PRIME MINISTER ② AT 21/6

21 June 1985

REVIEW OF STUDENT SUPPORT

Keith Joseph is holding a series of meetings with the Chancellor and other relevant Ministers, to develop an agreed consultative paper on student support. The present draft paper will be discussed at a further meeting in the Treasury next week, and may then be changed again.

There is no need for you to intervene at this stage. But you may wish to note the progress made so far.

Like earlier drafts, the paper:

1. describes the difficulties of the present system - £500 million cost, parental contribution, students getting DHSS benefits as well as grants, etc.

2. lays down the principle that both students themselves and the taxpayer should help to pay for higher education, since both student and society at large benefit;

3. identifies options for reform other than the introduction of loans - eg better administration of parental contributions, different arrangements for support of students on long courses, a system of scholarships and bursaries, a 'higher education tax', etc.

The loans section of the paper is now considerably altered. Under pressure from the Chancellor, the basic suggestion is that students should be given:

- an interest-free loan to replace the grant;

- with the debt revalued to allow for inflation;

- but with a maximum revaluation of 5% pa;

- and with students protected in two ways: (1) no repayments until two years after the course ends, (2) no repayment in any year when the student's income is les than 85% of the average wage, (at present this would be 85% of about £9,000 = c.£7,500).

Option 6 of the Annex

The figures have changed slightly in the latest draft.

With these arrangements, the parental contribution could be reduced by 5% a year, beginning six years after the introduction of loans, and still yield substantial savings in the middle to long-term, with no risk of increased costs in the early years.

Graduates, whose average earnings over a lifetime are now about £13,000 pa would be faced with a total bill of about £30 per month in real terms for 15 years, starting two years after the end of their course; those who had incomes below about £7,500 pa would pay nothing.

Next Steps

Keith will undoubtedly report to you at the end of next week. You may then want to hold a meeting, since both the timing and the substance of the consultative paper are politically delicate.

We recommend that you should wait for the report before taking any action.

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FROM THE SECRETARY OF STATE

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
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CONFIDENTIAL

20 June 1985

Dear Nigel

REVIEW OF STUDENT SUPPORT

Following our meeting on 13 June, I enclose a further draft of the consultative paper. It has been reduced in length by about one quarter, and takes account of the views of colleagues expressed at the meeting.

The section on loans has been recast, and your proposal for an interest-free loan scheme with repayments indexed has been given prominence. This option, together with variants on it, have been costed and are exemplified in Annex B to the paper. The variants incorporate suggestions for mitigating the repayment burden on students from lower income families, and also for reducing and (in one variant) abolishing the parental contribution. We shall need to decide which of the options is to be displayed in the consultative paper, and whether the Government should indicate a preference.

George Younger has emphasised the need to take account of the impact of a loan scheme on students taking longer courses, in particular in Scotland. His officials have suggested a way to deal with this, which is described in paragraph 26 of the draft paper. I doubt, however, whether the expenditure implications of this approach, which could reduce the eventual savings accruing from a loan scheme on the lines you propose by some £30-40M, would be acceptable. An alternative approach would be to build in softer repayment terms for students on longer courses. If we are not to embark on a full loan scheme, the problem might be resolved by adopting the proposal aired in paragraph 13 of the draft paper, namely, to limit grant support to a fixed period of years, and leave it to students on longer courses to look for additional support from elsewhere.

CONFIDENTIAL

I am copying this letter to those who attended the meeting (George Younger, Nick Edwards, Douglas Hurd, Peter Rees, David Young, John Wakeham, Peter Morrison and Tony Newton) and also for information to the Prime Minister, Quintin Hailsham, Patrick Jenkin, Norman Fowler, Tom King and Norman Tebbit.

Yours,

Keith

REVIEW OF STUDENT SUPPORT - CONSULTATIVE PAPER

INTRODUCTION

1. The Secretary of State for Education and Science announced on 5 December 1984 that the Government proposed to consider - and consult widely about - whether a radical change in the student support system, which might include loans, should be made so as better to meet the needs of students and their families whilst safeguarding the interests of the taxpayer. The terms of reference of the review are to examine financial support for students in higher education, concentrating on support at first degree and sub-degree levels.

SECTION I

THE EXISTING SYSTEM

2. The present arrangements for providing financial support for students undertaking higher education had their origins in the report of the Anderson Committee of 1960.(1) Its principal recommendations were implemented in 1962 following the enactment of legislation which still underpins the system of student awards today. The main principles which the Committee advocated were: equality of opportunity of access to higher education; freedom of choice of institution and course (subject to an offer of admission); and the availability of grants for the full period of any designated course. The Anderson Report prepared the way for the expansion of higher education recommended in a report by the Robbins Committee in 1963,(2) and the adoption of the principle that "courses of higher education should be available for all those who are qualified by ability and attainment to pursue them and who wish to do so".

3. These two reports set the scene for the massive expansion in the number of students entering higher education which accelerated in the 1960s and which has continued to the present time. A combination of demographic factors

(1) "Grants to Students", Cmnd 1051
(2) "Higher Education Report", Cmnd 2154

and increased opportunities to participate in higher education has led to a threefold increase in the number of award-holders between 1962 and 1983/84. There has also been a threefold increase in the real level of public expenditure on student maintenance grants in the last 20 years. There are now about 450,000 award-holders, and public expenditure on their maintenance is expected to total some £530M in 1985/6(3). This excludes additional payments to students or their families through social benefits (around £130M) and tax concessions accruing through deeds of covenant (about £70M). There is in addition a much larger subsidy still which is given through the provision of free tuition: at an average annual cost of tuition in the region of £3500 per student per annum, this is currently in excess of £1,500M a year. This massive expenditure on higher education is concentrated on only 1 person in 7 in the 18-21 age group in England and Wales (1 in 5 in Scotland).

4. The essential features of the present system (a detailed description of which is in Annex A) have remained unchanged since 1962, except that contributions from families to the payment of tuition fees ended in 1977. In particular, student support has been oriented almost exclusively towards a system of higher education which is based on full-time degree or degree equivalent study from the age of 18 (17 or 18 in Scotland). There has been some widening in the scope of courses which entitle students to an award, such as the extension to Higher National Diploma and DipHE courses in 1975. Nevertheless, there are many advanced courses which do not at present carry an automatic entitlement to awards. More emphasis is now being placed on continuing education and more flexible methods of study.(4) If these developments are to be encouraged further, the present awards system will need to be adapted.

5. The case for reform is highlighted by the social changes since the 1960s. As long ago as 1960 the majority of the Anderson Committee recommended the abolition of the parental contribution, but this was not accepted by the Government of the day. Since then the age of adult responsibility has been

(3) All figures are for GB, unless otherwise stated.
(4) See Sections 4 and 6 of the Green Paper, "The Development of Higher Education into the 1990s", Cmnd 9524

reduced from 21 to 18; and social and financial independence are now expected by young people at an earlier stage than in the past. In consequence the requirement in the present awards system that students should be financially dependent on their parents until the age of 25 is increasingly being criticised. Another criticism is that it does not place a legally enforceable requirement on parents to make their contributions, and the fact that some parents do not pay the assessed amounts has adverse consequences for their student children. Also, the present system enables some parents to exercise considerable skill in order to avoid their liabilities by reducing their assessable income to a minimum.

6. The escalating cost of awards has, however, made it difficult to contemplate radical changes to the awards system. For example, in England and Wales alone, extension of mandatory awards to all full-time students on advanced courses (including those students at present receiving discretionary awards) would cost about £70M; abolition of the parental contribution would cost an additional £280M; and reduction in the age of independence from 25 to 21 would cost £75M. Moreover, the public expenditure pressures in recent years have made it difficult to maintain the real value of the grant year by year.

7. There is also a need to rationalise the relationship between student awards and social benefits. Students are currently eligible to claim social benefits, particularly in the long vacations which the mandatory award is not designed to cover. Student claims for supplementary benefit and housing benefit have risen sharply since the 1960s and up to perhaps one half of all students are claiming housing benefit and supplementary benefit during part of the year. The Government believes that in the long term it is right in principle to remove students from the benefit system, and to make support available under the awards system for those in need throughout the year.

8. Our membership of the European Community and with it the impetus towards mobility between Member countries - and particularly the mobility of students - is another dimension which should be taken into account. As our existing student support arrangements are very different from those of most of our Community partners, there would be advantage in considering whether changes could be made which in the long run would make harmonisation easier.

9. For all these reasons, the time is ripe to examine from first principles the arrangements for supporting students entering higher education in the

light of higher education policy and recent developments, and taking account of what the country can afford.

SECTION II

UNDERLYING PRINCIPLES

10. Higher education may be regarded as an investment in the future, both for the individual student and for the community at large. The national life and the national economy stand to benefit from the contribution that suitably qualified students can make; indeed the Government believes that it is vital for our higher education system to contribute more effectively to the improvement of the performance of the economy.(4) This aim might be furthered by building into the awards system incentives for students to study subjects yielding particular benefit to the economy, such as science, engineering and technology. There is also scope for more sponsorship by employers. At the same time the individual also stands to benefit from higher education both in tangible ways - through the ability of most graduates to command higher than average earnings in later life - and also (less tangibly and more personally) through the opportunity to broaden horizons and through an added enrichment of life.(5)

11. The question therefore needs to be addressed whether the cost of higher education is fairly distributed between the taxpayer on the one hand and the student (and his family) on the other. Under the present system the overall direct contribution of students and their families towards the students' higher education is only some 10% of the total expenditure on maintenance and tuition costs (and, where no parental contribution is made, that contribution is nil). The other 90% is met by taxpayers who in the generality of cases are likely to earn less throughout their lives than the students they are supporting. It is

(4) Ibid, 1.2

(5) One means of measuring the contribution of higher education to the economy as a whole is the social rate of return of first degrees which, on the basis of certain assumptions, has in recent years been in the region of 5 to 8%. The private rate of return of higher education to the student is considerably higher than the social rate, even allowing for graduates' generally higher tax payments.

acknowledged(4) that it will be necessary for the Government to continue to use taxpayers' money to meet the greater share of the cost of higher education, including the cost of tuition fees.(6) But higher education should be considered not just as an individual right, for those qualified to receive it, but also as an individual benefit towards the cost of which its recipients should make a realistic contribution. It may be thought that students who later enjoy higher earnings will contribute towards their subsidised higher education by paying higher taxes than most people. But higher taxes cannot be counted as a repayment of student support when the same rates of tax apply to non-graduate higher earners. The introduction of loans might, for example, provide a suitable and fairer means of repayment. This and other ideas are considered below.

SECTION III

POSSIBLE CHANGES TO THE EXISTING SYSTEM

12. Without embarking on large reforms of student support, there may be some scope for redeploying resources within its general framework. As noted in Section I, the parental contribution system has been the subject of some criticism. But it does at least provide a means of relieving the taxpayer of, and shielding the student from, a greater share of the cost of higher education. And it could be made to operate more fairly by further adjustments to the parental contribution scale, by assessing contributions on the basis of taxable rather than residual income or by recovering them via the tax system. The assessment of a parental contribution on the basis of income before tax would simplify administration. It would also be more equitable, since it would ensure that those parents already enjoying tax relief, eg mortgage payers, would no longer derive a double benefit by virtue of the residual income assessment. Recovery of contributions through the tax system would protect those students whose parents do not make up the full parental contribution and would enable the full grant to be paid to all students.

(4) Ibid, 1.9 and 9.4

(6) The Jarratt Report recommends that consideration should be given to fees being subsumed in the general funding of institutions: ibid, 3.9.

Recovery from parents could be either on the basis of a flat-rate or "student tax", or it could be related to the assessment made for individual parents each year. [Use of the tax system could, however, present Inland Revenue with difficulties, particularly if individual assessments were to be involved; but this would be offset by the savings resulting from abandoning existing arrangements for administering student support.]

13. Another area in which some adjustment to the existing system could be made is in the length of courses for which mandatory awards would be available. The Government is concerned at the extra costs of first degree courses which last for longer than three years (four years in Scotland).(4) This trend could be halted by limiting mandatory support to a set period rather than to a set (first degree) level. This could be fixed at three years - and four years in Scotland. [Support might instead be limited to courses with a general educational content leaving those wishing to study purely vocational subjects to look to sponsors and potential employers, or to discretionary awards, for support. Subjects such as medicine and architecture, which comprise both general educational and vocational elements, could be supported by mandatory awards up to the point where the vocational training began. Thereafter sponsoring employers (including the Government itself in some cases) would step in. Any approach on these lines would presuppose that the vocational and general educational elements of courses could be separately identified.]

14. As noted in Section I, the Government believes that it is right in principle to remove students from entitlement to state benefits throughout the whole year.(7) One of the criteria to be applied in considering any new scheme of student support will be the extent to which it is compatible with this aim. In particular, arrangements will have to be devised to make available appropriate assistance for those in need during the long vacations for which the awards system does not at present provide support. Another aspect which will need to be reviewed is the present multiplicity of systems of supporting the dependants of students. It seems likely that general changes in the supplementary benefit scheme arising out of the review of social security may achieve some simplifications in the treatment of these students for benefit purposes. But there

(4) Ibid, 6.8

(7) See the Green Paper "Reform of Social Security", Cmnd 9517

is clearly a case, on administrative grounds and in line with the Government's policy to remove students in general from benefit, for rationalising the various systems of support for students' dependants.

15. The existing awards system or any new scheme of support which is introduced could incorporate features designed to encourage trends which are considered to be desirable. For example, if it is thought that students should be encouraged to take time off between leaving school and entering higher education, the level of support could be reduced or even be suspended in the case of those who had been out of school for less than a year. At present, in contrast with most other countries, nearly 90% of our students study away from home at an estimated additional cost of £80M. If it was thought desirable to encourage students to study from home, the level of the grant or other support available could be based on the present home rate. However, such measures would need to be applied flexibly if students' ability to choose when and where to study is not to be unduly impeded. Nor should they encourage students to rely more heavily on state benefits, thus running counter to the Government's general aim of removing students from benefits.

16. There are other, more radical, changes which might be contemplated in order to promote the Government's general objectives and increase motivation. One possibility would be to introduce scholarships (awarded on merit on the basis of A-level or undergraduate study) or bursaries (awarded to encourage students to take certain subjects judged to be in the national interest) alongside existing arrangements for free tuition and either in place of, or supplementary to, any other general support arrangements. The administration of scholarships and bursaries would however be complex. The former would impose extra burdens on the institutions of higher education and the latter would involve central Government in difficult and invidious decisions; and scholarships would not make for the fairer distribution of higher education costs sought by the Government.

17. One means of achieving a fairer distribution of the cost of higher education might be through a Higher Education tax (sometimes called a "graduate tax"). Under this approach every student would receive a flat rate grant covering maintenance which could be made available in blocks taken up according to the student's means and at his discretion. The overall cost to the Government would be recouped by a proportional tax levied through Inland Revenue on graduates' subsequent earnings. The repayment period and tax rates could be balanced in a variety of ways and related to the amount borrowed or to earnings. It

would anyway be important to ensure that those with low or no earnings paid less than the better off, or nothing at all. The main advantages of this approach would lie in equity, since payment for higher education would be determined by future success, and in the removal of the dependence on parents. If full integration into the tax system could be achieved, it would be easy to secure repayments and to keep default rates to a minimum. There would, however, still be some scope for avoidance and evasion of the HE tax - for example by artificially depressed earnings or through emigration. It is uncertain what the psychological impact on the will to succeed of an earnings related tax would be, but any potential disincentive must already exist in a progressive tax system.

SECTION IV

LOANS

18. The most widely canvassed alternative to the present system is one involving loans in whole or in part. Many believe that a personal investment by a student in his or her higher education through loans would be timely; and this could be held to be justified by the logic in Section II. It could also help to overcome some of the difficulties in the existing system mentioned in Section I. In particular loans could go some way to redistributing part of the cost of higher education which at present falls heaviest on the majority of taxpayers who do not enjoy higher education or the lifelong advantages it can bring. Moreover, the present system contains no incentive to students to look carefully at higher education opportunities in considering what will offer them the best available personal and career opportunities. The introduction of loans could be beneficial in encouraging students to take more care in deciding whether they want to go into higher education. It could also influence choice of subject and institution, and encourage a greater degree of commitment by students to their studies. This in turn could influence the type of provision and help to increase the standards offered by the institutions themselves.

19. Replacing the present grant system, wholly or partly, by a loan scheme would produce substantial net savings in the medium to long term. Some of these would enable the Government to find the necessary resources with which it could progressively make desirable reforms, such as extending mandatory support to other groups in higher education, and decreasing students' dependence on their parents. The level and timing of savings would depend on the terms of repayment, the concessions offered, the incidence of default, and

administrative costs. In the short-term there would be minimal reduction in cost and possibly a significant increase if, for example, there were no parental contribution to loans as there is at present to grants.

20. Loans have already proved a practical proposition elsewhere. Indeed the UK system of student support, being based entirely on grants, is virtually unique in the western world. Although there is a great diversity of systems elsewhere, most countries support students through loans to a greater or lesser extent. West Germany switched in 1983 from a part loan/part grant-based system of student support to one based predominantly on 100% interest-free loans administered by the Federal Government. In Sweden, the small basic grant received by all students is supplemented by a loan, which now amounts to 90% of the total award. The complicated Federal and State arrangements for student support in the USA also give prominence to loans, with limited value grants available for the most needy. Caution is necessary in making international comparisons, since the interaction of the higher education, student support, social benefits and tax systems varies from country to country. But there is much in the experience of these countries that should encourage us to look to loans as a possible way forward in the UK.

21. But the case for loans is not unanswerable. The introduction of loans in place of, or alongside, the present system of grants might radically alter the expectations and plans of potential students and their parents, particularly those from the poorest families who now receive 100% grant. There is concern that loans might discourage potential students from participating in higher education at all, particularly those who intend to defer entry to work to raise families, and older potential students who are well established in jobs and have built up commitments. Some point to the social implications of the burden of debt on young adults at the start of their careers and in many cases married lives; and to the difficulty of repayment for those on low incomes. This in turn has implications for the ability of low-paid vocational professions to attract graduates, and for those on long courses. There would also be great administrative difficulties and costs in running a loan scheme. These points are considered below in more detail.

22. <u>Effect on participation</u> - A consequence of giving students, through the introduction of loans, more incentive to consider carefully the costs and benefits of higher education might be that some would conclude that it was no longer worthwhile. Others might be deterred by the responsibility of servicing a loan. Some of these effects on participation would no doubt

be transitory and would decline as loans became accepted as the normal means of financing higher education; employers too might adjust their patterns of reward to ensure that they could continue to attract the right number and kind of graduates. However, the impact on participation of the introduction of loans cannot be accurately predicted. Experience from other countries serves as only a limited guide, since the introduction of loans abroad has often been linked to increases in public support available for education and has opened up access to higher education for many for whom it would not otherwise have been available. There is no precedent for a change from a universal system of grant as of right to one of loans or loans and grant in combination. Nevertheless, other countries operating loans schemes have high rates of participation in higher education. In West Germany 73% of students qualified to do so enter higher education: this is 18% of the relevant age range.(8) The experience of other countries also shows that many students are prepared to participate in higher education even without any grant or loan support. For example, in the USA and Canada around 50% of students receive no support. In Sweden 20% receive only the small basic grant, while under the relatively new West German scheme over 60% of students fall outside the scope of the loans scheme.

23. Terms of repayment - Careful thought would have to be given to setting rates and periods of repayment at levels that were geared both to what the taxpayer could afford through Government expenditure and to the former students' ability to repay the loan. In some countries interest rates are charged but are subsidised compared with commercial levels. In West Germany no interest is charged unless there is default by the borrower; and good examination results can also reduce the amount to be repaid. Repayment periods may be quite short, for example 10 years in the USA. It is difficult to gauge what the optimum conditions for a UK system might be; but the more significant the shift towards loans, the milder the loans terms might be. For example, repayments might be spread over 15 years, and no repayment might be required until some time after course completion; and the outstanding debt may be revalued in line with inflation instead of being subject to a true rate of interest.

(8) Measures for Great Britain do not allow exact comparisons to be made; but the present GB qualified participation index of around 80% and age participation index of around 14% do indicate broad similarities with the position in West Germany.

24. The extent to which loans would produce savings in public expenditure will depend in part upon the level of repayments that can in fact be collected. Inevitably there will be a wilful or negligent minority of defaulters the pursuit of whom may involve disproportionate difficulty and expense. (A grant recovered through the Inland Revenue would largely remove this problem.) Experience of other countries provides useful lessons on how a loan scheme can be tailored so as to minimise default at acceptably low administrative cost. And there is no reason to believe that experience in the UK would be very different from that abroad, namely that the great majority of students can be expected to meet their obligations. On this basis, the default rate might reasonably be assumed to average around 10%.

25. Large debt burdens might prove especially hard to bear for students from poorer families, who have hitherto been heavily reliant on grants and who would not have a ready made source of parental support to draw upon. Consideration would also have to be given to easing the terms of repayment for those raising families, students aiming at the less well-paid careers, and others on low incomes. One option here might be to defer payments in years when income has fallen below, say, 85% of average earnings (currently £170 per week gross). Repayment of debts might also be based on individual, not marital, status and not be recoverable from spouses. Debts could be written off altogether at death or retirement.

26. Longer courses - One potential difficulty with any loan scheme is the additional repayment burden on students on longer than average courses. In England and Wales the standard degree course is three years, but there are a number of courses, for example in the fields of medicine and veterinary science, which are considerably longer. A particular problem arises in Scotland where, because of the characteristics of the Scottish education system, Honours degree courses last for four years. [A dual loans and grant system might be one way round this difficulty. Under this system a flat rate loan could be made available to all students to cover the cost of maintenance for three years irrespective of the length of course and the subject covered, with fourth or subsequent years covered by a grant awarded on the basis of existing schemes. Safeguards would of course be required to avoid abuses of the system. An extended loan might be available for students who failed to fulfil the criteria for a grant for any additional year or years. Repayment of the loan would be subject to the same arrangements for repayment as would apply to a straight loans scheme. Such an approach would however carry an extra cost, both in non-repayable grant and also in administration, since the awards

system would have to remain in being alongside the new loan scheme.] [One way round this difficulty would be to be to build in softer repayment terms for the additional loans required for longer courses.]

27. Administration of a loan scheme - In principle, responsibility for making the loans, monitoring repayments, authorising deferments, recovering from defaulters and writing off debts, might lie either in the public or the private sector. In practice, however, the commercial banks are unlikely to be willing, without Government guarantees, to take on the administration of a loan scheme which would be available as of right to all students qualifying for admission to higher education, whatever the commercial risk. In most other countries the banks are not involved in loan schemes. In Sweden, administration of the loan scheme passed from the banks to a state agency in the 1960s, partly because of the Government's determination to pursue bad debts and partly to maintain interest rate subsidies. A state-run scheme also operates in West Germany and other European countries. In the USA, reliance on Government agencies has been minimised through the operation of a variety of schemes administered by the banks. However, the schemes are underwritten by the Federal Government which is faced with problems of escalating cost and unacceptable levels of default. Experience therefore seems to argue for a centrally-run scheme as the likeliest option for any UK switch to loans. Preliminary estimates suggest that this could cost up to about £10M a year in administration.

Loan options

28. The options discussed below and exemplified in Annex B cover the main loan/parental contribution permutations which the Government believes represent a reasonable starting point for public debate on loans. Students already on courses during the transition period would carry on under the existing arrangements. For new students the level of support made available through loans or mixed parental contributions and loans would be equivalent to current grant levels. The number of students qualifying for support is also assumed to be constant at the present England and Wales figure of 380,000. However, experience from abroad shows that take-up and participation are not invariably linked. Table 1 of Annex B exemplifies a spread of possible take-up rates although, as noted there, take-up will vary between options and in any event is unlikely to be as high as 100%.

29. The most straightforward option for the introduction of loans would be to substitute loans for the present grant element of the award, while retaining

the parental contribution in its present form. Clearly, any major shift of this kind from the present arrangements would not be without its difficulties. The effects on participation and take-up rates of a total switch from grants to loans would, in particular, be uncertain. But these difficulties could be mitigated by the mild repayment terms spelt out in the notes to Table 1 of Annex B, and by inflation indexing the loans rather than charging interest. Moreover, a limit of, say, 5% could be applied to the annual indexation. This would mean that, in years of high inflation, the repayable amount outstanding would actually fall in real terms. Retention of the parental contribution would also mitigate the abuse sometimes associated with student loans of providing subsidised loans for those of ample means to use for purposes other than student support. An option on these lines would ensure that the Government's contribution to student support was maintained at present levels in the early years of the scheme, and that significant public expenditure savings would eventually accrue in due course.

30. A number of variants can be developed on this option. The rate at which savings accrued could be increased by limiting the repayment period to, say, 10 years; and the savings could also be increased if there were no cap on indexation or if a true rate of interest were charged. However, these modifications might be considered too harsh, particularly for students from lower income families. Alternatively it would be possible to incorporate phased reductions of the parental contribution, although complete abolition would have a high cost. One approach would be to use some or all of the loan repayments to effect reductions in parental contributions of, say, 5% per annum: this rate might be increased in the longer term as the flow of loan repayments increased. Further softening of the terms of repayment could be incorporated to reduce the adverse impact on participation from lower income families. For example, indexation of the debt could be postponed until repayment began, and waived during subsequent periods when repayment was deferred. A finite term could be set on repayments, with any debt outstanding at the end of the period written off. This approach would work to the advantage of graduates with lower earnings, but might in some cases act as an incentive to default or as a disincentive to seeking employment. Finally a system of part grant and part loan could be introduced, perhaps leading to the gradual phasing out of the grant element.

31. The option described in paragraph 29 and some variants on it are displayed

in Table 1 of Annex B. Tables 2 illustrates repayment rates for individual students, expressed in cash terms. Table 3 compares average graduate and other earnings. [The Government believes that .... is to be preferred.]

SECTION V

CONCLUSIONS

32. This paper has argued that there is a need to re-examine our system of student support in order to measure it against developments in higher education that have taken place in recent years and which may be expected in the years ahead. Changes may also be called for in the light of the escalations in expenditure that have taken place since the system was introduced in 1962 and in the current national interest. It is the Government's view that a more rational and fairer system of supporting students should now be seriously considered; and one which places more of the financial burden on those who benefit from higher education, and less on the taxpayer at large. The introduction of loans would be one way in which greater equity could be achieved, and the Government sees considerable attractions in this approach. There are, however, other possibilities, some of which could be adopted in combination with a loan scheme. There is also the possibility of modifying the present system.

33. The Government would welcome the widest possible public debate on these propositions. In particular, it invites views on the following questions:

<u>Sections I and II</u>

(a) What adjustment in the burden of student maintenance should be made as between the taxpayer on the one hand and students and their families on the other?

(b) Should entitlement to mandatory support be extended to other types of courses? If so, which ones?

(c) Should students be financially less dependent on their parents? If so, is the priority a reduction in parental contributions across the board, or should any reduction be directed at achieving more independence for the 20 to 25 year olds?

Section III

(d) If the parental contribution system is to remain, what if any adjustments should be made?

(e) Equally, should either of the two administrative changes described in paragraph 11 be introduced, viz -

(i) a switch to gross (or taxable) income assessment and

(ii) recovery through the tax system, if workable?

(f) Should entitlement to mandatory support be based on a standard period (with exceptions)?

(g) Should the period for support be limited, in the case of vocational courses, to the (initial) period of general education?

(h) If benefits are no longer to be available to students, what kind of hardship scheme (with or without loans) should be set up, and who should administer it?

(i) In view of the cost implications, should students be encouraged through the support arrangements to study at a local higher education institution?

(j) Should the support arrangements encourage students to take a year off between school and entry into higher education?

(k) Should awards be applied selectively on merit as with scholarships, or according to national needs, as with bursaries? If so, how should the schemes be administered and by whom?

(l) Should the cost of student support be repayable by means of a Higher Education tax levied on the former students? If so, should the tax be assessed -

(i) individually according to the amount of support received; or

(ii) on a flat rate earnings-related basis?

Section IV

(m) Should loans be introduced? If so, should there be mixed grants and loans, leading eventually to 100% loans?

(n) Should the loan terms be subsidised heavily, moderately or not at all? In particular -

(i) should there be reductions and/or deferrals of repayments when former students are on low incomes or unemployed?

(ii) should there be a true interest rate or simply inflation-proofing?

(iii) should the standard repayment period be 10 to 15 years, or longer?

(iv) what should be done about longer courses?

(o) Taking account of public expenditure costs, which of the options illustrated in Table 1 is to be preferred?

[Note - Some of these questions will be omitted or amended when the paper is agreed.]

STUDENT AWARDS

1. Under present arrangements students on advanced courses who have been ordinarily resident in the UK for the three years before their course are eligible for mandatory awards. In England and Wales these awards are administered by local education authorities and in Scotland by the Scottish Education Department. Although the Scottish arrangements cover a slightly larger number of courses, and deal differently with students' travel costs, it has been the policy of successive Governments to maintain parity of treatment for students on both sides of the border so far as main rates of grant and parental contribution scales are concerned.

England and Wales

2. Mandatory awards are made to students on designated courses of advanced further education. These are full-time degree or degree comparable courses: DipHE courses, HND courses run by BTEC, and courses of initial teacher training. Awards for other courses - other than for certain postgraduate study - are discretionary: each individual award-making body decides the number of such awards it can make and the rates and conditions of grant and bears the full cost itself. The remainder of this note will concern mandatory awards.

3. A student has a right to an award for only one attempt at a basic advanced qualification and so those who have undertaken previous advanced study (irrespective of whether an award was received for that study or not) are rendered ineligible. Students must also satisfy certain residence conditions to be eligible for support.

4. The award covers a student's maintenance, including a flat-rate sum for travel, and fees. For those resident in the parental home the basic maintenance grant is £1480.* For those living outside of the parental home it is £2165 for those in London, and £1830 for those elsewhere. Those receiving free board and loding are entitled to a grant of £780. The grant is assumed to cover the Christmas and Easter vacations and 30 weeks of term-time. In addition to the basic maintenance grant, the student may also be eligible for additional maintenance. The main supplementary allowances are for extra weeks of study and for dependants.

5. The cost of maintenance is shared between the State, students and their families. Students aged 25 or over, or who have supported themselves for 3 years before the start of their course are regarded as independent of their parents for awards purposes. A parental contribution is assessed for all other mandatory award holders.

6. The parental contribution is based upon the parents' residual income: the income of both parents is taken into account in its calculation. Residual income is defined as the parents' gross (taxable) income in the preceding financial year less certain deductions including those for other dependants, interest payments (including mortgage interests), superannuation, life insurance and pension scheme contributions. After residual income has been calculated, and parental contribution assessed, a further deduction is made in respect of any other dependent children of the family: £240 if the child is an award holder, or £85 otherwise.

7. A nil parental contribution is asssessed where parents' residual income is less than £8100. At £8100 a contribution of £20 is assessed; contributions are then assessed at the rate of £1 for each £7 of additional income to a residual income of £10,300, then £1 for every £5 to a residual income of £15,000, and £1 for every £4 thereafter subject to a maximum contribution of £4000.

8. For the spouses of independent students the contribution is again based on residual income. No contribution is assessed on incomes below £6300. At £6300 a contribution of £10 is assessed; contributions are then assessed at £1 in £5 to a residual income of £10,2000, and beyond that at the rate of £1 in every £10.

9. The student's contribution is not based on residual income. On incomes (net of tax, national insurance, child benefit and earnings) beyond £425 the student is assessed to contribute pound for pound towards his grant. However, scholarship income to a limit of £1280 (or £1600 in the case of an Industrial Scholarship) is disregarded.

10. The maximum contribution towards the grant from whichever source(s) is limited to the maintenance element of the award. Fees are met in full by the State, and are not subject to parental or other contributions. They are paid direct to the college by the award-making body.

11. In addition to the main rate of grant, there are a number of supplementary allowances which certain students - for example those who are over 26, or who are disabled, or who have dependants - are eligible to receive. The main awards regulations provide for the dependants only of students defined as "independent" (ie those who are over 25 or who have support themselves for three years) and married before the start of their courses. (Dependants of other students are supported under a hardship scheme administered by DHSS on behalf of DES under regulations made specifically for the purpose.)

Scotland

12. For students who are ordinarily resident in Scotland, Students' Allowances are paid at the discretion of the Secretary of State. The range of courses for which students' allowances are offered by the Scottish Education Department is wider than that covered by the mandatory scheme in England and Wales, but it includes all courses which are designated by the Department of Education and Science for mandatory award purposes, and conditions of eligibility for entitlements are similar. SED also offers students' allowances for courses in social work, professions supplementary to medicine, adult education and certain other courses for which in England and Wales support is offered on a discretionary basis by local education authorities or other award-making bodies. Limited numbers of postgraduate students' allowances are also available from the Department.

13. A significant recent difference in the Scottish arrangements is that main rates of maintenance grant are slightly lower than in England and Wales, but students may claim repayment of essential travelling expenses in excess of £50 per annum. For those living in the parental home the grant is £1365; the grant for students living elsewhere (outside London) is £1775 and for those at an educational establishment in London £2110. The features of the mandatory awards scheme in England and Wales which are described in paragraphs 5 to 11 above apply equally to the SED Students' Allowances Scheme, with the single exception that the maximum contribution towards the grant (paragraph 10) extends to travelling expenses.

*<u>Footnote:</u> All rates quoted are for the 1985-86 academic year.

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ANNEX B

TABLE 1

STUDENT LOAN SCHEME EXEMPLIFICATIONS

EXPENDITURE EFFECTS £M (1985/86 PRICES) ENGLAND AND WALES

OPTIONS	Take-up rates	Years 1	2	3	5	7	10	15	20	Steady State
BASIC SCHEME - Interest free loan available up to 100% of assessed maintenance; loan debt revalued throughout in line with inflation, subject to ceiling of 5% pa; 15 year repayment period. Parental contribution retained.										
1. Inflation 5% pa or less	100%	0	0	0	0	- 28	- 83	-193	-310	-353
	80%	-31	- 62	- 92	- 92	-115	-159	-246	-341	-375
	60%	-62	-123	-185	-185	-201	-235	-300	-371	-397
2. Inflation 10% pa	100%	0	0	0	0	- 18	- 54	-125	-201	-229
	80%	-31	- 62	- 92	- 92	-107	-135	-192	-253	-275
	60%	-62	-123	-185	-185	-195	-217	-259	-305	-322
3. 10 year repayment period. Inflation 5% pa or less.	100%	0	0	0	0	- 42	-125	-289	-341	-353
	80%	-31	- 62	- 92	- 92	-126	-192	-323	-365	-375
	60%	-62	-123	-185	-185	-210	-259	-358	-389	-397
4. Debt not revalued during years of course. Inflation 5% pa	100%	0	0	0	0	- 25	- 75	-174	-280	-319
	80%	-31	- 62	- 92	- 92	-112	-152	-231	-317	-348
	60%	-62	-123	-185	-185	-200	-230	-289	-353	-376
5. Debt not revalued during years of course, or grace and deferral periods. Inflation 5% pa	100%	0	0	0	0	- 23	- 66	-150	-239	-264
	80%	-31	- 62	- 92	- 92	-110	-145	-212	-283	-304
	60%	-62	-123	-185	-185	-198	-224	-275	-327	-343

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	Take-up rates	Years 1	2	3	5	7	10	15	20	Steady State
6. Parental contribution reduced by 5% pa beginning year 6. Inflation 5% pa or less	100%	0	0	0	0	- 2	- 20	- 75	-152	-293
	80%	-31	- 62	- 92	- 92	- 94	-108	-152	-214	-327
	60%	-62	-128	-185	-185	-186	-197	-229	-276	-361
7. Immediate parental contribution reductions of 5% pa year 1-10, stopping at 50% of present levels. Inflation 5% pa or less	100%	+ 4	+ 17	+ 38	+64	+ 59	+ 36	- 97	-245	-323
	80%	-27	- 48	- 62	- 41	- 45	- 64	-170	-288	-351
	60%	-59	-113	-162	-146	-149	-163	-243	-332	-379
8. Immediate parental contribution reductions of 10% pa years 1-10. Inflation 5% pa or less	100%	+ 8	+ 34	+ 76	+127	+146	+154	- 1	-180	-293
	80%	-24	- 34	- 31	+ 10	+ 25	+ 31	- 93	-236	-327
	60%	-56	-103	-139	-108	- 97	- 92	-185	-293	-361
9. Immediate parental contribution reductions of 10% pa years 1-5, stopping at 50% of present levels. Inflation 5% pa or less	100%	+ 8	+ 34	+ 76	+127	+ 96	+ 28	-110	-260	-323
	80%	-24	- 34	- 31	+ 10	- 16	- 70	-181	-301	-351
	60%	-56	-103	-139	-108	-127	-168	-251	-341	-379
10. 50% loan throughout. Immediate parental contribution reductions of 10% pa years 1-5, stopping at 50% of present levels (set against grant then loan). Inflation 5% pa or less	100%	+ 9	+ 34	+ 77	+128	+111	+ 74	0	- 80	-112
	80%	-10	- 4	+ 18	+ 65	+ 51	+ 22	- 37	-101	-127
	60%	-28	- 42	- 41	- 3	- 8	- 30	- 74	-122	-142
11. 50% loan initially rising by 5% pa to 100% in year 11. Immediate parental contribution reductions of 10% pa years 1-10 (set against grant then loan). Inflation 5% pa or less.	100%	+ 9	+ 34	+ 77	+127	+158	+186	+ 53	-120	-293
	80%	-10	- 7	+ 7	+ 41	+ 58	+ 63	- 50	-188	-327
	60%	-28	- 49	- 63	- 45	- 42	- 59	-153	-257	-361

Notes:

(1) In addition to the variants on the basic scheme described above, a cut-off point could be introduced so that debts were written off 20 years after the first repayment was due. This would reduce the steady state savings by some £8M pa.

(2) Take-up rates are difficult to predict and, while likely to vary between options, are unlikely ever to be 100%. The expenditure effects of 70% and 90% take-up rates can be determined by calculating the relevant mid-points between the figures shown.

ASSUMPTIONS:

The following assumptions are common to all options:

(a) The student population is a constant 380,000 and all are on 3 year courses.

(b) Loans are for new students only - continuing students carry on under existing arrangements.

(c) There is a repayment grace period until the second year after course completion.

(d) Repayment is in equal real tranches.

(e) Repayment is deferred in years when income falls below 85% of average earnings.

(f) Debts are written off on death or retirement.

(g) Ten per cent of repayments are defaulted.

(h) Administration costs are excluded.

(i) 100% of assessed maintenance is the estimated average full value award, including allowances, for 1985/86 of £1885.

TABLE 2

REPAYMENT PROFILES: CASH TERMS*

	A. LOAN = 50% MAINTENANCE			B. LOAN = 100% MAINTENANCE		
REPAYMENT YEAR	REVALUED DEBT £	CASH REPAYMENT £	OUTSTANDING DEBT £	REVALUED DEBT £	CASH REPAYMENT £	OUTSTANDING DEBT £
(3 study	991		991	1979		1979
years)	2080		2080	4156		4156
	3277		3277	6546		6546
(Grace	3440		3440	6874		6874
period)	3613		3613	7217		7217
1	3793	253	3541	7578	505	7073
2	3718	265	3452	7427	530	6896
3	3625	279	3346	7241	557	6684
4	3514	292	3221	7018	585	6433
5	3382	307	3075	6755	614	6141
6	3229	322	2907	6448	645	5803
7	3052	339	2714	6093	677	5416
8	2849	355	2494	5687	711	4976
9	2618	373	2245	5225	746	4479
10	2358	392	1966	4703	784	3919
11	2064	411	1652	4115	823	3292
12	1735	432	1303	3456	864	2592
13	1368	454	915	2722	907	1815
14	960	476	484	1905	953	953
15	508	508	0	1000	1000	0

Notes:

A. At 1985/86 prices the loan would be £943 pa for 3 years, and the real terms repayments would remain the same at £188 pa

B. At 1985/86 prices the loan would be £1885 pa for 3 years, and the real terms repayment would remain constant at £377 pa

*assuming 5% pa inflation (higher inflation would not affect these cash profiles if the 5% pa ceiling on debt revaluation were applied, and would have the effect of reducing the outstanding debt in <u>real</u> terms).

TABLE 3

GRADUATE EARNINGS

Age	Graduates £pa
20-24	7400
25-29	9800
30-39	13200
40-49	16100
50-59	16000
All ages (20-69)	13100

(1) Average figures are given, uprated to 1985 levels from the 1980-1982 General Household Surveys (the latest available data). They are for graduates in both full and part-time work.

(2) A student taking out a 100% loan of £1885 pa for 3 years would accumulate a debt of £5655, to be repaid in equal instalments over 15 years amounting to £377 pa (at 1985/86 prices).

(3) The average earnings of all full-time workers on adult rates of pay is at present estimated to be some £9000 pa. The costings shown in Table I assume that loan repayments would be deferred in years when graduates were on incomes below 85% of this figure (ie about £7500 pa or less). The effect of this is assumed to be that only some 50% of graduates would begin to repay their loans immediately after the 2 year grace period following completion of their course.

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