Inland Revenue administration and IT costs, will be made as part of the tertiary education package for Budget 2012

36. **agree** to delegate authority to the Minister of Finance and the Minister of Tertiary Education, Skills and Employment to approve changes to the Student Support Package and the resulting changes in appropriations by 26 April 2012

37. **note** that Cabinet decisions on this paper are proposed to be announced as part of Budget 2012.

Hon Steven Joyce
Minister for Tertiary Education,
Skills, and Employment

_____/_______/______

Hon Peter Dunne
Minister of Revenue

_____/_______/______