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## **A NEW SYSTEM OF TOP-UP FEES: A BRIEF ON THE MARKET RESPONSE OF ENGLISH UNIVERSITIES AND COLLEGES \***

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**John Aubrey Douglass**  
UC Berkeley

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### **ABSTRACT**

Fees will become an increasingly important funding source for public universities in the UK and throughout the OECD, caused in part by declining government subsidization and rising costs, as well as by an increasingly entrepreneurial drive by institutions themselves to increase revenues. Beginning in September 2006, universities and Further Education colleges in England and Wales will charge variable fees within limits set by a defined cap and by ministry demands for increases in institutional aid for lower income students. This essay chronicles the response of England's universities. Not surprisingly, most will charge the maximum amount allowed; at the same time, levels of bursaries (financial aid) will vary between institutions. The response and plans of English universities, and the subsequent response of both the market and students, will likely have a significant influence on other OECD nations, particularly those in the European Union, as they gradually consider a similar variable fee scheme.

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While fees for graduate programs, particularly in business, have been charged for some time in EU institutions, the UK is the first member to embark on a national course of variable fees at the undergraduate level – particularly in England and Wales. The successes or failures experienced in the UK will likely have a significant influence on the rest of Europe, and elsewhere, as other nations also struggle to both adequately fund higher education and bolster participation rates.

### **England's Path to Top-Up Fees**

In 1997, the Labour government adopted the recommendation of the Deering Committee to initiate a £1,000 fee for all students. Under the 2004 Higher Education Act passed by

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Parliament, universities and further education (FE) colleges are allowed, beginning in September 2006, to charge full-time students up to £3,000 for a course.

There are 122 universities in England and Wales. FE colleges are local institutions that thus far serve primarily to prepare students for A-Levels and to provide vocational degrees and credentials, but many now offer a growing number of "higher education" courses leading to the new Foundation Degree (given in conjunction with a particular university) or other degree form. More than forty FE colleges offer formal higher education courses leading to a degree or credential.

The proposal by Prime Minister Tony Blair and his ministers to increase fees, as part of a larger government attempt to increase funding for higher education, caused great consternation in England and within the Labour Party itself. New Labour essentially diverged even further from its historical ideological roots by embracing the idea of markets. The deciding vote in Parliament was narrowly won; its defeat would have forced a premature election for Blair.

Fees will become a more substantial source of income for England's financially starved higher education sector. And England is further distancing itself from the higher education funding norms found in most of Europe, where universities by and large remain free (although we might wonder for how long). England is even distancing itself from Scotland, a fellow member of the UK. Under devolution, Scotland has set a distinct path of charging no fees, yet also offering needy students loans that can be repaid later.

England has a significantly deeper passion for maintaining key elements of the welfare state, but as in the US, the concept of increasing the financial contribution of students and their families to their university or college education is a political paradigm that is new and worrisome to many. How will this fee structure influence access to higher education for England's lower classes and minorities? And more specifically, how might it influence the Labour government's goal of having 50% of all 18 to 30 year-olds entering higher education by 2010? The current rate is approximately 43% (depending on how one counts).

Labour recognized that higher education needs an infusion of funding, in part to maintain or increase quality *and* to provide the sector with the ability and incentive to grow in enrollment capacity. In earlier policy debates, government ministers contemplated setting the new fee limit at £5,000 as advocated by vice chancellors from a number of elite UK universities. The compromise with critics within the party and in Parliament was not only to lower that amount to £3,000, but also to also create a deferred, post-graduate repayment plan.

Students will be able to defer these "top-up" fees by applying for a student loan from the national government rather than paying the fees in advance. The student loan is repayable directly to the government via the national income tax system, and only when the graduate starts earning more than £17,000 a year (recently raised from approximately £15,000). This loan to students will incur no interest and will increase only with the rate of inflation. Graduates will repay the loan at a rate of 9% of their income above £17,000 until it is fully paid. Currently, England has among the highest university graduation rates leading to the assumption that most students will relatively quickly gain employment and the ability to repay their loans.

The net effect of the top-up scheme is that some students will pay in advance (those whose family can afford to), while others will choose to shoulder the full cost themselves. The Higher Education Funding Council for England (HEFCE) anticipates that some 30% of students will qualify for a loan for the full amount of the fees and more than 50% will qualify for at least part of it. "So someone earning £20,000 a year will only have to repay £8.65 a week, or someone earning £25,000 a year will only have to repay £17.30 a week," explained higher education minister Bill Rammell in June, 2005. The government plans a £3.5 million television and radio campaign to explain the new "top-up" fee system—clearly intended not only to inform students, but also to alleviate criticism and reported confusion among lower-income students.

Under Blair and the advocacy of Charles Clark, then head of HEFCE, the Labour government moved ahead with its variable-fee plan. One major assumption is that this new quasi-market ("quasi-" in that the fee level is restricted to what, in American terms, is a relatively modest level) will create greater competition among public institutions and, as a consequence, greater focus on their mission (e.g., teaching versus research).

### **The Market Response**

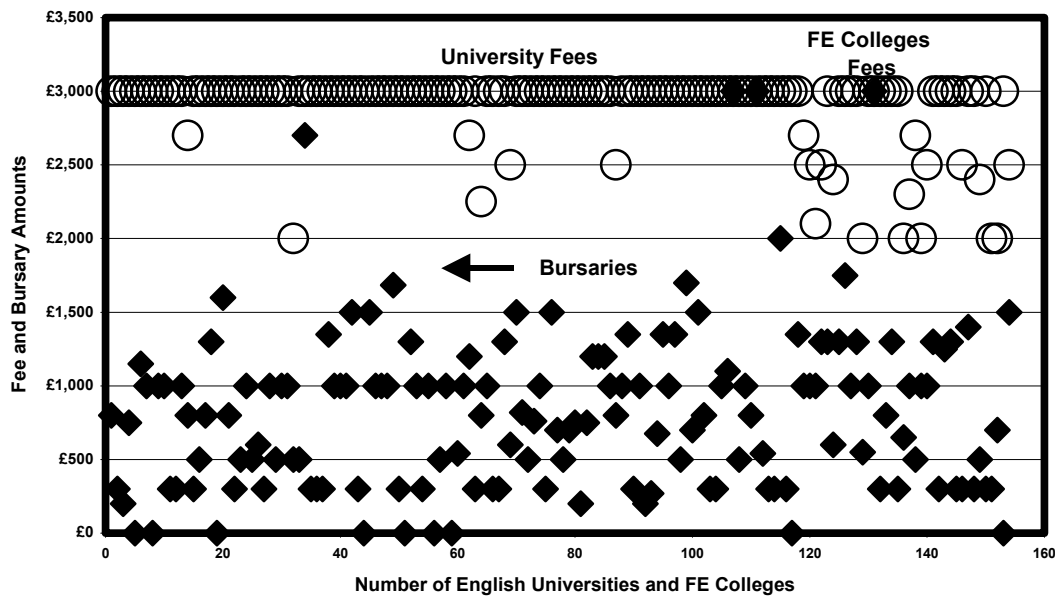
As required by HEFCE, universities and FE colleges have submitted their planned undergraduate fees and outline of bursaries. Not surprisingly, virtually all institutions—universities and FE colleges alike—will charge the full £3,000 fee. Among the major reasons for this are:

- the need for additional revenue in the face of past declines in government investment rates on a per-student basis;
- a sense that under-pricing courses will indicate to consumers that the institution's product is of lower quality; and
- the general tendency of producers of a product or service with relatively high demand to move to the highest price the market (or the quasi-market, in this case) will bear.

One sees a similar response in the US HE market: most elite private universities, even without any formal regulatory restraints, charge similar rates and have great similarities in their bursaries.

Figure 1 provides a chart of the fees that will be charged by universities and FE colleges, and the distribution of cash bursaries for students from families who make less than £17,500 in a year—the current threshold for national student loans and grants. Among the 122 universities in England, only eight will charge below the £3,000 limit, although there are a few exceptions for certain courses. Within the FE sector there is a bit more diversity in the planned fee levels: of the thirty-three that have reported their plans, fourteen will charge below the limit of £3,000 pounds, but none are planning fees lower than £2,000.

**Figure 1.** Planned Fees and Bursaries in English Universities and Further Education Colleges: 2006-07



Source: Universities UK, 2005

While there is a relatively uniform response from institutions to setting fees, cash and other forms of institution-based financial aid support (or bursaries) will vary greatly. Labour government policy requires institutions to state their planned fee levels and the bursaries intended to offset fee costs for lower-income students (beyond aid offered by the national government, primarily for living expenses). The government also requires all institutions to state their strategy for increasing admissions to disadvantaged students, requiring the approval of the new Office of Fair Access (OFFA) to approve their plans and to set specific goals.

Figure 1 provides the stated bursaries offered to students on full government support (hence, in addition to normal financial aid offered). These stated bursaries generally range from £500 to £1,250 at universities and colleges that are moderately selective in admissions, to as much as £3,000 at Cambridge and Oxford, and £2,700 at Imperial College.

Under the relatively new rules of devolution (giving regional governments in Scotland and Wales authority in policy areas such as education), Wales will allow its universities to charge up to the £3,000 level as well beginning in fall 2006, but in contrast to England the government has set a required bursary contribution from each university and college that will then be placed in a central fund and distributed to needy students. Scotland, with a substantially different postsecondary system, continues to charge no fees.

In England, OFFA represents a new regulatory regime intended to hold universities accountable for meeting national access targets. If an institution does not expand access to lower-income groups and fails to meet negotiated targets, HEFCE may reduce funding as a penalty.

One can imagine that the response of universities and FE colleges in setting their fee levels would have been far more diverse if the fee limit had been set at £10,000 or more. Indeed, many members of the Russell Group (a self-chosen and loose alliance of fourteen of England's most prestigious universities) have advocated open-market pricing for their courses. One professed reason is the need for a large infusion of resources so that England's best universities can compete in the international market for faculty—in particular, to compete with the Americans.

Although the various bursary schemes add substantial complexity to the final outcome (in terms of new revenue generation and influence on access), one possible scenario is that the most prestigious universities, such as Oxbridge, will benefit the most from the new fee structure. With fewer students from low-income families than many other—and largely urban—universities, bursary distributions would likely be less (even while offering full reimbursement to low-income students). As yet, this is obviously speculation, and must await the outcome of the first year of top-up fees.

### **Creating a New Model?**

In developing its top-up fee policies, the Labour government looked at the lessons offered by Australia's earlier effort to both raise student fees and delay repayment. One concern both among the higher education community and government ministers and officials was tying fees into an overall plan to increase funding for universities and colleges in England. In Australia, government pushed hard to create its top-up fee policy and universities generally embraced the shift, thinking it would generate new revenues. However, to the great frustration of the university sector, the Australian government proceeded to make significant cuts in funding for higher education.

The Labor government, under Tony Blair and Charles Clarke, then the minister responsible for higher education, promised to avoid that trap—in part to gain the support of the university officials, and in part because of recognized need to boost funding for higher education. While enrollment in England had exploded between 1989 and 1997, public funding per student declined by some 36%. Labour promised to turn that tide. As part of its new £3,000 fee limit, Blair and Clarke, along with Chancellor of the Exchequer Gordon Brown, promised an annual 6 percent increase over three years for both teaching and research, representing a total three year commitment of £2.3 billion (or approximately \$3.6 billion).

What this means is that at the beginning of the next fiscal year in England, not only will the government need to continue to increase funding for university operating expenses, but it will also need to pay a sizable bill for those students who choose to delay paying their universities fees. While given the option to pay up front, most students will qualify for the new top-up fee loans and will delay their repayment under the lenient repayment scheme offered by the government, as noted above. Finding the funds for this new and sizable expense will be politically difficult. Brown and the Labour government have been criticized for borrowing too much. Even without this new expense, the UK faces the problem of reducing government debt, which already exceeds the 3% of GDP limit set by the EU—from an American view a rather enviously low level of debt.

It appears that Labour will honor its financial commitments to higher education in the UK. But an interesting question is how increasing debt and the predictable criticisms

regarding the top-up fees (for example, it may have an initial negative impact on university access rates among disadvantaged groups) will influence the standing of the Labour government and Brown, the prime minister heir apparent.

Another major question is the trajectory of the variable-fee trends in the UK. In England, many view the £3,000 limit on fees as simply a temporary restraint that will lead to an eventual increase to a figure like £10,000. Already, business schools in the UK are allowed to charge substantially higher fees that align with EU and American competitors. At this time, business schools form the only major aberration to the otherwise uniform constraint on fees in the EU.

In the US, with similar political and regulatory constraints on what public universities and colleges can charge, the push will be to converge with graduate program fees in the private institutions (fee rates that do not often relate directly to program costs, but rather to what the market will bear) and to approach undergraduate fees. Yet another variable in both the US and the EU is the potential growth in international students, expanding the pool of potential students and revenues alike.

The response and plans of English universities, and the subsequent reactions of both the market and students that will unfold over the next year, will likely have a significant influence on other OECD nations, particularly those in the European Union, as they gradually consider a similar variable fee scheme. With governments in the OECD and elsewhere looking for other funding sources besides government coffers to fund and expand national higher education systems, it is perhaps inevitable that many countries will move toward a moderate fee and high financial aid model. Within the EU context, England's successes and failures over the next year therefore will be closely watched.