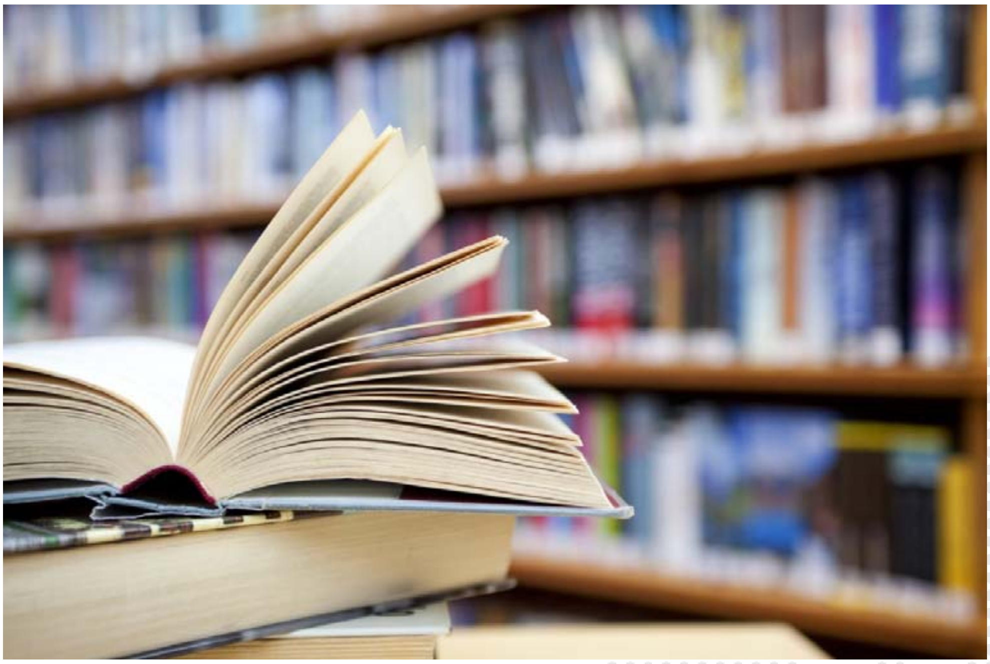
The Higher Education fees and funding reforms in England

What is the value of the RAB charge on student loans for the Treasury to break-even?



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About London Economics

London Economics is one of Europe's leading specialist economics and policy consultancies and has its head office in London. We also have offices in Brussels, Dublin, Cardiff and Budapest, and associated offices in Paris and Valletta.

We advise clients in both the public and private sectors on economic and financial analysis, policy development and evaluation, business strategy, and regulatory and competition policy. Our consultants are highly-qualified economists with experience in applying a wide variety of analytical techniques to assist our work, including cost-benefit analysis, multi-criteria analysis, policy simulation, scenario building, statistical analysis and mathematical modelling. We are also experienced in using a wide range of data collection techniques including literature reviews, survey questionnaires, interviews and focus groups.

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Summary

The higher education funding system in England has changed radically. Following the May 2010 General Election and the formation of a Coalition Government which pledged to eliminate the structural deficit by 2014/15, a number of changes to the higher education funding regime were proposed and voted through Parliament in December 2010. These reforms were implemented for the 2012/13 cohort of undergraduate students. The most significant changes to higher education funding at undergraduate level included:

- The removal of teaching funding provided by the Higher Education Funding Council for England (HEFCE) relating to predominantly classroom taught subjects;
- An increase in the maximum tuition fee that higher education institutions are able to charge to £9,000 per annum for full-time undergraduates, subject to agreement with the Office for Fair Access;
- An increase in the scale of tuition fee loans available to cover increased undergraduate tuition fees;
- An increase in the maintenance loans and grants available to eligible full-time undergraduates;
- The introduction of tuition fee loans for eligible part-time undergraduates;
- The introduction of higher tuition fee loans for individuals studying at private institutions;
- Amendments of tuition fee and maintenance loan conditions to incorporate
  - A positive and variable real interest rate on outstanding loans (dependent on earnings);
  - An extension of the repayment period before debt write off;
  - An increase in the nominal earnings threshold before loan repayment commences; and
- The introduction of the National Scholarship Programme with matched funding from the higher education sector[1]

In previous work undertaken on behalf of million+[2], London Economics modelled the changes in HE fees and funding between the 2010/11 system and compared this to what might have been expected to occur under the substantially changed arrangements in 2012/13. This is presented in the first two columns of Table 1. Estimates of Treasury costs have also been broken down by expenditure item[3]. The table illustrates the headline savings to the Treasury that were previously estimated. The analysis demonstrated the following:

- *The contribution from the Treasury associated with the smaller 2012/13 cohort is expected to be* ***£5.781 billion*** *compared to a contribution of* ***£6.947 billion*** *associated with the larger 2010/11 cohort. This represents a reduction of* ***£1.166 billion*** *in Treasury expenditure, which is driven primarily by the shift away from the provision of HEFCE teaching grants towards increased loan-supported tuition fees.*
- *The primary saving or reduction in expenditure achieved by the Treasury results from the* ***£3.871 billion*** *reduction of HEFCE teaching funding between the 2010/11 and 2012/13 cohorts of students, and*
- *The write offs on full-time student fee and maintenance loans will cost approximately* ***£2.418 billion*** *(per annum) more for the 2012/13 cohort compared to the 2010/11 cohort (an increase from* ***£1.678 billion*** *in 2010/11 to* ***£4.096 billion*** *in 2012/13). The biggest item of expenditure for the Treasury associated with the funding of higher education is the maintenance and fee loan subsidy/write-off (the* ***RAB charge***[4]*).*

[1] Note that HEFCE have announced a revised approach to the distribution of National Scholarship Programme funds in 2014-15. See http://www.hefce.ac.uk/media/hefce/content/pubs/2013/201302/HEFCE%202013-02.pdf

[2] Million+ (2013), Behind the Headlines: Are the changes to HE funding in England cost-effective? (here)

[3] Note that Exchequer expenditure under the 2012-13 system underestimates actual Exchequer expenditure, as there has been a significant increase in the number of students receiving student loans and grants who are enrolled with private sector providers. Currently, it is not possible to model the Exchequer resource implications as many of these students are undertaking sub-degree qualifications, which are shorter in length than full degrees, but are also associated with different lifetime earnings profiles compared to graduates (and this might be expected to have a significantly higher RAB charge).

[4] **Resource and Accounting Budget charge (RAB charge)** The size of the Treasury maintenance and fee loan subsidy is measured by the **Resource Accounting and Budgeting** charge (RAB), which calculates the proportion of the nominal loan value that would not be expected to be repaid (in present value terms). Under the current student support regime, non-repayment occurs as a result of the interest subsidy; low earnings; debt forgiveness after 30 years; or in the case of permanent disability; or death. Based on graduate

Table 1: Exchequer Expenditure – (net present value over 30 year period)			
	2010-11	2012-13 (current)	2012-13 (breakeven)
FT Student Maintenance grants	(£1,027m)	(£1,259m)	(£1,259m)
FT RAB Maintenance loan cost	(£870m)	(£1,298m)	(£1,604m)
FT RAB Fee loan cost	(£808m)	(£2,798m)	(£3,461m)
PT RAB cost		£33m	(£10m)
PT Fee Grant	(£31m)		
PT Course Grant	(£24m)		
National Scholarship Fund		(£47m)	(£47m)
Total Student Support	**(£2,760m)**	**(£5,369m)**	**(£6,381m)**
FT HEFCE grant	(£3,849m)	(£292m)	(£292m)
PT HEFCE grant	(£335m)	(£22m)	(£22m)
Total HEFCE funding	**(£4,185m)**	**(£314m)**	**(£314m)**
FT RAB cost for private students		(£71m)	(£192m)
FT Maintenance grants for private students		(£28m)	(£60m)
Total Treasury Funding	**(£6,947m)**	**(£5,781m)**	**(£6,947m)**
Treasury saving compared to 2010/11		**£1,166m**	**£0**
FT RAB charge (% of loan value)	26.1%	**39.6%**	**48.6%**
PT RAB charge (% of loan value)		-7.5%	2.6%

London Economics (2013). The original analysis (presented under '2012-13') is based on 299,640 FT and 47,243 PT first time undergraduates attending public institutions, and 6,000 students attending privately funded institutions (equivalent to 18,000 student 'years'). However, given the dramatic increase in the numbers of student attending private institutions, in the "2012-13 (breakeven)" column, we have increased the number of students attending private institutions to 13,000 (equivalent to 39,000 student years).

What is the value of the RAB charge for the Treasury to break-even compared to the 2010-11 funding system?

In this analysis, the term "**break-even**" refers to the point at which the estimated costs to the Treasury of the 2012-13 higher education reforms have the same long run economic cost as the system that operated in 2010-11 (i.e. **£6,947** million per cohort). Given recent reports that the RAB charge has been underestimated by the Government (and the several revisions to date[5]), we estimated the RAB charge that would result in a break-even position for the Treasury compared to the previous (2010/11) system.

The analysis indicates that the Treasury would break-even with a RAB charge of **48.6%**; however, if the estimated RAB charge (i.e. if the proportion of the fee and maintenance loans never recovered) increases beyond **48.6%**, the economic cost of the 2012-13 higher education reforms will exceed the 2010-11 system that it replaced.

earnings profiles (from the Labour Force Surveys) and the administrative information relating to the criteria for repayment of loans, our estimates of the RAB Charge stand at approximately 39.6%, which implies that for every £1,000 in loans that are provided by the government, approximately £604 would be expected to be repaid (in present value terms) with the remaining £396 being 'lost' to the Treasury as a result of write-offs and subsidies.

[5] For estimates of the RAB charge (in brackets), see BIS Regulatory Impact Assessment (June 2011 (28-32%) here), Times Higher Education (May 2013 (35%) here), Hansard (09 December 2013 (35-40%) here), and Hansard (19 December 2013 (40%) here).

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