Explanatory Memorandum to the Education (Student Loans) (Repayment) (Amendment) (No.3) Regulations 2021

This Explanatory Memorandum has been prepared by the Higher Education Division and is laid before Senedd Cymru in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1.

Minister for Education and Welsh Language's Declaration

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of the Education (Student Loans) (Repayment) (Amendment) (No.3) Regulations 2021. I am satisfied that the benefits justify the likely costs.

Jeremy Miles MS
Minister for Education and the Welsh Language
9 September 2021

Part 1

1. Description

1.1 The Education (Student Loans) (Repayment) Regulations 2009 (SI 2009/470), as amended ("the 2009 Regulations"), provide the basis for the repayment of student loans made by the Welsh Ministers. The 2009 Regulations include provision for interest to be charged on student loans.

1.2 The Education (Student Loans) (Repayment) (Amendment) (No.3) Regulations 2021 ("the 2021 Regulations") amend the 2009 Regulations to set a maximum interest rate on student loans, resulting in a lower rate of interest being charged to Welsh borrowers with Plan 2 or Plan 3 loans. Plan 2 loans are post 2012 undergraduate loans and Plan 3 loans are postgraduate degree loans. The rates will apply for a fixed period of three months, when they will be re-assessed.

2. Matters of special interest to the Legislation, Justice and Constitution Committee

2.1 The Education (Student Loans) (Repayment) (Amendment) (No.2) Regulations 2021 came into force on 1 July 2021 to introduce a time-limited cap on the maximum Plan 2 and the Plan 3 interest rates a period of 3 months, ending on 30 September 2021. MA/JMEWL/1728/21 refers.

2.2 The repayment of student loans is a complex legal area due to the nature of the devolution settlement and the division of functions between the Welsh Ministers and the Secretary of State for Education. Repayment of loans is provided for in the 2009 Regulations which are made on a composite basis by the Secretary of State and, in respect of those functions transferred to them, by the Welsh Ministers. The Welsh Ministers legislate in relation to Wales in respect of those functions transferred to them and the Secretary of State in relation to England and, insofar as the Secretary of State retains functions, Wales.

2.3 The 2021 Regulations are composite regulations. As the Regulations will be subject to UK Parliamentary scrutiny, it is not considered reasonably practicable for this instrument to be made or laid bilingually. Therefore, the amending regulations are made in English only.

3. Legislative background

3.1 Sections 22 and 42 of the Teaching and Higher Education Act 1998 enable the Welsh Ministers to make regulations relating to the provision of financial support to students ordinarily resident in Wales who are enrolled on designated courses of higher education, including provision for the repayment of loans.

3.2 The 2009 Regulations provide the basis for the repayment of student loans made by the Welsh Ministers and include provision for interest to be charged on student loans. The enabling powers for the 2021 Regulations are sections 22(2)(g), (3)(a), (4)(a) and 42(6) of the Teaching and Higher Education Act 1998.

3.3 The Welsh Ministers and Secretary of State are required by section 22(4) (a) of the Teaching and Higher Education Act 1998 to ensure that the student loan interest rate is either below the prevailing market rate (‘PMR’), or equal to the PMR with better T&Cs.

3.4 Section 44 of the Higher Education Act 2004 (‘the 2004 Act’) provided for the transfer to the National Assembly for Wales of the functions of the Secretary of State in relation to Wales under section 22 of the 1998 Act (except insofar as they relate to the making of any provision authorised by subsections (2)(j), (3)(e) or (f) or (5) of section 22). Section 44 of the 2004 Act also provided for the functions of the Secretary of State in section 22(2)(a), (c) and (k) of the 1998 Act to be exercisable concurrently with the National Assembly for Wales in relation to Wales.

3.5 The functions of the Secretary of State under section 42(6) of the 1998 Act were transferred to the National Assembly for Wales, so far as exercisable in relation to Wales, by the National Assembly for Wales (Transfer of Functions) Order 1999 (SI 1999/672).

3.6 The functions of the National Assembly for Wales were transferred to the Welsh Ministers by virtue of section 162 of, and paragraph 30 of Schedule 11 to, the Government of Wales Act 2006.

3.7 Each year, a number of functions of the Welsh Ministers in regulations made under section 22 of the 1998 Act are delegated to the Student Loans Company under section 23 of the 1998 Act.

3.8 These Regulations are being made under the negative resolution procedure.

4. Purpose and intended effect of the legislation

4.1 In addition to the duty on the Welsh Ministers and Secretary of State as outlined above, student loan interest rates must also be below the PMR, or equal to the PMR with better T&Cs, to remain exempt from the Consumer Credit Directive (‘CCD’). While student loans are exempt from the CCD, they do not have to show on borrower’s credit files meaning that student loans will not affect a borrower’s credit rating. If the CCD exemption were removed, student loans would have to be included within a customer’s credit file, potentially affecting their credit rating.

4.2 Student loan interest rates are set according to the 2009 Regulations (as amended) and currently give no consideration to the PMR. The interest charged on Plan 2 loans is set out in regulation 21A of the 2009 Regulations and varies from the "*standard rate*" to the "*standard rate plus the additional rate*" to the "*standard rate plus 3%".* The standard rate is the greater of 0% and an amount equal to the percentage increase between the retail prices all items index published by the ONS for the two Marches immediately before the commencement of the academic year. The rate charged on Plan 3 loans is set out in regulation 21B of the 2009 Regulations as RPI+3%. "RPI" is defined for these purposes as "*the percentage increase between the retail prices all items index published by the National Office for Statistics for the two Marches immediately before the commencement of the academic year*". The regulations leave the potential for the student loan interest rate to exceed the PMR, which, as set out above, would be unlawful.

4.3 The PMR has generally been declining over recent months. A previous amendment to regulations introduced a time-limited cap on the maximum Plan 2 and the Plan 3 interest rates for July-September 2021. The decline has continued and the PMR has remained below the current maximum Plan 2 and Plan 3 student loan interest rates for a further three consecutive months.

4.4 At the point of monitoring, for the months of May 2021, June 2021 and July 2021, the Bank of England's effective interest rate dropped 0.1 percentage points, or more, below the current maximum, Plan 2 and the Plan 3 student loan interest rate. As this has occurred for three consecutive months, it has been agreed with UK Government for amending regulations to be made, to implement the PMR cap on interest rates for three months.

4.5 The 2021 Regulations extend the implementation of a maximum student loan interest rate for the above loans for a period of three months, to bring the student loan interest rates in line with PMR. For Plan 2 student loans, this will mean a maximum interest rate equal to PMR. For Plan 3 loans, this will mean an interest rate equal to PMR.

4.6 The maximum interest rate will be set at 4.1% for a period of 3 months from 1 October 2021. After expiry of the Regulations on 31 December 2021, the interest rate on post 2012 undergraduate loans and postgraduate degree loans will return to the rate specified in the 2009 Regulations, unless they remain above the PMR, in which case, further amending regulations will be made.

5. Consultation

5.1 No consultation has been undertaken.

Part 2 – Regulatory Impact Assessment

An RIA has been conducted for the 2021 Regulations.

6. Options

Option 1: Business as usual

6.1 If the 2021 Regulations are not made, Welsh Ministers will be in breach of their duty to ensure that the student loan interest rate is either below the prevailing market rate (PMR), or equal to the PMR with better T&Cs.

6.2 In addition, student loans would no longer be exempt from the Consumer Credit Directive and, as such, will show on borrowers credit file and may affect their credit rating.

Option 2: Make the Regulations

6.3 Making the 2021 Regulations ensures that the consequences outlined above are avoided.

7. Costs and benefits

Option 1: Business as usual

7.1 There would be no additional costs or particular benefits in continuing with business as usual.

7.2 Leaving the existing regulations in place would mean Welsh Ministers will be in breach of their duty to ensure that the student loan interest rate is either below the PMR, or equal to the PMR with better T&Cs.

7.3 Student loans would no longer be exempt from the CCD and, as such, will show on borrowers credit file and may affect their credit rating.

Option 2: Make the Regulations

7.4 Making the 2021 Regulations would ensure that there is no breach of Welsh Ministers' duty in relation to the student loan interest rate (section 22(4)(a) of the Teaching and Higher Education Act 1998).

7.5 Under the 2021 Regulations, the effect of a temporary decrease in the prevailing market rate below the maximum student loans interest rate would be to temporarily reduce the interest rate applied to the loans of some student loan borrowers in Wales. The affected categories of student loan borrower would be: all Plan 3 borrowers (both in-study and post-study); all in-study Plan 2 borrowers; and some post-study Plan 2 borrowers. The latest estimates suggest that approximately 2,200 (or 1.8% of) post-study Plan 2 borrowers will benefit from the temporary reduction in maximum interest rates between 1

October and 31 December 2021. The majority of post-study Plan 2 borrowers would remain unaffected unless the prevailing market rate were to drop below the minimum Plan 2 interest rate, which is considered to be highly unlikely. Further detail on the proportion of post-study Plan 2 borrowers that may be affected by the changes is presented in Technical Annex A.

7.6 The potential changes to student loan interest rates associated with making the 2021 Regulations may have a small cost impact on the Welsh Government. The Resource Accounting and Budgeting (RAB) charge is the estimated cost to Government of borrowing to support the student finance system. It is based on predicted future loan write-offs and interest subsidies in net present value terms. A temporary reduction in student loan interest rates would lead to relatively less interest being accrued on some borrowers' student loan accounts, therefore their loan balance would decrease and those borrowers who go on to fully repay their student loan will repay a relatively smaller amount. Predicted repayments may fall overall, and thus the RAB charge, which the Welsh Government must fund, may rise. However, the majority of student loan borrowers (both Plan 2 and Plan 3) are predicted to repay less than the principal of their loan before the loan is written off. Any reduction in the interest rate would have no impact on the predicted repayments of this majority; therefore the potential impact on the overall RAB charge is expected to be relatively small.

7.7 In this instance, where the maximum Plan 2 and Plan 3 interest rate is to be reduced by 0.4 percentage points from 1 October to 31 December 2021, the latest modelled estimates suggest a negligible impact (less than £0.2 million) on the amount of non-cash provision required for the 2021-22 financial year.

7.8 In general, the anticipated potential expenditure associated with any future interest rate reductions, should the PMR remain below the maximum student loans interest rate over the coming months, can be met from within existing resources.

7.9 The new arrangements under the 2021 Regulations will also have implications for Welsh student loan borrowers. These will be positive, as affected borrowers would see a reduction in their loan balance as a result of the change. However, it would only be those who fully repaid their loan who would see an impact in terms of the repayments made against the loan.

7.10 Student loans would remain exempt from the CCD and, as such, the current position where student loans do not show on a borrowers credit file would be maintained.

8. Competition Assessment

8.1 The making of the 2021 Regulations has no impact on the competitiveness of businesses, charities or the voluntary sector.

9. Post-Implementation Assessment

9.1 The 2021 Regulations implement the PMR cap on interest rates for three months. Monitoring of the level of the PMR will be carried out on a monthly basis. Further amending regulations will be made if, at any point, the Bank of England's effective interest rate drops 0.1 percentage points, or more, below the current maximum, Plan 2 and the Plan 3 student loan interest rate for three consecutive months.

Technical Annex A

It was explained in Section 7 that under the 2021 Regulations, the effect of a temporary decrease in the prevailing market rate below the maximum student loans interest rate would be to temporarily reduce the interest rate applied to the loans of: all Plan 3 borrowers (both in-study and post-study); all in-study Plan 2 borrowers; and some post-study Plan 2 borrowers. This Technical Annex provides further detail on the proportion of post-study Plan 2 borrowers that may be affected by the changes.

Under the current student loans terms and conditions, the post-study interest rate applied to Plan 2 student loans is equal to RPI plus X percentage points, where X is calculated for each individual borrower on a sliding scale between 0 and 3 percentage points, based on the borrower's gross income above the Plan 2 repayment threshold. The highest-earning Plan 2 graduates are charged an interest rate of RPI plus 3 percentage points, while those who earn below the repayment threshold are charged an interest rate of RPI.[1]

For illustrative purposes, Table 1 shows the approximate proportion of post-study Plan 2 borrowers whose student loan interest rate would be reduced if the prevailing market rate falls to certain levels (in percentage point terms) below the maximum Plan 2 interest rate, and if a cap is implemented accordingly. The analysis is based on administrative data from the Student Loans Company (SLC), which show the variable interest rates applied to Welsh Plan 2 borrowers' accounts as at 30 June 2021. The 0.4 percentage point reduction, as is to be applied between 1 October and 31 December 2021, will benefit 1.8% of post-study Plan 2 borrowers, and is emboldened in Table 1.

Table 1: Approximate proportion of post-study Plan 2 borrowers whose student loan interest rate would be reduced under the 2021 Regulations, if the maximum Plan 2 interest rate were to be reduced by various increments

Percentage pt. reduction in maximum Plan 2 interest rate	Proportion of post-study Plan 2 borrowers affected
0.1%	1.4%
0.3%	1.6%
0.4%	**1.8%**
0.5%	1.9%
1.0%	3.1%
2.0%	8.8%
3.0%	22.3%
more than 3.0%	100.0%

It is clear from Table 1 that a slight reduction in the maximum Plan 2 interest rate would affect only a small proportion of post-study Plan 2 student loan borrowers; and the majority of the borrowers would be unaffected by a decrease in the prevailing market rate as long as the PMR does not fall below the minimum Plan 2 interest rate, equal

[1] For the 2021-22 financial year: the Plan 2 repayment threshold is set at £27,295 per annum; and individual Plan 2 borrowers are charged a post-study interest rate of RPI plus 3 percentage points if their gross income is more than £49,130 per annum.

to the RPI rate. This is because the majority of Plan 2 graduates earn an income below the Plan 2 repayment threshold or are otherwise not required to repay their student loan. The case in which the PMR falls to a level below the minimum Plan 2 interest rate is considered to be highly unlikely.