Office for National Statistics

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The Rt Hon. The Lord Forsyth of Drumlean
Chair, Lords Economic Affairs Committee
House of Lords
London
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23 January 2018

Dear Lord Forsyth,

I am writing in response to your call for evidence for the economics of higher, future and technical education inquiry.

In particular, we understand your Committee are interested in how student loan transactions impact fiscal aggregates, such as Public Sector Net Borrowing (PSNB) and Public Sector Net Debt (PSND). In addition, information on how the impacts on fiscal aggregates are decided and whether there is any scope for government to change the fiscal treatment of student loans.

We are providing this information to assist your inquiry and would be very happy to provide further clarification and advice on any points of interest to yourself and the Committee, as required.

Yours sincerely,

Jonathan Athow

How are student loans recorded in the public sector finances?

Different student loan transactions will impact the fiscal aggregates differently. The below table summarises the impact of a variety of different transactions.

Table 1: Effect on key fiscal aggregates of student loan transactions

Transaction	Public Sector Net Borrowing (PSNB) 'the deficit'	Public Sector Net Debt (PSND)	Public Sector Net Cash Requirement (PSNCR)
Issuing of student loan to individual	No effect	Increases by value of portion of loan issued directly to individual[1]	Increases by value of portion of loan issued directly to individual[1]
Tuition fee is passed to university	No effect	Increases by value of tuition fee passed directly to university[1]	Increases by value of tuition fee passed directly to university[1]
Interest is accrued on student loan	Decreases as interest accrues	No effect	No effect
Student makes repayment of student loan interest	No effect	Decreases as repayment made	Decreases as repayment made
Student makes repayment of student loan capital	No effect	Decreases as repayment made	Decreases as repayment made
Government impairs a student loan in Department for Education Accounts, as a result of assessment of likelihood to pay	No effect	No effect	No effect
Student loan interest is written off by Government after 25 / 30 years	Increases by value of write off	No effect	No effect
Student loan capital is written off by Government after 25 / 30 years	Increases by value of write off	No effect	No effect
Student loan capital is sold off below face value prior to being written off	No effect	Decreases by value of cash received from sale	Decreases by value of cash received from sale
Student loan accrued interest is sold off below face value prior to being written off	No effect	Decreases by value of cash received from sale	Decreases by value of cash received from sale
Student loan capital is revalued below face value prior to sale, and then sold	If written off prior to sale then increases by value of write off,	Decreases by value of cash received from sale	Decreases by value of cash received from sale

[1] We have partitioned the loan into the part paid directly to the individual and the part paid directly to the university.

off	otherwise no effect		
Student loan interest is revalued below face value prior to sale, and then sold off	If written off prior to sale then increases by value of write off, otherwise no effect	Decreases by value of cash received from sale	Decreases by value of cash received from sale
Accrued interest not yet received when loans are sold off or written off	When sold off no effect When written off increases by value of write off In both cases (sold off or written off) there will be no future PSNB benefit from further accrual of interest on the loans sold/written off	No effect	No effect

The public sector finances, and the key fiscal aggregates they contain, are based on the principles and building blocks of the National Accounts, which is an international statistical framework published by the United Nations. The National Accounts are a single coherent and exhaustive description of economic activity in the UK and the public sector fiscal aggregates are based on National Accounts principles and definitions. One implication of this is that transactions should impact creditors and debtors in a consistent and symmetric manner. It is for this reason that National Accounts records loans at their nominal value (i.e. initial amount of loan, plus interest accrued, less repayments).

To put this in the context of student loans, an individual in receipt of a student loan is liable for repayment of that loan capital, and the accrued interest on the loan, up until that loan is written off or cancelled (either for death, disability or reaching cancellation threshold). Government impairment of student loan assets and sale of those loans below the nominal value has no impact on the student liability and so is not recognised within the government accounts, as compiled under National Accounts. It is for this reason that student loan write-offs impact the fiscal aggregates differently to student loan impairments or sales.

Who decides on how to record student loans in the public sector finances?

UK fiscal policy is set by HM Treasury and since 1998 Treasury have based its fiscal framework on National Accounts principles. This means that the key fiscal measures of PSNB and PSND are based on the concepts of National Accounts.

However, it is the responsibility of ONS to compile PSNB and PSND ensuring that the underlying economic reality of transactions and financial instruments is followed when deciding whether or not a particular transaction should impact PSNB or an instrument be included in PSND. ONS reaches these decisions in compliance with the international (UN) statistical guidance for National Accounts.

In the case of student loans, ONS has concluded that these should be classified as “loans” in National Accounts. This means that only accrued interest and write-offs impact PSNB whilst PSND impacts reflect the cash flows on issuance and on receipt of interest and capital repayments.

The recording of student loans as loans in National Accounts, and so the fiscal aggregates, is based on the fact that they have the following features:

- are bilateral agreements agreed between the lender (government) and borrower (student)
- are taken out on the initiative of the borrower
- are interest bearing
- are not compulsory requirements for all higher education students
- are an unconditional debt to the borrower that has to be repaid (subject to meeting certain conditions).

Could student loans be recorded differently in the public sector finances?

In the opinion of ONS, student loans meet the definition of loans in the National Accounts and it follows from this that they impact the key fiscal aggregates in the ways set out in Table 1.

Student loan repayments have been dubbed by some a “*graduate tax*”, however they do not meet the definition of a tax in National Accounts as they are not compulsory, unrequited payments but are payments linked directly to funds extended by the government. Similarly, student loan payments by government are not subsidies in National Accounts as they are not unrequited payments.

It might be conceivable to consider student loans as a series of transfers out of government, at the point of loan issuance, and into government when interest and capital repayments are made. Such a recording would mean that all cash paid at issuance would be recorded as government spending and all cash received in repayments as revenue, with both spending and revenue impacting PSNB.

There are no doubt other creative ways, to that described in the above paragraph, by which student loans could be recorded. However, it should be reiterated that ONS is firmly of the view that the economic nature of student loans closely matches the definition of a loan in National Accounts and should be recorded as such in both the National Accounts and the UK fiscal aggregates.

As noted by the Office for Budget Responsibility (OBR) in its Fiscal Risks Report[2], it is the case that the recording of student loans in the National Accounts means that PSNB is reduced by accrued interest that may never be paid. However, “*eventually this over-recording will be resolved by writing off any outstanding portion of the loan. But this may not be until years later*”.

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[2] Fiscal Risks Report, OBR, July 2017, pg 219 can be found here: http://cdn.budgetresponsibility.org.uk/July_2017_Fiscal_risks.pdf