House of Commons Library

By Paul Bolton

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Higher education funding in England

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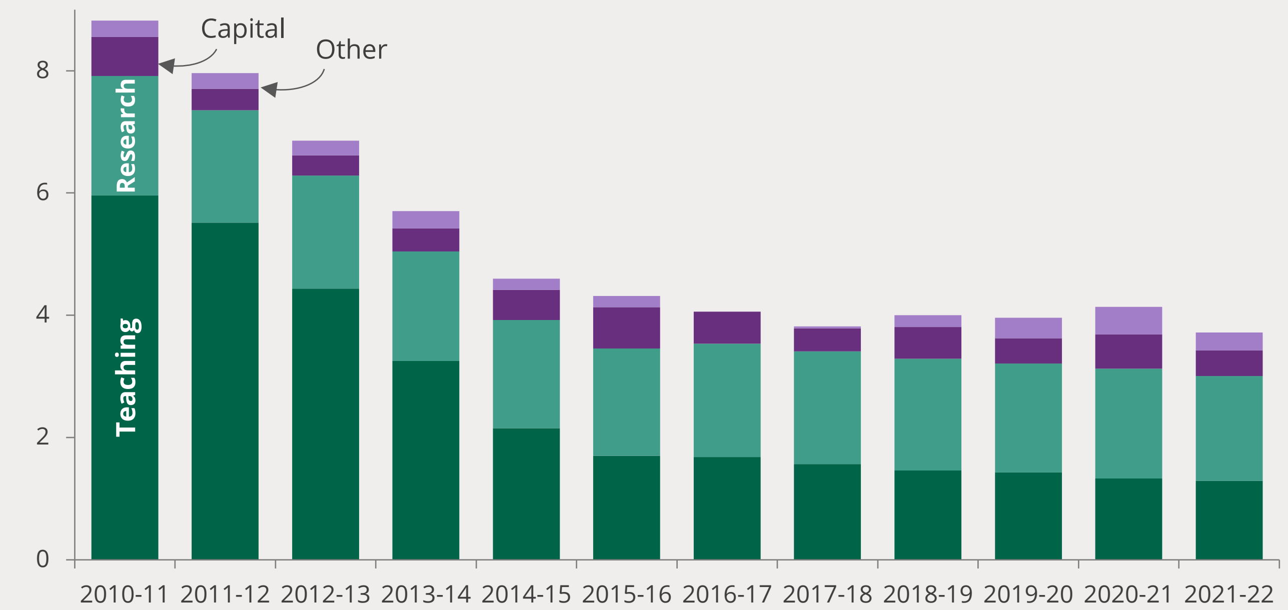
Summary -funding

There are two main elements of public spending on higher education –direct funding through the funding councils for teaching and research and student loans. In the past maintenance grants were an important element of spending, but these were abolished for new students from 2016.

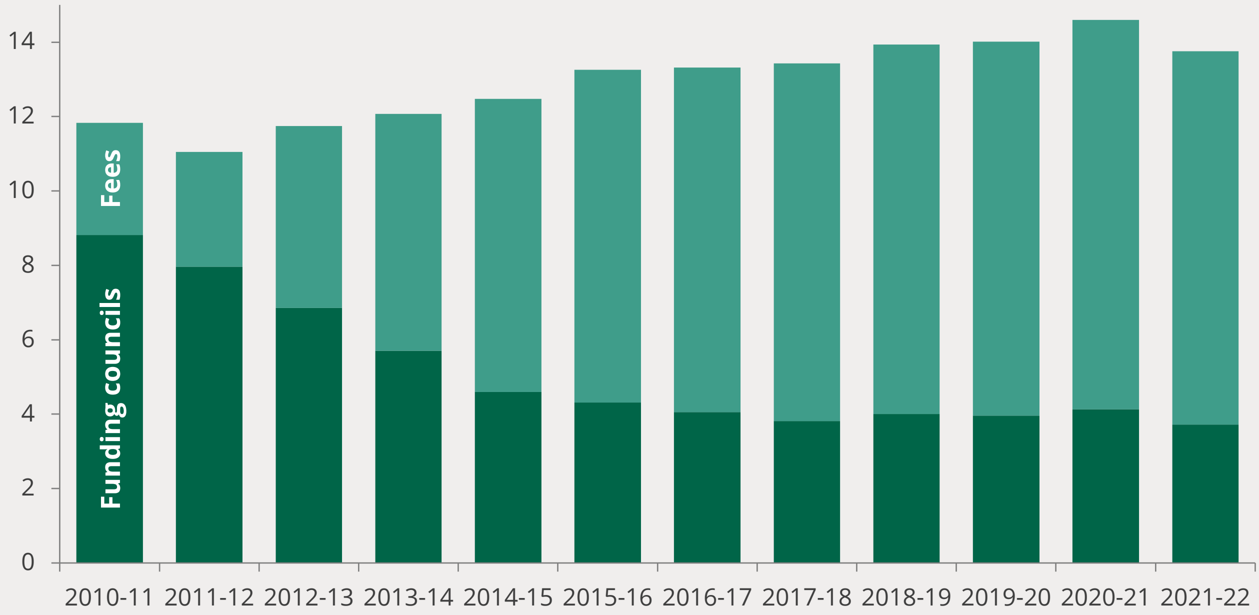
Funding council allocations: Teaching cut, research stable

£ billion 2020-21 prices



Funding for universities shifts towards fees

£ billion 2020-21 prices



Support through the funding council for teaching fell even before the 2012 reforms and was cut particularly quickly from 2012 to 2015. **The 2020-21 total for teaching is 78% below the 2010-11 figure in real terms**.

Research funding has been broadly maintained in real terms since 2010.

Spending on maintenance grants was just over £1.6 billion in 2015/16. Grants were abolished for new students from 2016/17 and **it fell to £0.2 billion in 2018/19 and is expected to be near zero from 2019/20**.

The cash value of all student loans has increased from below £6 billion in 2011-12 to more than £17 billion in 2019-20 and is forecast to be more than £21 billion in 2024-25. This increase was driven primarily by higher fees from 2012, but also replacing grants with loans, higher student numbers and expansion of loans to part-time and postgraduate students.

The ultimate cost to the public sector is currently thought to be around 54% of the face value of loans to full-time undergraduates. This subsidy element of loans was not included in the Government's main measure of public spending on services for some years and hence did not count towards the fiscal *deficit*. Recently an estimate of this subsidy has been included in overall UK public borrowing again. There is considerable uncertainty about the final size of the subsidy element of loans and the Government's estimate of it increased sharply after the 2012 reforms were first announced and increased in the latest forecasts in response to lower earnings forecasts following the coronavirus pandemic.

The total cost to the public sector has varied little in real terms over these years if the subsidy element of loans is included. This is despite the increase in student numbers. A recent increase reflects new estimates of the subsidy element of loans which has only been made for 2019-20 and 2020-21. **Cuts in support for teaching over the first half of this decade were balanced out by increases in loans and grants.** More recently the main change has been the shift from maintenance grants to loans.

Summary -policy related to funding

The Government raised the cap on tuition fees for new student to £9,000 in 2012/13 and cut most ongoing direct public funding for teaching in England. This shifted the balance of higher education funding further away from the state and further towards the individual who benefits.

In his summer Budget 2015 Chancellor George Osborne announced the biggest changes to student finance since 2012:

- Maintenance grants will end for new students from 2016/17 and be replaced by loans.
- A consultation on freezing the student loan repayment threshold for five years
- Allowing universities offering 'high teaching quality' to increase fees in line with inflation from 2017
- A review of the discount rate applied to the accounting treatment of loans.

After consultation the Government decided to freeze the repayment threshold for all post-2012 borrowers. The discount rate used for the public accounting of loans was reduced from 2.2% to 0.7%. These changes were expected to result in savings to current spending when grants are ended, and a substantial cut in the subsidy element of loans.

On 1 October 2017 Prime Minister Theresa May announced a number of changes to these policies: The fee cap would be frozen in 2018-19, the repayment threshold would rise to £25,000 and a there would be a review of the student finance system. The Department for Education subsequently confirmed that the freeze on the repayment threshold would also be removed.

On 19 February 2018, Prime Minister Theresa May announced that there would be a "wide-ranging review into post-18 education" led by Philip Augar. The review is to look at how future students will contribute to the cost of their studies, including "the level, terms and duration of their contribution." More detail on the review can be found at: Review of Post-18 Education and Funding.

The Review report was published on 30 May 2019, *Independent panel report to the Review of Post-18 Education and Funding*. The report was a detailed analysis of the post-18 education sector and the funding issues faced by stakeholders. The Library's briefing paper *The Post-18 Education Review (the Augar Review) recommendations* gives more detail. On 21 January 2021 the Government published its 'interim conclusions' to its review of post-18 education and funding. It announced that the maximum tuition fee cap would be frozen again in 2021/22 at £9,250 and that decisions on further changes to student finance would be put off until the next spending review later in the year. At the autumn 2021 spending review the Government said its response to the Augar report would be published "…in the coming weeks" alongside details of the higher education settlement up to 2024-25.[1]

The forecasts summarised in this note assume the current system is kept in place.

This paper looks at recent levels of funding for higher education in England, particularly the period from 2015 onwards. It builds on and replaces Changes to higher education funding and student support in England from 2012/13 and HE in England from 2012: Funding and finance which looked in detail at the impact of the 2012 reforms and subsequent announcements on graduates, universities and public spending.

The Student Finance Explained series of articles looks at financial flows under the current system and the impact of different hypothetical changes to student loan repayment terms, tuition fee levels and grants.

The briefing paper *Higher education student numbers* looks at how student numbers have changed over time, gives some insight into the impact of the 2012 higher education reforms on different types of students and courses and summarises the last evidence on applications. Readers may also be interested in the following briefing papers:

- Review of Post-18 Education and Funding
- Prime Minister's announcement on changes to student funding
- Higher education finance statistics
- Student loan statistics
- Tuition fee statistics
- The value of student maintenance support
- Support for postgraduate students in England
- Higher education tuition fees in England

Impact of the coronavirus pandemic

The Government has announced a number of different support measures to help universities deal with the expected drop in income following the coronavirus pandemic. These are detailed in the briefing paper Coronavirus: Financial impact on higher education along with a discussion of the possible size and effect of the drop in income.

1 Autumn Budget and Spending Review 2021, HM Treasury (para 4.16)

1 Background

1.1 '2012' reforms

The 2012 reforms increased the cap on fees to £9,000. Student loans increased to pay for this but the reforms made repayments more 'progressive'

The Independent Review of Higher Education Funding – the Browne Report[2]- was published in October 2010. It made recommendations on the future funding and organisation of the higher education sector and on student finance. The main recommendations directly connected to funding were:

- Remove direct public funding for most undergraduate courses and retain a much smaller amount for higher cost subjects.
- Remove the cap from tuition fees. Institutions would keep all the income up to £6,000 per year and share any more with Government.
- Extend student loans to part-time students
- Increase the loans repayment threshold from £15,000 to £21,000 and increase it in line with earnings in the future.
- Introduce a real interest rate on loans for those earning above the threshold equal to the Government's cost of borrowing (inflation plus 2.2%) and ensure no one repaying their loan sees its real value increase.
- Extend the write-off period of loans from 25 to 30 years
- Increase student numbers by 10% to remove excess demand

The report concluded that, with static numbers of students, the reforms would eventually cut core public spending on undergraduate study by around £1.8 billion or almost 30%, graduates would repay more (55% more with fees of £8,000) but additional repayments would come from higher earning graduates and institutions could see an increase in their income[3] with fees of around £7,000 or more (10% with fees of £8,000).[4]

The Government announced its plans for reform of higher education and student finance in November 2010.[5] These followed many of the recommendations set out in the Browne Report. The major differences with an impact on funding were:

- A cap on fees of £9,000, no levy on fees above this level, but obligations on the institution to spend more on access for disadvantaged students

2 Securing a sustainable future for higher education –An independent review of higher education funding & student finance
3 Income from these fees and teaching grants only
4 ibid. pp43-44
5 Reform for higher education and student finance, BIS (3 November 2010)

- A real interest of 3% above inflation for graduates earning above £41,000 (in 2016) with a sliding scale rising from 0% (real) at £21,000
- Annual uprating of both thresholds in line with growth in average earnings[6]
- No growth in student number

1.2 Comprehensive Spending Review 2010 and later spending rounds

Funding for higher education was cut dramatically in the 2010 CSR as funding reforms shifted the balance from taxpayers to graduates

Further smaller scale cuts were announced in 2013 alongside the decision to remove the cap on student numbers

The Comprehensive Spending Review 2010 (CSR) set out the parameters for public spending over the period 2011-12 to 2014-15. Total resources for higher education (excluding research) was to fall from £7.1 billion in 2010-11 to £4.2 billion in 2014-15;[7] a cut of 41% in cash terms and 44% in real terms.[8]

The Spending Round 2013 announced a series of further savings from the higher education budget –the continued cuts in funding for teaching as the 2012 system applies to more students, freezing grants, requiring HEFCE to make additional savings and cutting access spending.[9] Autumn Statement 2013 announced the cap on student numbers would be raised in 2014-15 and lifted in 2015-16 which would increase spending compared to what it would otherwise have been. The Government expected to fund this through the sale of some older student loan debt.

1.3 Summer Budget 2015 and Spending Review/Autumn Statement 2015

In his Summer Budget 2015 the Chancellor announced that maintenance grants would end for new students from 2016/17 and be replaced by loans. He also announced consultations on freezing the repayment threshold for five years, allowing some universities to increase fees in line with inflation from 2017 and a review of the discount rate applied to the accounting treatment of

6 The initial proposal was for five-yearly upratings.
7 BIS news release 20 October 2010, *The Department for Business Innovation and Skills Spending Review Settlement*
8 Adjusted using March 2015 GDP deflators and OBR projections.
9 Spending Round 2013, HM Treasury

loans.[10] These are the biggest changes to student finance since the 2012 reforms.

The Government published a consultation on freezing the loan repayment threshold in July 2015. This set out two options for change:

- Option 1 (preferred): Freeze the threshold at £21,000 from April 2016 for all existing and new borrowers for five years. Reviews the threshold from April 2021
- Option 2: Freeze the threshold for new borrowers only for five years from April 2020

2015 saw the announcement of the biggest reform of student finance since the 2012 reforms. Grants would be ended, the fee cap raised and the loan repayment threshold would be frozen –making the system less 'progressive'.

The consultation estimated that option 1 would generate £3.2 billion (current/discounted values) in additional graduate repayments from existing borrowers. On top of this one-off amount there would be an additional £0.9 billion for each £15 billion of loans to new students.[11] Under Option 2 only the amount for new students (put at £1.0 billion per £15 billion of loans) would apply.[12]

The Government published its response to the consultation in November 2015.[13] It accepted that most responses did not support freezing the threshold, but said it would implement its preferred option –freeze the repayment threshold for all post-2012 borrowers at £21,000 until at least April 2021. An equality analysis was produced alongside the consultation response.[14] This looked at the impact on different types of 'protected characteristics' such as age, sex, disability and ethnicity.

The Spending Review and Autumn Statement 2015 made some headline announcements about funding paid through the funding council, the extension of maintenance loans to part-time students and new loans for Master's degrees. It also announced that the discount rate applied to loans would be reduced to 0.7% and set the spending totals for the Department for Business, Innovation and Skills which will eventually feedthrough to annual funding allocations for higher education.

The Library briefing papers on maintenance support and loans look at the impact of these changes on students/graduates. Some estimates of the impact on public spending are included in the next sections which look at each main element in turn.

10 Summer Budget 2015, HM Treasury
11 This volume of loans is approximately the amount that might be lent to each cohort of new students.
12 *Consultation on freezing the student loan repayment threshold*, BIS (July 2015)
13 *Freezing the student loan repayment threshold Government response to the consultation on freezing the student loan repayment threshold*, BIS (November 2015)
14 *Freezing the student loan repayment threshold, Equality analysis*, BIS (November 2015)

1.4 Prime Minister's October 2017 announcement

Changes announced by the PM in October 2017 reverse some of the 2015 decisions and make each £ of student loans more expensive to the public sector

On 1 October 2017 Prime Minister Theresa May announced[15] that there would be changes to the student finance system including:

- freezing tuition fees at the 2017/18 level of £9,250
- raising the student loans repayment threshold from £21,000 to 25,000
- a review of the student finance system

The Secretary of State gave more detail on the changes to student finance in a Written Statement on 9 October:

- The lower repayment threshold will increase to £25,000 from the start of financial year 2018-19.
- The upper repayment threshold will be increased at the same time
- Both thresholds will be adjusted annually in line with average earnings.
- These changes apply to borrowers taking out post-2012 loans. Around 600,000 borrowers would benefit from lower repayments in 2018-19

This means that as well as the one-off increase in the threshold these changes reverse the earlier policy to freeze the threshold.

The freeze on fee levels means a small cut in the amount the Government expects to lend as fee loans and a drop in fee income for institutions (compared to the earlier policy). Raising and unfreezing the threshold has a greater impact on the public finances in the longer term as it cuts the loan repayments and hence increases the subsidy element or cost of loans. More detail is given in the section on loans in section 2.2 and in the briefing paper Prime Minister's announcement on changes to student funding.

On 19 February 2018 Prime Minister Theresa May announced that there would be a "wide-ranging review into post-18 education" led by Philip Augar. The review is to look at how future students will contribute to the cost of their studies, including "the level, terms and duration of their contribution." More detail on the review can be found at: Review of Post-18 Education and Funding

The Review report was published on 30 May 2019, *Independent panel report to the Review of Post-18 Education and Funding*. The report was a detailed analysis of the post-18 education sector and the funding issues faced by stakeholders. The report contained 53 recommendations on the future structure of the sector and funding proposals. The headline recommendations related to funding for higher education were:

- the reduction of higher education tuition fees to £7,500 per year
- Government to replace lost fee income by increasing teaching grant
- extending the student loan repayment period from 30 years to 40 years

15 "Theresa May pledges help for young on student fees and housing", *BBC News*, 1 October 2017

- reducing the interest charged on student loans while students are studying
- capping the overall amount of repayments on student loans to 1.2 times their loan
- reducing the income threshold for student loan repayments from £25,000 to £23,000
- reintroducing maintenance grants of £3,000 for disadvantaged students

The proposals are expected to cost an additional £0.3-0.6 billion in annual ongoing annual costs. The changes to student finance and funding are expected to reduce costs when taken on their own. They shift the balance of taxpayer funding from loan write offs to more direct funding for teaching and maintenance. The Government has not yet responded to these proposals with its own review of post-18 education and funding. This is expected to be published alongside the spending review in autumn 2020.

The Library's briefing paper *The Post-18 Education Review (the Augar Review) recommendations* give more detail.

On 21 January 2021 the Government published its 'interim conclusions' to its review of post-18 education and funding. Much of this dealt with reforms to technical education and skills. On HE finance it announced that the maximum tuition fee cap would be frozen for another year in 2021/22 at £9,250 and added that "…further changes to the student finance system will be considered ahead of the next Comprehensive Spending Review." At the autumn 2021 spending review the Government said its response to the Augar report would be published "…in the coming weeks" alongside details of the higher education settlement up to 2024-25.[16]

The Commons Library Student Finance Explained series of articles aims to help people better understand what is a complex system, ahead of the Government's final conclusions on its review. The first two articles in this series give an introduction to the system and the current financial flows. The rest look at the impact of different hypothetical changes to loan repayment terms, fee levels and grants.

16 Autumn Budget and Spending Review 2021, HM Treasury (para 4.16)

2 Public spending on higher education in England

Until recently there were three main elements of public spending on higher education –direct funding through the Higher Education Funding Council for England (HEFCE) which covers both teaching and research, student maintenance grants and student loans. With grants abolished for new students from 2016 there are now only to main elements, direct funding and loans.

HEFCE closed in March 2018 and its role in funding teaching was taken over by the Office for Students and funding research by Research England

2.1 Direct funding through the funding council

The Secretary of State normally writes to the funding councils around the turn of each year to set out funding, priorities, student numbers and related matters for the following financial year. Occasionally these letters cover more than one year and sometimes revised versions are published. The most recent funding letters for the Office for Students and Research England were published in January 2021 and July 2020 respectively. These give teaching allocations up to 2021-22 and research up to 2020-21. Earlier funding letters can be found at: www.hefce.ac.uk/funding/annallocns/Archive/

The table below summarises this funding and estimated fee loans from the latest funding letters. More detail is given in the separate reference table for this paper.

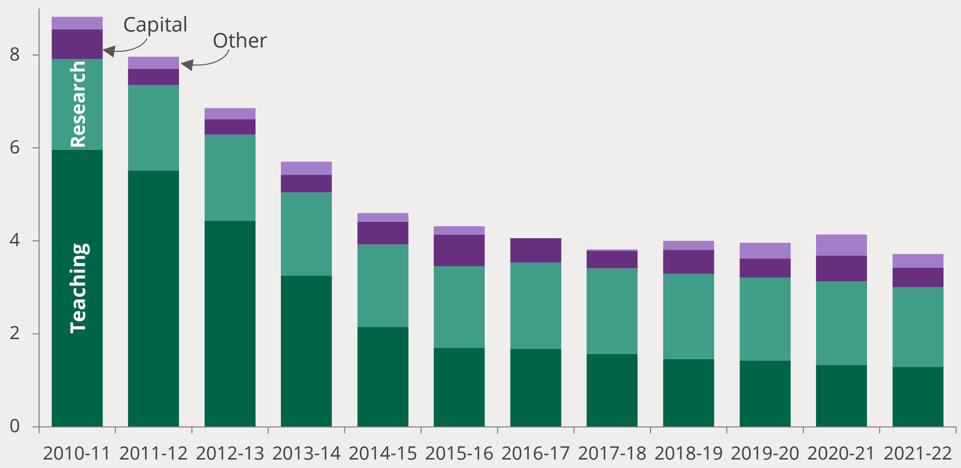
Funding for the HE sector in England
£ billion cash

	2011-12	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Recurrent grants								
Teaching	4.6	1.5	1.5	1.5	1.4	1.4	1.3	1.3
Research	1.5	1.6	1.7	1.7	1.7	1.7	1.8	1.8
Capital	0.3	0.6	0.5	0.4	0.5	0.4	0.6	0.4
Other	0.2	0.2	0.0	0.0	0.2	0.3	0.4	0.3
Total via funding councils	**6.7**	**3.9**	**3.7**	**3.6**	**3.8**	**3.8**	**4.1**	**3.8**
Estimated regulated fee	2.6	8.0	8.6	8.9	9.4	9.8	10.5	10.3
Funding council and fee income	**9.3**	**11.9**	**12.3**	**12.5**	**13.2**	**13.6**	**14.6**	**14.2**

Sources: See reference table

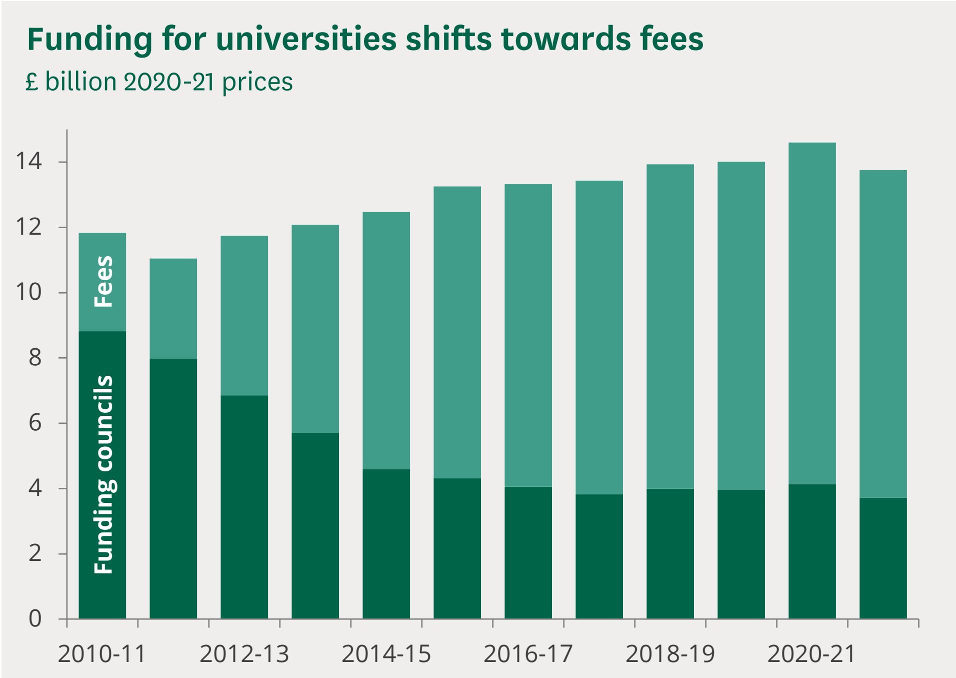
Changes to the main elements in real terms are illustrated in the following chart. Total levels of funding for HEFCE fell even before the 2012 reforms came in. Annual cuts in funding were in the £0.8-0.9 billion range from 2011-12 to 2015-16. After this, with almost all students on the new funding regime, cuts have been much smaller.

Funding council allocations: Teaching cut, research stable
£ billion 2020-21 prices



Sources: See reference table

The large increase in regulated fee income (from home and EU students) mean that the *total* funding for institutions through both sources increased in real terms in each year from 2011-12 to 2019-20. This, and the balance between the two sources, is shown below.



Sources: See reference table

Accounting for inflation in 2020-21 and 2021-22

The pandemic has caused unusual movements in the GDP deflator, which is used to measure inflation in the economy and produce the real terms figures in this paper. This means that for 2020 and 2021 the GDP deflator does not provide an accurate representation of price changes and any real-terms figures calculated from it will not provide a reliable indicator of the actual purchasing power of funding in these years.

This paper uses the **average** Office for Budget Responsibility GDP deflator growth forecast for the two years 2020-21 and 2021-22 to smooth the distortions caused by pandemic-related factors.

Teaching

The table above shows that direct recurrent funding for teaching fell by £830 million or 20% in real terms in 2012-13. This was the first year that included some students under the 2012 funding arrangements. This funding is in financial years, which precede academic years, so in effect it only includes the reduced funding for just over one half of one year of students under the new arrangements. Further cuts of around £950 million were made in 2013-14 and 2014-15 and £250 million in 2015-16.

The initial 2015-16 total was 66% below the below the 2011-12 level in real terms. The subsequent cuts (revised figures) meant it was around 69% below the 2011-12 total. In 2015-16 almost all full-time undergraduates came under the post-2012 funding arrangements. This means that later cuts in funding for teaching have been more modest. Spending Review 2015 announced that the teaching grant would be cut by £120 million in cash terms by 2019-20, but within this reduced total funding for high cost subjects would be protected in real terms. The student opportunity fund, which supports institutions in their efforts to widen access, would be cut by "…up to half."[17]

The 2020-21 indicative total was 76% below the 2011-12 figure in real terms. The impact on what the funding councils planned to distribute up to *academic year* 2020/21 is given later in this paper.

2021-22 allocation

The Government published its funding letter to the Office for Students (OfS) on 21 January 2021. This kept teaching funding totals for financial year 2021-22 at virtually the same cash values as in 2020-21; £1.33 billion for recurrent and £0.15 billion for capital spending.

The letter also instructed the OfS to make a number of changes to how this funding is allocated in academic year 2021/22. These included changing high-cost subject funding and removing London weighting.

The change to high-cost subjects is to prioritise:

> …high-cost, high-value subjects that support the NHS and wider healthcare policy, high-cost STEM subjects and/or specific labour market needs.

These subjects include, medicine, dentistry, nursing, some subjects allied to medicine, science, engineering and IT. Non-priority high-cost subjects will see a 50% cut in their funding in 2021/22.

The Government has scrapped London weighting from 2021/22; costing London universities an estimated £64 million

On London weighting the letter said:

> While London providers face some higher costs, these reflect the overall weighting of the UK economy towards London and it is not clear they can be justified when excellent HE provision can be delivered across the country. The levelling-up agenda is key to this government, and we think it is inconsistent with this to invest additional money in London providers, the only such regional weighting that exists in the grant.

Removing London weighting cuts funding to these institutions by £64 million in academic year 2021/22. Modelled funding for 2021/22 suggests that London institutions would see a cut of around 14% in their teaching grant (after all changes are implemented) compared with increases of 6-7% for most other

17 *Department for Business, Innovation and Skills' settlement at the Spending Review 2015*, 25 November 2015

regions. London weighting applied to teaching grant for high cost courses, the nursing, midwifery and allied health supplement and to student premium funding which supports disadvantaged and underrepresented students and includes the disabled students premium. London weighting still exists in many other areas of public funding including for schools and further education institutions.

The letter also included an additional £5 million for student hardship, £15 million for student mental health, a £10 million increase for specialist providers, a £20 million cut in funding for Uni Connect and announced that capital funding would move from a formula allocation to a bidding process.

Research

The 2012 changes in university funding directly affect teaching rather than research. Plans were set out for each year to 2014-15 soon after the 2010 CSR was published. The earlier table shows that recurrent funding for research broadly maintained its cash value up to 2014-15. The 2013 Spending Round kept the total resource (recurrent) science budget for 2015-16, which includes funding for Research Councils and other areas, at the same cash level as earlier years. Total capital funding for science was increased, partially reversing earlier cuts.[18]

Spending Review 2015 announced that total science funding, which includes HEFCE research grant and funding paid through the Research Councils, will be protected in real terms to the end of the (then) current Parliament.[19] The table and chart and the previous page show that research funding has been broadly maintained in real terms since 2010. The 2020-21 recurrent grant allocation for research is lower than previous years, but increases in specific research funding mean the total current funding for research maintains its real value. The 2021-22 recurrent grant allocation was slightly lower than in 2020-21 and there were also small in other elements of recurrent funding and in capital funding.

Research funding paid to higher education institutions through HEFCE and now Research England funds the research capacity and infrastructure –such as the salaries of permanent academic staff, premises, libraries etc- while the Research Councils fund specific research projects.

Other

The 2014-15 letter incorporated the cut to the National Scholarship Programme announced in the Spending Round 2013, ended separate funding for the Access to Learning Fund (which provided hardship payments),

18 Spending Round 2013, HM Treasury

19 *Department for Business, Innovation and Skills' settlement at the Spending Review 2015*, 25 November 2015

directed HEFCE to combine this with its student opportunity funding[20] for institutions and also included the implications of the Autumn Statement 2013 for funding through HEFCE. The 2015-16 letter confirmed earlier allocations. The 'other' line in 2018-19 and later includes additional funding for research linked to specific objectives rather than general research funding grant.

2.2 Student loans

1 Changes to student loan accounting rules

In December 2018 the Office for National Statistics (ONS) announced that it would change the way that loans are included in public spending figures. In summary this means treating the amount which is expected to be repaid as a *loan.* The remainder will be reclassified as *public spending* and count towards the deficit. [21]

In June 2019 the ONS published Student loans in the public sector finances: a methodological guide which gave a detailed account of the reasons behind the change and how they planned to implement it. The new method is known as the 'partitioned loan transfer approach'. This guide was updated in January 2020.

The August 2019 Public sector finances release was the first to include the revised student loan expenditure figures and their impact on borrowing. Further revisions were made in the September 2019 release. In 1999-00 the new treatment of loans increased UK public sector borrowing by 0.1 billion, rising to £10.6 billion in 2020-21.[22]

The 'grant equivalent element of student lending' is included as part of Departmental budgets under 'depreciation'. While the economic costs of loans are now included in aggregate public sector borrowing figures, it is still excluded from the Government's main measure of public spending -public expenditure on services- as depreciation does not scores as spending in the National Accounts.

This change has no direct effect on the loan figures included in this paper under the sections on the subsidy element of loans and overall public spending. These already include the share of 'English' loans which the Government expects will not be repaid as public spending as this is the true long term costs of loans. They are the author's own calculation.

There are two types of student loans –fees and maintenance. Full-time home and EU students on qualifying courses can take out a loan to cover the tuition fees for their course. From 2012 new part-time students on courses with an intensity of 25% or greater became eligible for loans. Maintenance loans for part-time students will be introduced in 2018/19. Master's loans for

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20 The student opportunity stream is meant to support institutions' efforts to widen participation and allow then to meet the higher costs of supporting disadvantaged and under-represented students through their courses

21 *New treatment of student loans in the public sector finances and national accounts*, ONS

22 Figures from 2019-20 from the OBR's Economic and fiscal outlook – October 2021

postgraduates of up to £10,000 were introduced in 2016/17 and Doctoral loans in 2018/19. These loans are intended to contribute towards fees and living costs.

Maintenance loans are available to home students only. The amount someone can take out as a maintenance loan depends on their household income, where they live and where they study. Maintenance loans entirely replaced by grants for new students from 2016/17. The value of student maintenance support gives more details and Student loan statistics gives more background about the system.

The Government has forecast that the total value of new loans to higher education students in England will increase from £15.0 billion in 2017-18 to £18.0 billion in 2020-21 and £21.6 billion in 2024-25. This increase is driven by replacing grants with loans and increases in underlying student numbers but also by the expansion of loans to cover maintenance for part-time students, fee loans for master's and doctoral courses and replacing nursing bursaries with loans.

Subsidy elements of loans and loan accounting

The earlier table gave government estimates of the face value of fee loans to English students and EU students studying at English institutions. There are different treatments of the costs associated with loans in different parts of the Government's accounts. The subsidy element of loans made in any one year - the present value of the amount not expected to be repaid- can be viewed as the 'true' economic cost of loans in the longer term. The Department for Education includes an estimate of this in its accounts. It is what they expect the subsidy element to be and is viewed as the permanent costs of the loan to the taxpayer.

This system is known as resource accounting and budgeting (RAB) or accruals accounting and has been in place in the public sector for more than a decade. The subsidy element is calculated as the face value of loans made in any one year less the discounted or present value of future repayments. This can be thought of as the amount of money lent to students that the Government does not expect to get back. It is frequently expressed as a proportion of the value of loans, the so-called RAB charge.

The reclassification of loan outlays into loan (expected to be repaid) and public spending (not expected to be repaid) follows this approach. The data from the reclassification (revisions to deficit) are not included in this briefing paper as they apply to the UK as a whole. There is no reason to suspect that data for England on this new method, when published, will be much different from the estimates included in this paper.

[23] Student loan forecasts, England: 2019 to 2020, DfE

Earlier recording of loans in the deficit and national debt

Until the recent reclassification spending on student loans (cash outlays) was classed as a financial transaction and not included in the Government's main measure of public spending on services. It therefore did not count towards the fiscal *deficit*[24]. Similarly, loan repayments had no impact on this fiscal aggregate either. Under this measure only loan interest and write-offs were counted. The interested added to the outstanding debt on loans counted as income and write-offs as expenditure.

The impact of student loans in the *national debt*[25] was, broadly speaking, the opposite of that on the deficit. Loan outlays increase the debt by their face value, loan repayments reduce the debt also by their face value. Interest and write-offs had no impact. This had not been changed by the recent reclassification

Loans therefore were treated very differently in the fiscal deficit and national debt. The difference was really one of timing with the costs being recorded upfront in the debt and only after they are written off (after 30 years for most) in the deficit. Overall costs for a cohort of loans would eventually be the same under each method. In July 2018 the Office for Budget Responsibility published a paper that looked at the 'fiscal illusions' resulting from the different accounting treatment of loans in government accounts and made suggestions for alternative approaches.[26]

Estimates of the resource costs of loans from 2012

Pre-2015 reforms

The Government made estimates of the percentage RAB rate on new loans from 2012 when it published proposals for changes to funding. These are discussed in some detail in Changes to higher education funding and student support in England from 2012/13. The estimated RAB rate on new loans was put at 'around 30%', but subsequently increased to 'around 35%' [27] then to 35%-40%[28], revised upwards again to 'around 40%'[29] and later to '**around 45%**'.[30] These increases were largely due to changes in economic forecasts, particularly on earnings.[31] These less optimistic forecast reduce the expected cash value of repayments and or delay when they will be made. Other factors behind the increase in the RAB rate include the higher than expected level of

24 Public Sector Net Borrowing
25 Public Sector Net Debt
26 Working paper No.12 Student loans and fiscal illusions, OBR July 2018
27 HC Deb 4 July 2013 c775-6W
28 HC Deb 9 December 2013 c5W
29 HC Deb 19 December 2013 c780W
30 HC Deb 20 March 2014 c706W
31 The OBR links lower earnings growth to "…much weaker-than-expected growth in productivity." They also note that the data now used for modelling repayments, including that from the Student Loans Company, have widened the modelled distribution of earnings among graduates. This wider distribution cuts expected repayments, even if average earnings remain unchanged. Fiscal Sustainability Report – July 2014, OBR

average tuition fee loans, a change to the timing of repayment threshold uprating, lower assumed repayments from the extra students who start higher education because the numbers cap is lifted[32] and improvements to the Governments loan repayment model which is used to forecast repayments and hence calculate the resource costs of loans.[33] Much more detail on these increases are given in the paper HE in England from 2012: Funding and finance

Post 2015 reforms

The different elements of the changes to student finance announced in the Summer Budget all have an impact on student loan outlays and the RAB rate/charge. Replacing maintenance grants with loans will increase the cash amount loaned. This on its own would increase the RAB rate, but as the increase will be largely for those from lower income backgrounds –which is linked to some extent to lifetime earnings- the increase will be larger still as a smaller amount is expected to be repaid.

Freezing the repayment threshold will increase repayments and hence cut the RAB rate. Allowing some institutions to charge above £9,000 will increase tuition fee loan amounts and increase the RAB rate slightly.

Reviewing the discount rate applied to loans is meant to bring this in line with the Government’s long-term cost of borrowing. It has no impact on loan outlays or the cash value of repayments and hence no impact on *borrowers*. It is an accounting change that has a large impact on the *RAB rate*, cutting it substantially.

The Government’s estimates of the savings from freezing the repayment threshold from 2016 were set out earlier; £3.2 billion additional repayments from existing borrowers plus £0.9 billion for each £15 billion of loans to new students. It did not include any estimate of the combined savings from the Summer 2015 ‘package’ in Spending Review 2015, but a subsequent written answer estimated that the RAB charge would be reduced to **20-25%**.[34]

Post October 2017 announcement

The Government has estimated that the changes to the loan repayment thresholds will increase the RAB charge rate from “…around 30%”, ie. somewhat higher than their earlier estimates, “…to between 40% and 45%”.[35] This latest range, **40-45%** is broadly equivalent to the estimate from before the 2015 reforms despite the cut in the discount rate used to calculate this figure.[36]

32 HC Deb 10 December 2013 c130W

33 These are summarised in the National Audit Office report Student loan repayments

34 PQ HL 5098 [on Mature students: Loans] 18 January 2016

35 PQ 116250 [On Students: Loans] 1 December 2017

36 In other words the actual expected cash flows are fiscally ‘worse’ under the latest arrangements, but the lower discount rate counteracts this in accounting terms

June 2018 estimates

The Department for Education published new estimates of the RAB charge alongside various forecasts connected with loans in Student loan forecasts, England: 2017 to 2018. These gave different estimates for different types of loan made in financial year 2017-18:

- Full-time: 45%
- Part-time: 40%
- Master's 0%

The estimates for full-time and part-time students under are in line with the earlier 40-45% range. Because the total value of loans to full-time students is so much larger a weighted average of the two is 44.9%. Master's loans are made under different terms[37] and this, alongside the smaller total value of loans and expected higher earnings, means that the RAB charge is much lower. In fact the calculated rate from the model and standard discount rate is -6%, but under Government accounting rules RAB charges "…cannot be negative".[38]

June 2019 estimates

Updates to loan forecasts and RAB charges were published in Student loan forecasts, England: 2018 to 2019. These gave forecasts for individual (future) years for the first time. The 2018-19 rate for full-time students increased (from 45%) to 47%, although this is expected to fall after 2019-20 to 44% in 2023-24. The part-time rate for 2018-19 was also higher than previous estimates at 41%. This is expected to increase to 46% in 2023-24.

September 2020 estimates

Updated forecasts[39] of the RAB charge for full-time undergraduate students show a jump to 53% in 2019-20 and 54% in 2020-21. Unlike the 2019 publication no future years or steady state estimates are made. The estimate for part-time students increases to 45% in 2019-20 and 47% in 2020-21. Lower earnings assumptions, and hence, repayments are the main reason for these higher RAB charges. The Department for Education said:

> Though this is not the only driver, the use of OBR Central Covid scenario projections for RPI, bank rate and earnings growth increases the RAB charge for all plan types in comparison to forecasts as of June 2019. Updates and improvements to the forecast models are responsible for the largest changes in forecasts relative to those published for 2018-19.

Earlier estimates for 2018-19 loans were not revised. However, the estimated stock charge for loans in 2019-20 is 52% compared to the 2019-20 estimated

[37] Plan 3 repayment system. Borrowers repay 6% of any income above the threshold (currently £21,000). Interest is RPI+ 3%. Repayments are made alongside (in addition to) any undergraduate or Plan 2 loans.

[38] Student loan forecasts, England: 2017 to 2018, DfE (Table 4)

[39] Student loan forecasts, England: 2019 to 2020, DfE

published in 2019 of 47%. The stock charge is the proportion of the entire stock of loans (in present values) that the Government estimates will not be repaid. This highlights that changes to earnings assumptions and modelling affects earlier loans, not just those made in 2019-20 or 2020-21.

The latest loan forecasts also gave rates for the 'transfer proportion'. Under the ONS's partitioned loan transfer approach the transfer proportion is the fraction of the loan outlays identified as government spending when the loan is made. The values differ from the RAB charge because repayments are discounted is a different way.[40] The forecast transfer proportion in 2020-21 is 58% for full-time higher education loans, 46% for part-time and 17% for Master's loans.

June 2021 estimates

Government estimates of the subsidy value of loans have varied greatly due to changes in modelling and policy. The latest are 53% of the face value of loans

The most recent forecasts[41] make little change to the earlier estimates of the RAB charge. This is estimated at 53% for full-time Plan 2 loans in 2020-21, reducing to 51% by 2025-26. The RAB charge for part-time Plan 2 loans is 46% in 2020-21, this also falls slightly over time to 44% in 2025-26. The stock charge for Plan 2 full-time loans is kept at 52% in 2020-21.

The forecast transfer proportions in 2020-21 are slightly lower than previous estimates at 57% for full-time undergraduates, 45% for part-time undergraduates and 15% for Master's loans.

Department for Education Accounts 2019-20

The DfE accounts for 2019-20 were published on 6 November 2020 and gave a detailed account of the changes to the valuation of the stock of student loans. These said that **adopting the OBR's central estimate of Covid-19 on the economy has reduced the fair (economic) valuation of the stock of loans by £2.5 billion as of 1 April 2020**. The repayment model is affected by the revised assumptions about earnings growth, inflation and interest rates, but not graduate unemployment which is not yet included in the model. There remains considerable uncertainty about the impact of the pandemic on the economy and hence on student loan repayments.

Impact of loans on the national debt

Office of Budget Responsibility projections of the impact of all (UK) loans on the national debt are illustrated in the chart below. These were made in Summer 2018. The (cumulative) addition to debt increases rapidly from 5.5% of GDP to a peak of 12.1% in the early 2040s before falling back towards 11%

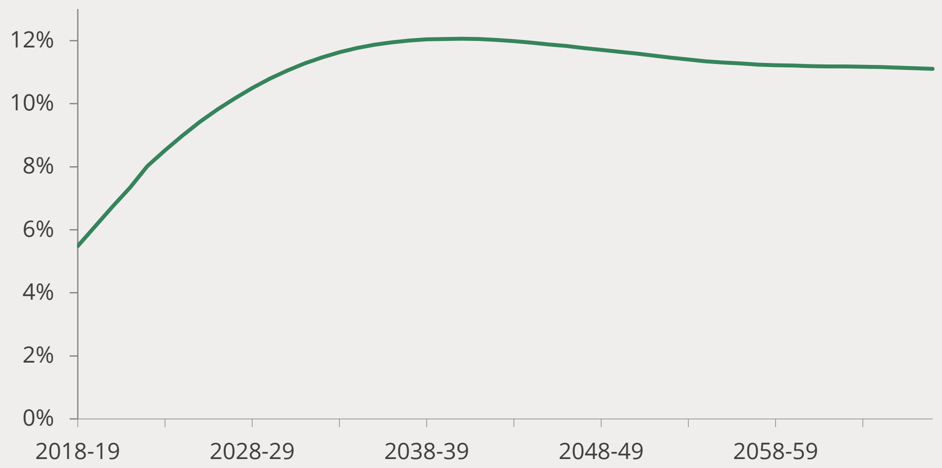
40 "The RAB cost values future repayments by taking into account the effect of inflation and the estimated cost of government borrowing over time, whereas under the ONS partitioned loan-transfer model, future repayments are valued by taking into account the interest rates charged on student loans. Therefore, where a borrower's interest rate is higher than the combined impact of inflation and government borrowing, the repayments are discounted by a higher value under the partitioned loan-transfer model so the partitioning capital transfer will be higher than the RAB cost"

41 Student loan forecasts for England 2020-21, DfE

from the late 2050s. 10% in the 2050s. Additions to national debt are net lending (loan outlays minus repayments) plus accrued interest and write offs.

Student loans to add 12% to national debt in early 2040s

Additions to net debt from student loans, UK, % of GDP



Source: Fiscal sustainability report – July 2018, OBR

Loan repayment models

Government estimates of the RAB cost of student loans are calculated using a student loan repayment model. This makes long term forecasts of repayments for individual borrowers and is highly complex. There is a substantial amount of uncertainty about future repayment levels which are connected in large part to earnings growth forecasts. The paper HE in England from 2012: Funding and finance looks in depth at changes/improvements to the loan model over time.

Student loan forecasts for England gives an idea of the sensitivity of the model to assumptions about inflation and earnings. If RPI were one percentage point *higher* (or lower) than forecast then the RAB charge on loans made to full-time students after 2012 would five percentage points *higher* (or lower) than the model suggests. Similarly if earnings growth were one percentage point *higher* than forecast then the RAB charge would be five percentage points *lower* (and *vice versa)*.

A simplified version of the model used to produce estimates for their accounts was made public to inform debate around the changes to funding in 2012. An updated version of the publicly available model was made available in

January 2014. This model was revised and updated in June 2014 and in July 2015.

The Institute for Fiscal Studies published its Student finance calculator in September 2021. This allows users to change different parameters of the student finance system and see the impact on overall public finances, graduate repayments, different income groups and the different impact on men and women.

2.3 Student support

Summer budget 2015 announced that for new students from 2016/17 loans would entirely replace grants and the total maintenance support available would be increased for students from lower and middle income households

Spending on student maintenance grants[42] was just under £1.3 billion in academic year 2010/11 and increased in cash terms in each subsequent year to just over £1.6 billion in 2015/16.[43] It overtook funding for teaching and for research (both via HEFCE) as the most important single source of direct[44] public expenditure on higher education in 2015/16. With research funding protected and support for teaching reduced to high cost and priority subjects this was the one remaining area where substantial savings to direct public expenditure could be made.

In his Summer Budget 2015 Chancellor George Osborne announced that maintenance grants would end for new students from 2016/17 and be replaced by loans. The Government estimated that abolishing grants and replacing them with loans for new students from 2016 could save £2.5 billion (cumulatively) by 2020-21.[45] The amount awarded in academic year 2016/17 was £1.05 billion; a drop of almost £0.6 billion or 36%. Spending has fallen in each subsequent year to a provisional total for 2019/20 of £36 million.[46]

2.4 Overall public spending

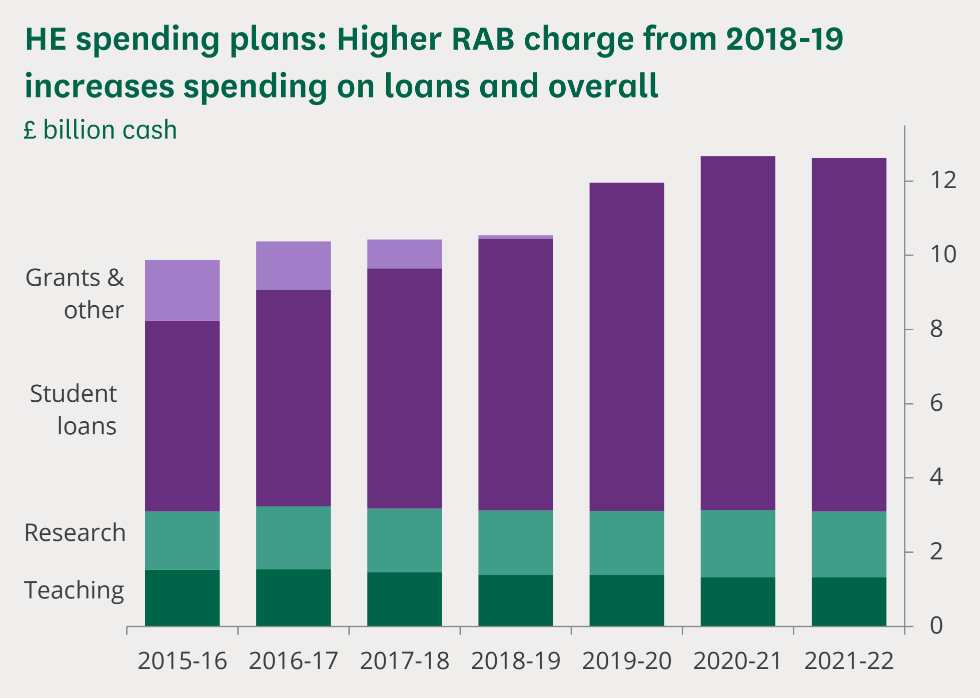
Overall spending levels (including the subsidy element of loans) up to 2015-16 are given in HE in England from 2012: Funding and finance.

The shift in expenditure away from direct funding from 2010 to 2016 was marked. Overall spending changed little in cash terms as higher loan subsidy amounts outweighed cuts in funding for teaching.

42 Includes special support grants
43 *Student support for higher education in England 2016*, SLC. (Table 2)
44 Excludes loan funding which is indirect.
45 Summer Budget 2015, HM Treasury
46 Student Loans Company, Student Support for Higher Education in England 2020 (Table 2)

Up to 2021-22

Estimated overall spending levels up to 2021-22 are given below. They include the subsidy element or economic cost of loans. For this chart an estimated RAB charge of 45% has been applied to loans up to 2017-18, then the higher rates (detailed earlier) for 2018-19 to 2021-22.[47]. In reality it is likely that this exaggerates the increase in loan spending in the final two years especially. But without any published revisions to the earlier RAB charges this is unavoidable. Cuts in maintenance grants have been projected forward and converted to financial year figures. The funding council data is that shown in the earlier table.



Sources: See reference table and House of Commons Library estimates

The main pattern over these years is the shift from (maintenance) grants to loans. The chart gives cash values. The **real value** of estimated total public spending varied little over the period to 2018-19 at just under £11 billion a year in 2020-21 prices. The higher RAB charges in the final three years increases this to £12.3 billion in 2019-20 and £12.7 billion in 2020-21 before falling to £12.3 billion in 2021-22. After 2021-22 we would expect little change in the real value of these figures without any major changes to policy, RAB charge estimates or in student numbers.

[47] Plan 2 loans for full-time and part-time HE students only.

3 Funding for institutions from the funding councils

Links to details of final allocations from the funding council to individual institutions are given below:

- 2012/13
- 2013/14
- 2014/15
- 2015/16
- 2016/17
- 2017/18

2018/19, 2019/20 and 2020/21 allocations from the two new funding bodies can be found at:

- Office for Students
- Research England

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