

Student Loan Scheme Amendment Bill

*Officials' report to the Finance and Expenditure
Committee on submissions on the bill*

February 2012

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OVERVIEW

The Student Loan Scheme Amendment Bill introduces changes announced in Budget 2011. The bill introduces three major changes:

- Losses will be excluded from the calculation of income for student loan repayment purposes and, as a consequence of this change, the pay-period assessment policy will be extended to the salary and wage earnings of all borrowers.
- Inland Revenue will be able to receive details of a borrower's contact person from StudyLink, which manages student loan applications. Every new loan application will have to include a contact person as a condition of accessing a student loan.
- The repayment holiday will be reduced from three years to one. Borrowers will be required to apply for their repayment holiday and provide the name of a contact person when they do so.

In addition, during the implementation of the reforms included in the Student Loan Scheme Act 2011, officials have identified a number of other minor amendments that need to be made to the Student Loan Scheme Act 2011. The amendments proposed are intended to bring the legislation up-to-date with changes in the IT systems used to implement the reforms, and to ensure that the legislation achieves its original policy intent.

The student loan reforms were originally based on Inland Revenue implementing a new computer system to administer student loans. However, during the passage of the bill, it became apparent that Inland Revenue would not be able to implement the reforms in a new system in time and therefore the reforms were implemented in the existing FIRST computer systems. Reverting to the original system to implement the student loan reforms resulted in a number of changes being made to the bill at the Select Committee stage, and the deferral of the application date of some provisions until 1 April 2013.

At the Finance and Expenditure Committee's meeting with officials on 8 February, the Committee raised a number of questions on the student loan scheme. Officials' responses to these questions are in the section at the end of this report.

Matters raised in submissions

PROVIDING ALTERNATIVE CONTACT DETAILS

Clause 7

Submission

(National Council of Women)

The bill does not require borrowers to supply details of a contact person as a prerequisite to accessing a loan, so there is still potential for losing contact with borrowers.

Comment

The Ministry of Social Development, through its StudyLink service, provides information on student loan entitlements, assesses applications for student support and makes student loan payments. Inland Revenue manages the collection of loan repayments through the tax system and this is governed by the Student Loan Scheme Act 2011.

Loan eligibility is assessed by StudyLink and is authorised in cabinet minutes. As a condition of accessing a student loan, StudyLink will require the borrower to provide alternative contact details. The proposed amendments contained in this bill allow those details provided to the loan manager (StudyLink) to be received and used by Inland Revenue once the loan is transferred.

Recommendation

That the submission be noted.

USE OF ALTERNATIVE CONTACT DETAILS

Clause 29

Submission

(National Council of Women)

A contact person's rights and duties should be clearly defined, so as not to find themselves inadvertently liable for another's debt. The "contact person" should be just that – and have no other responsibilities.

The administration fee could escalate and interest might then be charged on it.

Comment

Clause 29 inserts new section 193A authorising the Commissioner to request a borrower's contact person to assist where the borrower is in default and cannot be located. The Commissioner may only request the contact person to:

- provide the borrower's address details; or
- ask the borrower to contact Inland Revenue.

There is no ability for the contact person to inadvertently be liable for the borrower's student loan debt.

Currently, the bill prescribes that Inland Revenue may only communicate with the contact person when the borrower is in default. As noted below, officials recommend that Inland Revenue be given the ability to pro-actively communicate with the contact person to notify the individual that they have been nominated and to explain what is required of a contact person if and when Inland Revenue contacts them. This ability will assist in ensuring the contact person understands that they will only be called upon for very specific information.

This change is not expected to increase the administration fee.

Recommendation

That the submission be noted.

EXCLUDING LOSSES FROM THE CALCULATION OF INCOME FOR STUDENT LOAN REPAYMENT PURPOSES

Clauses 8–16

Submissions

(National Council of Women, Lenore Bamfield)

Women often cluster in small business enterprises, and the move to exclude business losses in calculating liable income may stifle entrepreneurship or contribute unnecessarily to small business failure. Women may therefore be more disadvantaged by this change. *(National Council of Women)*

The proposal to remove business and investment losses from the assessment base of New Zealand-based borrowers' student loan repayment obligations should not proceed. *(Lenore Bamfield)*

Comment

Amendments in the bill exclude investment and business losses, such as rental losses, from the calculation of net income for student loan repayment purposes. The purpose of the amendment is to maximise repayments from New Zealand-based borrowers and ensure fairness across the student loan scheme.

The policy rationale is that although such losses may reduce an individual's economic income, the Government should not provide for the ability to gain a student loan repayment benefit as a consequence of offsetting those losses against income. In addition, denying the ability to offset both business and investment losses is consistent with other social assistance programmes – for example, claiming Working for Families' tax credits.

Recommendation

That the submissions be declined.

APPLYING FOR THE REPAYMENT HOLIDAY

Clause 17

Submissions

(National Council of Women, Lenore Bamfield)

Requiring a borrower to apply for the repayment holiday, and to supply details of a contact person in New Zealand as part of the application, is long overdue. However, there is concern expressed by the Ministry of Education that reducing the time of the repayment holiday will not be effective in encouraging repayments, and could even have the opposite effect. Shortening the repayment holiday may delay the return of some borrowers.

The three-year repayment holiday should be retained but tailored to each borrower's circumstances.

Comment

Officials acknowledge that there are uncertainties when anticipating behavioural responses to policy change. However officials note that recent research undertaken by the KEA Foundation surveyed 15,600 New Zealanders living abroad and asked participants about the factors that influence their decision to live overseas.¹

The survey found that economic factors were the primary factor, followed by family and lifestyle considerations. Student loan debt was not raised as a factor. Inland Revenue's own research conducted in 2011 corroborates these findings.

For borrowers who do not meet their obligations, the reduction in the repayment holiday will likely increase their indebtedness. However officials do not believe that the reduction will lead to more borrowers defaulting on their obligations.

The current automatic three-year holiday is generous and can result in borrowers not resuming repayments when the repayment holiday comes to an end. The application process, combined with the requirement to supply a New Zealand-based contact person, seeks to address this behaviour and signals to borrowers the importance of repaying their loan when the repayment holiday comes to an end.

To the extent that borrowers can still choose whether or not to apply for a repayment holiday, the policy allows an element of tailoring to suit a borrower's individual financial situation.

Recommendation

That the submissions be declined.

¹ A copy of the research is available at:
http://www.keanewzealand.com/sites/default/files/Every_Kiwi_Counts_2011_Kea_NZ_final.pdf

OVERSEAS-BASED REPAYMENT OBLIGATION

Submission

(Lenore Bamfield)

The repayment obligation for overseas-based borrowers should be set at levels to ensure that:

- the amount that overseas-based borrowers are required to pay is fair compared with what New Zealand-based borrowers are required to pay; and
- the loan is repaid in a reasonable timeframe.

Comment

The bill does not change the policy on the calculation of the repayment obligation for overseas-based borrowers; therefore the submission is outside the scope of the bill.

Recommendation

That the submission be declined.

Matters raised by officials

OFFSETTING A SIGNIFICANT OVER-DEDUCTION AGAINST UNPAID AMOUNTS

Clause 12

Submission

(Matter raised by officials)

The bill should be amended so that a significant over-deduction may also be offset against an unpaid amount prior to being refunded. The amendment should apply from 1 April 2012.

Comment

When a borrower has both a significant over-deduction for one period and a significant under-deduction for another period, the bill allows the two significant deductions to be offset against each other.

Officials have identified situations when a borrower has a significant over-deduction and an unpaid amount. Such borrowers should not receive a refund of the over-deduction while still leaving a debt due to Inland Revenue.

Recommendation

That the submission be accepted.

MEANING OF “REPAYMENT OBLIGATION” FOR DETERMINING EXCESS REPAYMENTS

Clause 22

Submission

(Matter raised by officials)

To correct an oversight, officials recommend that the bill amend the excess repayment legislation to provide that whatever repayment deductions are made from salary and wages satisfies the borrower’s repayment obligations from that income. The amendment should apply from 1 April 2012.

Comment

For a borrower to have an excess repayment, and therefore qualify for the excess repayment bonus, they must have made repayments in excess of their repayment obligations for the year.

In determining whether a borrower has met their repayment obligations for the purposes of calculating excess repayments and the bonus, the policy intent was that whatever repayment deductions were made from salary and wages would satisfy a borrower’s repayment obligations. If there is an under-deduction then there are other mechanisms available to collect the debt.

However, the legislation does not achieve this outcome. Instead, the excess repayment legislation incorrectly refers to repayment obligations from salary and wages being what *should* have been deducted not what was actually deducted. The result is that if a borrower has an under-deduction, whether significant or not, they will not have met their repayment obligations in relation to their salary and wage income and their bonus entitlement will be reduced or cancelled.

Recommendation

That the submission be accepted.

DATE PAYMENT CREDITED FOR CALCULATING INTEREST

Submission

(Matter raised by officials)

To ensure consistency between the student loan administrative system and the legislation, officials recommend that the legislation be amended to provide that for the purposes of calculating interest, payments are treated as being received on the day after payment was made.

Comment

Under the student loan scheme, the loan balances of New Zealand-based borrowers are interest-free. Only overseas-based borrowers are subject to interest on their loan balances. For overseas-based borrowers, the system imposes interest on outstanding loan balances up to and including the date of payment. For example, if an overseas-based borrower repays his or her loan in full on the 10th of August, interest is imposed on the outstanding loan balance up to and including the 10th of August.

However, the legislation does not reflect this practice, and instead imposes interest up to the date of payment being 9th August, not including the date of payment on 10th of August.

Recommendation

That the submission be accepted.

DECLARATION OF WORLDWIDE INCOME

Submission

(Matter raised by officials)

With the enactment of the Student Loan Scheme Act 2011, a legislative oversight has resulted in one of the obligations that need to be fulfilled before an overseas borrower can qualify for an interest-free loan under special exemption criteria being omitted from the new Act. Officials recommend that a borrower who qualifies for one of the exemptions be treated as physically in New Zealand and be required to file a declaration of worldwide income to qualify for the exemption or continue to qualify for the exemption. This amendment should apply from 1 April 2012.

Comment

A borrower who goes overseas but meets one of the exemption criteria can still be treated as physically in New Zealand for determining their New Zealand-based status. The exemptions include when the borrower is working for an approved overseas charity, undertaking full-time study overseas (including study at undergraduate or post-graduate level), or living in Niue, the Cook Islands, Tokelau or the Ross Dependency.

Under the Student Loan Scheme Act 1992, a borrower had to meet a number of requirements to qualify for the exemptions, including the requirement to file a declaration of their worldwide income and do so in future years to continue to qualify.

Recommendation

That the submission be accepted.

TREATMENT OF NEW ZEALAND-BASED BORROWERS WHO ARE NON-RESIDENT

Submissions

(Matters raised by officials)

Officials recommend that an amendment be included in the bill to enable New Zealand-based borrowers who are non-resident to apply for an extension of time to file their information, and for the Commissioner to have the discretion to provide an extension of time when satisfied that the borrower would not be able to provide the information by the original due date, being 7 July.

The late filing penalty provisions also need to be consequentially amended to ensure that the penalty is only imposed on New Zealand-based borrowers (including those non-resident and those with pre-taxed income) when the extended time to file a declaration or provide information has expired. This amendment should apply from 1 April 2012.

Officials also recommend that the legislation be amended to ensure that New Zealand based borrowers who are non-resident be required to pay their annual repayment obligation on the same remaining payment dates that apply to borrowers with other income. This amendment should apply from 1 April 2012.

Comment

Two problems have been identified in relation to New Zealand-based borrowers who are non-resident. The first relates to the provision of an extension of time to file information and the second relates to the due date for payment of remaining repayments.

The Student Loan Scheme Act 2011 requires a New Zealand-based borrower who is non-resident, such as a borrower studying overseas or working for an overseas aid agency, to provide the Commissioner with information on the borrower's annual gross income and annual total deductions. This information must be provided in the same timeframe as New Zealand-based borrowers who are required to file an IR3 tax return or declaration of pre-taxed income. For most borrowers, this is 7 July.

Extension of time for New Zealand-based borrowers who are non-resident

While New Zealand-based borrowers who reside here are able to apply for an extension of time to file their income tax return, no similar extension of time applies to the provision of income and deduction information of New Zealand-based borrowers who are non-resident.

Due date for payment of remaining payments

Once a New Zealand based borrower who is non-resident provides information on their annual income and deductions to the Commissioner, the Commissioner then assesses the borrower's repayment obligation for the year. The policy intent was that the borrower's repayment obligation would be payable on the same dates that New Zealand resident borrowers with other income pay their remaining repayments.

However, a legislative oversight has resulted in the policy intent not being reflected in legislation.

Recommendation

That the two submissions be accepted.

USE OF THE SPECIAL REPAYMENT CODE (STC)

Submission

(Matter raised by officials)

A change is required to reflect the current administrative practice of using the standard income tax and student loan repayment codes, for example “M SL”, when only student loan repayments are at a non-standard rate.

The use of the “STC” repayment code should be reserved for situations when there is a special deduction rate for both income tax and student loans or only income tax. The amendment should apply from 1 April 2012.

Comment

The Student Loan Scheme Act 2011 enables a borrower to apply for a special deduction rate to take account of an unused repayment threshold on their main source of salary or wages, or to reflect a lower repayment obligation – for example, due to hardship relief.

When a special deduction rate (a rate other than 10%) applies to student loans only, the Student Loan Scheme Act 2011 requires the borrower to use the “STC” repayment code in conjunction with their income tax code, for example “M STC”. This treatment was designed in anticipation of Inland Revenue having a new computer system to deliver student loans. However as the current FIRST computer system will be retained, an amendment is required to reflect current administrative practices.

Recommendation

That the submission be accepted.

DATE STUDYLINK CEASES CHARGING INTEREST

Submission

(Matter raised by officials)

A change is required to the Student Loan Scheme Act 2011 to change the date StudyLink cease charging interest from 1 January 2012 to 1 April 2012.

Comment

Currently, both StudyLink and Inland Revenue charge interest on loan balances. StudyLink charges interest while the borrower is studying and Inland Revenue continues this once the loan is transferred to Inland Revenue for collection. When the borrower is a New Zealand-based borrower, the interest charged is written off by Inland Revenue, leaving interest charged on overseas-based borrowers.

With the introduction of the student loan reforms, the Student Loan Scheme Act 2011 provides that StudyLink will cease charging interest with effect from 1 January 2012, and Inland Revenue will begin charging interest from that date. However, it would be more administratively efficient for both agencies if StudyLink ceased charging interest from 1 April 2012 rather than 1 January 2012. For the three-month period from January to March 2012, StudyLink will continue to charge interest and Inland Revenue will delay charging interest until 1 April 2012. Officials therefore recommend that the Act be amended to delay the date StudyLink will cease charging interest, and Inland Revenue will start charging, from 1 January to 1 April 2012.

The change will not adversely affect borrowers.

As the bill will be enacted after January 2012, this amendment should apply retrospectively from 1 January 2012.

Recommendation

That the submission be accepted.

KEEPING ALTERNATIVE CONTACT DETAILS UP-TO-DATE

Submission

(Matter raised by officials)

The obligation on the borrower to keep details up-to-date should also apply to the alternative contact person details provided to StudyLink and transferred to Inland Revenue as part of the loan application process. The bill currently does not require the borrower to keep the details held by Inland Revenue up-to-date.

Comment

When a borrower applies for a repayment holiday, the bill states that whenever the contact person's details change, the borrower must notify the Commissioner of the changed details. There is no similar obligation for borrowers to keep contact details up-to-date when Inland Revenue receives contact details from StudyLink through the student loan application process managed by StudyLink.

Recommendation

That the submission be accepted.

COMMUNICATING WITH AN ALTERNATIVE CONTACT PERSON

Submission

(Matter raised by officials)

There should be a provision allowing the Commissioner to notify an individual that they have been nominated as a contact person for a borrower. Inland Revenue can then explain that the department may contact them if the borrower has an unpaid amount and they may be asked to provide a contact address or to ask the borrower to contact Inland Revenue as prescribed by section 193A(2) of the Student Loan Scheme Act 2011.

Comment

Currently, the bill provides that Inland Revenue can only communicate with a contact person when the borrower is in default. There is no ability for Inland Revenue to proactively communicate with the contact person advising them that they have been nominated by the borrower to explain what it means to be a contact person. This ability will assist in ensuring the contact person understands that they will only be called upon for very specific information.

Recommendation

That the submission be accepted.

TRANSITIONAL PROVISIONS FOR DETERMINING DUE DATE FOR PURPOSES OF IMPOSING LATE PAYMENT INTEREST

Submission

(Matter raised by officials)

To ensure that borrowers are not disadvantaged, officials recommend that late payment interest for both interim payments and remaining repayments for the 2012–13 tax year apply from the final instalment date onwards.

Comment

The Student Loan Scheme Act 2011 changes the way late payment interest is imposed from 1 April 2013. However, payments for the 2012–13 tax year (both interim payments and remaining repayments) occur both before and after 1 April 2013. Having different late payment interest rules for repayment obligations that relate to the same tax year depending on when the payment is due will cause confusion and be difficult for borrowers to understand and comply with.

Recommendation

That the submission be accepted.

Minor technical matters

MINOR TECHNICAL MATTERS

Issue: The order in which deductions and payments are offset against the consolidated loan balance

Submission

(Matter raised by officials)

Two corrections are proposed to the provisions in the Student Loan Scheme Act 2011 that deal with the order in which payments are to be offset against a borrower's consolidated loan balance.

The first correction relates to a legislative oversight whereby the section that deals with overseas-based borrower deductions satisfying their repayment obligations (section 117) incorrectly overrides the general ordering rules (section 194) from 1 April 2012.

The second correction relates to an error whereby from 1 April 2013 section 117 incorrectly overrides sections 194 to 194D instead of only overriding section 194A(1) and (2). Officials recommend that amendments be included in the bill to correct these two errors.

Recommendation

That the submission be accepted.

Issue: How interest is calculated, charged and compounded

Submission

(Matter raised by officials)

The Student Loan Scheme Act 2011 provides that for the 2012–13 tax year, interest on outstanding loan balances is calculated each day, charged and compounded annually. Although interest is only charged annually, the current administrative practice is for statements issued to borrowers to show the amount of interest that has been calculated and accrued up to the date of the statements. This practice is not reflected in the legislation and officials recommend that for the 2012–13 tax year, the Act be amended to provide that interest be accrued on a daily basis.

The way interest on outstanding loan balances is charged and compounded will change from the 2013–14 tax year onwards. Therefore there will be no need to accrue interest from that point.

Recommendation

That the submission be accepted.

Issue: Student loan repayment codes

Submission

(Matter raised by officials)

There are two problems relating to student loan repayment codes.

The first is that the Student Loan Scheme Act 2011 incorrectly refers to a tax code instead of a repayment code. Although the Tax Administration Act refers to tax codes, the Student Loan Scheme Act refers to a repayment code. This error occurs in three places, sections 38 and 39, and clause 1 of schedule 2. Officials recommend that this error be corrected in the bill and that the amendments apply from 1 April 2012.

The second problem relates to income-tested beneficiaries who do not have to have repayment deductions made from their benefit. The Student Loan Scheme Act requires these borrowers to apply the “SL” repayment code even though they do not have student loan deductions made from their benefit. To ensure that both the Ministry of Social Development and beneficiaries do not incur costs in complying with this requirement, officials recommend that the legislation be amended to remove the requirement for income-tested beneficiaries to advise the Ministry of Social Development to apply the “SL” tax code. The amendment should apply from 1 April 2012.

Recommendation

That these submissions be accepted.

Issue: Notification period for significant over-deductions

Submission

(Matter raised by officials)

The Student Loan Scheme Act 2011 provides that where a borrower considers that a significant over-deduction has been made, the borrower can ask the Commissioner to investigate within six months of the date the borrower identifies the significant over-deduction. This gives the borrower an unduly long period to seek an investigation. What was intended was that the borrower would have six months from the date on which the significant over-deduction occurred to request the Commissioner to investigate the over-deduction.

Officials recommend that the bill be amended accordingly and that the amendment apply from 1 April 2012.

Recommendation

That the submission be accepted.

Issue: Repayment obligations of overseas-based borrowers

Submission

(Matter raised by officials)

An overseas-based borrower's repayment obligation for a year is based on the size of their consolidated loan balance at the end of the previous income year, increased by the annual administration fee and reduced by the amount of the excess repayment bonus.

Because of the way the legislation is drafted it could be construed that the excess repayment bonus is added to the borrower's loan balance instead of being subtracted from it as intended. Officials recommend that an amendment be included in the bill to ensure that the excess repayment bonus is subtracted from these loan balances for the purpose of calculating the repayment obligation for overseas-based borrowers.

Recommendation

That the submission be accepted.

Issue: Information to be provided by the loan manager

Submission

(Matter raised by officials)

Section 16 of the Student Loan Scheme Act 2011 requires the loan manager (StudyLink) to notify Inland Revenue of all persons who become borrowers and to provide the information set out in the section and any further information specified in subsequent regulations. The bill inserts a new section 16A, requiring the loan manager to notify Inland Revenue of the contact details of an alternative contact person provided by the borrower. There is no requirement to provide Inland Revenue with any further information specified in regulations. This appears to be a drafting oversight. Therefore, officials recommend that a similar requirement be included.

Recommendation

That the submission be accepted.

Issue: Issuing an additional deduction rate or a special assessment to collect a significant under-deduction

Submission

(Matter raised by officials)

Where a significant under-deduction has occurred because of an employer error or an error or omission on the part of a borrower, the Commissioner can issue an additional deduction rate for the recovery of the under-deducted amount. If the Commissioner cannot obtain the additional deductions the Commissioner can issue a special assessment to the borrower.

In implementing the reforms, Inland Revenue has identified a risk that the additional deduction rate and special assessment provisions would not apply in situations when the employer omitted or deliberately intended not to make a deduction, as this is not an employer “error”. This was not the policy intent as the special assessment provisions should be available for all situations when significant under-deduction occurs.

Officials therefore recommend that an amendment be incorporated into the bill to enable the additional deduction and special assessment provisions to apply to significant under-deductions when an employer has omitted or deliberately intended not to make a deduction.

Officials also recommend that a minor amendment be made to the provision for issuing an additional deduction rate notice to clarify that when the Commissioner issues an additional deduction rate notice, that notice replaces all previous notices issued to that employer in relation to a borrower. This amendment would overcome the situation where a notice issued to one employer could replace all previous notices issued to all employers of the borrower, which was not intended.

Recommendation

That the submission be accepted.

Issue: Transitional provision for small amounts of unpaid and uncollected repayments obligations

Submission

(Matter raised by officials)

When changes were made to the Student Loan Scheme Act 2011 to defer the application date of some of the reforms for a year, a legislative oversight resulted in the transitional provision relating to small amounts of unpaid repayment obligations applying from 31 March 2012 instead of 31 March 2013. Also, the provision incorrectly referred to one of two legislative references, omitting the reference to section 139(1) of the Student Loan Scheme Act which applies to small amounts of late payment interest.

Officials recommend that the bill be amended accordingly and that the amendments apply from the date of assent of the bill.

Recommendation

That the submission be accepted.

Matters raised by FEC

At the Committee's meeting on 8 February the Committee raised a number of questions about the bill. Officials' responses to these questions are outlined below.

Submission

(Finance and Expenditure Committee)

The Committee asked how the student loan repayment threshold is set.

Comment

The student loan repayment threshold is currently \$19,084 and set by the Student Loan Scheme Act 2011. The threshold applies for the tax year commencing on 1 April 2012. The threshold can be changed by way of a legislative amendment or by regulation.

Until the 2005–06 tax year, the student loan repayment threshold was set relative to the Domestic Purposes Benefit rate for a sole parent with two children. The threshold was then inflation-adjusted based on the movement in the Consumer Price Index until 2009. The Government has decided to hold the repayment threshold at the current level of \$19,084 until 2015.

The rationale for retaining the current threshold was to increase repayments and increase the value of the interest-free Student Loan Scheme.

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked for further clarification on how excluding losses from the calculation of income for student loan repayment purposes will impact on borrowers, and specifically on a borrower who is in business for the first six months, who makes a loss, and then derives salary and wages during the last part of the year.

Comment

The bill proposed two changes to the way repayment obligations are calculated for borrowers who have income other than salary, wages and New Zealand-sourced investment income ("other income").

First, a borrower who has a loss from a business or investment activity will not be able to use that loss to offset other income and thereby reduce their repayment obligation.

When a borrower undertakes two or more similar or related businesses or investment activities – for example, a landscaping business and a lawn-mowing service, or a café and a catering business, the activities can be combined and treated as a single endeavour. This would mean that losses could be offset against income earned from similar or related activities. This provision is also found in the legislation that excludes losses from the calculation of income for Working for Families.

Secondly, borrowers who receive “other income” as well as a salary or wage will no longer have their salary or wage repayment obligations calculated on an annual basis. Instead, they will shift to pay-period assessments.

From 1 April 2012 student loan borrowers with salary, wage and New Zealand-sourced investment income only (87 percent of New Zealand-based borrowers), will not have an end-of-year square-up of student loan deductions taken from their salary and wages. Rather, the amount to be paid will be assessed against a weekly, fortnightly or monthly repayment threshold. This policy is known as “pay-period assessments” and was introduced in the Student Loan Scheme Act 2011.

Pay-period assessments work on the principle that student loans should be repaid in periods when a person has the ability to do so. The following example compares pay-period assessments with the existing end-of-year square-up.

Example

Jane is paid an annual salary of \$72,000. She is paid monthly and receives \$6,000 each pay-period. The monthly student loan repayment threshold is \$1,590.

Monthly income liable for student loans: $\$6,000 - \$1,590 = \$4,410$

Monthly student loan deductions: $\$4,410 \times 10\% = \441

She works for six months during the 2011–12 tax year but stops working at the end of September. She has earned \$36,000 and had \$2,646 deducted for her student loan.

Under pay-period assessments, the amount deducted from monthly salary satisfies her repayment obligations. There is no further amount to pay or refund.

Under the end-of-year square-up, Jane’s repayment obligation would be assessed by taking 10c out of every dollar over the annual threshold of \$19,084.

Annual income liable for student loans: $\$36,000 - \$19,084 = \$16,916$

Annual repayment obligation: $\$16,916 \times 10\% = \$1,691.60$

Jane can request a refund of \$954.40, the difference between her annual obligation and her deductions.

A borrower who has a business loss in the first part of the year and then earns salary and wage income in the second part of the year will be affected by both of the repayment obligation changes contained in the bill. This is illustrated by the following example.

Example

Joe has a small business which he operates from 1 April 2012 to 30 September 2012. He incurs a \$10,000 loss during this time. During this period Joe does not have the ability to make repayments.

From 1 October 2012 to 31 March 2013 Joe is employed at an annual salary of \$60,000. He receives \$30,000 during this time and has the ability to make loan repayments. He has \$2,046 deducted for student loans.

Under the current legislation, Joe's repayment obligation would be assessed by taking 10c out of every dollar over the annual threshold of \$19,084. His annual income would be \$20,000 (\$30,000 wages minus his \$10,000 loss) so his annual repayment obligation would be $\$20,000 - 19,084 = \$916 \times 10\% = \$91.60$.

Joe would be able to receive a refund of \$1,954.40, the difference between his annual obligation and his deductions.

Under the pay-period assessment approach, Joe's repayment obligation would reflect his ability to pay at different points in time. While Joe is in business he incurs a loss and does not have the ability to repay his loan. However when Joe goes into employment he has the ability to make repayments. Under the changes proposed in the bill Joe would not be able to offset his business loss against his wage income, so his liable income would remain at \$30,000. His repayment obligation for the period he was earning wage income would be equal to the deductions withheld.

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked officials to provide examples of how borrowers can structure their affairs in order to reduce their student loan repayments.

Comment

Currently, borrowers are able to structure their affairs in order to reduce their student loan repayments liability. As part of Budget 2011, the Government asked officials to report to Ministers on options to address this issue. Officials are in the process of developing proposals and will shortly be reporting to Ministers.

Two examples of how borrowers can structure their affairs are outlined below.

Trustee income

Currently, the income of a trust can be taxed as trustee income at a final rate of 33% and the trust can later distribute this income to beneficiaries of the trust tax-free. While beneficiary income is taxable at the beneficiaries' level, and therefore included for student loan purposes, the distributed trustee income is not included in the taxable income of beneficiaries.

For example, Rachel is a borrower who earns \$40,000 per annum working for Rachel's Contracting Company (the Company). Rachel is also a sole director of the Company.

The Company is wholly owned by a family trust (the Trust). Rachel is both the settlor and a trustee of the Trust. Rachel's family are discretionary beneficiaries of the Trust.

The taxable income of the Company is \$200,000, on which it pays \$60,000 tax. The Trust receives a \$140,000 imputed dividend from the Company. The Trust then distributes \$120,000 (which has already been taxed as trustee income) to Rachel's family.

The family receives \$152,790 (\$32,790 salary after tax + \$120,000 distribution from the Trust) excluding WFF tax credits, but the distribution from the Trust is not counted for student loan purposes. As a result Rachel's repayment obligation does not match the income she has had available to meet her loan obligations. If the business income of the Company were included in Rachel's income, she would have a much higher repayment obligation.

Unlocked PIE income

Income from portfolio investment entities (PIEs) is currently not counted for student loan purposes. This exemption is appropriate for PIEs that are mainly intended to provide retirement benefits and cannot be easily accessed.

However, the exemption may not be appropriate for unlocked PIE investments which are readily available. Unlocked PIEs are where the funds are not sufficiently locked-in until a person's retirement. Examples include cash PIEs, which are akin to on-call bank accounts, PIEs that are unregistered superannuation schemes and listed PIEs.

A borrower who chose to invest in a savings account would face repayment obligations on this income if they earned enough. A borrower who invested in an unlocked PIE would not.

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked why borrowers cannot have the repayment holiday entitlement reset once they pay off their loan and get a new repayment holiday if they take out another loan.

Comment

Government policy is that the repayment holiday is available once, rather than repeatedly.

Taking a repayment holiday tends to increase, rather than decrease, a borrower's lifetime loan obligations, so a further entitlement to a repayment holiday would not necessary advantage borrowers over their lifetimes. It would also increase the cost to government by extending the term of the loan. The repayment holiday enables people who leave New Zealand briefly, such as for an "OE", to prevent penalties increasing their loan balances due to missed payments while they holiday or set themselves up overseas. However, interest charges continue to apply during the repayment holiday, so that loan balances will continue to increase if the borrower makes no payments during a repayment holiday.

There is no repayment holiday for borrowers who remain in New Zealand, so if the policy was changed to provide a further entitlement to a repayment holiday, the change could be seen as inequitable to people who remain in New Zealand and have no temporary break from making loan payments.

Changes to the repayment holiday in Budget 2011 reinforce that the break from making compulsory repayments is a privilege rather than a right, and increase equity between borrowers who remain in New Zealand (and do not have any repayment holiday) and people who move overseas. These changes include the reduction in length of the repayment holiday, and the requirement to apply for the repayment holiday and provide a contact person.

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked what the impact of the three-year repayment holiday has been on borrower compliance since its introduction, and has there been enough time to properly gauge the impacts.

Comment

The Government considered that the current three-year repayment holiday provided to overseas-based borrowers was generous compared with New Zealand-based borrowers who contribute to New Zealand society and who are required to make repayments as soon as their income exceeds the repayment threshold. It therefore seemed reasonable for overseas-based borrowers to begin making repayments after a 12-month period away from New Zealand.

The first group of borrowers to come off a 3-year repayment holiday occurred in the 2010–11 tax year. These borrowers would have had a repayment obligation due in that year.

In 2011 Inland Revenue undertook research to evaluate the provision of the repayment holiday. The research concluded that the repayment holiday was not seen to have any significant influence on whether borrowers would start repaying their student loans at the end of their holiday or on whether they return to New Zealand. It also found that borrowers involved in the research had generally travelled and had casual work in the first 12 to 18 months of their “OE”, but after this they aimed to gain professional overseas experience and to remain in the one city, and have steady employment. Other research has also shown that around three quarters of overseas borrowers have income above NZ \$30,000 per annum.

A recent study undertaken by KEA foundation of approximately 15,000 New Zealanders living overseas found that the major factors influencing borrowers’ decision to live overseas were the economic factors and family lifestyle. Having a student loan was not seen as significant.

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked what the revenue impact of the proposals is? What are the valuation impacts/cost of lending and what are the assumptions?

Comment

The extension of pay-period assessments is estimated to lead to an additional \$5 million per annum collected through student loan deductions, which is 8 percent more than would be required for these borrowers under the current end-of-year square-up policy (\$65.6 million).

These estimates are based on 2010 tax year data from borrower returns and employer monthly schedules.

The change to exclude losses from the calculation of repayment obligations affects approximately 13,000 borrowers and will increase student loan repayment obligations by an estimated \$9 million per annum.

This estimate is based on 2010 tax year data from borrowers’ returns and has been adjusted for the anticipated impact of the Budget 2010 changes to depreciation which is expected to reduce losses incurred in some sectors.

The overall impact of the Budget 2011 package on the cost of lending was calculated at the time of Budget 2011 to reduce the cost of lending from the current level of 45.25 cents to 43.74 cents in the dollar, once the package is fully implemented. The impacts on the operating balance for the initiatives included in the bill are forecast to be as follows:

Table A: Operating impact of the student support package

Proposals	Operating (\$ million)					
	2010/11	2011/12	2012/13	2013/14	2014/15	Total
Excluding (adding back) losses to income for student loan repayment purposes	-	-	(1.400)	(1.400)	(0.140)	(2.940)
One-year application based repayment holiday	-	-	-	-	-	-
Require a contact person for all new loan applications	-	0.284	0.071	-	-	0.355

The pay-period assessment was done outside the Budget process and is not included in the above figures.

Costing assumptions have been designed to be conservative, so that savings and improvements to the valuation are not overstated. In the case of the repayment holiday and contact person initiatives, that has meant that we have assumed no increase in repayments in the short term. In the case of the initiative to exclude losses from income, that has meant we have assumed the initiative has most impact in its first two years and then has a smaller on-going impact. The valuation of the Student Loan Scheme as at 30 June 2011 assumed no impact on the valuation from these initiatives.

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked what proportion of women borrowers are in default?

Comment

Of the total number of borrowers in default, 47 percent are female. The following table provides a breakdown of the number of males and female borrowers in default and the amounts in default by residence status.

		Number	Amount in default
NZB	Female	15,888	\$38,778,074.00
	Male	17,535	\$62,272,860.00
	Undisclosed	15	\$54,427.00
OBB	Female	21,821	\$135,690,211.00
	Male	24,871	\$175,510,963.00
	Undisclosed	78	\$618,707.00
Total		80,208	\$412,925,243.00

Recommendation

That the submission be noted.

Submission

(Finance and Expenditure Committee)

The Committee asked what information is held on Inland Revenue’s examination of student loans by English language students that are in default.

Comment

Inland Revenue does not hold information on courses undertaken by borrowers. We are therefore unable to provide information on the extent to which English language students are in default.

There was a significant increase in student loan borrowing by English language students, particularly new permanent residents in older age groups, in 2007. There was a concern that new permanent residents were using student loans as income support. The Government has responded to this increase, including through:

- Budget 2010 changes to create a stand-down period of two years for all new permanent residents, consistent with the existing stand-down period for income support; and
- Budget 2011 changes to limit student loan borrowing to fees only for people aged over 55 years.

Officials are monitoring the impact of these changes.

Recommendation

That the submission be noted.