

Financing Higher Education

Answers from the UK

**Nicholas Barr and
Iain Crawford**

 **Routledge**
Taylor & Francis Group
LONDON AND NEW YORK

First published 2005
by Routledge
2 Park Square, Milton Park, Abingdon, Oxon OX14 4RN

Simultaneously published in the USA and Canada
by Routledge
270 Madison Ave, New York, NY 10016

Routledge is an imprint of the Taylor & Francis Group

© 2005 Nicholas Barr and Iain Crawford

Typeset in Baskerville by
Florence Production Ltd, Stoodleigh, Devon
Printed and bound in Great Britain by
The Cromwell Press, Trowbridge, Wiltshire

All rights reserved. No part of this book may be reprinted or reproduced or utilised in any form or by any electronic, mechanical, or other means, now known or hereafter invented, including photocopying and recording, or in any information storage or retrieval system, without permission in writing from the publishers.

British Library Cataloguing in Publication Data

A catalogue record for this book is available from the British Library

Library of Congress Cataloging in Publication Data

A catalog record for this book has been requested

ISBN 0-415-34620-7 (hbk)

ISBN 0-415-34857-9 (pbk)

Iain Crawford

Iain Crawford died in March 2004 after a long illness. In 1988 he and Nick Barr, while holding down their respective 'day jobs', embarked upon a sustained campaign for an income-contingent student loan system for the UK. Their message, often not well understood, was for a long time unpopular with the stakeholders, reluctant to reform. The process took its many interesting twists and turns, and for years it seemed that it was easier to deliver the Barr-Crawford message abroad than at home.

The campaign, like their friendship, was provocative and enduringly positive, the sum being greater than its parts. There was a solid foundation. Dubbed at times 'fanatics' by some, it is an enormous tribute to them both that the 2004 Higher Education Bill, which contains a good deal of their model, was given a Second Reading by the House of Commons in January this year.

It was just that Iain lived to see it, and for those of us who knew him personally, it serves as a mark of his political ability, his lateral thinking and downright determination.

Louise Crawford
Ardnamurchan
June 2004

Contents

<i>Foreword</i>	xi
<i>Preface</i>	xv
<i>Copyright acknowledgements</i>	xx
1 Higher education in Britain, 1987 to 2004	1
PART 1	
Introducing student loans	27
2 1987 Income-contingent loans: a central theme	29
Nicholas Barr (1987), <i>The Economics of the Welfare State</i>	29
3 1988 Setting universities free from central planning: a second central theme	34
John Barnes and Nicholas Barr (1988), 'Some Specific Policy Proposals', in <i>Strategies for Higher Education: The Alternative White Paper</i>	34
<i>Newspaper article</i>	
Nicholas Barr, 'Eight Votes for a Voucher System', <i>Guardian</i>	40
4 1989 A specific loan proposal	43
Nicholas Barr (1989), 'National Insuranced Based Loans', in <i>Student Loans: The Next Steps</i>	43
<i>Newspaper articles</i>	
Nicholas Barr, 'Student Loans Made Easy', <i>The Times</i>	60
Nicholas Barr, 'Student Loans: Disentangling the Myths of the White Paper', <i>Financial Times</i>	63
5 1990 The government loan scheme: a critique	66
Nicholas Barr (1989), 'The White Paper on Student Loans', <i>Journal of Social Policy</i>	66
<i>Newspaper article:</i>	
Nicholas Barr, 'Baker's Proposal: A Better Class of Drain', <i>Independent</i>	75

viii Contents

6 1991 Pulling the arguments together 77

Nicholas Barr (1991), 'Income-contingent Student Loans: An Idea Whose Time Has Come', in G. K. Shaw (ed.), *Economics, Culture and Education: Essays in Honour of Mark Blaug* 77

PART 2**The chickens come home to roost: the Dearing Report 99****7 1993 Alternative funding sources for higher education 101**

Nicholas Barr (1993), 'Alternative Funding Resources for Higher Education', *Economic Journal* 101

Newspaper articles

Iain Crawford and Nicholas Barr, 'Baker's Time Bomb Defused', *The Times Higher Education Supplement* 114

Iain Crawford and Nicholas Barr, 'A Loan Source of University Income', *The Times Higher Education Supplement* 118

8 1995 Education and the life cycle 120

Howard Glennerster, Jane Falkingham and Nicholas Barr (1995), 'Education Funding, Equity and the Life Cycle', in Jane Falkingham and John Hills (eds), *The Dynamic of Welfare: The Welfare State and the Life Cycle* 120

9 1997 Evidence to the Dearing Committee: funding higher education in an age of expansion 138

Nicholas Barr and Iain Crawford (1998), 'Funding Higher Education in an Age of Expansion', *Education Economics* 138

10 1998 The Dearing Report and the Government's response: a critique 169

Nicholas Barr and Iain Crawford (1998), 'The Dearing Report and the Government's Response: A Critique', *Political Quarterly* 169

Newspaper articles

Nicholas Barr and Iain Crawford, 'Opportunity Lost', *Guardian Education* 185

Nicholas Barr and Iain Crawford, 'A Better Class of Students', *Guardian Education* 188

Nicholas Barr and Iain Crawford, 'Universities in the First Division Should Charge Top Prices', *Guardian Education* 190

11 1998 An international view 193

Nicholas Barr (1998), 'Higher Education in Australia and Britain: What Lessons?', *Australian Economic Review* 193

PART 3	
Shifting tectonic plates: the 2004 legislation	209
12 2000 The benefits of education: what we know and what we don't	211
Nicholas Barr (2000), 'The Benefits of Education: What We Know and What We Don't', in <i>Economic Growth and Government Policy</i>	211
13 2002 Evidence to the Education Select Committee 1: funding higher education, policies for access and quality	231
Nicholas Barr (2002), 'Funding Higher Education: Policies for Access and Quality', House of Commons, Education and Skills Committee, <i>Post-16 Student Support</i> , Sixth Report of Session 2001–2	231
14 2002 Evidence to the Education Select Committee 2	262
Iain Crawford (2002), 'Funding Higher Education: Policies for Access and Quality: Supplementary Memorandum', House of Commons, Education and Skills Committee, <i>Post-16 Student Support</i> , Sixth Report of Session 2001–2	262
<i>Newspaper articles</i>	
Nicholas Barr and Iain Crawford, 'Access for All', <i>Guardian Education</i>	265
Nicholas Barr, 'A Way to Make Universities Universal', <i>Financial Times</i>	267
15 2003 The Higher Education White Paper: a critique	269
Nicholas Barr (2003), 'Financing Higher Education: Lessons from the UK Debate', <i>Political Quarterly</i>	269
<i>Newspaper articles</i>	
Nicholas Barr and Iain Crawford, 'Myth or Magic', <i>Guardian Education</i>	283
Nicholas Barr, 'A Good Deal for All the Family', <i>The Times Educational Supplement</i>	287
PART 4	
Onwards and outwards	289
16 Financing higher education: a universal model	291
<i>Index</i>	309

Foreword

Professor Lord Desai

This is the book that launched a revolution, one that is yet to finish its course, but I have no doubt that it will come to fruition. Like Lincoln Steffens I have seen the future and know it works. Indeed I had my first glimpse of the future in 1988 when Nicholas Barr, as a younger colleague at the LSE, sent me the first draft of his paper on loan-funded higher education. It was the summer holiday, in France, which for a university academic meant spending the time reading, writing and catching up with academic work not done in term-time. The proposal was quite innovative and I was immediately engaged by it. Nick Barr was exploring whether one could charge for higher education by giving income-contingent loans to the students in higher education, who (if full time and not ‘mature’) were then receiving it free. As a member of the Labour Party – and indeed Chair of one of its constituency parties – I was perfectly entitled to wear blinkers and argue that free higher education for all was the core of our beliefs, or of the British welfare state, or of socialism. Some of my House of Commons colleagues did just that when the Higher Education Bill was finally introduced early in 2004. But I knew then, as I know now, that we do not have universal free higher education at all. Only those who went on to higher education immediately after A levels were likely to receive full funding from their Local Education Authorities. The rest – part-time or mature students, or those in further education – were likely to be charged a fee. I did not cavil at the Barr idea because I knew that higher education, far from being a necessity, is a career choice. It benefits the receiver in terms of higher income over the life cycle of employment. Thus, while higher education may benefit society by various externalities, it is also a gift to those selected to receive higher education. Are the recipients deserving? This is where the debate gets muddled.

As of now the middle classes (A and B, and a few C1 in occupational categories) are overrepresented in higher education, and thus *prima facie* the gift of free higher education is a regressive transfer. The working-class students (C2, D and E) do not get their proportionate share. Originally this had nothing to do with fees charged, because if they qualified to go in at 18 years there was no fee; and there was until 1998 a maintenance

xii *Foreword*

grant on a means-tested basis. So the low incidence of working-class students had nothing to do with the expenses incurred. The reason for the low incidence was that few working-class students ‘stayed on’ in school beyond 16 years, i.e. beyond O levels or GCSEs. This could be partly due to the quality of schooling, especially the low expectations teachers had of those students, or because of higher value placed on earning an income immediately. The former requires a better schooling system; the latter is a matter of cost-benefit calculus. If there is an unhealthy myopia among working classes, it can be ameliorated by better information and counselling. Some pupils who do not go on to A levels or higher education may, of course, choose to go back in later years as mature students. Thus the inequity of the lower representation of working-class students can be dealt with by measures independent of the mode of financing higher education.

Alas, politics is never that simple, and the fact that higher education provision is financed almost exclusively from public funds – much like health care – makes politics central to the issue. Economists have known for a long time that the sectional interests of the entrenched receivers of public subsidies are often dressed up as the national interest. Thus during the Corn Law agitation, landlords argued how vital agriculture was to England’s military strength and public welfare. They also accused manufacturers of exploiting their workers, hoping thereby to split the alliance of industrial workers and industrialists against the Corn Laws. Karl Marx, no slouch at denouncing exploitation, still took the view that the Corn Laws needed to be abolished because cheap grain was good for the economy as well as for the buyers of grain. But between Ricardo’s discovery (simultaneously with Malthus and Barton) of the theory of rent in 1814 and the abolition of the Corn Laws in 1846, there is a gap of 32 years. What is more the Anti Corn Law League was a formidable political machine which put up candidates for Parliament and carried out a vigorous campaign for voter registration.

No such popular campaign has taken place for higher education financed by income-contingent loans. Indeed the campaign has been entirely for regressive subsidies masquerading as one for access of working-class students to higher education. The English middle classes have an ability to defend their subsidies on the grounds that if abolished poorer people will suffer. Universality becomes a battle cry in the full knowledge that despite universality the particular benefit will be a middle class capture. Indeed the Conservative Party which has its antennae close to the heartbeats of middle-class England (Scotland is a separate case and Wales is beginning to be different after devolution), took this into account when it expanded access to higher education in the Great Education Reform Bill (GERBIL). Instead of charging the better-off for money to fund greater access, it kept the higher education grant pretty much the same and allowed the unit of resource to shrink. This cowardice cost the universities dear, and for ten

Foreword xiii

years after 1989 the steady impoverishment of universities was the untold horror story of English social life.

The story remained untold because English higher education is crippled by the existence of Oxbridge; and the public image of universities on TV and in the print media is of dreamy spires with clean-cut lawns, lazy summer punts and fellows running around in gowns and mortar boards. The great English public thinks all universities are places of privilege and prosperity. This has deprived the universities of any public sympathy in their fight for more money, and given politicians a stick to beat universities with. This is the cry for access, i.e. access to Oxbridge colleges for students from comprehensive schools, especially those from working-class background. This issue is separate from that of funding but mixing the two up has benefited the opponents of the Barr-Crawford proposals. The result has been a sorry mangled debate on the Higher Education Bill in the Commons with the simplicity of the original proposals messed up by many restrictions and concessions.

But even so I believe that the Barr-Crawford proposals will win support in the end in their full simplicity. The other part of the duo, Iain Crawford, was politically savvy and knew the electoral pressures that drive such debates. He was not himself from a privileged background and had made his way to LSE as a mature student. He knew the Scottish angle and could translate his proposals to suit other systems, as they did in Hungary. Barr and Crawford are acutely aware of equity issues as they are on the ground, rather than as mythologised by middle-class pressure groups to terrify MPs. If you have income-contingent loans you are borrowing against your future income to pay for the education which guarantees you that higher future income. Thus while parental incomes of potential entrants to higher education are unequal, their future incomes after higher education are much less unequal. Thus *ex post* equity is a better way of judging the proposals than equity *ex ante*. This is where the beauty of the proposal lies, because given the uncertainty it is better to rely on *ex post* outcomes. Of course the payments have to be upfront. The loan proposal says that the government pays up front and then collects the money from the beneficiaries as a fraction of their subsequent earnings. Those MPs who have put constraints on the proposals have kept the present inequities even as they claim to speak for the less well-off.

The intellectual journey is set out very clearly in this collection of articles. What is harder to convey is the sheer thrill of being part of a revolution in the mode of thinking about the finance of higher education. This was partly because Nicholas Barr is a superb pedagogue but also because Iain Crawford could tell great stories and make even the most technical economic argument lively. I feel lucky to have been there right from the beginning, and hope to be still here when the revolution is complete.

Meghnad Desai
May 2004

Preface

In November 1987, the Secretary of State for Education, Kenneth Baker (now Lord Baker of Dorking) published a White Paper (UK Department for Education and Science 1987) foreshadowing the 1988 Education Reform Act which, in effect, nationalised Britain's universities. On 27 January 2004, the House of Commons, after bitter dispute and by a majority of only five, gave a Second Reading to a Higher Education Bill which restored a measure of autonomy and competition. The Bill received Royal Assent in July 2004.

In policy terms, therefore, this is a story with a happy ending. But it is clearly also a long one. Iain and I first met by chance in late 1987. He was finishing an undergraduate degree at the London School of Economics (LSE), which he had started as a mature student, but from which he had taken time out to fight a Parliamentary seat in the 1987 General Election. At the time, he had just accepted a part-time job with a specific remit to consider the School's position in connection with some of the White Paper's proposals. I had recently published the first edition of *The Economics of the Welfare State* (1987), which applied the then fairly new economics of information to the welfare state, considering in particular where markets were likely to work well (e.g. food) and where badly (health care, school education). The book included a short section on student loans (Chapter 2, this volume).

We both attended a meeting at LSE in March 1988 to discuss how academics might head off the worst features of the Education Reform Bill. Iain's view was blunt: 'Don't start from here.' Instead, he argued, we should set the scene for the next time the issue became salient. In short order, he engineered a slot for me to appear on the 'Today' programme on BBC Radio 4, with more to follow, and encouraged me to write an article for *The Times Higher Education Supplement* about my current research on student poverty.

The mix worked instantly, so that we were able to do together what neither of us could have done alone. To some extent, my main contributions were the analytics and the writing, Iain's the political nous and understanding of the media, but that oversimplifies the nature of the joint

xvi *Preface*

creative process, which was driven by a shared passion to widen access and an increasing fascination with the broader topic of higher education finance. That passion emerged in very different ways from two very different people. I remember at an early stage making the academic's comment that 'it's nice to get the argument right'. Iain, the politician, commented darkly, 'it's nice to win!'.

The process involved endless discussion. Writing together would often see Iain pacing up and down the room talking; I would sit at the keyboard, assembling words whose correlation with what Iain was saying could be total, partial or zero; periodically he would peer over my shoulder to approve or to suggest revisions. Over time, there was some crossover in our skills, though we continued to rely on each other when the chips were down.

The process was also enormous fun. Much of this book was originally written for academic journals, government inquiries or Parliamentary Select Committees (we were always prepared to talk to politicians of any political party who wanted to talk to us), so that the language tends to be formal, but I hope that some of the fun emerges even there, and perhaps more obviously in some of the newspaper articles interspersed among the chapters.

Apart from the first and last chapters, which are new, the rest of the book is a selection of our published work. Articles are left almost entirely as they were written. The inevitable price – some repetition – is deliberate. The book is not only about the state of play today, but an account of the 16-year campaign as it really was, and a sobering reminder of how many times an idea has to be pressed before it is translated from journal article into legislation.

This volume is aimed at a broad readership. Though much of the writing is about the UK debate, the book is written to bring out the more general lessons for other countries, and is thus acutely relevant to policy-makers in the OECD, and in post-communist and middle-income developing countries, including officials in Ministries of Finance and Education, and in international organisations such as the International Monetary Fund, the World Bank and the United Nations. In the academic world, it should be of interest to economists and colleagues in departments of social policy and public policy. It should be of interest also in related areas such as political economy, as illustrating the difficulties of implementing change and pointing to some of the tools necessary to bring it about. Readers who are short of time should read Chapters 1 and 16, after which any of the remaining chapters can be read as free-standing.

Our ideas were clear from an early stage. They would not, however, have come to fruition without generous help from many friends and colleagues – none of whom should be blamed for the result. Our starting point was to advocate student loans with income-contingent repayments, i.e. repayments calculated as $x\%$ of the borrower's subsequent earnings, rather than a fixed sum of £ x per month, like a mortgage or bank overdraft. The history of the idea is set out more fully in Chapter 6: it was first proposed by Milton Friedman (1955; see also Friedman 1962, pp. 103–5)

Preface xvii

and, in a UK context, by Peacock and Wiseman (1962) and Prest (1962) in evidence to the Robbins Report (UK Committee on Higher Education 1963) and by Glennerster, Merrett and Wilson (1968). The 1960s debate is summarised by Blaug (1970, pp. 293–307), and Robbins' conversion to this type of loan in Robbins (1980).

More immediately, many people helped me with *The Economics of the Welfare State* which was the intellectual foundation of our work. Early in our higher education campaign, the persistent advocacy of education vouchers by John Barnes, then in LSE's Department of Government, gave me the impetus to think things through and to realise that the analytical basis of my hostility to vouchers for school education did not follow through into higher education: students are better informed than school children and hence better able to make choices; and it is possible to construct voucher schemes with a strong redistributive gradient.

Mervyn King (then a colleague in the Economics Department at the School, now Governor of the Bank of England) suggested in a conversation in July 1988 that piggy-backing student loans on National Insurance contributions, as well as having administrative advantages, also made clear the idea that student loans are a form of redistribution to oneself over the life cycle, analogous to pensions, thus providing an idea with great resonance, which did a great deal to build early support for income-contingency.

Many others gave enthusiastic help in the early days and hence had a major impact on the writing in Part 1. Meghnad (now Lord) Desai took time from his summer holiday, as did Gail Wilson, to comment on early drafts. Mark Blaug patiently tutored me in the economics of education. Alan Peacock gave generous support, both through supportive comments, and in a practical way by encouraging the David Hume Institute to co-publish two early pieces of writing. Tony Atkinson and Nicholas Stern, successive Chairs of LSE's Suntory-Toyota International Centre for Economics and Related Disciplines, gave consistent support including research funding for an early study of student poverty (Barr and Low 1988), for a conference on 'The Future Funding and Management of British Higher Education' at the LSE in September 1988 and for co-publishing some of our work with the David Hume Institute. I am grateful also to Gervas Huxley and Maureen Woodhall.

The chapters in Part 2, particularly the quantitative estimates of the effectiveness of different loan regimes, draw on joint work with Jane Falkingham using LIFEMOD, a microsimulation model she had helped to develop. Some of those chapters, and even more those in Part 3, owe a great deal to Colin Ward, till 2003 Chief Executive of the UK Student Loans Company, the publicly-owned loans administration, who shared our commitment to student loans as part of a strategy to promote access and contributed in important ways on factual matters, policy thinking and technical design. From 1999–2001 we advised the Hungarian government on the design and implementation of an income-contingent student loan

xviii *Preface*

scheme in collaboration with Colin Ward and his colleague Hugh Macadie, from whom we learned a huge amount about the practicalities of loans administration, which fed into our evidence to the UK Education Select Committee (Chapters 15–17).

Government and Parliament – notwithstanding that for most of the period we were guerillas fighting government policy – also deserve thanks. Early loan proposals were sent to Robert Jackson, then Minister for Higher Education. We come from different political backgrounds, and disagreed strongly over some aspects of the proposals; but the disagreement was always constructive and helped to improve the scheme. The House of Commons Education Select Committee also played an increasing role under the chairmanship of Margaret Hodge in the immediate aftermath of the 1997 Dearing Report, and of Barry Sheerman around the time of the 2003 White Paper and 2004 Higher Education Bill.

We have also benefited from colleagues and events in other countries, including many useful conversations with Bruce Chapman and Gary Hawke. I am grateful for spells as academic visitor at the University of Melbourne and the Australian National University, and for assistance from colleagues at the IMF, while visiting their Fiscal Affairs Department, on the intricacies of national income accounting.

We are also grateful for financial support to the Suntory-Toyota International Centre for Economics and Related Disciplines at the LSE; to the Esmée Fairbairn Charitable Trust for financing much of our work in 1989 and 1990; and to British Petroleum for financing work on widening access which included the research with Jane Falkingham on simulating different loan schemes. Much of our work on either side of the publication of the Dearing Report in 1997 was supported by two grants from the Nuffield Foundation.

Thanks are due also to Meghnad Desai and Neil Gregory who first suggested this book, and to John Ashworth, Gyula Gilly, Adrian Hall, Hugh Macadie, Erika Papp, Gus Stewart and Colin Ward for helpful comments on drafts of Chapters 1 and 16.

Our final thanks are to our wives, Gill and Louise, who have been argumentative, opinionated, exasperated (fortunately not with us), and unfailingly supportive. Over the years, the duo turned into a quartet.

Nicholas Barr
London
June 2004

References

- Barr, Nicholas (1987), *The Economics of the Welfare State*, London: Weidenfeld & Nicolson, and Stanford, Calif.: Stanford University Press.
- Barr, Nicholas (ed.) (2001), *Economic Theory and the Welfare State, Vol. I: Theory, Vol. II: Income Transfers, and Vol. III: Benefits in Kind*, Edward Elgar Library in Critical Writings in Economics, Cheltenham and Northampton, Mass.: Edward Elgar.

Preface xix

- Barr, Nicholas and Low, William (1988), *Student Grants and Student Poverty*, Welfare State Programme, Discussion Paper WSP/28, London: London School of Economics.
- Blaug, Mark (1970), *An Introduction to the Economics of Education*, London: Penguin.
- Friedman, Milton (1955), 'The Role of Government in Education', in Solo, A (ed.), *Economics and the Public Interest*, New Brunswick, NJ: Rutgers University Press, pp. 123–44.
- Friedman, Milton (1962), *Capitalism and Freedom*, Chicago: University of Chicago Press, Ch. 6, pp. 85–107, reprinted in Barr (2001, Vol. III, pp. 547–69).
- Glennerster, Howard, Merrett, Stephen and Wilson, Gail (1968), 'A Graduate Tax', *Higher Education Review*, Vol. 1, No. 1, pp. 26–38, reprinted in Barr (2001, Vol. III, pp. 570–82), and in *Higher Education Review*, Vol. 35, No. 2 (Spring), pp. 25–40.
- Peacock, Alan and Wiseman, Jack (1962), 'The Economics of Higher Education', *Higher Education: Evidence – Part Two: Documentary Evidence*, Cmnd 2154-XII, pp. 129–38. London: HMSO, 1963.
- Prest, Alan (1962), 'The Finance of University Education in Great Britain', *Higher Education: Evidence – Part Two: Documentary Evidence*, Cmnd 2154-XII, pp. 139–52. London: HMSO, 1963.
- Robbins, Lionel C. (1980), *Higher Education Revisited*, London: Macmillan.
- UK Committee on Higher Education (1963), *Higher Education* (The Robbins Report), Cmnd 2154, London: HMSO.
- UK Department of Education and Science (1987), *Higher Education: Meeting the Challenge*, Cmnd 114, London: HMSO.