INCREASING POSTGRADUATE OPPORTUNITIES

Proposals for funding

October 2013
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Australia
United States
Canada
France
This Government is in no doubt that postgraduate education matters. It is good for students, good for universities and good for the economy.

Universities play a vital role in developing a highly skilled workforce by training postgraduate students. We need these top level skills to compete and succeed in a global knowledge economy.

Our postgraduate courses have a reputation for excellence across the world. Each year more top graduates from other countries are choosing to come here to study after their first degree and we have seen unprecedented growth in postgraduate education in the past decade.

However, we cannot afford to be complacent. There are concerns about whether we can expect a similar level of demand from students in the future.

In particular we want talented graduates to feel inspired and able to pursue their education, regardless of their background.

We are investing £75 million to help universities and colleges to attract and support less-advantaged students into postgraduate education. The competition for the recent £25 million round of bids closed in September. We were delighted to see a higher than anticipated demand from the sector.

This will give us the evidence to understand the challenges ahead and present us with potential scalable solutions. Our intention is that it will also leverage further significant funding.

The 1994 Group has been one of the most prominent voices flagging up areas of concern in the postgraduate landscape. I welcome this report, and in particular its attempt to put forward possible solutions for the future financing of postgraduate education.

It is important to remember that institutions have been able to operate dynamically and grow their own markets without government intervention and regulation for many years. It therefore cannot be for the public purse alone to tackle the issues of access, participation and finance.

I am keen, for example, to explore what more banks could do to support postgraduate students.

With institutions, the Government and lenders working together, I am confident that Britain will continue to be one of the very best places in the world to pursue a postgraduate education.

Rt. Hon. David Willetts MP
Minister for Universities and Science
EXECUTIVE SUMMARY

In January 2012, we published The Postgraduate Crisis, an important policy paper which warned of a looming flashpoint in English higher education. The report highlighted the failures of the Professional and Career Development Loan (PCDL) system and the declining availability of financial support from high street banks. We warned that, without action, the UK’s successful postgraduate system would be in jeopardy.

21 months on, there is consensus across the higher education sector, and increasingly across all three major political parties in Westminster, that the current system of student support for English postgraduates is not working. Since 2012, a number of potential solutions to the postgraduate financing problem have been put forward. This report takes a comprehensive look at the options and makes recommendations on what Government, business and universities themselves should do to improve the situation.

List of Recommendations

Recommendation 1: The Government should put in place an income-contingent loan system for full-time postgraduate students using a modified version of the model put forward by Tim Leunig.

Recommendation 2: Further research is required on the needs of part-time postgraduates with a view to identifying how support might best be provided for this heterogeneous group. As resources allow, the Government should seek to identify opportunities to extend the support available to some part-time postgraduates.

Recommendation 3: Representatives of the HE sector and the main professional bodies should establish a Council for Universities and the Professions to monitor take-up of postgraduate courses in professional disciplines, and encourage the introduction of profession-wide mechanisms of student financial support.

Recommendation 4: HM Revenue and Customs should encourage employers to support postgraduate education by removing the £10,000 cap on the extra-statutory tax concession for employer loans towards the cost of study at Higher Education Institutions.

Recommendation 5: Any future review of higher education student support should explicitly consider integrating undergraduate and postgraduate student support.

Recommendation 6: The Government should continue to monitor the expansion of integrated masters’ degrees beyond the areas where they have traditionally been delivered, providing student loans for new four-year courses only where a genuine academic case can be made.

The optimal solution: a low-cost state-backed student loan scheme

We recommend that the Government put in place an income-contingent loan system for full-time postgraduate students using a modified version of the model put forward by Tim Leunig.

This system would have the following characteristics:

- Loans of up to £10,000 available to students with first or upper second class degrees.
• Repayable at 9% on income between £15,000 and £21,000.
• Postgraduate and undergraduate loans will be rolled together for higher earners, such that once a graduate has finished repayments on one loan, he or she will continue to make repayments towards the other loan at a rate of 9% of all income above the £15,000 threshold.
• Any outstanding debt will be written off 30 years after beginning the course.

We calculate that the long-term cost of a loan scheme, if existing recruitment patterns hold, will be less – probably substantially less – than £50 million per year, a sum which can be found easily through redirecting money from existing funding pots. The Professional and Career Development Loans system for postgraduate courses should be scrapped: realising an annual saving of £12 million. The remainder of the funding required should be taken from the £50 million the Government has earmarked for a new postgraduate National Scholarship Programme.

The low cost of the scheme means that regulation of postgraduate student numbers will be unnecessary – the natural cap on student numbers posed by universities’ own capacity constraints provides a sufficient limitation.

Options for higher education institutions

We examine the options available for individual universities, and groups of universities who might wish to provide their own sources of financial support to prospective postgraduates. These options include risk-sharing with banks, and offering institutional loans financed through funds obtained from the capital markets.

Should the Government prove unwilling to develop a system of state-backed postgraduate loans along the lines we propose, institutions should investigate the feasibility of providing a similar scheme on a pooled basis.

We are clear that this would be less preferable to a national solution. Institutions are unlikely to be able to borrow as cheaply as Government to fund the scheme, and would struggle to administer an income-contingent repayment system. In addition, the risk profile of such a system is likely to be less balanced than that of a national system. An institution-led solution would be more complex for prospective students to navigate and may also result in a situation where comprehensive financial support for postgraduates was available for students attending some universities, but not others.

We envisage that institutions will continue to offer support through fee waivers and scholarships to maintain a pipeline of future researchers and to support students who might otherwise face financial hardship. They may also want to continue to use these tools to attract the brightest and best graduates.

Employer contributions

We envisage that employers will continue to contribute to financial support for postgraduate taught (PGT) students in two ways:

Firstly, a small group of qualifications should be excluded from the loan scheme – principally MBAs and qualifications leading to entry into the law profession. Employers and the relevant professional bodies should take a strong lead in providing funding for these courses. We also encourage other industries, particularly those where postgraduate qualifications are increasingly de facto requirements for entry, to consider carefully whether there is a need for concerted action on their
part to provide financial support for students undertaking postgraduate education. To support such a dialogue we recommend that representatives of the HE sector and the main professional bodies convene a Council for Universities and the Professions to monitor take-up of postgraduate courses in professional disciplines, and encourage the introduction of profession-wide mechanisms of student financial support.

Secondly, employers will continue to invest in co-financing postgraduate education which they value as being integral to workforce development and employee retention. We envisage that employer support in the form of sponsorship (as opposed to loans) will be unaffected.

A number of employers have led the way in supporting employees wishing to undertake postgraduate education through provision of loans at preferential or interest-free rates. We recommend that HM Revenue and Customs should encourage employers to support postgraduate education by removing the £10,000 cap on the extra-statutory tax concession for employer loans towards the cost of study at Higher Education Institutions. This change would have a negligible impact on government tax receipts.

Integration of undergraduate and postgraduate funding

We consider the case for full integration of undergraduate and postgraduate funding, but conclude that there is a lack of political will to reopen the undergraduate funding settlement so soon after the Browne Review. We also find that incorporating postgraduate study into the current undergraduate funding system would be one of the more expensive mechanisms of tackling the problems in postgraduate funding. We recommend that any future review of higher education student support should explicitly consider integrating undergraduate and postgraduate student support.

We also consider recent trends in the prevalence of integrated masters’ degrees, noting that their numbers have expanded substantially over the last decade. A number of universities have taken advantage of the additional funding and access to student finance provided by integrated masters’ degrees through expanding their provision into new subject areas. We recommend that the Government should continue to monitor the expansion of integrated masters’ degrees beyond the areas where they have traditionally been delivered, providing student loans for new four-year courses only where a genuine academic case can be made.

Tax incentives

We also explore the potential impact of introducing tax incentives for postgraduate study, but conclude that whilst they may have the effect of reducing the real-term cost of undertaking education and training for individuals, they would do little to improve access to finance. We do not believe they would be sufficient on their own and would only work as an additional measure, alongside other policy interventions, to free up the supply of credit to prospective postgraduate students. Tax incentives involve the state co-funding education rather than simply underwriting costs, so the long-term costs are likely to be much greater than those associated with most alternative interventions.

Conclusions

We conclude by highlighting the consequences of not tackling the postgraduate funding challenge – relative underinvestment in postgraduate education by UK-domiciled students, which will, in the longer-term, lead to a decline in British competitiveness. In 2014, the first students subject to the new funding regime will begin to decide whether they wish to undertake postgraduate study. These
decisions will have consequences not just for individuals, but for universities and for wider society, and will be shaped by the funding environment for postgraduate study. The postgraduate crisis is no longer a theoretical challenge: it is an urgent issue which must be addressed now.
CHAPTER 1 – INTRODUCTION

In January 2012, the 1994 Group warned of a looming ‘postgraduate crisis’ and called for immediate action “to address the risks posed to the future of UK postgraduate education”.¹ The report highlighted the difficulties many students were facing in obtaining funding toward the cost of undertaking postgraduate study, detailed the failures of the Professional and Career Development Loan system and looked at the declining availability of financial support from high street banks. Since then, a number of reports which discuss the instabilities of the postgraduate market have followed which have fleshed out the multiple dimensions of the funding challenge and floated various solutions.

The problems in postgraduate funding are particularly acute for PGT courses (those which typically lead to the award of a master’s degree) due to the lack of public funding towards meeting the costs of tuition fees and student maintenance. The UK Research Councils, who fund over a third of British PhD researchers, have all but withdrawn funding for taught masters’ students.² Meanwhile the Higher Education Funding Council for England (HEFCE) provides a limited amount of support to institutions, but no direct funding to students in England. By contrast, the Scottish Funding Council provides direct part-funding for 850 PGT places at Scottish universities. The overwhelming majority of masters’ students are self-financing but, unlike undergraduates, they are not eligible for student loans.

Postgraduates and the Browne Review

The Browne Review of Higher Education was specifically tasked with addressing the needs of postgraduate funding, with the terms of reference clearly stating that “its primary task is to make recommendations to Government on the future of fees policy and financial support for full and part-time undergraduate and postgraduate students.”³ Unfortunately the review team failed to do justice to this mandate and ultimately allocated only one page of their report on the funding of higher education to postgraduates. They conclude that “postgraduate education is a successful part of the higher education system and there is no evidence that changes to funding or student finance are needed to support student demand or access”.⁴ In making this statement the review group were sidestepping the remit not only of their own report, but the steer given by Professor Adrian Smith, the then BIS Director General responsible for Higher Education, in his March 2010 Report, One Step Beyond: Making the most of postgraduate education. Professor Smith explicitly recommended that the Browne Report should look at the financial and access challenges facing postgraduates as part of his survey of the entirety of the higher education sector.⁵

The Browne Review argued that the primary benefits of postgraduate study are individual, with the report claiming that “the private benefits of taught postgraduate education are predominant over the public benefits”. The review group went on to argue that these benefits have:

² The focus of this publication is on postgraduate students on taught masters’ courses, as opposed to postgraduate researchers working towards a PhD. Unless otherwise noted, all data and references to ‘postgraduates’ and ‘postgraduate students’ should be understood to refer to PGT students.
⁵ A. Smith. 2010. One Step Beyond: Making the most of postgraduate education, p. 7.
“clearly tended to be sufficient to generate private investment. Many postgraduate students have already been in work and so may have savings as well as a financial track record which helps for obtaining credit. Some are supported by employers in doing their degree”.\textsuperscript{6}

The review group rejected the argument that taught postgraduate students should receive the same support as undergraduates, but failed to consider the wider question of how postgraduate study should be funded, and whether taught postgraduates should receive some degree of state support, an omission we attempt to address in this report.

The review group did acknowledge that the next generation of undergraduates may be unwilling to take on the debt necessary to start a postgraduate course, warning that “it is possible that, in the future if students are paying higher fees to enter undergraduate education, they will be less likely to participate in postgraduate study”\textsuperscript{(p.55)}. This observation led the group to recommend that trends in postgraduate study should be carefully monitored once tuition fees were raised. We are likely to see the first signs of this impact next year, when students due to graduate from three-year degree courses begun in 2012 apply for postgraduate courses starting in September 2015.

This publication is intended, in part, to respond to Browne’s call for further research. However, we also aim to challenge its view: both the simplicity of the statement that postgraduate study is something which produces only an individual benefit, and the assumption that a sufficient number of postgraduate students can fund their studies either through personal resources or through employer contributions. In 2011/12, half of all PGT students were aged 21-24. Most would never have had the opportunity to accumulate sufficient savings to fund themselves through a postgraduate course. Without a functioning system of support for postgraduate students, access to postgraduate study is restricted, with disturbing implications for social mobility, the pipeline of future academic researchers, the UK’s skills base, and ultimately the British economy.

**Enrolment trends**

Over the past decade, the number of students taking taught postgraduate courses has increased by 42%. On the face of it, the sector looks relatively healthy. However, this masks some concerning trends. Firstly, this increase has been largely attributable to the rise in the number of overseas students coming to the UK to take courses, which is up by 90% in the last decade.\textsuperscript{7} The number of UK students has increased by a much more modest 23%. UK students account for just a quarter of the growth in the postgraduate population. In 2002, there were four UK taught postgraduate students for every three from overseas. Since 2008, they have been outnumbered every year. Since the majority of these students will eventually return to their home countries, taking their newly gained skills, knowledge and expertise with them, this trend has consequences for the UK’s global competitiveness.

Secondly, while overall numbers have increased, far fewer students enjoy financial support. In 2011/12, there were 149,560 British students taking postgraduate courses. 94,115 (63%) were self-financing; 17,520 (12%) were funded by industry or their employer and just 825 (0.55%) were funded by a Research Council.\textsuperscript{8} The remaining students were funded by a combination of charitable, scholarship, combined awards and institutional fee waivers. The number of Research Council funded students has more than halved over the past decade, with the bulk of the fall coming in the last year. Likewise, the number of postgraduate students with industry funding, which remained stable in absolute terms over the previous decade, fell by 10% in 2011. The findings of the Browne Review

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\textsuperscript{6} Browne. 2010. p. 55.
\textsuperscript{7} HEIDI data. This figure includes both EU and non-EU students.
\textsuperscript{8} HEIDI data.
effectively licensed changes to the balance of funding, encouraging the funding councils to withdraw some of the remaining support for postgraduate students, and instead “targeting investment on courses that are a priority for the public interest.”

The value of postgraduate taught education

Undoubtedly there are substantial private benefits to postgraduate study. Both the additional knowledge gained and the skills developed during a postgraduate degree make individuals better prepared for the workplace and more attractive to employers. This is reflected in the ‘postgraduate premium’: Lindley and Machin estimate that a master’s degree adds a premium of 15% to a graduate’s lifetime earnings. In an increasingly crowded graduate market, obtaining a postgraduate qualification is one way for candidates to stand out to employers. Indeed, in some jobs a postgraduate qualification is becoming something close to a prerequisite for admission or promotion. The number of postgraduates who are supported by their employers indicates that there is a definite ‘market value’ for postgraduate study, over and above its intellectual value.

In addition, there are substantial public benefits to be derived from increased participation in postgraduate study. Postgraduates develop specialised areas of knowledge and skills which are of inestimable benefit to the economy as a whole. The government has recognised the value of research and innovation in a number of ways including ring-fencing the science budget (which includes Research Council funding streams) and through new investment in postgraduate funding pilots which we will detail later in this chapter.

As the 1994 Group have previously put it: “Postgraduates are an essential part of the knowledge economy and their skills are highly valued by many different business sectors. The unique skills of postgraduates are also important to the work of the public and not for profit sectors. The heightened skills and knowledge of postgraduates enhances public services and brings long-term societal benefits”. In an age where politicians worry about the UK’s competitiveness in the ‘global race’, our postgraduate population is the future: if we fail to invest in it, our economy will be all the poorer as a result.

Existing funding

The Government currently provides public funding for postgraduate taught education in a number of ways.

1. Teaching grant funding

HEFCE provides public funding for taught postgraduate courses as a component of universities’ teaching grant, to the value of £120 million in 2012/13. This includes support for high-cost subjects. In 2011, HEFCE announced they would withdraw this funding for subjects in Band C, a decision which was subsequently reversed following concerns about the implications that this would have on the health of the affected disciplines.

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9 Browne. 2010, p. 47.
2. **Integrated master’s funding**

The next largest slice of funding PGT provision comes in the form of support for the final year of integrated masters’ degrees. This is not usually recognised as funding for postgraduate study as it is accounted for within the undergraduate funding regime.

Integrated masters’ degrees are undergraduate courses, typically of four years (five years in Scotland), that lead to a masters-level qualification. Most combine an undergraduate course with an extra year of masters-level study. In some cases, the student can graduate after three years with a bachelor’s degree. Effectively, funding for the final year of study should be considered as spending on postgraduate education. Integrated masters’ degrees are treated by the Student Loans Company in the same way as undergraduate degrees, with students entitled to tuition and maintenance loans for all four years, including the master’s year. Students are also eligible for other forms of support available to undergraduates, such as bursaries and scholarships.

The Government subsidises integrated masters’ courses in the same way as it does undergraduate qualifications: through underwriting losses on student loans. This is reflected in a RAB (Resource Accounting Budget) charge, which the Government currently estimates to be 35%.\(^\text{12}\) We estimate that on this basis the long-term cost of loans to integrated masters’ students could be in excess of £80 million per annum.\(^\text{13}\) The actual cost of providing integrated masters’ courses is likely to be higher, as they are most often offered in high-cost subjects, which attract additional funding through the HEFCE teaching grant.

Over the last five years for which statistics are available, the number of students undertaking integrated masters’ degrees in the UK has increased by 75%, compared to an 18% increase in the total number of undergraduates. The availability of integrated masters varies enormously by subject. They are currently far more prevalent in the science disciplines than in the arts, humanities and social sciences.\(^\text{14}\) In 2011/12, 93.8% of the 74,920 students in the fourth year of an integrated master’s degree were studying in STEM disciplines. Three disciplines – engineering and technology, physical sciences and subjects allied to medicine – continue to dominate, accounting for 81% of all enrolments (slightly down from 84.5% in 2006/7).

The distribution of postgraduate funding through integrated masters’ degrees may raise concerns about equality. Despite making up 54.9% of the undergraduate population and 53.4% of the postgraduate taught population, female students make up only one third (33.7%) of the integrated master’s population. This element of funding provides a largely male subset of students with four years of funding for a combined undergraduate and postgraduate degree. In the wider context of low numbers of women studying STEM subjects, the equality dimension of this funding is an area that could be investigated further.

\(^\text{12}\) The Higher Education Policy Institute has warned that the official estimate of the RAB charge may be too low, as it is based on earnings projections which now appear over-optimistic. Conversely, the figure may also overstate the true cost to Government of borrowing to finance loans.

\(^\text{13}\) Estimated total cost of 35% RAB charge on loans taken out by the 25% of the current cohort (74, 920) in their final year. It assumes each student take out loans of £8,263 for fees (OFFA’s average fee for 2013 after fee waivers) and £4,125 for maintenance (75% of the maximum loan available for students outside of London). There is no separately available estimate of the RAB charge for integrated masters’ students: it is likely that integrated masters’ students have higher levels of repayment, given that they are not only more highly qualified at the end of their course, but also because they are disproportionately male students, whose lifetime earnings are in general substantially higher than those of comparable female graduates. The RAB charge is taken from D. Willetts. 2013. Speech to HEPI Conference. 15 May 2013.

3. **Professional and Career Development Loans**

The more explicit way in which government funds loans for postgraduate study is through the system of Professional and Career Development Loans (PCDLs). These loans are currently only offered by Barclays and the Co-operative Bank. The Government pays the interest accrued – currently a relatively high 9.9% - whilst the postgraduate is studying. The student becomes liable to begin repayment one month after the end of their course, and repays over a period of between one and five years. The Government currently spends around £15 million on support for PCDLs,\(^{15}\) of which approximately 90% relates to taught postgraduate courses.

As explained in Chapter 4, PCDLs are not only expensive, but poorly targeted. Many graduating students will have no assets, no long-term earnings history, and no credit record, and will therefore fail to meet banks’ lending criteria. Conversely, those who can obtain the loans could probably obtain cheaper credit elsewhere. However, as the Government meets the interest in the first year, it makes sense to at least take advantage of the interest free-period. In effect, the Government ends up wasting money on financing expensive loans for those graduates who least need government support.

4. **Research Council Funding**

A small number of Research Councils continue to offer masters’ studentships. The Arts and Humanities Research Council (AHRC) retains two masters’ schemes, while the Economic and Social Research Council (ESRC) provides master’s funding for just one course. However, the majority of Research Councils no longer award masters’ studentships and the total number of studentships awarded has been in sharp decline, from 1,555 in 2006/07 to just 635 in 2011/12.\(^{16}\) Less than 1% of the 149,560 British students on postgraduate courses are principally funded by their Research Council.

5. **New initiatives**

2013 has seen the Government introduce two other new funding streams for postgraduate taught courses, worth £25 million between now and 2015, and £50 million annually post-2015. We will discuss these funding initiatives in more detail at the end of this chapter.

**Recent developments: recognising the problem**

In Summer 2011, Professor Geoff Whitty, Director Emeritus of the Institute of Education, drew attention to the absence of a system of postgraduate support, and highlighted the economic and social implications of a fall in postgraduate training levels, as well as the long-term imbalances threatened by any restrictions on access to postgraduate courses. He concluded that there was a grand irony facing the sector – the risk that reforms to undergraduate finance could be more equitable than its critics fear, but end up reintroducing inequities by failing to consider the implications for postgraduates.\(^{17}\)

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\(^{16}\) This number is somewhat smaller than the number of students in receipt of a scholarship as a minority of scholarships are for courses lasting more than one year.

The 1994 Group’s report on *The Postgraduate Crisis* was published in January of the following year. It highlighted the potential risks to postgraduate study arising from the rise in the maximum annual tuition fee for undergraduate study to £9,000 from 2012, together with changes to the teaching grant funding. The report argued that this could create upward pressure on masters’ course fees and identified the cohort of students graduating from 2015 as a potential flashpoint. Will they be more likely to accept borrowing as a precondition of studying? If so, they may view additional debt as a necessary and acceptable step towards a career. Alternatively, graduating with a nominal debt of £40,000 or more, will they be reluctant to take on a further liability? It was this latter scenario which led Browne to conclude that trends in postgraduate study should be carefully monitored once tuition fees were raised.

The British Academy published a position statement in July 2012 which underlined the vulnerability of postgraduate study, particularly in the arts, humanities and social sciences. They pointed to a lack of investment impacting upon continuation rates and the sustainability of academic disciplines, and concluded that a loans scheme would be the most sustainable way of ensuring a future for home postgraduate students.

In October 2012, Alan Milburn reached the same conclusion, and called on the government to establish an independent review to look at how a loan scheme could work. He argued that there was “a real risk that the ability to pay up front, rather than an individual’s potential, will increasingly become a determining factor in who can access postgraduate education”. A follow-up report from the Social Mobility and Child Poverty Commission, published in June 2013, reiterated this and described the government’s decision not to commission an independent report as “very disappointing”.

In February 2013, the Sutton Trust contributed to the postgraduate debate with an economic study of the impact of the ‘postgraduate premium’ on social mobility in the UK and the US. The thrust of their argument was that the premium (estimated to be £5,500 per annum) is increasingly unavailable across the spectrum, and that the system as it stands is increasing social inequality. The report focused on the wastage of talent, and the narrowing of the professions as a result of the insistence on a postgraduate qualification as a condition of entry.

In fact, evidence that access to financial support skews access to postgraduate education is also present in the Browne report. Browne quotes Sutton Trust data showing that privately-educated students are almost three times as likely as state-educated students to undertake postgraduate study but concludes that the problem lies with the socio-economic make-up of the undergraduate population. In fact, the data shows that even controlling for access to undergraduate study, there is a significant remaining social imbalance: 14% of the undergraduate population is privately-educated, but this rises to 17% among postgraduates (Browne, p. 55). Whatever the underlying reason for this discrepancy, the result is that privately-educated graduates are around 25% more likely to go on to postgraduate study than state-school educated graduates.

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18 Albeit one to be repaid in income-contingent payments through the tax system and written off if not fully repaid within thirty years.


If candidates from modest backgrounds are effectively frozen out of postgraduate study, then this means that the best jobs and enhanced career opportunities will remain the preserve of the better off. Attempts to widen participation in higher education could prove futile if all that happens is that obstacles to undergraduate study, and therefore graduate careers, are replaced with obstacles to postgraduate study and graduate careers which now require a postgraduate qualification.

**Recent developments: offering solutions**

In October 2011 CentreForum published *Mastering Postgraduate Funding*, a report by Tim Leunig, formerly Chief Economist at CentreForum and now an advisor to the Secretary of State for Education, which called for the introduction of a postgraduate loans system based on the undergraduate model. The Government would loan prospective students £10,000 up front, which would be repaid later through a series of income contingent repayments administered via the tax system (as is the case with undergraduate loans). The postgraduate loan would be repayable on earnings between £15,000 and £21,000, rather than £21,000 plus, as is the case with undergraduate loans. Borrowers would repay £540 a year if their income was £21,000 or more. Leunig predicted that graduates should easily be able to repay their loan over thirty years, and argued that any long-term costs would be outweighed by increased tax receipts attributable to the higher earning potential of postgraduates. We look in detail at the Leunig proposal in Chapter 5.

CentreForum published a follow-up report, *Postgraduate Education: better funding and better access*, in June 2013 which collated views on the means of securing the future of postgraduate study from a range of sector experts: reaffirming the value of Leunig’s loan scheme and looking at the potential of institutional bonds, philanthropic donations and scholarships to stabilise the sector’s future.  

In October 2012, the Higher Education Commission published the final report of their nine month-long inquiry into the future of postgraduate education, chaired by Graham Spittle CBE, Vice President of IBM and outgoing Chair of the British government’s Technology Strategy Board. The report offered a comprehensive overview of the ‘perfect storm’ facing the sector and called for stronger industry links, a bolstering of postgraduate skillsets and the rapid introduction of a targeted postgraduate loans scheme.

Targeted student loans, in this case for STEM students, was also a recommendation made by the House of Lords Science and Technology Committee in their Autumn 2012 report on the state of STEM education. They identified a “triple whammy” of risks:

“There is a potential compound effect of policy reforms on stand-alone Masters provision. The new higher fees regime combined with the lack of student finance is a threat to the number of UK domiciled students who decide to pursue postgraduate education. Added to which, immigration reforms are already having an impact on certain HEIs who may in turn reduce Masters provision significantly.”

In a report published in November 2012, the National Union of Students proposed the introduction of three discrete small-scale income contingent loan schemes which would collectively improve

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access to postgraduate finance. The first scheme would promote access to the professions for those from lower socio-economic backgrounds; the second scheme would constitute an employer-backed student loan scheme, designed to maximise the reach of employer contributions, to postgraduate finance. The final scheme would be more generalised, designed to support “a controlled number of students” through a master’s degree.

The latest contribution to the postgraduate debate came in June 2013 from IPPR’s Commission on the Future of Higher Education, A Critical Path: Securing the Future of Higher Education in England, which emphasised the contribution that postgraduate study makes to the national skills base and economic renewal more widely. It reinforced the case for a postgraduate loans system and also looked at how postgraduate students might be supported should a future government replace higher education tuition loans with a graduate tax.

**Government responses**

The Government has acknowledged the value of postgraduates and the issues with the current funding system, but has been reluctant to commit to either a full funding review or the introduction of new funding mechanisms. Their early response to policy pressure was to focus on encouraging banks to make more postgraduate loans. This has had mixed results – whilst the PCDL success rate has increased over the last 12 months this is due to a significant decline in the number of loan applications received. Indeed, the number of loans offered has actually fallen.

In June 2013, in response to the policy pressures we have identified, the government announced two new funding streams for postgraduate education.

Between now and 2015 HEFCE will make a one-off investment of £25 million in postgraduate funding pilots (through awards to institutions of between £500,000 and £3 million). The pilot programme will prioritise schemes which:

- Address skills needs identified by industry that support the Government’s growth sectors.
- Support the progression of under-represented groups into the professions and into postgraduate research.
- Enhance our understanding of the part-time taught postgraduate economy, of the barriers to the admission and retention of part-time students at this level, and of the ways in which these could be addressed.
- Support students who would not otherwise have undertaken taught postgraduate education.
- Attract matched funding from other sources which would not otherwise have been provided.

From 2015/16, the undergraduate National Scholarship Programme (NSP), worth £50 million per year, will be redirected to support disadvantaged students who want to study for a postgraduate qualification.

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27 R. Ratcliffe. 2013. ‘Minister urges banks to offer more loans to postgraduates’. The Guardian. 27 Feb 2013
28 E. Gibney. 2013. ‘Banks on ‘list of shame’ can expect a visit from Willetts’. Times Higher Education. 18 July 2013.
This interim action is a welcome step, but we believe that a longer-term settlement is needed. Last year, the Universities Minister, David Willetts stated he would “welcome policy ideas on how to finance postgraduate study in future”. This report is intended to rise to his challenge.


CHAPTER 2: ANALYSIS OF THE OPTIONS – CRITERIA FOR SUCCESS

There are three policy objectives underpinning the need for improvements to postgraduate financing. Better postgraduate funding is necessary to:

- Promote upward social mobility and fair access to the professions. Our aspiration is for a postgraduate education system which is open to all students with the required ability and aptitude, regardless of their social background, income or wealth.
- Underpin Britain’s economic future. The Prime Minister has rightly argued that the UK is in a ‘global race’. Economic success requires a population equipped with the high-level skills necessary to attract and retain high-tech investment and jobs. Postgraduate education has a large part to play in up-skilling the population to meet this challenge.
- Secure the future of the UK research base. Postgraduates are the lifeblood of the UK’s research community. The postgraduate taught students of today are the doctoral students, academics and innovators of tomorrow. A vibrant and healthy PGT sector is required to sustain the pipeline of talent feeding both academia and research-intensive businesses.

We will judge potential solutions to the PGT funding challenge against the following criteria. Funding solutions should:

1. **Have a proportionate long-term cost**
   
   In light of the economic climate and constraints on current spending, funding solutions should avoid necessitating large long-term costs for Government.

2. **Have a low deadweight cost**
   
   Funding solutions should avoid crowding out the multiple funding streams that already exist. They should not create incentives for organisations to reduce or remove their current investments in postgraduate education.

3. **Preserve the autonomy of universities**
   
   Funding solutions should not involve excessive additional regulatory burdens for universities. In particular we believe it would be damaging for student number controls to be introduced into the postgraduate sector. We also believe that any solution should ensure that admission decisions are not skewed by considerations relating to a candidate’s ability to repay loans.

4. **Be progressive and have a positive impact on access**
   
   Funding solutions should tackle the financial barriers to postgraduate study identified by Alan Milburn and others. Solutions should avoid providing disproportionate benefits for relatively better-off students at the expense of supporting wider access.

5. **Be scalable**
   
   We are searching for solutions to the postgraduate funding challenge that could work for students at institutions across the full diversity of English higher education. Solutions must either be scalable to work across the sector, or be capable of being part of a portfolio of solutions that, taken together, provide funding options for all students.
6. **Be practical, simple and understandable**

Finally, the package of funding options which we recommend must represent a fair sharing of the costs of postgraduate education across the four principal beneficiaries of postgraduate education – students themselves, society and Government, employers, and higher education institutions.

In the sections that follow we will look in detail at a multitude of systems and new approaches to financing, assessing what contribution they could make to the PGT funding challenge against the criteria outlined above.

We will look both at long-term methods of financing and ideas which could help improve the funding situation in the interim.
CHAPTER 3: TAX INCENTIVES

Tax incentives are used in a number of countries around the world to encourage both employers and individuals to invest more than they otherwise would in education and training. Whilst the UK does have incentives for employers who invest in research and development, educational tax incentives have been almost entirely missing from the debate about the future of higher education funding.

In this section we will focus on incentives designed to encourage individual investment in postgraduate education. In Chapter 7, we will consider whether employers should also be incentivised to provide sponsorship to employees engaging in postgraduate education.

Types of incentive and current usage

There are three main forms that tax incentives could take: 31

Tax relief and allowances

These involve some taxpayers or activities benefitting from lower, or zero, rates of taxation. Relevant expenditure is either deducted from the amount of tax due (tax relief) or deducted from the total amount of taxable income (tax allowance). For example, in Ireland a 20% tax relief is applied to money spent on tuition fees. The size of the relief has different effects depending on the size of overall income. Those from lower incomes, with smaller tax liabilities, are likely to benefit less.

Tax credits

Tax credits involve a fixed sum refunded through the tax system or deducted from the total amount of tax owing – in recognition of expenditure made toward the cost of study. Tax credits provide more equal relief, in that they are payable regardless of the overall size of income and in equal amounts. They tend to be focused on specific groups of taxpayers or activities. For example, the student loan interest deferral scheme which operated in France from 2005 to 2008 allowed graduates to offset 25% of the amount paid in interest during the first five years of the loan against their tax liability, subject to a maximum of €2,000 per annum. If the value of the credit exceeded the tax owed, the difference was returned to the taxpayer.

Tax exemptions

Tax exemptions allow a particular type of income to be exempted from an individual’s taxable income. For example, wages earned by apprentices or students in France are not subject to income tax. Similarly, in the UK, Research Council studentships are also tax-exempt.

Case Studies: Tax incentives in practice

Australia

Australia currently offers tax deductions for education and training activity which is “directly connected” to current employment. This includes both continuous professional development and

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31 Classification adapted from that used in European Centre for the Development of Vocational Training (Cedefop). 2009. Using tax incentives to promote higher education and training.
education “which is likely to result in an increase in income”. The deduction covers both formal education, such as undertaking a course of study at a college or university, and informal study such as attendance at a seminar. Last year, 638,000 people, 5% of all Australian taxpayers, claimed a deduction for formal education.

As Figure 1 shows, the distributional effect of the deduction is uneven, with higher income earners tending to spend more on education and thus claiming larger amounts of relief. In an attempt to rein in spending on this deduction the Government announced in May 2013 that it would impose a cap, of AUS$2,000, on work-related education expense deductions in order to fund increases in investment in secondary education. The Government argues that introducing the cap would “retain an incentive to invest in work or business-related education, while ensuring the deduction is fair and does not provide an opportunity for people to enjoy significant private benefits at taxpayers’ expense”. Much of the debate focused on perceived abuses of the system, such as taxpayers claiming relief on study visits which combined both educational instruction and overseas holiday.

Figure 1: Median claim for formal education by taxable income range 2010-11
(Source: The Australian Government, the Treasury)

The reform was fiercely criticised by the higher education sector and by professional groups, and was dubbed a “tax on learning” by umbrella group Universities Australia. On the eve of the announcement of the 2013 Federal Election the Government said that it would defer the reforms for a year in order to conduct “further consultation on how best to target excessive claims while ensuring the impact on university enrolments and genuine continuing professional development is minimised”.

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33 Australian Government Treasury 2013, p. 5.
United States

The United States offers three main kinds of tax credit for education. The first two of these credits apply on a household basis, so parents can claim tax relief on contributions made to the cost of their children’s education.

- The **Lifetime Learning Tax Credit** is available “for all years of postsecondary education and for courses to acquire or improve job skills”\(^{37}\) and can be used to off-set the costs of educational expenses such as tuition fees, books, supplies and equipment. Taxpayers can claim 20% relief for the first $10,000 of educational expenses. The credit is designed to benefit low to moderate income taxpayers: the amount of credit one is eligible for declines as income increases, reducing to zero once income reaches $62,000 for individuals or $124,000 for married couples.

- The US also offers a **Tuition and Fees Deduction**, which reduces taxable income by up to $4,000, for those earning less than $80,000 per year.\(^{38}\) Both of these credits can also be claimed for educational expenses incurred by dependants.

- Following graduation, students may also be able to deduct student loan interest repayments from their taxable income. This deduction is capped at $2,500 and targeted at taxpayers earning $75,000 or less.

Ireland

The Republic of Ireland offers tax rebates to individuals or to parents for spending on both undergraduate and postgraduate tuition fees. The relief can be claimed at the standard rate (20%) for courses undertaken both in Ireland and overseas, and is capped at €7,000 per annum per course. The first €2,000 of any claim is disregarded.\(^{39}\) Again, this must again be seen in the context of other forms of student support. The Irish Government offers full means-tested grants of up to €6,270 to cover the cost of tuition fees for students with a household income of less than €22,703. Partial grants of €2,000 are also available.

Lessons from international implementation

Lessons from international experience of implementing education tax incentives are not encouraging:

**Distribution of benefits**

The benefits associated with tax incentives for higher education are not evenly distributed. Tax allowances in particular tend to be poorly targeted as, unless reliefs are restricted, they are worth more to those on higher income tax rates, less to those on the basic rate, and potentially nothing to those who do not earn enough to pay tax. Moreover, the benefit will be greater for those with more income to spend on their own education. In the current uncapped Australian system richer taxpayers tend to make larger claims than poorer Australians.

The US Government sought to avoid this problem, and reduce the total cost of education tax incentives, by introducing restrictions on eligibility such that only households with income below a

\(^{37}\) US Internal Revenue Service website:
http://www.irs.gov/publications/p970/ch03.html

\(^{38}\) US Internal Revenue Service website:

\(^{39}\) Irish Tax and Customs website:
ceiling are entitled to claim tax relief. The credit is of limited benefit to many lower income families, who do not have sufficient tax liability to get the greatest benefit from the programme. This has had the effect of concentrating the benefit among the middle class (those earning between $30,000 and $75,000). The Congressional Research Service concludes that “tax credits are regressive in that the more income taxpayers have, the more benefits they receive”.

Targeting the credit at the middle-class meant that the credits system has not had the desired effect on participation levels. An evaluation carried out by Professor Bridget Long, now Chair of the US National Board for Education Sciences, found “no evidence that the policy impacted attendance behavior”. There is also evidence to suggest that some US universities have sought to capture the benefits of the scheme for themselves by increasing charges for tuition. This had the effect of increasing the real-terms cost of tuition for students from families with incomes that are too low to take the maximum benefit from the tax incentive. For these students, study was actually made less affordable by the introduction of the tax incentive.

Complexity

International experience highlights that tax incentives often suffer from being overly complex and have a low profile in the public consciousness. Many people do not claim the relief they are entitled to simply because they either do not understand it is available in the first place, or if they do, they are unsure how to claim it. Evaluations of the US schemes highlight a number of issues arising from the complexity of post-secondary tax provisions. One study found that 27% of those claiming tax credits failed to make the most of the credits available to them. This would be a real barrier to successful intervention in the PGT market: tax incentives cannot have their desired effect, i.e. stimulation of uptake of education, if individuals are unaware of the full potential benefit of a scheme.

Collection and payment

We also need to consider international differences in tax collection practices. In the UK, unlike many other jurisdictions, the majority of the working population does not file an annual tax return – paying their taxes primarily through payroll deductions (PAYE – Pay As You Earn). Thought would thus have to be given to tackling the implementation issues which may arise from this difference – in particular the difference that any lag in tax refunds would have on students’ cash flow.

Costs

Long-terms costs for a tax incentives system are likely to be large unless restrictions on eligibility are incorporated into the system design. Tax incentives involve the state co-funding education rather

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43 Ibid.
than simply underwriting costs – so the long-term costs are likely to be much greater than those associated, for example, with a loan scheme. The scheme would also likely suffer from high deadweight costs, which are an inherent problem when using tax incentives. There will be a number of students who will have enrolled on a course regardless of whether the support on offer was in place, meaning that Government is subsidising activity that would have happened anyway. At a time of austerity, a more targeted intervention would provide better value for money.

Conclusions

Tax credits score poorly against the tests we set out in Chapter 2. In the international examples considered above, the policy objective underlying the creation of the tax incentives was a desire to see an increase in participation, i.e. an increase in demand for education. The principal challenge in the UK postgraduate taught market, whether we have enough latent demand for postgraduate education, is one that is rarely raised. The findings of the longitudinal Futuretrack survey suggest that there is a large amount of demand for postgraduate education among UK-domiciled undergraduate students, but insufficient financial assistance to convert that demand into enrolments.

This is less of an issue in Australia and the US, where the tax incentive schemes co-exist alongside state-supported loan systems. In Australia, students can make use of HELP (Higher Education Loan Program), an index-linked student loan system which covers both undergraduate and postgraduate study. In the United States, as we explore in the Appendix, students are able to benefit from a multitude of other sources of financial support, including federal loans and institutional schemes.

Tax incentives would not tackle the access to finance issue, as the experience of the French Government demonstrates. Between 2005 and 2008, France offered a tax deferral for students taking out private loans to finance their education. The benefit offered a tax credit of 25% of the amount paid in interest during the first five years of the loan. The scheme was little-used because students were unable to persuade banks to make loans. The Government subsequently scrapped the scheme and introduced a new scheme whereby the Government provided guarantees for bank loans, although the take-up of that scheme has also been poor.

Were tax incentives to be used as the only policy intervention in this area, there would be a risk that they would cement or even exacerbate existing inequalities by cutting the cost of higher education for those able to access credit or other sources of finance, whilst leaving credit-constrained students still unable to access postgraduate provision. They would only work as an additional measure, alongside other policy interventions to free up the supply of credit to prospective postgraduate students. As Cedefop has argued, incentives work better “as a supplementary measure rather than the main instrument in the policy-makers’ arsenal”.

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48 Cedefop. 2009. Using tax incentives to promote higher education and training.
49 Ibid, p. 1
CHAPTER 4: LOANS – NON-GOVERNMENT OPTIONS

Much of the recent policy literature on funding postgraduate education has concentrated on increasing the availability of loans for students wishing to undertake postgraduate study. Loans are the starting point for almost all analyses – there is near-universal acceptance that postgraduates should make a contribution towards the cost of their study. Even the National Union of Students, who have opposed student contributions in other contexts, have called for the introduction of a loan scheme for postgraduate taught students.

Problems with the current loan system

There are two ways in which banks currently lend to postgraduate students. Two banks, Barclays Bank and the Co-operative Bank, participate in the government supported system of PCDLs. The Government pays the interest accruing whilst the postgraduate is studying and the student becomes liable to begin repayment, and liable for interest, one month after the end of their course, regardless of their employment status.

Additionally, a number of banks offer professional loans which operate outside the PCDL scheme. These are overwhelmingly designed for courses which are likely to add significant value to a graduate’s earning potential, such as an MBA or a course related to the legal profession. For example, the Bar Council offers a “Preferential Loan Scheme” in partnership with HSBC that offers loans of up to £25,000, no repayments during study (although interest does accrue) and a six month moratorium on repayments after the end of the course.50

Lack of availability

The PCDL system suffers from a number of problems, which for the most part are attributable to a lack of information by lenders about a student’s circumstances. The principal problem is lack of appetite by the banks to make loans. Graduating students will often have little by way of previous earnings or credit history. What employment history they have may bear little relation to their post-graduation earnings potential. They may not have collateral. This makes them, according to conventional lending criteria, poor credit risks. This is, in turn, reflected in the relatively high interest rate.

As Chris Hearn, Director of Education at Barclays Corporate, stated in an interview with *Times Higher Education* in 2012:

"The cost of [loan] facilities reflects the risk. If we've got graduates who don't have an earnings track record, or a strong earnings track record, it is going to be difficult to find the right price to lend into that client group if they go into postgraduate study."51

Conversely, postgraduates with good credit histories, sustainable incomes and collateral will probably find that there are more affordable sources of credit available than PCDLs. Nonetheless, financial advisers sometimes recommend that such students should still apply for the PCDL in order to take advantage of the interest-free period, immediately taking out a cheaper commercial loan and repaying the PCDL upon completion. Indeed, a leading financial website suggests that those who do not need a loan at all should take out a PCDL in order to reinvest the money during the interest-free period and then repay it before the interest becomes repayable. This suggests that PCDLs are poorly

50 http://www.barcouncil.org.uk/becoming-a-barrister/finance-and-funding/funding-and-scholarships/
targeted: failing to provide support for those who need it most, while channelling public support to better off students who do not need it.

PCDLs are not limited to postgraduate qualifications, but are only available for courses which have been accredited by the Skills Funding Agency as vocational qualifications. This has the somewhat surprising result that students cannot obtain a PCDL for certain professional qualifications and non-vocational masters’ courses, but can obtain it for diplomas in Chinese homeopathy.52

Critics have identified two other major problems with the current loans. The requirement that repayment begins almost immediately after graduation can be problematic for those who have not already secured employment at the end of their course. The 2012 report by the Higher Education Commission suggested that banks should consider allowing students to apply for repayment holidays in order to allow them to transition to sustainable employment rather than having to take the first job offered, however unsuitable. Secondly, questions have been raised as to whether the £10,000 maximum loan is enough – with the average PGT fee now standing at £5,93853 and many institutions charging much more, it is often the case that even students awarded a full PCDL loan still have to search for other additional sources of funding in order to be able to undertake study.

A shrinking market

There is limited competition within the postgraduate loan market, with the number of banks operating both types of loan having fallen over time. With the departure of the Royal Bank of Scotland from the PCDL scheme, postgraduate loans are now only offered by two financial institutions. Even the professional market is not seen as sufficiently attractive by some banks, with NatWest terminating agreements with the Association of MBAs and a number of Law Schools in 2011, citing “transformation of the personal loans market”.54

The Higher Education Commission’s report highlighted the low rate of success enjoyed by prospective students applying for PCDL loans. This trend has been a source of frustration for the current Universities Minister David Willetts, who has called on banks to “step up to the plate”55 and offer more loans to postgraduate students. Since the report was published the success rate has increased dramatically, from 44% to 76%; unfortunately this is due not to an increase in bank lending, but to a huge reduction in the number of students making applications. Indeed, the number of loans made actually fell last year.

<table>
<thead>
<tr>
<th>Financial Year</th>
<th>Loan applications</th>
<th>Loans offered</th>
<th>% success rate</th>
<th>Loans taken up</th>
<th>% taken up</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009/10</td>
<td>20627</td>
<td>12,239</td>
<td>59%</td>
<td>8320</td>
<td>68%</td>
</tr>
<tr>
<td>2010/11</td>
<td>19229</td>
<td>8333</td>
<td>43%</td>
<td>7679</td>
<td>92%</td>
</tr>
<tr>
<td>2011/12</td>
<td>22716</td>
<td>10105</td>
<td>44%</td>
<td>8884</td>
<td>88%</td>
</tr>
<tr>
<td>2012/13</td>
<td>12784</td>
<td>9733</td>
<td>76%</td>
<td>8338</td>
<td>86%</td>
</tr>
</tbody>
</table>

Figure 2: Availability of PCDLs

Stimulating bank lending

Higher education is not the only area which suffers from a lack of bank lending. Banks have also been criticised for their failure to make loans to small businesses and to first-time buyers. In the mortgage market, loans have been made available with parental assets acting as a guarantee, but utilising this approach in higher education would raise issues of inequality, given that it will typically be relatively advantaged borrowers who are able to obtain such guarantees.

The banks may have more appetite for lending if part of the risk is shared with other bodies. We are unlikely to see any large-scale increase in bank lending without risk-sharing.

Risk-sharing with Government

Risk-sharing has been used by a number of Governments as a means of providing higher education finance. In the United States, the Federal Family Education Loan Program was a mechanism through which the Government made payments to lenders making loans to students, guaranteeing them

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56 Adapted from HE Commission. 2012. Supplementary data for 2012/3 obtained from the Department for Business, Innovation and Skills.
against “significant loss in the case of default” and funding some of the administration costs.\textsuperscript{57} The scheme was scrapped by President Obama in his first term. He described it as a “system that's rigged to reward private lenders without any risk.”\textsuperscript{58} Loans are now instead being made directly from federal lending; a reform which the Congressional Budget Office has estimated will save $86.8 billion between 2010 and 2019.

A similar system was introduced in France in 2008, after a loan interest tax credit initiative failed because students were unable to persuade banks to make loans. Government-guaranteed loans of up to €15,000 are now being made available to students by four French banks. The Government guarantees 70% of the capital of the loan, excluding interest, although European data suggest that take-up of this loan is very low, with just 0.1% of the student population taking out such a loan.\textsuperscript{59}

One option might be to incorporate postgraduate lending to banks into the government’s flagship Funding for Lending scheme. This scheme, the successor to the £40 billion National Loan Guarantee Scheme, is designed to encourage banks to lend to small businesses and those looking to obtain a mortgage by allowing them to borrow from the Bank of England at below market rates. The scheme is structured to be low-risk to Government and the Bank of England, with banks themselves remaining responsible for the risk on individual loans they make. There is therefore no guarantee that inclusion of postgraduate loans in such a scheme would make postgraduates more attractive to banks and thus boost lending. Indeed, critics have argued that Funding for Lending has done little to encourage banks to lend to small businesses: analysis of lending figures by the Financial Times suggests that whilst homeowners have benefited from the scheme “the UK’s banks have continued to lend less and less to the country’s smaller companies.”\textsuperscript{60} This suggests a clear preference by the banks for more secured lending, such as mortgages, over unsecured personal loans.

For government risk-sharing to work, a more specific arrangement, similar to that operated in France whereby Government gives a specific guarantee, is likely to be necessary. It is worth noting that there is a small amount of risk-sharing in the current PCDL system, with the cost estimate for the scheme including a small provision for ‘defaults’.\textsuperscript{61} There is considerable uncertainty surrounding whether more substantial risk-sharing would be feasible, with much depending on the ability of Government and banks to reach a mutually acceptable agreement.

Firstly, there is no guarantee that risk sharing would increase lending rates to the prospective students who are currently struggling to obtain credit under the existing PCDL scheme. The design of the scheme will have an impact on the lending decisions of the banks. If banks remain liable for a significant portion of default they are likely to remain conservative in their lending policies. Banks could conceivably continue to lend to the same profile of student they are lending to at the moment.

Secondly, this type of lending, as the United States has found, is likely to be more expensive than direct provision of loans. The cost implications associated with the scheme also limits the scale of any risk-sharing solution considerably. For larger scale solutions there are other sources of finance which would be more appropriate. This solution is also unlikely to be useful as a vehicle for directing targeted investment and access to credit to those groups currently struggling to obtain it.

\textsuperscript{58} http://www.whitehouse.gov/the_press_office/Remarks-by-the-President-on-Higher-Education/
\textsuperscript{60} T. Powley & C. Jones. 2013. ‘Funding for Lending Scheme viewed as a mixed success’. \textit{Financial Times.} 12 Aug 2013.
The uncertainties surrounding this scheme make it very difficult to evaluate it against the criteria which we set out in Chapter 2, but it is very hard to envisage how government sharing risk with the banks could provide a satisfactory solution to the postgraduate funding challenge. Any government contribution could be more usefully spent elsewhere.

**Risk-sharing with institutions**

An alternative might be for risk to be shared with universities. This scheme might be structured in a number of ways. Universities could agree to underwrite the first £X of any loss through default, or the university and the bank would agree how losses would be apportioned between themselves. Another option might be a hybrid solution, with both Government and universities underwriting the risk together. This is an idea which is explored in a 2010 Policy Exchange report\(^{62}\) which considers the potential role for private finance in undergraduate education. The report proposes the establishment of a private loan system backed by a ‘reserve fund.’ The reserve fund, which Government, donors and universities would pay into, would share some of the risk associated with the student loan system – leading, in theory, to more appetite among the commercial banks for lending to students at competitive rates.

Both of these systems do carry risks. With either of these options universities would have to earmark funds to cover non-repayment. These funds would either have to be found through reallocation of existing spend or through new forms of income. It may be necessary for institutions to pass on some of this risk through a small increase in postgraduate fees. In effect, this would be a limited sharing of risk between cohorts of students, rather than sharing of risk with the university.

Furthermore, if universities sought to minimise losses on loans in order to reduce the costs of the scheme, there would be a risk that the scheme would lead to distortions in decisions on admissions, such that an incentive would be created for universities to admit, and make loans to, those more likely to repay their loans. Barr and Shephard suggest this could be avoided through pooling of risk amongst institutions\(^{63}\) – but there is not likely to be appetite for this across the full diversity of the current UK higher education sector. There may be scope for smaller groups of similar universities, perhaps on mission group lines, to establish collaborative arrangements between themselves and a financial institution. This would also bring the added benefit of allowing administration and start-up costs to be shared across the group of institutions.

As with government risk-sharing, the feasibility of such a scheme will come down to whether universities and banks were able to agree on mutually acceptable terms. One of the benefits of university-led bank lending would be that universities, who are more attuned to the financial pressures of their students than Government are, may decide to target lending on a particular group of prospective students who presently face difficulties in obtaining finance. This could include, for example, those who are hoping to progress into research careers or other professions.

In the immediate term initiatives such as this are likely to be small. The lack of certainty around the future of postgraduate funding is not conducive to institutions making investments in larger-scale schemes. In addition, as we highlight below, institutions wishing to create larger-scale schemes might secure better value for money through pursuing other methods of financing. There are also doubts around whether stimulation of banking lending is a full system solution, with significant uncertainty around the affordability of risk-sharing for institutions with less attractive risk portfolios. For some universities, the cost could be prohibitive.

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\(^{63}\) N. Barr & N. Shephard. 2010. *Towards setting student numbers free.*
Institutional lending

An alternative means of financing loans may be for institutions themselves to make loans, using money obtained either from donations and philanthropy, or from the capital markets. Such loans, provided at competitive rates of interest, would provide an alternative to the existing system of PCDLs.

Universities would need to forge partnerships with financial institutions to make such a scheme work. Financial institutions are likely to bring expertise in areas such as managing collection and default that universities are unlikely to have, as well as play an important role in sourcing financing for the scheme.

Sources of finance

Although some universities in the US do use donated funds to finance loans, for most UK universities this would be unattractive. Firstly, as we explore further in Chapter 7 there are huge differences in the philanthropic income universities generate, with Oxbridge alone accounting for over half of philanthropic giving to the UK higher education sector. Furthermore, reliance on philanthropy to fund lending would reduce the potential scale of a scheme – a larger-scale loans scheme would require larger amounts of working capital.

Increasing conservatism in bank lending has led a number of other sectors to shift the focus of their lending toward the bond markets. Social landlords, for example, who have traditionally obtained 89% of their finance requirements from banks, are increasingly issuing their own bonds or participating in club deals. Analysis by Ernst and Young suggests that larger companies across the EU are similarly looking to the bond markets, though the report also concludes that this is not a realistic response for smaller and medium-sized organisations.

Banking professionals forecast strong demand in the bond markets for financial instruments issued by universities. A number of commentators, most notably Jon Wakeford of universities’ estates company UPP, have suggested that universities could leverage their strong financial position to raise funds from the markets at a comparable rate to Government. This could be used to provide a facility for student loans at rates below those currently offered commercially. As figure 3 shows, a number of universities have recently raised substantial funds for new capital projects through the bond markets at competitive rates of borrowing.

64 See for example, Auburn College, Alabama
http://www.auburn.edu/administration/business_office/loans/institutional.html
66 ‘Club deals’ involve a third party issuing bonds on behalf of a ‘club’ of several borrowers.
68 For example, Chris Hearn, Education Director at Barclays Corporate has previously stated that demand for such products would “be enormous.” [A McGettigan. ‘The Third Revolution. Part 2 – Bonds: the market’. Research Fortnight. 21 September 2011.]
**Figure 3: Sample of the capital raised on the bonds market**

It is likely that institutions would need to collaborate in order to reach the scale required to make a bond issue viable. Whilst there is disagreement among financial experts about how large this minimum viable size is, most estimates range between £100 million and £300 million. Subsequent issuances could be done on a smaller scale through ‘taps’ which involve selling bonds from a previous issue. Collaboration would also have other benefits beyond cost-sharing. Through collaboration institutions would be spreading the risk associated with the scheme across several institutions.

**Challenges**

There are a number of challenges posed by bond financing.

Firstly, there are concerns that bond issuances are insufficiently flexible because it is very difficult to renegotiate the terms of a bond issue. Conditions attached to bond instruments are usually less stringent than those required by banks – so it is unlikely that the loan targeting policy, for example, would be incorporated into the issuances’ terms.

Secondly, at least one university leader has expressed concern about the impact the institutional lending might have on their ability to manage other aspects of their finances. Referring to the need for institutions to borrow for capital investment and to meet the liabilities of the Universities Superannuation Scheme pension fund, Dame Glynis Breakwell, Vice Chancellor of Bath University, characterised the existing financial demands being placed on universities as a “a series of things being stacked, one on top of another, which assumes that we [universities] are a good credit bet.”

Thirdly, a number of commentators have argued that a government guarantee is needed to make university bonds more attractive to investors. This is likely to dampen government enthusiasm for such initiatives.

Finally, there is uncertainty surrounding whether this will be a viable option for all institutions within the higher education sector. Inevitably, some institutions will be more attractive to the bond markets. It may be that for less attractive institutions the cost of borrowing proves prohibitive. So, whilst institutional lending could be a solution for some universities it is probably not a system-wide solution.

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Employer Funding

Another potential source of financial support for postgraduate study is a prospective student’s employers. Financial support may take the form of sponsorship, or alternatively lending on competitive or preferential terms.

Just as some employers offer interest-free loans for travel season tickets, employers could consider offering finance to employees, to be repaid on similar terms or perhaps over a longer period, in order to cover the cost of tuition fees for postgraduate courses being studied on a part-time basis. The Treasury has recently doubled the cap on the size of the loans that employers can offer tax-free to employees to £10,000, making this a more realistic and attractive option. We have previously argued that HM Revenue and Customs should consider providing an extra-statutory concession for employer loans made to cover the costs of study at Higher Education Institutions. The cost of this would be negligible, with a small amount of tax revenue foregone on notional interest rates for loans advanced worth more than £10,000.71 The concession could send an important signal about the value of postgraduate education to both Government and employers.

Recommendation: HM Revenue and Customs should encourage employers to support postgraduate education by removing the £10,000 cap on the extra-statutory tax concession for employer loans towards the cost of study at Higher Education Institutions. Such loans could be used to meet course fees, living costs and other expenses.

As one element of their tripartite proposal for postgraduate finance, which we highlighted in Chapter 1, NUS proposes the creation of a new employer-backed student loan scheme, designed to maximise the reach of employer contributions to postgraduate finance.72 Under the proposal, loans would be made by Government, but participating employers would be required to pay an upfront cash fee, equivalent to 12% of the loan amount. This fee is designed to cover the estimated collective RAB charge on the loans, thus transferring the risk of non-repayment from Government to employer. NUS argue that the scheme would allow employers to underwrite loans for around 10 employees at the same cost as covering the course fees of one employee in full. This scheme would also provide a cashflow benefit for firms who already offer employee loans.

This model has merit, but has currently only been developed to outline policy level. Without further detail on the likely parameters of the scheme, it is difficult to accurately model how it is likely to operate and verify the estimated RAB charge. It is vital that the RAB charge estimate is accurate, as the costs of any variance would almost certainly have to be met by the taxpayer. We would also need to develop a better understanding of the impact that such a scheme would have on employers’ and employees’ behaviour. A number of employers may, as NUS state, use the scheme to leverage their existing financial commitment over a greater number of employees. Some may be able to offer financial support for postgraduate study to their employees for the first time as a result of the scheme. Others may choose to ‘bank’ the cashflow benefit the scheme would bring, rather than offer finance to a greater number of employees. Turning to employees, there is a risk that participation in postgraduate study could decline for certain groups, particularly those with families and other existing financial commitments, if they were asked to take out loans, rather than benefit from direct employer funding.

72 NUS. 2012.
Philanthropy-backed loans

Research and testimony from both employers and graduates suggest that there are a number of fields and professions where postgraduate qualifications are becoming a de facto requirement for initial employment. There is a strong case to be made for engaging with employer and professional bodies in these sectors to explore what the sector itself can do to overcome the barriers to the profession which the lack of postgraduate financing currently poses. There is a case for the professions to make direct investment in those seeking to enter the field – either through sponsorship, which we explore further in Chapter 7, or through making loans available.

NUS, as a further element of their tripartite blueprint for postgraduate funding, proposed a distinct loan system being established for students seeking to enter the professions. Loans would be restricted to students who were eligible for the full maintenance grant as an undergraduate and, in order that the system did not lead to an oversupply of graduates in each area, “could demonstrate high levels of academic achievement and a clear ambition and propensity for the profession in question”. NUS envision that the scheme would be run in partnership with professional bodies, and would also seek “philanthropic investment from the private sector” such as employers, but that “government should incur any cost of failure to repay, as part of the social mobility agenda”.

This model also has merit – but its success or otherwise hinges on securing buy-in from employers and professional bodies in the relevant sectors. In order to encourage such collaboration, we recommend the creation of a Council for Universities and the Professions to bring together representatives of the main professional bodies with representatives from higher education institutions and Government. In the first instance, the committee would be charged with monitoring take-up of postgraduate courses in professional disciplines, making recommendations, and encouraging profession-wide mechanisms of financial support for students.

Recommendation: Representatives of the HE sector and the main professional bodies should establish a Council for Universities and the Professions to monitor take-up of postgraduate courses in professional disciplines, and encourage the introduction of profession-wide mechanisms of student financial support.

Conclusions

The options considered in this chapter could, individually or collectively, contribute to a loosening of the flow of credit into the student financial system. However, there are a number of disadvantages in pursuing these options, rather than government-supported loans. There is a real risk that the funding system would continue to be a patchwork with substantial funding gaps. A number of students will still wish to attend a university which has not put its own financing arrangements in place, and they will be unable to obtain finance from a bank, an employer or a philanthropic organisation. For these students postgraduate education will continue to be out of reach. For this reason, the government should actively consider the case for state-backed student loans, which we will consider in detail in the next chapter.

73 HE Commission. 2012.
74 NUS. 2012, p. 9.
CHAPTER 5: GOVERNMENT-BACKED LOANS – DEVELOPING THE LEUNIG MODEL

In the last chapter we considered a number of ways in which loans could be made available to students without government intervention, concluding that whilst it could be done, a larger-scale scheme should also be considered. Such a scheme would bring a number of benefits:

Firstly, it is likely that Government will be able to secure finance for a large-scale scheme on far better terms than institutions or employers could achieve for smaller-scale schemes.

Secondly, the risk profile of a larger-scale scheme is likely to be more balanced. Loans made to students who have a lower prospect of paying off the entirety of the loan are hedged by loans made to those likely to become high earners. The risk profile of smaller-scale schemes is likely to be less balanced.

Thirdly, there is also a risk that the cost of underwriting these loans means that employers and institutions choose not to offer other forms of financial support to postgraduates. If a well-designed postgraduate loan scheme was in place the money which would otherwise be spent by institutions on providing loans could be spent, for example, on targeted scholarships and bursaries.

Finally, a system of discrete loans schemes would be more complicated for students to navigate than a single system.

For these reasons we believe that the Government should consider introducing a government-supported student loan scheme.

The Leunig Model

A number of schemes have been proposed in the past two years, of markedly different scales. Below, we will explore and develop the most oft-cited option, which was first proposed by Tim Leunig.\(^{75}\)

The CentreForum model is a large-scale scheme, under which students would be able to borrow up to £10,000 towards study for any subject. CentreForum caution against restricting eligibility on the basis of subject which they characterise as “picking winners”.\(^ {76}\) They suggest instead that the principal limitation on the scheme should be restricting loan eligibility to those who have attained a first class or upper second class undergraduate degree. This approach has also been endorsed by the Institute for Public Policy Research.\(^ {77}\)

As noted earlier, the cost to the Government of underwriting undergraduate loans is reflected in a RAB charge. This is not direct expenditure, but results from the cost to Government of writing off loans which are not fully repaid because students are lost to the system, die, or fail to pay off their loan within thirty years. The CentreForum proposal would result in higher repayment rates and a lower RAB charge than undergraduate loans for a number of reasons.

Firstly, loans would be restricted to graduates with a first or upper second class degree. BIS data suggest that graduates with a First or 2:1 earn between £48,000 and £62,000 more over their

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lifetime than a student with a 2:2, and consequently are far more likely to repay their student loan in full.  

Secondly, those with postgraduate qualifications are more likely to be in work than graduates, are likely to earn more, and are more likely to repay their loan in full.

Thirdly, loans would be limited to UK students. Around one in five EU students cannot be traced by the Student Loans Company, compared to around 2% of UK students, which means that loans to such students carry a much higher RAB charge.

Fourthly, repayments would begin when the student was earning £15,000, not the current £21,000. Since the number of graduates who earn over £15,000 is necessarily higher than the number earning over £21,000, this would prioritise repayment of the postgraduate loan.

Using the Government’s own ‘ready reckoner’, which estimates the cost of student loans on the basis of 4,500 modelled student careers, CentreForum estimates that the up-front costs to the Government of its proposal would be between £0.5 billion and £1 billion per annum, but that the long-term costs would be outweighed by increased tax receipts attributable to the higher earning potential of postgraduates.

CentreForum note that the figures used in its report “will overstate the loss to government because it includes in its estimation of lifetime incomes both graduates with weak first degrees, and graduates with no master's degrees. Were we to have access to data that was restricted to graduates with good first degrees and masters’ degrees we would find lower losses”.  

Our modelling confirms that the RAB charge for each loan would be in the “£100s, rather than £1,000s”, as CentreForum suggest.

Although BIS’s modelling of lifetime earnings does include a factor for whether a student goes on to postgraduate study, this is not included in the ready reckoner. As a proxy, we identified from the 4,500 modelled students those whose earnings in the first year, or first to third years, after qualification were zero, but subsequently had an income (so as to exclude students who died or were permanently incapable of earning). On an assumed undergraduate debt of £30,000 the cost to Government is £6,684. If an additional £10,000 were borrowed, but the repayment threshold dropped to £15,000, the combined cost of borrowing for both degrees rises to £7,652.

That is to say, the effective cost of funding an additional £10,000 loan over thirty years is £968: not on its own cost-neutral, but relatively small. To put it in context, the amount is less than the current cost to Government of meeting just the first year's interest on a PCDL.

As an alternative, we modelled the impact of the changes if they were applied to students in the top third of lifetime earnings (reflecting the impact of the ‘postgraduate premium’ on lifetime earnings). These students have a negative RAB charge of 2% (i.e. the Government makes a small profit on the

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79 Although undergraduate loans for tuition are available to EU students, the maintenance element is not and government-backed Professional and Career Development Loans are likewise limited to students who are ‘settled’ in the UK. J. Clappison. Hansard (Commons). 5 March 2013. Col. 922W; Student Loans Company. Income contingent repayments by repayment cohort and tax year 2000/01 to 2010/11 inclusive (provisional). 19 June 2012. http://www.slc.co.uk/media/333186/slcosp022012.pdf
80 T. Leunig. 2011, p. 36.
loans). If the repayment threshold is lowered, but the loan increased and the first year’s income reduced to zero, the overall result is to raise the RAB charge to zero. Again, this results in an additional cost of just a few hundred pounds—less than the first year’s interest on a PCDL.

On this basis, we estimate that the maximum cost of providing a loan system to cover 45,000 students for a year’s postgraduate study would be £43.5 million. The system could be fully-funded by scrapping PCDL loans for master’s study and redirecting funding for the National Scholarship Programme.

Reducing the cost – increasing repayment rates

This is not the end of the story, because a successful loan system would hopefully have far greater take-up rates than PCDLs (indeed, Leunig’s costing would seem to imply take up of between 50,000 and 100,000 students a year). Even if the per unit cost were less than current support for PCDLs and the National Scholarship Programme, the overall cost to Government could be greater. How might the cost be kept down further?

One approach would be to collect repayments at a higher rate than the 9% of salary applied to undergraduate loans. As borrowers would repay more of the loan when earning, reform would result in students repaying their loan at a faster rate. Consequently, periods of non-repayment, for whatever reason, would be less significant and so the change would reduce the likelihood that loans would not be fully repaid within thirty years. In theory, applying a second repayment rate of 9% to the postgraduate loan, for instance, would cut the RAB charge by as much as half. This cannot be accurately modelled within the confines of the ready reckoner, which allows only a single repayment rate. If this is set to 18% the RAB charge is more than halved, but this assumes that the 18% rate continues once the postgraduate element is repaid.

Leunig rejects this approach on the grounds that it results in high marginal repayment rates. For instance, once basic and higher rate income tax are taken into account, a 9% additional repayment for postgraduate loans would result in an overall marginal withdrawal rate of 50% of the borrower’s salary. He accepts that pre-2012 undergraduates (who already repay 9% of their salary over £16,365) should repay an additional 9% between £15,000 and £21,000 towards their postgraduate loan. Levied alongside income tax and National Insurance it would mean an effective marginal withdrawal rate of 50-60%. He argues that it is acceptable because the scheme is voluntary, and cheaper than anything else available.

This argument applies equally to post-2012 students. Even with a repayment rate of 18% of salary over £15,000, the total repayment on a postgraduate loan would still be less than for PCDLs, where repayment of capital and interest on a £10,000 loan would be around £2,500 a year. Indeed, a combined 18% repayment rate would still be lower than those on a PCDL for earnings up to £42,000. Beyond this point, which corresponds to the higher rate threshold, borrowers would face a marginal deduction rate of 60%. We do not believe that it would be feasible to levy a high rate of withdrawal beyond this threshold.

A more fundamental problem is that the Government makes a small profit on undergraduate loans to higher earning graduates (due to the income-contingent interest rate). If the repayment rate were increased, the loan would be paid off sooner, and the scope for profit would be reduced. Borrowers would be repaying more of their debt while on the lower levels of interest, leaving a smaller level of debt to accrue interest once their earnings put them at the higher rate.
Reducing the cost – rolling loans together

CentreForum envisages that the undergraduate and postgraduate loans should operate discretely. Alternatively, postgraduate and undergraduate loans could be rolled together for higher earners, such that once a graduate has finished repayments on one loan, he or she would continue to make repayments towards the other loan at a rate of 9% of all income above the £15,000 threshold. This would increase repayment rates, and bring down the cost to Government of underwriting the loans.

Such a measure would probably only be practical if the two loans were rolled together and administered jointly by the Student Loans Company (SLC). There is some uncertainty as to whether the SLC is capable of administering two loan schemes – although these concerns may not preclude combining two debts into a single liability.

The SLC now administers FE loans and PGCE loans as well as three different types of undergraduate loans (with the various funding differences which apply to loans in England, Wales, Scotland and Northern Ireland). On this basis, we believe that it should be possible for the SLC to administer a ‘rolled up’ postgraduate loan system.

Reducing the cost – loan targeting

The Government could also go further in targeting support at those both most likely to be suited to postgraduate study and most likely to repay their loan. The RAB charge for individual students is highly variable. For almost a third of students in the BIS modelling it is negative: the Government makes a profit on their loan. For the top earning third of students the RAB charge is, on average, zero.

On the basis that most masters’ students will have good first degrees, this is likely to mean that support would be automatically targeted at those with the best repayment prospects. There is a risk that if a new scheme of support were available, some institutions may seek to recruit a broader range of students with less good first degrees. To guard against this risk, Leunig proposes that the scheme is limited to those with a first or upper second class degree.

A number of other organisations have called for a more targeted loan scheme. The Higher Education Commission argued that although the total cost per loan is low, the current fiscal constraints militate against a universal scheme – and that loans should instead be targeted at access to the professions and subjects where the UK needed to develop a competitive advantage. This argument carries less weight if, as we discuss above, the long-term cost of the loan could be reduced.

The Higher Education Commission also impressed the need to avoid deadweight costs and expressed concern that a universal scheme would “crowd out existing funding streams.”81 This is a concern echoed by the IPPR who warn that “some employers who currently support students to take masters’ courses (such as the NHS) may stop offering support if they believe graduate students can take out a loan instead”.82 As we noted in Chapter 2 the solution to the PGT funding challenge needs to be nuanced. Other interventions, which we highlighted in Chapter 4, could be used to prevent employer exit.

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81 HE Commission. 2012, p. 64.
82 IPPR. 2013, p. 142.
Benefits

Extending state-backed loans would enable the Government to generate savings by scrapping support for PCDLs for postgraduate study. The Government currently spends £15 million on support for PCDLs, including programme costs, underwriting and the first year’s interest. 90% of these loans are used for postgraduate study, although, as we have seen, they are poorly targeted. By restricting PCDLs to courses which are not eligible for postgraduate student loans, the Government could save as much as £12 million a year.

Furthermore, since interest would accrue immediately, there would be no incentive for better off students to take out loans in order to take advantage of the interest-free period, with a view to repaying as soon as interest becomes payable. This would eliminate what is currently a direct transfer payment from the Government to students who do not need support.

While more detailed modelling using up-to-date projections of lifetime earnings is necessary, a scheme along the lines proposed by CentreForum would appear to be financially viable. Whether this scheme could be strictly cost-neutral would depend on how successfully it could be targeted at the best and brightest students. Given the potential savings to be made from scrapping PCDLs for postgraduate courses and redirecting the funds allocated for the new National Scholarship Programme for postgraduates, we are confident that a modified version of the Leunig scheme, where the loan is rolled up into the undergraduate loan, could be achieved at no aggregate cost to the taxpayer.

Impact on regulation

Responses to the various loan proposals which have been published in the last two years have a number of risks. We will consider policy responses to the two principal risks, the impact on regulation and the impact on tuition fees, in turn.

Responding to a House of Commons debate on postgraduate education in January 2013, the Universities Minister, David Willetts stated that:

“The biggest single risk is that as soon as we had a general public expenditure programme or loans scheme, the Treasury would immediately become interested in how many people were eligible, controlling postgraduate numbers and setting new conditions. It would be a great pity if this open and diverse sector found itself with a highly regulated loan scheme that constrained its growth.”

We agree with the Minister that a centrally planned system of funding would be undesirable. The adjustments to the design of the scheme and the terms of repayment which we propose render the long-term cost of the scheme so low as to avoid the need for additional regulation. There is already a cap on total numbers built in to the system – in that it is proposed that loans are restricted to students achieving either a first or upper second class degree. Any attempt to introduce a system of student number controls would be disproportionate and wasteful. We also note that the Government has not introduced number controls to deal with the expansion in novel four year integrated masters’ courses, notwithstanding the £80 million or so that it incurs underwriting loans.

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84 David Willetts. Hansard (Commons). 23 January 2013. Col. 438
for the masters’ years, although HEFCE have indicated that they are ‘monitoring’ increases in course length.

**Impact on tuition fees**

There is a risk that institutions may respond to the introduction of a student loan system by raising tuition fees, recognising that students now have a greater ability to pay fees. This would defeat the purpose of introducing a loan scheme – if fees were to be increased substantially, it would leave many students still unable to easily access postgraduate education, despite having access to a loan.

This risk has been identified by HEFCE, who have noted that “the scope for institutions to increase PGT tuition fees may be limited because publicly funded loans are not generally available to meet upfront costs”.

There is also evidence on this phenomenon from the United States, where some US universities have sought to capture the benefits of tax credits and subsidised loans by increasing tuition fees. In the case of the tax credit programme, this combination of actions perversely had the effect of making higher education less affordable for students from low-income families, as their household income was too low for them to get the maximum benefit from the tax incentive.

There is also a risk that large increases in fees could have a deterrent effect, whereby students decide not to enter postgraduate education. Research recently published by the Spatial Economics Research Centre at LSE suggests that “higher fees reduce student demand for postgraduate places” with a 10% increase in fees being associated with “a reduction in the probability of progressing to a postgraduate degree of between 1.7% and 4.5%”. This research only considers direct progression immediately from undergraduate to PGT study. Further research is required to investigate the motivations of older students as well as the reasoning underpinning these results – are students being deterred by the prospect of debt per se, or lack of access to finance?

There are a number of policy options which have been put forward to counter this:

- Tim Leunig suggests that offering a fixed amount of loan, which does not increase if fees increase, will preserve students’ incentives to ‘shop around’, leading to an increase in postgraduate places rather than postgraduate fees.
- NUS have suggested a hard cap, with universities wishing to participate in a loan scheme agreeing to keep fees for eligible courses to an agreed level, which they suggest should be £6,000.
- An alternative would be to create an expectation that universities who charge higher than average fees put in place suitable arrangements to supplement the financing available through a student loan scheme. This might include some of the measures we discuss above – such as scholarships and fee waivers. This could be made a condition of participation in the loan scheme. Existence of other forms of finance may provide more space for universities to better target their own support.

On balance, we believe that the first option is preferable. Capping course fees at £6,000 would create real problems for higher-cost disciplines, especially in STEM subjects. It would also create a discrepancy between undergraduate and postgraduate funding systems which bears no relation to the cost of providing courses. While we hope that allowing postgraduates access to student loans would enable universities to better target scholarships and fee waivers, we believe that making such targeting a condition of access to the loan scheme would be burdensome and disproportionate, effectively forcing institutions to enter into a second round of postgraduate access agreements.

Conclusions

Recommendation: The Government should put in place an income-contingent loan system for full-time postgraduate students using a modified version of the model put forward by Tim Leunig.

The system would have the following characteristics:

- Loans of up to £10,000 available to students with first or upper second class degrees.
- Repayable at 9% on income between £15,000 and £21,000.
- Postgraduate and undergraduate loans will be rolled together for higher earners, such that once a graduate has finished repayments on one loan, he or she will continue to make repayments towards the other loan at a rate of 9% of all income above the £15,000 threshold.

Any outstanding debt will be written off 30 years after beginning the course.

A number of courses have tuition fees far in excess of the average. For these courses an income-contingent loan at these institutions would be insufficient to cover the cost of study. We hope to see individual institutions take action to ensure that these courses are open to all students – making up the shortfall in funding for less advantaged students using some of the other mechanisms we discuss elsewhere in this report – be it through brokering access to further financial support or through refocusing of institutional financial support such as scholarships and bursaries.

We recognise that this scheme will not cover part-time postgraduates. Part-time students have distinct needs which may not be addressed simply by extending to them the support available to full-time students, and policy-makers need to reach a more detailed understanding of the diversity of the PGT community, and to assess the extent to which factors such as age and the nature and scope of paid employment are more significant divisions than mode or intensity of study.

Recommendation: Further research is required on the needs of part-time postgraduates with a view to identifying how support might best be provided for this heterogeneous group. As resources allow, the Government should seek to identify opportunities to extend the support available to some part-time postgraduates.
CHAPTER 6: INTEGRATING UNDERGRADUATE AND POSTGRADUATE FUNDING

In this chapter we will consider whether there is a case for integrating postgraduate education into the existing system for undergraduates. A number of commentators have recently written about the declining usefulness of the distinction between undergraduate and postgraduate education.

Writing in their new book on the modernisation of English higher education, Professor Claire Callender and Professor Sir Peter Scott observe that:

“the distinction between undergraduate and postgraduate education is becoming fuzzier. In many professional disciplines it has always been a contrived demarcation. So-called ‘undergraduate’ masters’ courses have proliferated. Many postgraduate courses are ‘postgraduate’ in time but not ‘postgraduate’ in level, often serving as conversion courses or elements in wider programmes of continuing professional development.”

Similarly, Professor Don Nutbeam, Vice Chancellor of the University of Southampton has argued that: “it is unhelpful to maintain the sharp division between undergraduate and postgraduate provision which exists today”.

Full integration of undergraduate and postgraduate support

One response to this would be to integrate the student financial support schemes for undergraduates and postgraduates. This is a model that has been used in Australia, for instance.

Realistically, this is not an option for the short to medium-term as there is little political appetite for another reconsideration of undergraduate financial support. Recent history suggests that it is inevitable that student support for undergraduates will be reviewed in the longer-term – the 12 year period between 1998 and 2010, for example, saw three separate overhauls of undergraduate financial support. The next review should be taken as an opportunity for exploration of the scope for greater linkage between undergraduate and postgraduate student support.

Recommendation: Any future review of higher education student support should explicitly consider integrating undergraduate and postgraduate student support.

4 years of funding?

Another alternative would be to offer students four years of student finance to spend on education as they saw fit. A substantial subset of students already benefit from four years’ worth of student finance support under the current undergraduate financial support system, including:

- Students studying for integrated masters’ degrees
- English students studying at Scottish universities on four year undergraduate courses
- Students resitting a year of their undergraduate degree
- Medical students

This adjustment would allow students completing three year undergraduate degrees to use the additional fourth year of public support to finance a master’s degree.

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Pursuing such a policy within the current undergraduate student loans system would come with significant costs and be disproportionately expensive in the long-term. The additional year of study, with loan levels analogous to those available for undergraduate study could potentially add £16,675 to a student’s total debt (tuition fee of £9,000 plus full London living cost loan for a student living away from home). Analysis of the current undergraduate student loan system by IPPR/London Economics suggests that only female undergraduates in the 80th income percentile and above and male undergraduates in the 50th percentile and above will pay off the full amount of debt over the lifetime of the loan, which is capped at thirty years.\(^{92}\) Whilst students with postgraduate degrees do earn more over their lifetimes, benefiting from a ‘postgraduate premium’ of around £5,500 per annum,\(^{93}\) these students are typically, at present, those with better first degrees and better job prospects – i.e. those more likely to pay off their loans in full. Extending four years of lending to all students is unlikely to translate into full repayment of the additional loan sum plus interest for most of the cohort. Consequently, the RAB charge for such students is likely to be higher than that of students solely studying towards a bachelor’s degree.

**Expanding integrated masters’ degrees**

As already noted, one way in which students can access full-funding for a master’s qualification is by taking an integrated master’s course which combines an undergraduate degree with an extra year of masters-level study.

Integrated masters have traditionally been offered for one of two purposes. Firstly, they are an important part of the pipeline of future academic researchers. They offer students the opportunity to design and carry out a substantive research project, providing the student with a ‘taste of’, and the skills needed for, doctoral research. The progression rate from integrated masters’ degrees to further study is high – analysis of DLHE\(^ {94}\) data suggests that around 20% of integrated masters’ students go on to study for a further qualification without working.\(^ {95,96}\) Secondly, integrated masters are sometimes used as a professional degree. For example, to be registered as a professional pharmacist, students must first complete a four year integrated MPharm degree. Similarly, in the engineering field, an integrated MEng degree is the most direct and recognised route to Chartered Engineer (CEng) Status.

There is some evidence that universities are looking to diversify the range of subjects in which they offer integrated masters. There are a number of disciplines which have grown from single figures five years ago to three figure headcounts today. The number of students on integrated masters’ degrees in historical and philosophical studies has increased from ‘10 or fewer’ to 145. At least one large civic University is offering new Integrated Masters’ degrees in Geography and History, along with a series of Integrated Masters’ programmes in Languages. The university explicitly uses the availability of funding as a marketing device, noting that ‘unlike free-standing masters’ programmes all four years of this programme are eligible for student loan support’.

Both HEFCE and the Department for Business, Innovation and Skills have recognised the potential for the Treasury to be exposed to greater financial risk should there be a large-scale expansion of integrated master’s provision in England. In January 2012, the Business Secretary, Vince Cable, and the Universities and Science Minister, David Willetts, made it clear that “the Government does not

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\(^{92}\) IPPR. 2013. p. 129.
\(^{94}\) Destination of Leavers from Higher Education Institutions
\(^{96}\) This compares to 14% of the undergraduate population as a whole, though the two figures are not comparable as many of these 14% will be going on to masters-level, rather than doctoral level, study.
expect to see any increase in the average length of undergraduate or postgraduate taught courses”. Consequently, HEFCE warned institutions that they would “deal, if necessary, with incentives and disincentives around course lengths by monitoring changes to providers’ average course lengths, and adjusting their student number controls accordingly”.

The government’s policy of liberalising student number controls has reduced the potency of such a sanction, as institutions are now allowed to recruit an unlimited number of undergraduates with ABB grades at A-level. The entry requirements for most integrated masters’ courses tend to be high – with the vast majority of students being required to offer A-level grades of ABB or higher. Most integrated masters’ students will not be counted for the purposes of student number controls. HEFCE’s own analysis indicates that integrated masters tend to be “most commonly offered” in high tariff institutions – who will be somewhat insulated from the impact of any resultant cut to student number allocations that follows an expansion in their integrated master’s provision.

Conclusions

It would not be desirable for the taxpayer to assume risks of non-repayment that should rightly fall elsewhere. One of the most remarkable trends in this area in recent years has been the explosion in integrated masters’ degrees in law, which have increased from zero in 2006/7 to 910 in 2010/11. In some cases degrees combine the academic and professional stages of legal training – offering students both a qualifying law degree and an exemption from having to undertake the Legal Practice Course or the Bar Professional Training Course. The regulations underlying eligibility for student finance specifically exclude courses which “lead to the award of a professional qualification” for which “a first degree (or equivalent qualification) would normally be required for entry.” Strictly speaking, these do not lead to a professional qualification, but instead exempt holders from the requirement for a professional qualification.

Integrated masters are a valuable part of the UK’s diverse postgraduate offer – and are particularly important in securing the pipeline of future researchers and doctoral candidates. In the absence of a more comprehensive funding solution we envisage that they will continue to play a vital role in the postgraduate funding landscape.

Any growth in integrated masters must happen in a systematic and strategic manner – and they should not simply be used to mitigate the impact of the current dearth of other means of postgraduate funding. Mass expansion of integrated masters is not a viable solution to the postgraduate crisis – they have a higher long-term cost than some of the other funding options outlined in this report.

Integrated masters’ degrees have a valuable role to play, especially in the STEM subjects where they have traditionally been used.

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Recommendation: The Government should continue to monitor the expansion of integrated masters’ degrees beyond the areas where they have traditionally been delivered, providing student loans for new four-year courses only where a genuine academic case can be made.
CHAPTER 7: SCHOLARSHIPS AND SPONSORSHIP

A small number of students currently receive funding from their employers or from the institutions they are enrolled at. In this chapter we will map current contributions, consider the prospects for increasing contributions from institutions and employers, and discuss how their contributions may interact with other sources of finance in a future funding system.

Employers and the professions

There is a growing appreciation of the vital role that postgraduate skills play in ensuring the future competitiveness and continued success of British business. Postgraduates have been described by Lord Leitch as “one of the most powerful levers for improving productivity” and by Sir Adrian Smith, then BIS Director General for Higher Education, as “major drivers of innovation and growth.” Boosting employer investment in training was a key part of the social compact proposed by Lord Dearing and the National Committee of Inquiry into Higher Education back in July 1997.

Given these imperatives it is surprising that the contribution made towards the cost of postgraduate education by industry and by employers remains relatively small. In 2011/12, less than 2% of full-time postgraduates received employer funding. Part-time postgraduates fared better, with 17% receiving funding. Previous 1994 Group analysis has shown that the proportion of employer-funded postgraduate taught students has been falling since 2003/4. In the three years to 2011/12, the number of new employer-funded postgraduates on taught courses fell by 28% (see Figure 4).

![Figure 4: Employer/industry funded students starting taught masters’ courses (HEIDI data)](image)

In this chapter we will consider two of the main types of sponsorship – those provided by individual companies to individual employees, and those offered on an industry-wide scale.

Individual sponsorship

Much employer funding is provided on a within-firm basis, with companies providing financial support to existing employees or to those who have undertaken to join the firm in the near future.

102 A. Smith. 2010, One step beyond. p. 32.
103 Analysis of HEIDI data – PGT students reporting UK industry/commerce or students employer as major source of their tuition fees.
Employers are not required to pay tax on contributions made towards study which is ‘work related.’ There may be value in a campaign to increase employer awareness of this concession.

One reason some employers are reluctant to invest in employees’ education is a fear that they will leave the company before the employer can enjoy a sufficient return on their investment. This can be prevented by reaching a ‘golden handcuffs’ agreement with the employee, whereby they agree to pay back some or all of the funding received if they leave the company before a designated point in time.

A number of organisations have called for further tax incentives to encourage businesses to invest more in PGT courses. Research literature and professional opinion on the effectiveness of tax incentives is, at best, mixed. Recent research published by the OECD concluded that tax incentives per se tend to principally benefit large companies, carry a large deadweight cost, and should only be used as a means of tackling aggregate under-investment. Where tax incentives have been implemented overseas they have, almost universally, included eligibility restrictions in an effort to contain costs. There is a scarcity of data on the effectiveness of existing tax incentive schemes, making it difficult to evaluate the effect a postgraduate tax incentive might have on employer decisions. Given these uncertainties, it is doubtful whether Government would be willing to extend tax incentives during a period of austerity.

**Industry-wide initiatives**

There are a small number of industries where employers and professional bodies have collaborated to make funding available to a wider pool of employees, as well as to individuals hoping to enter the sector. To date this has principally been in areas where there is a clearly identified skills shortage, a licence to practise arrangement whereby people cannot enter the sector without a particular qualification, or a recognised lack of diversity among current employees.

**Case Study: Law**
Both branches of the legal profession make funding available for professional legal education. The Law Society runs a diversity access scheme, supported by a number of legal firms, universities and other large companies, which makes awards towards the cost of the Legal Practice Course. The four Inns of Court collectively offer around £4.5m of support annually, awarded on the basis of means and/or merit, mostly towards the costs of the Graduate Diploma in Law and Bar Professional Training Course. The Inns actively fundraise to cover the cost of these scholarships.

**Case Study: Aerospace Engineering**
In February 2013, a new £6 million bursary fund was established under the Aerospace Growth Partnership to provide funding for individuals wishing to study aerospace engineering at master’s level. The scheme, which will be administered by the Royal Academy of Engineering and the Royal Aeronautical Society, will see the Government and the aerospace industry each contribute £3 million over the course of the next three years on a match-funding basis.

**Case Study: Petroleum Exploration**
The Petroleum Exploration Society of Great Britain has developed a master’s funding programme, which made awards to students in 2012. It is also looking to develop a means through which smaller

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companies can pool contributions. This illustrates the role which professional or trade bodies could play in acting as a conduit for collective employer investment across a sector.

The Aerospace Growth Partnership model could potentially be replicated in other sectors, particularly those which the Government has designated as ‘Industrial Strategy Sectors’ – civil nuclear; oil and gas; offshore wind; agritech security; education exports; information economy; automotive; construction exports; professional business services and life sciences. By definition, a match-funding scheme such as this would come with a cost to Government.

There are uncertainties around the feasibility of growing employer co-funding schemes further. A 2009 DIUS Select Committee report concluded that there was a need to “get beneath the welter of opinion and anecdote to establish hard evidence” on the willingness of employers to co-fund provision. To date, successful schemes have principally been focused in industries that are profitable, capital-rich, and made up of big firms. There is doubt around whether other industries, which have more marginal profit levels, would be able or willing to commit to similar levels of investment.

**Institutions**

**Graduate scholarships in the UK**

The number of PGT students receiving support from institutions, either in the form of cash scholarships or fee waivers, has doubled in the last 10 years, increasing from 7,115 in 2002/03 to 14,715 in England in 2011/12 (see Figure 5). Even if we control for the increase in the total PGT population over that period there is a clear upward trajectory. There is a considerable way to go to match the levels of support one would find in, for instance, the United States. In 2007/08, 21.3% of U.S. students received institutional funding towards their master’s degree.

UK universities tend to offer a combination of full and partial scholarships. Full scholarships, which cover the cost of tuition fees and a contribution towards living costs, tend to be very limited in number. Many full scholarships are designed to promote the international exchange of students, and are usually funded principally by external sources rather than institutions. For example, the Said Foundation offer scholarship funding for students from the Middle East to undertake postgraduate study at British universities. Similarly the Marshall, Commonwealth and Chevening Scholarships exist to fund postgraduate study for international students at British universities or for British students at selected overseas universities.

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Figure 5: Number of PGT students receiving institutional waiver/award (England)

A larger number of partial scholarships are offered – which often take the form of fee waivers. Whilst partial scholarships do reduce the cost of postgraduate study they are not sufficient in isolation – they instead act as a useful supplement to other sources of finance. As in the United States, full time PGT students in England often end up with a ‘portfolio’ of funding, made up of cash scholarships, fee waivers, loans, earned income and parental contributions. Institutional scholarships, which meet only part of the costs of study, will inevitably only be part of such a portfolio.

Scholarships are often aimed at a particular group of students - those on a particular course of study, those applying to a specific university department, or those resident in a particular region or country. To a large extent this is due to the link between scholarship funding and philanthropy, with benefactors making restricted gifts to institutions, specifying that funds can only be used for particular purposes. Given this, whilst scholarships do have a role to play in alleviating some of the financial challenges experienced by a limited pool of students, it is unlikely that such a patchwork of targeted scholarships could provide a satisfactory system-wide answer to the PGT funding challenges.

A number of institutions have introduced alumni scholarships – which provide discounts on postgraduate fees to students who have completed another degree at that institution. The University of Essex offers a 25% fee waiver to all students enrolling on masters’ programmes who have a first class undergraduate degree from any UK university. To be eligible, students must be self-funding, without external grant support towards tuition fees. Similarly, in 2013 the University of Sussex announced a new scholarship scheme that will offer 100 fee waivers worth £3,000 each to students who hold first class degrees from UK universities. The scholarships are awarded on the basis of current academic performance and future potential for conducting research.

Other institutions are now explicitly trying to develop a pipeline of future research and academic leaders by targeting postgraduate scholarships at the highest achieving undergraduates.

Graduate scholarships in the United States

As we have already established, institutional financial aid for graduates in the United States is more prevalent than in the UK, with 21.3% of students receiving some form of support. The profile of financial aid distribution is mapped out below – it is noteworthy that 3.2% of students receive more than $20,000 in support. At graduate-level financial aid is “typically awarded on the basis of non-
financial criteria”\textsuperscript{110} – this is in contrast to US support for undergraduate-level study, which tends to have a stronger needs-based element.

<table>
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<th>Amount</th>
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</tr>
<tr>
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</tr>
<tr>
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<td>4.5%</td>
</tr>
<tr>
<td>$10k-20k</td>
<td>4.8%</td>
</tr>
<tr>
<td>$20k +</td>
<td>3.2%</td>
</tr>
</tbody>
</table>

\textbf{Figure 6: Proportion of masters’ students receiving institutional support 2007/08 (USA)}\textsuperscript{111}

It must be recognised that there are substantial obstacles to developing systems of institutional support in the UK comparable to those available in the USA. British universities lack the resources of their US counterparts. An American university of comparable size and standing to 1994 Group institutions (as reflected in the Times Higher Education World University Rankings) might have an endowment of over $3 billion. For British universities to build up their endowments requires not just long-term fundraising activity, but also a change in philanthropic culture. It cannot be a quick fix to a short-term funding need. Moreover, American universities are able to cross-subsidise particular groups of students—in effect charging according to need—by charging much higher basic fees for courses than are currently conceivable in the United Kingdom.

\textbf{Feasibility of extending scholarships}

If universities are to invest more in postgraduate scholarships, a key question is where the additional funding should come from. Writing for CentreForum, the Sutton Trust’s Conor Ryan notes that UK university endowment funds are often primarily used for new buildings and other capital projects—he recommends that universities direct more of their philanthropic income into scholarships.\textsuperscript{112} Scholarships can be seen as an investment in the future resource base of an individual university and the broader higher education system. To be successful in the future, universities need a strong pool of human capital even more than research and teaching infrastructure – they therefore have a strong interest in investing in future research leaders.

It should also be noted that scholarships designed specifically to add capacity to the research pipeline will carry some degree of deadweight cost. Not all students receiving scholarships will go on to the academic route, whilst others would have entered research and teaching careers regardless of the financial support on offer. It is difficult for institutions to accurately identify students who are both likely to go on to research and teaching careers if given support, but not likely to go on to it without support.

A number of universities have, in recent years, launched fundraising campaigns aimed explicitly at boosting postgraduate scholarships, with some degree of success. Indeed, a recent review of higher education philanthropy found that many universities perceived funding scholarships and bursaries to


\textsuperscript{111} US Department of Education, National Center for Education Statistics. 2007-08 National Postsecondary Student Aid Study.

be a compelling prospect for new donors. Universities may however find it more difficult to raise funds for postgraduate scholarships from alumni who completed bachelors’ degrees, as they may not necessarily appreciate the importance of masters’ degrees.

It should also be noted that not all universities have the same fundraising capacity – in 2010/11 roughly half of all philanthropic income went to Oxford and Cambridge universities, despite these two universities accounting for only 1.82% of the UK student population. An alternative would be for universities to refocus existing unrestricted spend on PGT scholarships – but there is considerable uncertainty as to how feasible this is, particularly in light of the spending constraints the sector has already faced since 2009. Indeed, the on-the-ground impact of refocusing funding would be cuts to other areas of activity that are financed from unrestricted spend. Unless new sources of income—such as increased philanthropy—become available to British universities, a large scale extension of scholarships funded by institutions themselves could only be facilitated by changes to other forms of expenditure within institutions.

Conclusions

Employers and institutions both contribute to the current mixed economy of postgraduate funding through providing scholarships and sponsorship to students. There is some capacity to boost employer and institutional investment in scholarships in postgraduate education through the generation of new channels of philanthropic giving for institutions, and through persuading employers to invest in their workforces.

This is not a stand-alone solution. Institutional and employer scholarships could work effectively in tandem with other sources of funding. Scholarships could act as an incentive for individuals to enrol on courses where there would otherwise be lower levels of student enrolment than the economy is likely to require. The existence of other, better sources of financing, such as the government-supported student loan scheme we advocate in Chapter 5, may allow institutions to re-target their scholarship provision to students facing financial hardship.

115 Some of the other funding options outlined in this document could actually reduce the amount available for scholarships. For example, institutional loans to student could necessitate institutions diverting unrestricted scholarship funding into risk premiums.
CHAPTER 8: RECOMMENDATIONS

These measures, taken together should result in a system where postgraduate education is truly open to all UK students with sufficient academic merit, regardless of means.

Recommendations for Government

The Government should put in place an income-contingent loan system for full-time postgraduate students using a modified version of the model put forward by Tim Leunig. Our suggested modifications are detailed in Chapter 5.

The system would have the following characteristics:

- Loans of up to £10,000 available to students with first or upper second class degrees.
- Repayable at 9% on income between £15,000 and £21,000.
- Postgraduate and undergraduate loans will be rolled together for higher earners, such that once a graduate has finished repayments on one loan, he or she will continue to make repayments towards the other loan at a rate of 9% of all income above the £15,000 threshold.
- Any outstanding debt will be written off 30 years after beginning the course.

We calculate that the long-term cost of the loans, if existing recruitment patterns hold, will be less, probably substantially less, than £50 million per year. This £50 million can be found easily through redirecting money from existing funding pots. The Professional and Career Development Loans system for postgraduate courses should be scrapped – which will realise an annual saving of £12 million. The remainder of the funding required should be taken from the £50 million that the Government has earmarked for a new postgraduate National Scholarship Programme.

A number of courses at a number of institutions have tuition fees far in excess of the average. For these courses an income-contingent loan will be insufficient to cover the cost of study. We hope to see individual institutions take action to ensure that these courses are open to all students – making up the shortfall in funding for less advantaged students using some of the other mechanisms we discuss elsewhere in this report. This could take the form of brokering access to further financial support or refocusing institutional financial support such as scholarships and bursaries.

In order to ensure that the loans are targeted at those students best placed to take advantage of postgraduate study, to keep down the RAB charge associated with the scheme and to ensure that institutions do not use the availability of public funding to ‘lower the bar’ for postgraduate study, we propose that loans for full-time study should be limited to graduates with a first or upper second class degree.

Part-time students have distinct needs which may not be addressed simply by extending to them the support available to full-time students, and policy-makers need to reach a more detailed understanding of the diversity of the PGT community, and to assess the extent to which factors such as age and the nature and scope of paid employment are more significant divisions than mode or intensity of study. Further research is required on the needs of part-time postgraduates with a view to identifying how support might best be provided for this heterogeneous group. As resources allow, the Government should seek to identify opportunities to extend the support available to some part-time postgraduates.

116 PCDLs for vocational non-postgraduate courses, which make up only a small proportion of the PCDL scheme, should be maintained, at a cost of less than £3 million per annum.
There is a further question as to how best to deliver a system of postgraduate loans. It is not clear whether the Student Loans Company (SLC) would be able to integrate collection of postgraduate loans with the machinery for collecting undergraduate loan repayments. These are collected by HM Revenue and Customs (HMRC) using the individual’s tax code, and passed on to the SLC, who set repayments against the student’s account. In theory, there is no reason why a student cannot have more than one account with the SLC against which to offset repayments. For instance, if the Leunig model were to be adopted, the first £540 of any repayments could be offset against the postgraduate loan and any remainder against the undergraduate loan.

Failing this, it is possible that loan repayments could be made outside the tax system. For instance, one could easily design a system in which graduates automatically began repaying student loans at a rate of £540 per year by direct debit, unless they notified that their earnings were either below the threshold for repayment or at a level at which a lower level of repayment applies. Any substantial over-payments or under-payments could then be reconciled following the end of the tax year.

In addition, we recommend that HMRC should encourage employers to support postgraduate education by removing the £10,000 cap on the extra-statutory tax concession for employer loans towards the cost of study at Higher Education Institutions.

**Recommendations for employers and the professions**

One of the criteria which we set out at the beginning of this report was that the final package of funding options be one in which the costs of postgraduate education were fairly shared across students, society and Government, employers, and higher education institutions. Historically, the employer contribution has been the most difficult to establish. Under the system we propose it is envisaged that employers will contribute to the funding landscape in one of two ways:

Firstly, we propose that a small group of qualifications be excluded from the income-contingent loan scheme – principally MBAs and qualifications leading to entry into the law profession. We expect employers and the relevant professional bodies to take a strong lead in funding these courses.

We do not believe that problems in the MBA finance market are sufficiently strong to merit intervention. Many employers have continued to offer their employees sponsorship or access to loans and community finance schemes, such as Prodigy Finance, have entered the MBA loan market. MBAs continue to be a good investment for the majority of students.

The legal profession already has a strong tradition of providing scholarships and sponsorship for those studying toward the graduate diploma in law, the Legal Practice Course and the Bar Professional Training Course. We do not want to crowd out this funding – and indeed want to see it increase. As part of their response to the recently published Legal Education and Training Review the legal profession should consider how such funding could be expanded, particularly for those studying to practise at the Bar. We do not believe that it would be an efficient use of public resources for Government to play an active role in funding postgraduate professional legal education.

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117 See [https://prodigyfinance.com/](https://prodigyfinance.com/)

http://ials.sas.ac.uk/research/docs/LETR%20Report%20ALL%20Sections.pdf
Other industries, particularly those where postgraduate qualifications are increasingly de facto requirements for entry, will also need to consider whether there is a need for concerted action on their part to support postgraduate education.

In order to encourage such collaboration, we recommend the creation of a Council for Universities and the Professions to bring together representatives of the main professional bodies with representatives from higher education institutions and Government. In the first instance, the committee would be charged with monitoring take-up of postgraduate courses in professional disciplines, making recommendations, and encouraging profession-wide mechanisms of financial support for students.

Secondly, employers will continue to invest in co-financing postgraduate education which they value as being integral to workforce development and employee retention. We envisage that employer support in the form of sponsorship (as opposed to loans) will be unaffected. We welcome the focus that the current Government has placed on boosting long-term university–business engagement, particularly through the work being undertaken by Sir Tim Wilson and Sir Andrew Witty.

**Recommendations for Higher Education Institutions**

We envisage that institutions will continue to offer support through fee waivers and scholarships to help students who might otherwise face financial hardship and to maintain a pipeline of future researchers. They may also want to continue to use these tools to attract the brightest and best graduates.

Should the Government prove unwilling to develop a system of state-backed postgraduate loans along the lines we propose, institutions should investigate their ability to provide a similar scheme on a pooled basis. However, we are clear that this would be less preferable to a nationwide solution. Institutions are unlikely to be able to borrow as cheaply as Government to fund the scheme, and would struggle to administer an income-contingent repayment system. Consequently a scheme developed by institutions is likely to be less successful than a state-backed scheme.

**Conclusions**

The consequences of not tackling the postgraduate funding challenge are clear. There will continue to be relative underinvestment in postgraduate education by UK-domiciled students, which will, in the longer-term, lead to a decline in British competitiveness. The situation will also call into question the government’s commitment to improving social mobility.

In 2014 the first students subject to the new undergraduate funding regime will begin to decide whether they wish to stay on to undertake postgraduate study. These decisions will have consequences not just for individuals, but for universities and for wider society, and will be shaped by the funding environment for postgraduate study. The postgraduate crisis is no longer a theoretical challenge: it is an urgent issue which must be addressed now.
APPENDIX: POSTGRADUATE FUNDING – AN INTERNATIONAL COMPARISON

This section puts the support currently offered to postgraduate students in the UK into an international context, through making comparisons with four other mature higher education systems: Australia, the United States, Canada and France. There is limited literature on this issue: whilst numerous international comparative studies of undergraduate funding have been produced, we are not aware of any similar analyses at postgraduate level.

All of the countries surveyed have more comprehensive systems of postgraduate support than the UK. In particular, they have established loan systems to cover fees, and in some cases maintenance. All four countries surveyed also offer some form of tax incentive to support further education and training, though such interventions appear to be falling from favour – with both France and Australia looking to restrict and reduce their spending. The range of support available indicates the value that these countries place on supporting postgraduates’ development. All four countries have recognised the social and economic returns to be gained from backing their countries’ competitiveness in the ‘global race’.

Australia

Australia has an established and comprehensive system (the HELP scheme) of financial support to cover fees at both undergraduate and postgraduate level. Citizens are also able to offset expenditure on employment-related postgraduate education (as well as other forms of training) against their tax liability, although the Gillard and Rudd governments proposed that this benefit should only be claimable against the first AU$2,000 of expenditure. However, the system is not completely comprehensive – for example, there is no national system of maintenance support.

Fees: Fees vary across institutions, though QS data suggests that 50% of institutions charge AU$6-8000 (£3,500 – £4,700) per annum. A number of institutions charge significantly higher fees, with the average at Sydney University being in excess of AU$30,000. The fee charged depends on the type of place a student holds. A limited number of ‘Commonwealth-supported’ places are subsidised by the Federal Government – with students only paying a ‘student contribution’. Otherwise, students take up full-fee places. Most postgraduate courses do not have Commonwealth-supported places available.

Loans: Income contingent loans towards the cost of tuition are available for both Commonwealth-supported students (through HECS-HELP) and full-fee students (through FEE-HELP). Borrowing through FEE-HELP (the scheme for unsubsidised places) is subject to a lifetime cap. Loans are also available towards the cost of study at overseas institutions. HELP represents an attractive source of lending for prospective postgraduates. Whilst undergraduates are required to pay a loan fee of 25% of the amount borrowed, this fee is waived for postgraduates. The loans have no real rate of interest, with the government merely indexing the debt each year by the CPI rate of inflation. This carries a cost to government as CPI is often lower than the government’s own cost of borrowing.¹ The HELP scheme currently costs the Australian Government AUS$1.5 billion per annum,² a figure which has quadrupled in the last 20 years, although it should be noted that this covers loans for both undergraduates and postgraduates. Limited help is available towards the cost of student maintenance on a strict means-tested basis and subject to fulfilling particular conditions, such as being in a particular age group, or of Aboriginal descent.³

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² Norton, p. 44.
Tax incentives: A comprehensive system of tax deductions is in place, designed to incentivise take-up of education or training connected to employment. Citizens can claim tax relief on all education spending, including professional postgraduate education. The relief is primarily focused on professional development, as the deductible amount has to be “directly connected to the taxpayer’s current employment by either maintaining or improving the specific skills or knowledge required for the employment”, 4 though there is some provision for the education to be used to help boost income returns.

Last year, 638,000 people, 5% of all Australian taxpayers, claimed a deduction for formal education.5 In May 2013, the Government tried to introduce a cap on this deduction, such that citizens could only claim relief for the first AUS$2,000 of spending, but this has been postponed in light of protests from the professions and the higher education sector.6 We discuss this system more thoroughly in Chapter 3.

Grants and scholarships: The majority of maintenance support is provided directly to students by higher education institutions. There are two other national means-tested schemes, available to students on some postgraduate courses: the Youth Allowance (for 16-24 year olds) and AUSTUDY, a scheme for students in financial need aged 25 and over.7 Postgraduate research students (at both Masters and PhD level) can receive a merit based Postgraduate Award, equivalent to UK studentships, at a cost to the Government of AUS$25 million per annum. Each award is worth AUS$26,000 per annum tax-free.8

United States

The US predominantly relies on private and government loans to finance the postgraduate sector. In addition to this, many institutions offer relatively generous support to postgraduates, with 3.2% of graduate students receiving over $20,000 in institutional support. There is an established, though complicated, system of tax allowances.

Fees: Fees in the US vary hugely depending on both course type and institution. Data collated by QS demonstrates this spread – with 29 institutions featured with an average fee of less than $10,000 (£6,000) per annum and at least 21 institutions with an average fee in excess of $38,000 (£23,600) per annum.

Loans: There are a range of loans available to graduates, both private and public. ‘Stafford loans’ are available to graduates at an unsubsidised rate without any means-testing; currently students can borrow up to $20,500 per annum at a variable rate of 5.41% (10 year Treasury rate plus 3.6%, capped at 9.5%).9

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5 Ibid, p. 5.
The Graduate Plus scheme is a government guaranteed loan which is not based on financial need. This is a less generous scheme in that it is designed to meet the costs of studying over and above any existing financial aid, which is deducted from the loan offer. The interest rate is currently fixed at 6.41% (the ten year Treasury rate plus 4.6%, capped at 10.5%).\(^\text{10}\) In addition, there are many private loan providers willing to lend to graduates, often with little or no security.\(^\text{11}\)

**Tax incentives:** A number of incentives are available for both parents and graduates themselves.\(^\text{12}\) The Lifetime Learning Tax Credit, worth up to $2,000 to those earning less than $62,000 per annum, can be used to offset any relevant educational expenses: tuition fees, books, supplies and equipment. It is available to anyone studying to improve their skills, not simply those studying for a degree.\(^\text{13}\) Alternatively, graduate students may be able to claim for a Student Loan Interest Reduction, up to a value of $2,500, as long as their income is under $75,000.\(^\text{14}\) Graduates may also be eligible for the Tuition and Fees Deduction (worth up to $4,000), depending on the size of their income.\(^\text{15}\) Only one of these reliefs can be claimed in any one tax year.

**Grants and scholarships:** Financial aid is available on an institution by institution basis, or from the student’s home state. 21.4% of postgraduates access some form of support (with 3.2% of students receiving more than $20,000). Awards are not as dependent on the student’s financial circumstances as they are at undergraduate level, but are predominantly merit-based. At graduate-level financial aid is “typically awarded on the basis of non-financial criteria” – this is in contrast to US support for undergraduate-level study, which tends to have a stronger needs-based element.\(^\text{16}\)

**Canada**

The balance of Canada’s provision for postgraduates is weighted towards tax incentives. The majority of government loans are means-tested, which perhaps reflects the relatively low fees charged for postgraduate courses (CAN$2,000-8,000). A ‘Lifelong Learning Plan’ is available to support education or training, and each state awards tax rebates to encourage postgraduates to continue living and working in the area in which they trained.

**Fees:** Canadian fees are low, with most fees in the CAN$2,000-8,000 (£1,200-£4,800) per annum range.

**Loans:** Postgraduates in Canada are entitled to take part in the same Student Loan Program available to undergraduates, but they are constrained by a lifetime limit on eligibility. This varies between a standard 340 weeks and 520 weeks for students with disabilities. As Canadian undergraduate degrees can take up to four years, this effectively caps the amount of support available to postgraduates. Residential requirements and an assessment of financial need are also factors in determining the level of loan postgraduates receive.\(^\text{17}\) Loans are interest-free for the period of study, but they start accumulating interest on graduation, though they do not enter repayment until six

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\(^\text{10}\) http://www.gradloans.com/graduate-plus-loan/
\(^\text{12}\) http://www.irs.gov/Individuals/Tax-Incentives-for-Higher-Education-
\(^\text{13}\) http://www.nasfaa.org/students/Tax_Breaks_for_Higher_Education.aspx
\(^\text{15}\) http://www.irs.gov/publications/p970/ch06.html#en_US_2012_publink1000295078
\(^\text{17}\) http://www.canlearn.ca/eng/loans_grants/loans/qualify.shtml#before
It is important to remember that these conditions vary state by state, with some states (Northwest Territories, Nunavut and Quebec) operating their own loan programmes.

Tax incentives: The primary national tax initiative is the ‘Education Amount’, which allows eligible students to reclaim a fixed amount based on the number of months they have been in education or training. For full-time students this is set at CAN$400 per month of education.\(^\text{18}\) Individuals can also take part in the ‘Lifelong Learning Plan’, where they draw down money from their Retirement Plan (to which they have made tax-free contributions), up to a value of CAN$10,000 per annum (maximum lifetime value CAN$20,000) to fund a course of education or training at designated institutions.\(^\text{19}\) The Canadian Federation of Students estimates that the Canadian Government spends CAN$2.5 billion per year on education-related tax credits and saving schemes.\(^\text{20}\)

Grants and scholarships: Student grants are primarily designed to support undergraduates, but postgraduates with dependents, or who are disabled, qualify for support. This scheme is means-tested.\(^\text{21}\) There are a range of scholarship opportunities available at every level from undergraduate to postdoctoral, but as in the UK they are conditional on historically and geographically specific criteria, as well as being targeted at specific disciplines.

France

Postgraduate fees in France tend to be lower than in the UK, and loans towards fees are easier to obtain, with the Government guaranteeing a bank lending scheme. Reforms announced in Summer 2013 are expected to shift the balance of support away from tax incentives and towards grants.\(^\text{22}\)

Fees: Taught postgraduate fees in France (for non-engineering courses) are fixed by the French Ministry of Higher Education & Research at €245 (£210) per annum, although in practice universities have been able to levy additional fees for specific services, such as laboratory access. In private institutions fees are higher, and “can reach €3,000 to €10,000 (£2,500- £8,400) per annum”.\(^\text{23}\)

Loans: In 2008 the Government introduced a state-backed bank lending scheme, worth up to €15,000 per annum. Loans are available to all home students (and EU residents, provided they have lived in France for at least five years by the end of their studies) under the age of 28, with the Government guaranteeing 70% of the loan for a ten year period. However, a 2012 European Commission study suggests that only 0.1% of students have taken up the scheme since its launch.\(^\text{24}\)

Tax incentives: Parents are eligible for a tax relief of €183 for children enrolled in higher education who are financially dependent on them and under the age of 25. However, the French financial newspaper Les Echos has reported that it is likely that this will be eliminated in the next financial year\(^\text{25}\) – the French Government has already removed the tax break available to the parents of school age children.

\(^\text{18}\) [Website](http://www.cra-arc.gc.ca/tx/ndvdlsttpcs/ncm-tx/rtrn/cmplng/ddctns/lns300-350/323/dctn-eng.html)
\(^\text{19}\) [Website](http://www.cra-arc.gc.ca/E/pub/tg/rc4112/rc4112-12e.pdf)
\(^\text{21}\) [Website](http://www.canlearn.ca/eng/loans_grants/grants/dependants.shtml)
\(^\text{23}\) National Contact for France of the European Migration Network. 2012. *Immigration of International Students to France*. p. 37
In addition, a number of provisions in the French tax code also seek to reduce the income tax liability on wages earned by students. Students aged 26 or less do not have to pay tax on the equivalent of three months of earnings at minimum wage.\textsuperscript{26}

Grants and scholarships: Much of the support for graduates is coordinated at government level and is prioritised according to financial need, family circumstances, academic merit, and to promote students’ international mobility.\textsuperscript{27} 30\% of the total student population are eligible for a needs-based grant which exempts them from paying fees.\textsuperscript{28} Merit-based grants, worth between €1,800 and €6,100, are also available as a supplement for high performing students.\textsuperscript{29} Reforms to the system announced in 2013 will see grants increased for students from the lowest income families and for those who currently support their study through paid work.

**NOTES:** This is a fast moving area. Further change to student support is currently under discussion in France, Australia and the US. All information correct at the time of writing, Summer 2013. All tuition fee data extracted from QS Database.

\textsuperscript{26}Cedefop. 2009. *Using tax incentives to promote education and training*, p. 57.
\textsuperscript{27}http://www.etudiant.gouv.fr/pid20441/bourses-et-aides.html
\textsuperscript{28}Such grants also have an age cap – with recipients required to be under the age of 28.
\textsuperscript{29}http://www.etudiant.gouv.fr/pid20441/bourses-et-aides.html