EXPLANATORY MEMORANDUM TO

THE EDUCATION (STUDENT LOANS) (REPAYMENT) (AMENDMENT) REGULATIONS 2019

2019 No. 189

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Education and is laid before Parliament by Command of Her Majesty.

1.2 These are composite regulations with the Welsh Ministers and these regulations will also be laid before the National Assembly for Wales.

2. Purpose of the instrument

2.1 This instrument amends the Education (Student Loans) (Repayment) Regulations 2009 (S.I. 2009/470) ("the 2009 Regulations"), which govern the repayment of income contingent repayment (ICR) student loans. The purpose of this instrument is to make changes to the regulations to facilitate more frequent sharing of student loan data between Her Majesty's Revenue and Customs (HMRC) and the Student Loans Company (SLC). The changes to data sharing processes will apply to all ICR borrowers making student loan repayments via the Pay As You Earn (PAYE) system from the tax year 2019/20 onwards.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

3.2 As the instrument is subject to negative resolution procedure, there are no matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business at this stage.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is primarily England and Wales because it concerns the repayment terms of loans made to borrowers ordinarily resident in England and Wales. However, the administrative work of collecting student loan repayments is managed on a UK-wide basis by the SLC, working in partnership with HMRC. This instrument thus extends to all of the UK insofar as the 2009 Regulations impose any obligation or confer any power on HMRC, an employer or a borrower in relation to repayment under Parts 3 or 4 of those Regulations, or on any other person in relation to the retention or production of information or records. In addition to this, Regulation 80(3) of the 2009 Regulations ("Effect of borrower insolvency on student loans") extends to Northern Ireland.

4.2 The territorial application of this instrument is primarily England and Wales only.

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

6.1 This instrument amends the 2009 Regulations made under section 22 of the Teaching and Higher Education Act 1998, which govern the repayment of income-contingent repayment student loans.

6.2 The Chancellor of the Exchequer announced in the Government's Autumn Budget 2017 that, in order to tackle student loan over-repayments, from April 2019, HMRC and SLC would begin to share data about student loan repayments more frequently than the current annual return. These regulations make legislative changes to facilitate that more frequent data sharing.

7. Policy background

What is being done and why?

7.1 This instrument makes amendments to the 2009 Regulations to facilitate, from April 2019, more frequent sharing of student loans repayment data between HMRC and SLC, fulfilling a government commitment made in the Autumn Budget 2017 (published on 22 November 2017) to reduce student loan over-repayments. The sharing of data more frequently than the current annual return will address a number of operational issues in the student loans repayments system, in particular the value of over-repayments made by many borrowers at the end of their loans. Over-repayments occur because accounts are currently updated only annually, so a borrower may pay off their loan in full many months (up to 18) before HMRC is able to instruct the employer to stop collecting repayments. This creates a credit balance that needs to be refunded to the borrower.

7.2 To address this issue, HMRC and SLC are making operational IT improvements, which will enable More Frequent Data sharing (MFDS), under which data will be shared weekly rather than annually.

The student loans repayment system

7.3 Student loans are issued by the SLC, which also administers customers' accounts. The majority of repayments of student loans (82%[1]) are collected by HMRC, which then notifies SLC of repayments made. This instrument does not affect the way student loan repayments are collected by HMRC from borrowers, only how HMRC and SLC administer the repayments collected.

7.4 Since 1998, student loans have been repaid primarily via the tax system. Under these ICR student loans, repayments are directly linked to income. Borrowers pay back a percentage of their income above a minimum threshold (the exact percentage and threshold depend on which specific loan product they have taken out). This is similar to how the tax system works and, therefore, it is efficient to collect student loans via HMRC. It enables the repayments to be truly income contingent, and is an efficient way of administering a high volume collection system at low cost and low risk to the taxpayer.

[1] Based on government statistics *Student Loans In England Financial Year 2017-18*

7.5 Borrowers repay their ICR student loans as they do their taxes, i.e. via either PAYE or Self-Assessment or a combination of both (Mortgage Style student loans, issued up to 1998, are not in scope for this instrument, as they are not repaid via the tax system). The proposed changes affect PAYE repayments only (which make up 93%[2] of repayments via HMRC). Repayments via Self-Assessment are not in scope, as this is a separate process using a different collection system. HMRC is undertaking a wider, long-term transformation of Self-Assessment processes. Overseas borrowers will continue to repay via existing processes, i.e. direct repayments to SLC.

7.6 The current repayment system and regulations reflect the way the PAYE tax system operated when the 2009 Regulations were made. Since then, HMRC has made technical improvements to the operations of the wider PAYE system with the introduction of a requirement for employers to provide HMRC with Real Time Information (RTI).

7.7 PAYE employers make student loan repayment deductions from employees' salaries using the PAYE system and report payroll data and student loan repayments data to HMRC at the end of each payment period. The frequency of this (typically weekly or monthly) varies between different employers, but the data is effectively shared with HMRC in real time.

7.8 HMRC currently shares data with SLC about student loan repayments made via tax collections only once annually, after the end of the relevant tax year. HMRC sends the repayment files to SLC between April and the end of July. SLC processes the repayments as it receives them, and typically has all customer accounts updated by October. This process has a number of adverse consequences for borrowers:

a. **Over-repayments** – Currently, if a borrower pays off their loan in full during the tax year, SLC will not know this until the end of the tax year and, therefore, cannot ask HMRC to tell employers to stop making PAYE loan repayment deductions. This means that borrowers may over-repay on their loans, necessitating a subsequent refund from SLC. The average over-repayment amount is currently £608. Borrowers can switch to Direct Debit payments when they are within 23 months of paying off their loans, to avoid the risk of over-repaying, but the uptake of this option is low. Many borrowers do not keep their contact details up to date with SLC, which means that SLC are not able to contact these borrowers about the Direct Debit scheme. It also requires the borrower to take action to set up the Direct Debit, and they may not fully recognise the consequences of not doing so (i.e. risk of over-repayments).

b. **Account balances** – Currently, borrowers do not have easy access to up-to-date information about their loan balance. To get an up-to-date balance in-year, borrowers have to provide SLC with information about all their repayments made since their last year-end statement.

c. **Repayment dates** – SLC currently receives information from HMRC at the end of the tax year about the total amount repaid by each student loan borrower. This amount is then applied to each account in 12 equal instalments across the year (or as many equal instalments as the number of months an individual borrower had PAYE income during the tax year) based on an

[2] Based on government statistics *Student Loans In England Financial Year 2017-18*

operational assumption that the borrower's income has been consistent throughout the year, and interest will be applied on that basis. In reality, the profile of individual borrowers' repayments may be much more variable.

More Frequent Data Sharing

7.9 More Frequent Data Sharing (MFDS) will enable HMRC to share student loan repayment data with SLC on a weekly basis. This takes advantage of HMRC's improvement to the PAYE system (RTI data from employers) and will address the issues described above, which are inherent to the current annual data sharing system:

a. **Over-repayments** –The current proposed frequency of data sharing is a weekly data transfer from HMRC to SLC. This means that SLC will know much earlier when a loan is fully paid and SLC can instruct HMRC to stop taking repayments. Over-repayments will not be eliminated, but the amounts over-repaid will be reduced significantly. Under the current system, a customer can over-repay for almost a year (if they pay off their loan early in the tax year), and then it may take another 6 months to update their account with SLC. With weekly data sharing, over-repayments will stop much sooner. Furthermore, SLC will save money on the interest it is obliged to pay on credit balances.

b. **Account balances** – With MFDS, borrowers will be able to get up-to-date information about their accounts without having to provide payslips (and, subject to an SLC project to provide statements online, will be able to access the information directly themselves). However, due to the dependence on annual income to ascertain the appropriate rate of interest for post-2012 undergraduate loans (which have variable interest rates that increase as income increases), there will still be a need for an end-of-year adjustment for interest for some borrowers.

c. **Repayment dates** – With MFDS, repayments will be credited to accounts to reflect the date they were actually deducted by employers. This means that interest can be applied to the actual profile of repayments. The only exception is where certain adjustments are required, for example to adjust the amount of the repayment where an incorrect amount has been deducted. For operational reasons, some of these will have to be applied on the adjustment date and not backdated. However, these transactions account for only a very small proportion of all repayments made.

Regulatory amendments required to implement MFDS

7.10 In order to realise the benefits of MDFS, this instrument amends the 2009 Regulations effecting changes in the following areas:

Date of repayment

7.11 Currently, annual repayments for each borrower repaying via PAYE are applied to borrower accounts in twelve equal instalments (or as many equal instalments as the number of months an individual borrower had PAYE income during the tax year) across the tax year, after SLC has received annual borrower repayment information from HMRC. This is a simplifying assumption, necessitated by the limitations of the current annual cycle system.

7.12 With MFDS, repayments will be credited to accounts when they are made. This means that the application of interest will reflect the actual income profile of individual borrowers, which will of course not always be equal monthly instalments, as is the assumption under the current system. This change will have a positive impact for some borrowers and a negative impact for others. However, these impacts are a consequence of ensuring that repayments are credited when they are actually made.

7.13 HMRC will supply SLC with the date of repayments and, in most cases, this will be the actual date the deduction was made by the borrower's employer from their salary. There are a small number of scenarios where this will not be the case due to subsequent adjustments being made to deductions (e.g. to correct employer errors).

7.14 HMRC will send the any data on adjustments to SLC via MFDS, and SLC will apply the adjustments to accounts and recalculate interest as necessary, which will more accurately reflect the income profile of individual borrowers.

Application of variable interest rates in-year and end-of-year

7.15 In 2012, new undergraduate loans were introduced, with variable interest rates, determined by reference to the borrower's annual income. Currently, interest is applied at the end of a given tax year, once SLC receives information from HMRC about repayments and confirmation of income. Under MFDS, the standard interest rate (generally speaking, RPI) will be applied in-year, and an adjustment will be made (if needed) when the annual income is confirmed. SLC will ensure that the information provided to customers during the tax year will be clear about the potential for an end-of-year interest adjustment where necessary.

7.16 A borrower's annual income determines the interest rate to be applied to their account, but the annual income is not known until after the end of the tax year. MFDS, therefore, requires new rules on how to apply interest when a loan with variable (income-dependent) interest rates is fully repaid in-year via PAYE. The interest rate to be applied will only be known after the end of the tax year, so it is not possible to know exactly what the loan balance (including interest) is in-year and when it has been cleared. As a result, it is not possible to stop repayments accurately.

7.17 Under MFDS, SLC will use the previous year's income to determine the interest to be applied in the final year of PAYE repayment. The borrower would be entitled to request an adjustment, once the actual income for the current year is known in cases where that adjustment would be in the borrower's favour.

Allocation of repayments between different loans, where a borrower has more than one loan (with different interest rates and repayment thresholds)

7.18 It is possible for individual borrowers to have more than one loan, and these may have different interest rates and repayment thresholds, if they have taken out loans before and after 2012, when the terms and conditions for undergraduate loans changed. In the following paragraphs, the pre-2012 loans are referred to as "Plan 1" and post-2012 loans as "Plan 2".

7.19 Under the current annual system, the regulations provide for the situation where a borrower has both a Plan 1 and a Plan 2 loan and is earning more than the repayment threshold for both loans (with Plan 1 having a lower threshold than Plan 2). In this instance, the part of the repayment relating to income between the Plan 1 and Plan 2 repayment thresholds is allocated to the Plan 1 loan, and the part of the repayment relating to income above the Plan 2 repayment threshold is allocated to the Plan 2 loan. Any repayment relating to a Postgraduate loan is separate and is made concurrently with repayment to undergraduate loans. If a borrower's income is below the Plan 2 threshold, repayments are allocated only to the Plan 1 loan balance.

7.20 The Regulations currently provide for these allocations to be made based on annual thresholds. With MFDS, the allocation between loans will need to be made more frequently. Therefore, a monthly repayment threshold will be implemented to ensure that borrowers are able to know the balance for their different loans in-year, rather than wait until after the end of the tax year. The overall amount repaid annually by individual borrowers will not change. However, as the new system will more accurately reflect borrowers' actual income profile, the allocation between loan plans may be affected.

7.21 The 2009 Regulations provide a right for borrowers to request a refund of their repayments in a given year where their annual total income falls below the relevant threshold(s). This provision will remain unchanged. As is the case now, it will be the borrower's responsibility to contact SLC to request such a refund.

Timeline

7.22 MFDS is to be introduced from the 2019-20 tax year, i.e. 6 April 2019. Due to the nature of the operational changes, it is highly desirable to align the introduction of MFDS with the start of a new tax year.

7.23 The amendments made by this instrument will apply from 6 April 2019, and will not apply to repayments made up to and including 5 April 2019. In the first year of operation, there will be a period of up to six months during which the new system will be introduced operationally. This transition is an operational issue only; the amended Regulations will be in force from the beginning of the tax year and will apply to borrower's accounts in respect of the full tax year. During this initial period (April to October 2019), SLC will receive tax year 2018-19 repayment information from HMRC and apply this to customers' accounts. SLC will also be receiving new tax year 2019-20 repayments data, but will store this until all 2018-19 data has been processed. At this point SLC will then apply the new repayments received via MFDS, using the actual dates on which the deductions were made in accordance with the amended 2009 Regulations. When all accounts have been updated with both tax year 2018-19 and all available tax year 2019-20 data, SLC will display these up-to-date account balances to customers on their online portal and will continue to update them every pay period. This is expected to be from autumn 2019.

7.24 This instrument will be made jointly with Welsh Ministers, but the operational changes being put in place by SLC and HMRC under the MFDS system improvements will apply to the whole of the UK, as the tax system is UK wide. Scotland and Northern Ireland will be making amendments to their relevant regulations to facilitate the operational changes in their respective administrations.

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act 2018.

9. Consolidation

9.1 The Department for Education does not consider that consolidation of the 2009 Regulations is necessary at this time, but will keep the position under review.

10. Consultation outcome

10.1 No formal consultation was undertaken on this instrument.

11. Guidance

11.1 HMRC provides guidance to employers on matters relating to the collection of student loan repayments from employees. Updated guidance to employers on MFDS will be made available to employers in advance of its introduction.

11.2 SLC provides extensive guidance to borrowers on the operation of the student loan repayments system through its repayments website[3]. This includes details of how student loan repayment works; the current interest rates applicable to student loans; an explanation of how borrowers can find out how much they owe and how they can make voluntary repayments; and details on how borrowers can update their personal details and contact SLC. This guidance will be updated to reflect the changes being introduced to facilitate MFDS.

12. Impact

12.1 There will be no significant impact on business, charities or voluntary bodies, or on the public sector as a result of MFDS.

12.2 An Impact Assessment has not been prepared for this instrument. All employers will continue to make salary deductions for student loan repayments as per their current practice. The process changes introduced by this instrument will be handled by HMRC and SLC. Updated HMRC guidance will be made available to employers to make them aware of MFDS and its implications for their employees with student loans, but no additional burden on employers is expected as a result of these changes.

12.3 The Department for Education has considered the amendments with reference to the Public Sector Equality Duty and has concluded that borrowers with protected characteristics are unlikely to be adversely affected by the changes being introduced. The benefits of MFDS, including a reduction in the value of over-repayments and access to more up-to-date account balances online apply to all borrowers. The changes to the application of interest, which will reflect the actual profile of repayments instead of assuming equal-sized instalments throughout the year, will have a positive impact for some borrowers and a negative impact for others. However, these effects are simply a more accurate reflection of actual income profiles, which is not possible under the current system, and is unlikely to disproportionately affect borrowers with protected characteristics.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses, to the extent that they are employers and are making student loan repayment deductions from their employees' salaries. However, like all employers, they will continue to make deductions as per their current practice, and no additional burden on small employers is expected as a result of MFDS.

[3] http://www.studentloanrepayment.co.uk/portal/page?_pageid=93,3866794&_dad=portal&_schema=PORTAL

14. Monitoring & review

14.1 HMRC, SLC and the Department for Education will continue to monitor transfer of student loan repayment data as part of their ongoing work in this area.

15. Contact

15.1 Camilla Reinert at the Department for Education (camilla.reinert@education.gov.uk) can be contacted with any queries regarding the instrument.

15.2 Paul Williams, Deputy Director for Student Funding Policy, at the Department for Education can confirm that this Explanatory Memorandum meets the required standard.

15.3 Chris Skidmore, Minister of State for Universities at the Department for Education can confirm that this Explanatory Memorandum meets the required standard.