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Adjusting to the Future

In each chapter to this point, we have analysed shortcomings in the current university funding arrangements, but have stopped just at the point of making policy recommendations. This is because we have wanted to bring everything together in constructing holistic policies.

The objectives of changes of policy initiated by the Browne Report were:

1. to improve participation and in particular access from less advantaged groups;
2. to improve quality and student choice in a diverse system by creating a market leading to competition.

We believe that creating a market was neither necessary nor desirable in achieving the stated aims, which we otherwise completely support. However, we have taken the regime change on its own terms and will continue to do so in this chapter. It is for the government of the day to determine the funding regime, and the current government clearly supports the market elements arising from the Browne review.

Our problem is that the manner in which the Browne Report was implemented and the way in which subsequent policy has developed has led to a failure to achieve the stated objectives. The system constructed is simply inefficient in its inability to encourage competition and in how it rewards failure. Further, it has encouraged micromanagement of and within universities to the detriment of the traditional focus on the academic esprit that has been essential to the high standing traditionally enjoyed by our Higher Education system.

In the following, we present clear and concrete policies that follow recommendations made (for example) by Browne. Further, everything is not only 'costed' but we impose the rigorous rule that additional support from the taxpayer cannot be provided at this time. The sector has done extremely well in funding over the period of national austerity, and the priorities lie elsewhere.

The hierarchy of universities

The economics model of marriage is based upon the idea of 'assortative matching', where individuals of similar standing in characteristics form relationships. This model can be applied more widely and is relevant to universities. Suppose there are good and weak students. If learning is 'complementary', putting the good students together and the weak students together produces more learning than if there are two mixed groups. In this world, it is efficient to match together the good students. But, even if it is not efficient, this may be the outcome on the basis of individual interest. If the good students benefit from interacting with each other, they may prefer to work together even if the weak students could gain immensely from interaction. By 'good' we are using a shorthand in what follows for the highly focused academic qualities sought by traditional universities. This is not to imply negativity to other talents and abilities or the difficulty of identifying the 'good' and the 'weak' or the possible potential of a 'weak' student. But it shows a further reason why self-interest may not lead to efficient outcomes in this sector and why the sector is so very hierarchical.

The change to an uncapped, high fee system has actually increased the hierarchical nature of universities rather than leading to the intended competition across universities. This is for two reasons. The ability to expand has meant that a greater proportion of good students can go to a limited number of universities. The top universities can cream off the good students. But in addition, for reasons we have stated in Chapter Three, universities below the top have tended to go down-market, taking students from the next lower stage in the hierarchy. This has led to grade inflation and lowering of tariffs as marketing tools and the weakening of the academic content of programmes. The relative advantage to a good student of going to a top university has risen. In the past, an advisor could argue to a student that University X was better for their needs and interests than higher-ranked University Y. University X might be in a better location for them, have extracurricular provision that fits well with the student's interests in music or the sports, or have particular programmes that match the student's interests. But now it is hard to advise a student to turn down a place at a Russell Group university to go elsewhere.

This means that there is also now an increased payoff to being considered a top university rather than just a good university. For this reason, it is not surprising that the Russell Group developed itself as an extremely effective marketing tool. Politicians and the media, and consequently parents and students have come to believe that the Group comprises all of the top universities in the UK. In its marketing publication 'Profile', the Group emphasises the network externalities we have described – 'our students benefit from working with and learning from a highly-motivated and talented peer group'.

Prior to the changes in the funding regime, a second group of top universities existed. The '1994 Group' was founded in the same year as the Russell Group and was made up of universities with very strong research records that most would have seen as indistinguishable from the Russell Group. The main distinguishing factor was size and the original members of the Russell Group typically had medical schools and large engineering departments. The 1994 Group members were on the whole smaller universities based on a single campus offering high-class research and teaching in a collegiate atmosphere. But with the increased returns to establishing a place at the top of the hierarchy, individual members of the 1994 Group sought membership with the Russell Group. When the Russell Group admitted 1994 Group members Durham, Exeter, Queen Mary and York in 2012, the 1994 Group became unsustainable as a second group seeking to distinguish itself as also being leading research universities, and it disbanded.

A further group of top schools and colleges (that could demarcate themselves separately as universities) are those of the University of London. The University of London had developed as a more interlocked group than the Russell Group or the 1994

Group, with some quality control exercised across the colleges and some significant university facilities such as the Senate House Library. Imperial College left the University of London in 2007 and the university became decentralised well before the change in fee regime. More recently, City University joined the University of London, an indication of the value of the brand name.

While the University of London has diminished in effectiveness, it has not followed the 1994 Group and disbanded. The University of London contains the large Colleges: Queen Mary (Russell), City, Goldsmiths, SOAS, Birkbeck, UCL (Russell), LSE (Russell), Kings (Russell), Royal Holloway and the specialist Royal Veterinary College, the London School of Hygiene and Tropical Medicine and St Georges Medical School. The simple fact is that, for a College in the Russell Group, the University of London name carries little additional weight. The options were either to form a grouping of common purpose among the non-Russell colleges, or to have a diminished and secondary University of London that weights the preferences of the Russell Group members. The outcome was the second option, leaving the non-Russell Group members only marginally better off than non-Russell, non-University of London universities of comparable stature. This is an example of the inefficiencies of the current funding regime. The internationally recognised brand of the 'University of London' is being downgraded, affecting the recruitment of overseas students for whom the 'University of London' degree has traditionally had high cachet.

The extremely good non-Russell universities formerly in the 1994 Group or still within the University of London complain that life is unfair, that they are just as good as the Russell Group universities. This unfortunately fails to understand the nature of clubs such as the Russell Group. You are admitted to a club not because you'd like to be, or out of fairness, but because it is in the interest of the existing members. The standard economic theory of clubs is that there are fixed costs – for example, the costs of maintaining the club building – and adding another member allows these to be spread more widely. This was pertinent to the University of London, with its central Library and Administrative facilities, but is less pertinent to the Russell Group. Indeed, in some ways the raison d'être of the Russell Group is to somewhat arbitrarily take a portion of the good universities and self-certify some of them as 'elite' to give them a competitive advantage – there would be little point in this unless some good competitors were in effect 'declassified', making it harder for them to compete. Indeed, a cynical view is that the Russell Group admitted just enough universities to force the disbandment of the 1994 Group and even weaken the University of London. We wonder whether or not it was wise for the remaining 1994 Group universities to disband the organisation, given that it gave them a common voice in consultations such as the current review of Higher Education. Certainly, the post-1992 universities have gained a voice through their organisation, MillionPlus.

This somewhat long-winded discussion leads to the simple conclusion that the Russell Group universities have become disproportionate to the sector due to essentially network externalities. Their student numbers have grown massively at the expense of the very good universities next down in the hierarchy. This is economically inefficient but also damages the very brand of 'elite' that the Russell Group seeks to establish. Further, the dominance of this group effectively destroys rather than enhances competition. One way forward is to impose individual or group caps just for these universities. By limiting their student numbers, we would give other universities 'room to breathe'. However, as we discuss below, we think that there are other policies that better integrate the objective of restoring competition with effective mechanisms for widening participation.

Restoring competition

As we have described in Chapter Three, there is effectively no financial incentive to compete for the best students in the current framework. A university in the next tier below the Russell Group could have used the additional funding to cut its student–staff ratio (SSR) and otherwise enhance the academic value of its offering. It has been easier, and less costly, to simply go down the demand curve and admit students with lower entry points.

Browne gave a perfectly plausible mechanism for establishing competition – cap the overall number of students so that universities have to compete for students. In Chapter Three, we showed that under this regime, universities would find it effective to compete for top students. Consider, for example, the position of the LSE and other universities in London with good economics programmes. Even without the benefit of NSS (National Student Survey) scores and the TEF (Teaching Excellence Framework), prospective students know that – if they go to the LSE – they will likely be taught by PhD students and not by world-famous professors. As we have argued above, a good student will still be inclined to go to the LSE since they get to interact with other good students, even leaving aside the prestige of the LSE degree. Now suppose that one of the other London universities ups its game in Economics by significantly lowering its SSR and in other academic ways. Some good students will now be more on the margin between the LSE and this other university. The LSE, provided that the numbers of students involved are not too large, will not incur the costs of increasing its focus upon undergraduate teaching, which would involve doing so for all its students. The other university will therefore be able to 'poach' a limited number of top students away from the LSE and under the principle of assortative matching this would attract further top students.

That whole story relied upon two things – the other university, ranked lower in the hierarchy than the LSE, has to engage in real expenditure on academic aspects of the programme, and – even then – cannot be too ambitious in the number of students it is seeking to attract. In effect, the second university becomes a 'boutique' university, smaller in size and offering an experience tailored to a limited market. We think this is analogous to the hotel market. Depending upon one's desired expenditure level, there are hotel chains ranging from the Mandarin Oriental and the Four Seasons, working down through intermediate ranges of the Hiltons and Marriotts, before going to the Premier Inns. The brand name provides a labelling of the expected quality and level of services in the different hotels. But there remains a market for niche, boutique hotels of every quality and price level. Further, the Mandarin Oriental is not too bothered if a small boutique five-star hotel opens nearby and takes away a small number of its customers.

We expect that, once a system is set up that requires competition and universities realise that they have to compete and can no longer pile up lots of less-qualified students, we will move away from the 'cookie cutter' approach that has been adopted in the current environment. One of the most dispiriting features of the current markets without competition is that everyone is seeking to be in the same space and this is encouraged by league tables, where everybody is ranked by the same criteria. As we have commented, at present the only way to move up the tables is to mimic those above so that they encourage uniformity rather than the aim of diversity. Restoration of competition means that each university needs to find its niche, to find its USP.

During the Second World War, German artistic emigres landed at Black Mountain College in North Carolina. This obscure institution became the place to be for modern art and music. In England, Morley College in Lambeth had Gustav Holst as its Music Director, a post subsequently taken by Michael Tippett. Currently, London South Bank University is the home of the National Bakery School. If you want to hire apprentices for your bakery or restaurant, LSBU is the place to look. As you go through the list of universities in England, each institution jumps out as having particular strengths. Goldsmiths is the university of the Young British Artists, SOAS has its focus on ethnography, Birkbeck provides evening education of the highest quality. Everybody knows of the specialist work of the London School of Hygiene and Tropical Medicine and the Royal Agricultural College (now University). In these ways, each institution should strive to be among the best in a particular field.

Some universities, notably the former polytechnics, while having areas of research strength, are in general more focused on teaching quality. Without an expensive research overhead, these universities can operate on a lower cost basis than other, research-intensive institutions. The Browne proposals, and government expectations, were that universities would engage in price competition. However, participants in the sector considered this highly unlikely, since lowering the price would be taken as a signal of lower quality. Even if that were not the case, each university has some monopoly power and will not want to lower fees for all students in order to attract a few more. We propose to mitigate this factor by offering universities two fee options, where the university can either set the base fee (to be discussed below) or it can set a reduced fee, with additional support provided by a central grant per student making up a significant part of the fee differential. We will come back to this when we discuss the situation from the perspective of students.

The government has emphasised the potential role for private providers. Based upon the US experience described in Chapter Six, this should be limited to 'career colleges' that are tightly regulated and subject to external professional examinations. We see potential expansion of private providers in the traditional university sector as lessening quality competition, not raising it. If private providers take over 'bread-and-butter' provision in low-cost subjects such as Business Studies – a reliable source of income for universities – this just means that student fees for high-cost subjects will have to go up. We take the same view as the BMA does on private contracts in the NHS – they are a costly diversion from the main business of the health service, taking away more straightforward and risk free procedures, leaving expensive and more difficult cases for the specialists in the NHS.

QAA, NSS, TEF and all that

We have a clear proposal here. This is that the NSS and TEF should be discontinued, and that the functions of the QAA should be to assure quality in the sense of the validity of degrees through the examination process, notably by restoring the effectiveness of the external examination system, and to have a continuing role in assuring that systems for sound governance are in place.

League tables, based in part upon the NSS, have become extremely misleading. Our particular concern is that the great impact of these will be on the least informed potential students. A recent Guardian league table, which gives a strong weighting to NSS scores, headlines that Nottingham Trent University has overtaken the University of Nottingham. From the description, Nottingham Trent has undertaken significant steps towards improving quality of teaching. Except, however, in special circumstances, like it or not, few schoolteachers would recommend that a student offered a place at both attends Nottingham Trent instead of the University of Nottingham unless it offered a course of particular interest to the student. This is partly because of potential employer perception but, one has to say, also how the universities attended by their students affects the publicity and standing of secondary schools.

The NSS is intended to be a consumer satisfaction measure in the sense that Tripadvisor is a consumer satisfaction measure. If one looks up town centre hotels in Leeds on Tripadvisor, the top three hotels are expensive boutique properties. But the fourth is a mid-range aparthotel and the fifth is a Premier Inn. The listing is simply not comparing like-for-like. The top-rated Dakota Deluxe is not the right place to take a family with young kids, and the Premier Inn is not the ideal base for a romantic honeymoon. Those using Tripadvisor generally understand this. Before the flow of information on the internet and elsewhere, there may have been a point in government ratings of university teaching and student satisfaction, just as governments could rate hotels one star through to five stars. It should be noted however that the star rating for hotels was primarily about facilities available and not the quality of the service, which was left to private printed guidebooks. We have argued elsewhere that in any case the NSS is unreliable even on its own terms.

The TEF, like the access agreements for the OFFA (Office for Fair Access), seems mostly to involve considerable essay writing by senior administrators and marking by central assessors. We simply fail to see the point. We'd like our students, not our most senior administrators, to write essays.

When we began, we said that we saw the role for regulation to be similar to the airline industry. The government needs to ensure safety – in the case of universities, the validity of the degrees awarded. It doesn't have to set standards on the quality of the food served during the flight. In the same way, once the government through the QAA has restored the external examiner system and ensured that universities have sufficient governance to run their own business, the government should step out of the way and not micromanage. The remaining role can be through the OIA, which provides an effective ombudsman system to consider and record student complaints. The OIA, as currently, can also disseminate best practice through their workshops and publications.

In our view, the greatest beneficiaries of the restoration of the external examiner system would be the universities just below the Russell Group, who have traditionally offered research and teaching and standards comparable to Russell Group universities. It is precisely the grade inflation devaluing the meaning of a first- and upper second-class degree that has forced students to seek to go to a Russell Group university, even when another university offered a programme better tailored to their interests. We have argued that the external system needs to be restored by increasing remuneration and responsibilities of external examiners, not by writing bureaucratic descriptions of what a degree entails and providing online training for less experienced academics to fulfil the role. Externals should be senior, experienced academics whose standing is unquestionable and views respected.

Funding

The move away from the block teaching grant to income following student choice in the form of fees, is the foundation of having a market. As we have said on regular occasions throughout the book, and repeat again, we would not have gone in that direction. That is, however, a matter for the government of the day, so we have considered the system on its own terms. In that light, our proposals are to make the system work by restoring competition and otherwise achieving the stated aims more efficiently.

We see no reason why the base fee should not be set at roughly the cost of production, which – as Browne noted in 2010 – was then around £6000 per student. We have pointed out in Chapter Four that, for non-profits, surplus income is spent according to the preferences of dominant stakeholders. The increase in teaching funding of about 50 per cent – by setting fees at £9000 instead of the £6000 cost base – has coincided (and perhaps to some extent caused) greater managerialism in universities, an over-weighting of the preferences of senior administrators compared to those of academics and students. This has, in our view, caused additional distortions and inefficiencies in the use of taxpayers' funds. In any case, setting fees that far above the cost of production has overly encouraged universities to admit students who might not be best qualified or matched to the programmes on offer.

Figures show that universities have increased recurrent spend on students by about 20 per cent since the increase in fees. Either on a transitional or ongoing basis, that reality might mean that the appropriate cost basis is now around £7000–£7500. Recall however that universities were explicitly advised that fee levels above £6000 were predicated upon spending (at least 30 per cent of the differential above £6000) on widening participation. If widening participation is indeed a government priority we would expect universities to ‘earn back’ any fee level above £6000 by actually meeting targets for widening participation, not just agreeing plans with OFFA. Even then, we cannot see why the fee cap should not be lowered to the recurrent cost per student of £7000–£7500.

We have already indicated that some universities, with lower costs, might have a different fee level, as in the original Browne proposals and government expectations. Many of the post-1992 universities have lower cost bases, since they are not incurring the heavy costs of research at the international level for much of their subject offering. While university research is intended to be funded independently through the QR grant following on from the REF exercise, and from the research councils and indeed corporate and charitable foundation grants, in practice much falls upon the student. Insofar as there is research-led teaching, it is not unreasonable that, as at present, the student covers some of the research cost. It is noted that good universities generally consider 40 per cent of the time of the academic as spent on research, comparable to the time spent on teaching (the remaining on administration). This is already incorporated in the proposed base fee levels of £7000–£7500. High cost subjects requiring laboratories for teaching as well as research would continue to receive additional grant funding.

We can therefore envisage a system where, in addition to the base fee, there is a lower fee (perhaps £5000) at universities with less of a focus upon research. The choice between fee regime could be up to the university, with a block grant of perhaps £1000–£1250 per student making up a substantial part (in our example, half) of any loss due to the lowered fee. It is noted that some of these universities already effectively charge less through ‘hidden discounts’ of financial support to students. The university choosing the lower fee option would benefit from greater student demand, which they could use to adopt greater selectivity in the students admitted. Universities adopting this approach would make clear that although they do research, the reason for lower fees is their concentration on teaching and that this is reflected in their course profile. This allows the university to run more efficiently at still lower cost, and helps these universities to restore their reputations for high quality teaching and a distinctive course offering and, for example, taking an active role in supporting the need for more high-quality apprenticeships in partnerships with employers.

What is vital however is that any fee differential should not have a negative impact on widening participation at the top universities. Given what we perceive to be a greater price sensitivity on the part of students from lower income households, lower fees at some universities could unduly influence the choice of university. This risk would be reduced with a well-designed system of means testing for fees and maintenance awards, which we in any case favour over the current contingent-repayment loans system on grounds of economic efficiency as well as fairness, together with our proposals below for university caps tied to widening participation.

There currently remains some funding for block teaching grants. So a mechanism exists within Office for Students (OfS) to expand this to be used directly to incentivise universities to meet the objectives set by the government. One of these is widening participation. But also, as at present, different subjects can be prioritised. We have already discussed the irony that everyone jumps to saying that STEM subjects need support, when in fact there is good reason to think that currently out of favour subjects such as Modern Languages are the ones where the funding could better, or at least also, be directed.

We have great difficulty, on multiple grounds, with a system where subsidies take the form predominantly of forgiving debt when the investment turns out (from a financial point of view) poorly. On our rough assumption of 50 per cent non-repayment of student loans, the taxpayer is currently subsidising half of the £9000 fee, or £4500 per student. We think that these funds can be used much more directly and effectively, without rewarding failure in the way of the current system. If competition between universities is restored, and if education quality results from this competition, the remaining policy goal is to widen participation. We discuss below how best to use the funding to achieve this aim.

Student fees and loans

We are bemused why it is thought that we should charge the highest fees in Europe (in Denmark, to take an extreme example, all education is free, from generous nursery provision through to university) and, in particular, to charge fees in excess of the historical costs of university. We note that at present universities claim to spend around £1000 per student per annum on widening participation schemes which they put forward to OFFA. We will propose that the widening participation funds can better be spent on means-tested fees and maintenance awards. A first reduction of fee levels from £9000 to £8000, combined with the ending of the OFFA process as now designed, should therefore have no impact on the university balance sheet. The remaining reduction we contemplate to £7500 or £7000 would be a real reduction in unit funding.

There are good arguments for lowering fees as far as £6000 to reflect the historical cost of teaching and student support. The strongest counter-argument for fees higher than that – up to £7000 or £7500 – is that universities have increased the cost base by about 20 per cent due to higher expenditures on staffing and direct educational resources such as teaching rooms. We do not understand why expenditures in all recurrent categories have increased by roughly the same percentage, some of which do not reflect a commitment to improving the student experience for the students actually paying the fees. We note the recent *Student academic experience survey* undertaken by the Higher Education Policy Institute (HEPI).[1] While 'value for money' perceptions have improved from a low base, still only 35 per cent of students in England perceive 'good or very good' value. Students rate spending on teaching facilities (65 per cent) and teaching staff (60 per cent) as the most reasonable use of their money.

We question the logic in charging current students for the Student Centres and other luxury buildings, aimed more at attracting potential students rather than improving the educational experience, that have characterised university plans over the last few years. It is unlikely that a typical student would value access to a University Student Centre (as opposed to the Sports Centre) at much more than £100 a year. We have also commented on the unfairness of students having to pay for projects that will be enjoyed not by them but by future cohorts. If some universities have borrowed large sums to pay for facilities such as this, there is a legitimate issue of how and whether those universities would be able to survive or prosper in a lowered income regime. Neither equity nor economic efficiency, however, supports loading these costs onto current student fees.

Let us suppose in the first instance that fees are set to £7500. We can see no reason why the government seeks to make a large profit on the interest rates charged on student loans. Long-term borrowing costs for the government currently entail a negative real interest rate (the long-term rate is less than the rate of inflation), so even a zero real interest rate would more than cover the cost of finance. As we have discussed, we also see the current system of forgiveness of loans after 30 years as 'rewarding failure'. We begin therefore by looking at a possible loan system with a real interest rate of zero and no loan forgiveness (except in extreme cases of disability or death).

The best structuring of these loans, we would suggest, is as a 'mortgage' provided by the government in order to pay for university. If this mortgage runs over a normal career of 40 years, and was repaid at a uniform rate as with a typical repayment mortgage (but with fixed real rather than pound sterling repayments), a total fees mortgage amount of £22,500 (based upon £7500 per annum) would cost about £50 a month in current pounds. It is hard to see that this is unduly burdensome for anyone with a university degree. It is also a form of borrowing which is well understood. The same individuals who are taking out a university loan currently up to £60,000 may also soon be contemplating a further, more significant burden of a mortgage on properties of several hundred thousand pounds. In principle, therefore, properly supported student loans are feasible if the repayment system is rationalised along the mortgage model at a zero real rate of interest.

It is only the high fees, high current interest rates and the nature of the current repayment scheme that turns the monthly repayments into a large sum. If someone has a student loan of £60,000 but has to subsidise non-repayment by other students and pay an interest rate of 6.1 per cent, then the mortgage repayments become significant. Just the interest rate of 6.1 per cent rather than the rate of inflation (currently 3.1 per cent) significantly increases the repayment amount each month. Adding in cross-subsidisation of non-repayment, and the amount becomes even higher. The burden becomes so high that the taxpayer is left with an unpaid debt at the end of the 30-year forgiveness period of about 50 per cent. This simply and obviously does not make sense.

It may be felt that, even with repayments in the region of £100 a month on a £50,000 student loan (for fees and maintenance) at a zero real interest rate, this could be burdensome for someone on a low income. There might be a case for *ex post* redistribution on the basis that everyone should be insured against the possibility that their student experience has proven – at least financially – unprofitable. Even then, it is hard to see why the insurance and redistribution associated with student loans should differ from that already built into the income tax system. Currently, low income households pay a low or zero income tax, and rates are then set progressively. Rather than constructing a cumbersome contingent-repayment loan system, why not have a straightforward graduate tax as a surcharge on income tax payments, with a rate set to achieve repayment on average? Of course, this cuts the psychological link to the idea of having a loan rather than a tax surcharge. A way of maintaining the link, but largely using the insurance and redistribution inherent in the tax system, is to make repayments on a cohort basis. When the cohort has repaid its aggregate loan amount, the repayments stop. More financially successful members of the cohort support – in a clearly measurable way – less financially successful members.

In any case, we cannot see at all why the government should seek to make a profit on the interest on the loans, except for secondary purposes of selling off the loan book or making the costs to the taxpayer seem lower on the basis of arcane accounting devices. We have also been perplexed by the regressive nature of the current scheme, where middle-income graduates pay a higher total amount than the very well-off. If the government insists on setting interest rates well above its own costs of borrowing, it should in any case end the regressive nature of repayments. Recall that these arose since more successful individuals paid off the loans more rapidly, and thereby avoided the punitive interest rate. Students from better-off backgrounds might use parental contributions to avoid taking out the loans in the first place. Those who could afford it could even add their student loan to a commercially available fixed rate mortgage at a lower rate for a property purchase.

A way of avoiding these regressive effects is to assume that each graduate has taken out the full loan for the purposes of putting everyone on the same repayment scheme. The differential between any loan taken out and a full loan can be put into a notional account held by the government on behalf of the individual. Similarly, repayments by the individual are put into that account. The account should bear a real interest rate of zero. Then, at the specified terminal date of the loan (currently 30 years), the sum should be put to the loan and any residual returned to the individual. Under this procedure, the individual who has a high income and is repaying the loan early and thereby currently avoiding the punitive interest rates, or the individual with parental support who takes out a smaller loan or none at all, does not benefit relative to the lower income individual.

Student maintenance

The government has moved to a system where maintenance funding is handled in the same way as fees, with the student borrowing (up to) the full amount and repaying via the income-contingent loan. We have a number of problems with this in terms of equity and efficiency. For our expositional purposes, it does, however, have the simplifying feature that most of what we have said above about student loans can simply be carried forward to include maintenance, only doubling the figures involved. For a student living in accommodation in London, for example, the maintenance loans are roughly the same magnitude as current fees and treated in the same way in terms of repayment.

The amount of maintenance loan differs between London and the rest of the country, and upon whether or not the student is living at home or in accommodation. The amounts vary from about £7000 (living at home) to about £11,000 (living away from home in London). Our primary concern is for all students to make the right choice, given their preferences and qualifications, about where to go to university and about whether or not to live at home. We are not comfortable with students from lower-income families living at home either because of affordability or because of 'sticker shock' at the eventual loan amounts. We feel that it is particularly important that non-traditional students engage in the full university experience by living in student accommodation.

We would like to see support for widening participation in the form of ex ante grants for both maintenance and fees, not ex post writing-off of loans in 30 years' time. The importance of means-tested maintenance grants in encouraging participation has been demonstrated in a study by Dearden et al.[2] It is a daunting prospect for a family with a tradition of living hand to mouth to face a debt for fees even of £22,500 for a three-year course (under the fee reduction for all students that we favour). By returning to means-tested fee and maintenance support, available funds for subsidies are better targeted and also avoid rewarding failure. They are based upon limitations on the student's background support, financial and educational, and not upon any lack of effort or success on the part of the student – indeed, they reward the students from disadvantaged backgrounds who overcome these additional hurdles and achieve a place at university.

We have referred earlier to work done by London Economics for the Sutton Trust where they note various models for means testing. The particular model they use for illustration assumed current fee levels and a scheme where the wealthiest pay higher fees to subsidise the less advantaged. As a matter of principle, we do not think anyone should pay significantly above the costs of a public service and we favour lowering fees for all students. Any number of models are possible under assumptions of the end of the writing-off of loans and a zero real interest rate. Further, the £1000 per student currently claimed as spending on OFFA approved activities can be spent, we would argue more effectively, on means testing.

For example, assume for simplicity a fee level of £7500, and a maintenance loan of £7500 per year of study. Assume further that 10 per cent of students get a discount of 50 per cent and 10 per cent get a discount of 25 per cent. The total cost of the 50 per cent discount is then £750 per student across the whole cohort and the total cost of the 25 per cent discount is £375, making a total of £1125 per student across the whole cohort – a figure close to the money universities claim they are using for 'OFFA' supported activities. This means-tested support could therefore be supported just from re-directing those funds, and not even using our proposed savings from ending the non-repayment in the contingent-income loan system.

At these assumed levels for fees and maintenance for a three-year course a straightforward mortgage type scheme to pay back the loan over 40 years would cost the full-fee paying student £100 per month and £75 or £50 respectively for the discounted students. Any number of other models could be developed but this simple example shows the feasibility and – we would argue – clear desirability of this alternative to the current funding.

The upfront government funding in the 'mortgage scheme' could be arranged as at present through a loan company if the government wanted to continue the current accounting devices. Each graduate would have a personal account, repayments would be collected through the tax system with money accruing to the government current account and the graduate's account in the loan company credited. If the government, for accounting reasons, wished to sell off this student debt, it could still do so. In fact, this debt would be inflation index-linked, an asset class that is relatively absent from the market (except for existing government index-linked gilts), and for that reason would be attractive to pension and other investment funds.

When maintenance loans were increased to – for London students living in student accommodation – £11,000, it is perhaps not surprising that rents increased to roughly that amount! Student accommodation has become a lucrative business, with expansion in private and university provision. (This same phenomenon is apparent in the rocketing public cost of housing benefit following the transfer of large quantities of council housing stock to private landlords.) Some of the university provision has been monetised by selling off future revenue streams. Further, the inventory of student housing offered by a university will range from historical construction to new builds on newly acquired land, with very different costs to the institution. Students at UCL have gone on rent strikes and have achieved concessions from the university in terms of rent freezes on the lowest cost accommodation and significant bursaries to less well-off students.

Table 7.1: Weekly student accommodation and catering costs

Academic year	England	N Ireland	Scotland	Wales
2012	£176.40	£139.40	£183.26	£116.74
2013	£183.88	£136.10	£194.48	£124.50
2014	£196.10	£144.44	£200.51	£136.52
2015	£204.46	£147.73	£201.45	£137.84
2016	£211.46	£155.77	£194.14	£157.68

Source: HESA Estate Management Records 2012/13-2016/17

Due to data limitations (there is no direct data on rents), we construct Table 7.1 by taking rent and catering income and dividing by the number of bed spaces, and further allowing for a 40-week rental year. As can be seen, costs in England with a maximum maintenance loan of £6828 outside of London (for students from mid-income families) have risen sharply, compared in particular to Scotland where the loan is £4750. The figures in Table 7.1 will overstate the actual cost to a resident student since some catering income arises from non-resident students and staff. Nonetheless, this accurately shows the degree of inflation in these costs.

We favour some form of rent control, accepting the difficulties in implementation that are not unlike those currently facing housing associations or, historically, private rentals. However, if the government can regulate fees, it can also regulate the costs of accommodation. We would propose that each university be required to offer first year students single or double accommodation at centrally set rates (that differ across localities, as appropriate), with minimum standards set. We do not accept the current fear among economists about setting specific targets and rates. While there are potential inefficiencies, universities have a monopoly over on-campus housing, so there are also inefficiencies in uncontrolled rents. First year students, in our view, should prioritise living in on-campus housing, and are therefore particularly subject to monopoly pricing. What the regulatory agency should not do is micromanage and tell the university how to achieve the required availability and rent levels. If it is felt that a university needs to provide single accommodation in London to students for £150 a week, it is not for the regulatory agency to tell the university how best to do so, but simply to impose the rule upon the university.

Widening participation

Currently, universities agree a plan with OFFA and claim to be spending about £1000 per annum per student (out of fees paid by fellow students) on widening participation. We have argued that this money would be better spent on means-tested fees and maintenance grants. We feel that the activities of OFFA could be discontinued, with monitoring of achievements at improving access a direct responsibility of OfS – a task made easier by the data available from distribution of maintenance grants if these become means tested. This is consistent with our view that emphasis should be placed on results rather than micromanagement of process. Put more directly, since OFFA has not successfully generated widening participation in the system, and particularly at the more established universities, it has proved to be a waste of money. We note that the recent HEPI survey[1] shows wide gaps in the satisfaction rates of minority ethnic students compared to white students. Again, even on their own terms, the current arrangements are not 'fit for purpose'.

Achieving a greater diversity of background at top universities is not rocket science. Oxford University could fill its places with highly qualified state school students in proportion to the mixture in English schools as a whole, and not unduly rely upon those who have enjoyed a privileged private education. In saying this, we accept that admissions tutors at Oxford are admitting students fairly based upon traditional evaluations of 'merit', but we also accept the view of society that these measures and methods of determination may not be the best ones for a publicly-funded institution. In the same way, Oxford's students could reflect the social and ethnic make-up of England in general.

The question then becomes how best to achieve this diversity, not just for Oxford, but for other universities where the recruitment issue may be more difficult. We dismiss the essay writing and tick-boxes currently used in Access Agreements with OFFA as ineffective. This then leaves us with the standard methods for achieving a goal – taxes, subsidies or quantity targets – or coming up with a new proposal. We do not mind the imposition of taxes or subsidies, or even strict quantitative targets, but have decided on the following holistic proposal to address both the restoration of competition to the system and widening participation.

Our proposal is that the objectives of restoring competition and widening participation should be integrated in one simple mechanism. We begin with the first stage, which is to cap each university at its student numbers in 2011, when the higher fees came in, less 10 per cent. This will, given the growth in the system subsequently, have the greatest impact on the Russell Group, which has expanded disproportionately under the regime of uncapped numbers (and no effective OFFA intervention). We then allow each university to 'win back' its student numbers by admitting (and graduating) widening participation students, or – if it so desires and can compete effectively – go beyond its current numbers. We make no apology that – given their lower current numbers of widening participation students – the Russell Group would, if they don't compete, lose out the most. Widening participation students, under the means-tested regime we propose, will have been identified by their family household income. While it is possible to uncap only widening participation students, it is also possible to allow a university to enrol additional traditional-background students in proportion to the expansion in widening participation numbers.

All the government agency – the OfS – has to do to implement our proposals is to determine the actual base fee, the lower fee that can be set by primarily teaching institutions, a teaching grant to universities that choose to set a lower fee, and a teaching grant for specific subjects, the precise terms of fee and maintenance means testing, and any multiplier on additional overall numbers on top of widening participation numbers. We would suggest that the latter be greater than one, since some of the less advantaged students may be less well prepared than those who have benefited from 13 years of expensive private education. Universities must be prepared to give extra help if need be, particularly in the early stages of their university careers.

In Chapter Six, we gave the example of affordable housing in London and pitfalls that had to be avoided such as 'poor doors' where the individuals (often teachers and nurses) obtaining affordable flats were physically isolated from the purchasers of the more expensive properties. In the current system, students who repay their full loans end up subsidising the widening participation students. We feel that that is divisive. Under our proposal, the non-traditional students are not in the student number cap, so they are clearly additional and – because even a subsidised fee will likely be greater than marginal cost – are net contributors financially as well as academically and socially to the university. Further, if our proposal is followed and there is a multiplier applied – allowing additional traditional students for each non-traditional student – the direct benefit to all the students is enhanced. In these days of social media, the more non-traditional students recruited, the more places will become available for my Facebook friends from school, even if I'm from a traditional university attending background.

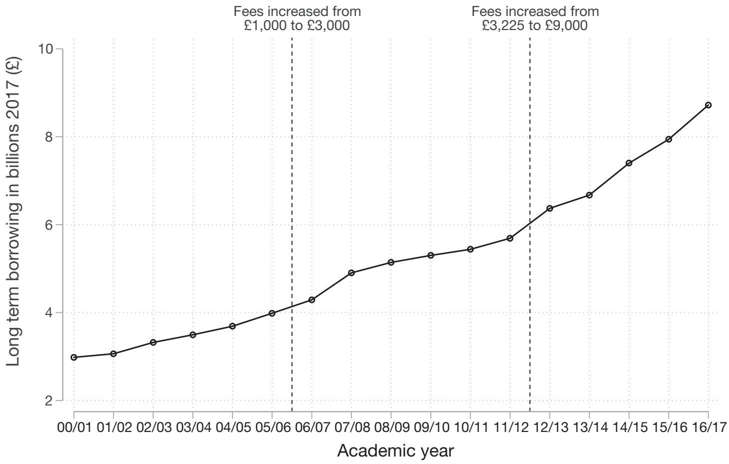
The risk or threat of bankruptcy

Universities rushed to spend the flood of extra funding in irreversible ways – they built new buildings. To those of us who care about architecture and design, this was a further unfortunate feature of the shift to the high fee environment. Rather than engaging in careful planning and rebuilding English universities with architectural innovation, there was a rush to build. Some of this was simply to keep up with others. It often looks as though some of the architects employed merged together disjointed schemes from different building plans already on their computers.

We do not suggest that UUK (the employers' body Universities UK) got together as a whole and decided to create a fait accompli that would require – with the increase in cost base – fees to remain at £9000 indefinitely with no caps on student numbers. However, economic equilibria – based upon the interactions of independent agents – often coordinate into what looks like a conspiracy!

This reality does, however, mean that, in considering policy changes, we have to confront the possibility that lowered funding will lead to bankruptcies in the system. We have looked at the increase in debt and in the ratio of debt to income (see Figures 7.1 and 7.2).

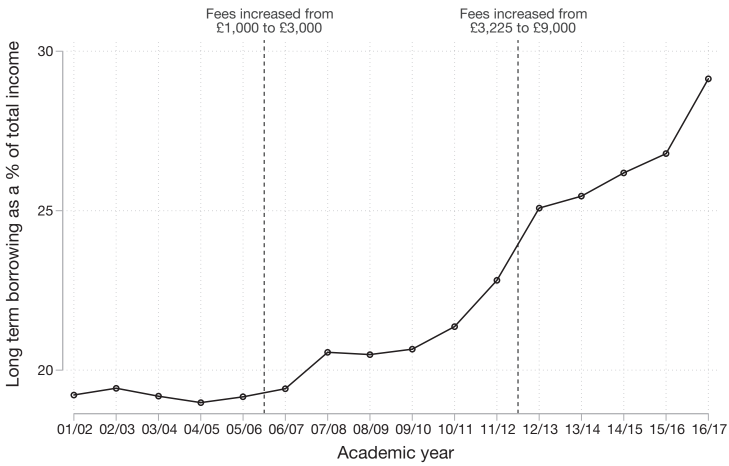
Figure 7.1: Debt in English universities



Note: HE institutions with fewer than ten students are excluded in this figure.

Source: HESA Finance Record 2000/01–2016/17

Figure 7.2: Debt relative to income



Note: HE institutions with fewer than ten students are excluded in this figure.

Source: HESA Finance Record 2001/02–2016/17

Although debt has gone up substantially, the overall ratio of debt to income remains at manageable levels of under 30 per cent. The increase in income would of course have allowed for a more prudent policy of increased debt for essential capital projects while still reducing the debt ratio. Some universities will have chosen to expose themselves more than others to the vagaries of student demand and government policy. Among large universities, the highest debt to income ratio in 2016/17 was about 100 per cent, with a significant number having debt to income of about 70 per cent.

The debt to income ratio may not be telling the full story of university exposure to risk. Thomas Hale wrote in the *Financial Times* on 7 February 2018 about the University of Swansea and its accommodation financing arrangements. University Partnerships Programme is a private provider that has arranged over £2 billion in new funding for university accommodation. It offers Special Purpose Vehicles for funding the accommodation, typically gaining the bulk of the student rents for a set time period (in the case of Swansea, 45 years), and structures the loan products into tiers with some of the loans guaranteed by the university (which is thereby taking on some of the risk). In effect, these arrangements are complicated mortgages that may not appear in the debt to income ratio we have described above.

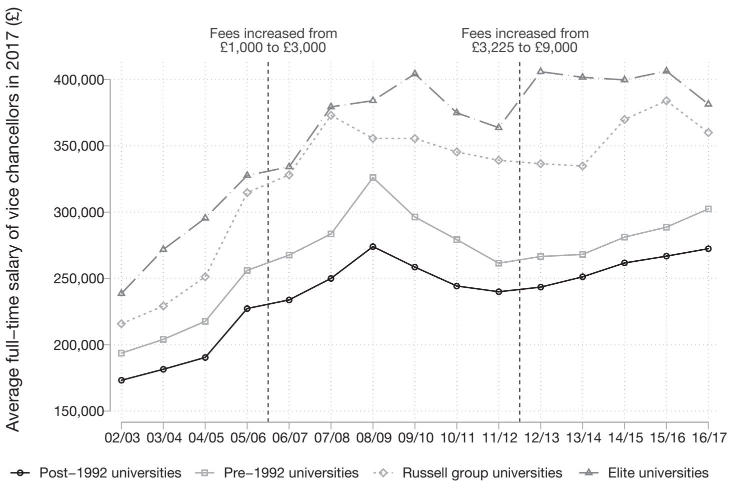
Insofar as high debt and financial engineering exposure is due to the prudence or otherwise of particular institutions, and has not yet become a systemic problem, we note that no university is 'too big to fail' in the way that banks demanded and received bail-outs during the financial crisis. The OfS should be prepared – as were its predecessors – to arrange mergers and other adjustments when a particular institution had failed its students and staff by poor decision-making, and the OfS should move quickly to ensure good governmental practice at all institutions going into the future. Interestingly, the government White Paper in 2016[3] envisages the possibility of bankruptcy with a view to requiring institutions to have a plan for protecting students (but not staff or the institution) in case of exit.

Senior management salaries, academic salaries and pensions

There has been considerable negative press coverage over the high level of Vice Chancellor remuneration. The stakeholder model suggests that the dominant stakeholders will shift resources to follow their own preferences. Part of this may include their own remuneration. Although the governing body will have a Remuneration Committee, this often includes the Vice Chancellor. Even if the Vice Chancellor leaves the room when their own pay is discussed, they might feel inclined to support pay rises for the senior staff just below them (which not inconsequentially raises a base comparison for their own pay), and they will return to the room after the Committee determines their own pay (see Figures 7.3 and 7.4).

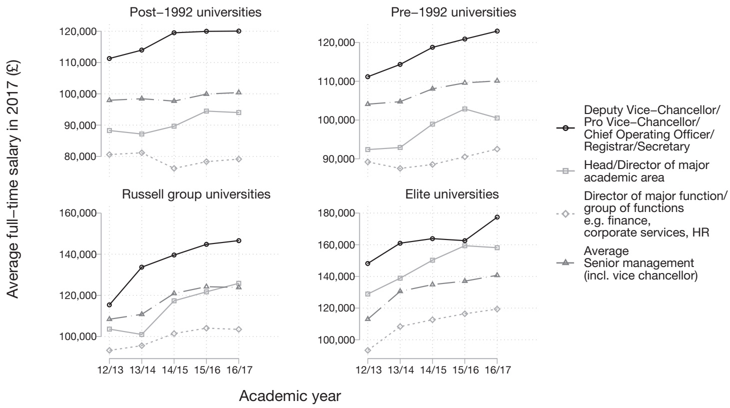
The data show significant pay rises for Vice Chancellors over the period, but even more dramatically for other senior managers. Interestingly, the pay of Vice Chancellors took off well before the fee rises. It may be that a preceding change in ethos to a more managerial approach led the sector to be receptive to the fee increases to £3000 and then £9000.

Figure 7.3: Vice Chancellor pay



Source: Annual Vice Chancellor's Pay/Remuneration Survey, *Times Higher Education* 2004–18 (usually published in a Late spring edition).

Figure 7.4: Average senior management pay



Source: HESA Staff Record 2012/13–2016/17

The American baseball player Babe Ruth is reported to have said, when confronted with the question why he was paid more than the President of the United States, 'I had a better year than he did.' The quality of management is vital to the success of an organisation – a university, a business or a football team is not a black box where inputs are entered and outputs naturally follow. Leadership matters. In fully competitive markets, Vice Chancellor and other senior management salaries might rise due to competition for the most outstanding and successful leaders. It is an empirical matter as to whether the increases in senior management pay are best explained as arising from vigorous competition for outstandingly successful individuals, or as a general push upwards in a managerial culture not directly related to improving the quality of education and research.

Although academic salary scales faced the public sector pay cap, there still remained the possibility for vigorous competition for the best researchers and teachers. Professorial scales are uncapped and a top, Nobel prize winning professor could – as in the US – make a salary in the hundreds of thousands of pounds. If teaching quality becomes the subject of fees-driven student demand, why shouldn't a notably good teacher similarly receive a very high salary? In fact, as we have observed, the sector has successfully contained the competition for academics and average real pay has significantly declined.

In terms of cost effectiveness, British universities are like the NHS in being relatively high quality for relatively low cost, and for much the same reason. Professional pay for the coalface workers – the doctors and the lecturers – is well below competitive market levels for individuals of high ability who have obtained high educational qualifications. Each system relies upon collegiality and the 'non-pecuniary' advantages of the post. For lecturers, the flexibility of the job and their ability to focus upon what they think is most important in their teaching and research is a large part of their pay-cheque. What a naïve Director of Human Resources might see as spare capacity to be exploited, or a troublesome lack of focus upon the NSS, is actually part of an efficient organisation of job tasks and time allocation. From a simple economic perspective, academic freedom is not just something to be valued on philosophical terms, but it is part of an overall compensation package.

Academics view their employment as being in the civil service model. Salaries are augmented by professional status and security. Effective academic freedom is only ensured by providing fairly ironclad employment security (once probation is passed). Otherwise a university could remove a lecturer espousing controversial or unpopular views under the guise of redundancy or through disciplinary and capability procedures. Although academic tenure was formally removed by Margaret Thatcher, it has remained effective at good universities both because it is fundamental to the mission and because it makes economic sense. A part of the differential in pay between an academic and a comparably educated and able individual in the private sector (such as in a financial firm in the City) is ascribable to this source.

Academics, like civil servants, also rely upon a secure and indeed generous pension scheme. Particularly given the public sector pay cap and the declining proportion of the university pay bill spent on academic salaries, along with the negative press coverage on Vice Chancellor pay packets, it seems a remarkable own goal for the sector to have (still unresolved) trade disputes over the pension system. Having already ended the final salary scheme in 2016, UUK sought to end defined benefits in total in 2018. Maintaining the scheme might involve an increase in employers' contributions of up to 7 per cent in the future, or – given the proportion of the relevant payroll in university budgets – an increase in overall budget costs of perhaps up to 2.5 per cent. This is clearly affordable, so resistance by Vice Chancellors must be more about the relationship between the different stakeholders in the university and the rise of 'managerialism'.

Returning the university to the academics and the students

When the government froze fees in October 2017, it became clear that overall university funding was likely to go down in real terms over the next few years, at least until demographics led to a rise in the number of 18 year olds. Further, the public sector pay cap is being relaxed, and academic salaries will therefore no longer decline at the same rate in real terms. Maintaining the pension scheme will require an increase in both employer and employee contributions. At the beginning of the book, we described the higher education sector as the lottery winner in public funding during a period of austerity. Reality is already beginning to seep into the discussions and universities are talking about cost cutting. Our own proposals are to jolt the system with real competition. Universities will have to earn back the revenue they now take for granted. They will need to offer a better product and ensure that their students are a diverse mix that reflects the make-up of England today.

Without a substantial shift in the funding system, universities are likely to respond with 'more of the same', mistaking 'marketing' for 'markets'. The academic payroll has gone down as a percentage of university expenditure and stands at about 30 per cent. These are the front-line staff. Trying to cut the academic side as real funding goes down would, in our view, be suicidal for the international standing and attractiveness to overseas students and businesses of our universities. In our view, universities can no longer afford large expenditure on marketing, whether it is spent on luxury student centres, expensive advertising or highly-paid senior administrators filling in TEF and Access submissions. This marketing is of zero sum benefit to the sector as a whole and of very little benefit to the students and the taxpayers who are being saddled with high levels of debt.

By focusing on the product – high quality education – we feel that universities can operate effectively in a system of 'just adequate resource'. In fact, it is a mystery why it was in the first place thought necessary to increase the teaching unit of resource by something of the order of 50 per cent on the basis of a professed aim to increase student numbers and improve the quality of education. Expansion with a constant unit of resource would in itself have produced a financial improvement since marginal expansion – if evenly spread across universities rather than concentrated in the Russell Group – can be achieved at marginal cost. This extra aggregate resource, rising with student numbers, could have been used for prudent refurbishment of the estate, improvements in SSRs and efforts to improve participation.

We have emphasised that the work of the university is done at the departmental level. The team is the academic staff, the technicians and the administrators within the department. Departmental administrators in particular tend to be on lower grades of the scale, and are the unsung heroes that largely determine the student experience. Students relate to the department, interact with the lecturers and other students, and often benefit from the administrators not only for their academic queries but for emotional and other support. All this happening at the departmental level avoids the anonymity and isolation that can lead students to feeling the levels of stress and inability to cope that have in turn led to serious student welfare concerns. One wonders why the increased demand for counselling is being met by more counselling staff rather than getting to the bottom of why there is such an increase in the first place.

At a time of just adequate resource a university must concentrate hard on its key priorities – teaching and research. Efficient professional administration is essential, but it is in service to the main objective. Concentration on the primary objective has the added bonus of improving the financial position through increasing research and consultancy income and attracting high quality overseas students, both undergraduate and post graduate. An administration cannot earn money, but an efficient, proportionate administration can ease the life of everyone in working to the common good. On the other hand, hiring one more administrator than strictly necessary is likely to create more work if new wheezes are proposed, more paperwork and meetings generated, more exchanges of correspondence and eventually demands for more administrative staff. All the administrative staffing for TEF and other government micromanagement has a multiplier effect, as administrators find the need to hire more administrators.

What appears to be unjustified growth in highly-paid, central administration can lead to resentment and an unfortunate divide in the community, undermining collegiality. But a deeper issue concerns management style. For example, a finance department has to be run on well-defined and documented procedures. Payroll has to work, cash flow managed, purchasing efficient, investments well managed. Each member of the administration has to know their clearly defined role and perform to procedures laid down by their line managers. Academic departments are different. Lectures and tutorials have to be given when promised, assignments marked with care and returned when promised. But how this is done is largely down to the individual, as is what goes into individual lectures and tutorials within the overall constraints of the agreed syllabus. This is not to say a department does not need managing, but a Head of Department's task and style differs from that of a first-rate head of administration, even though both should ensure humanity, commitment and collegiality within their departments. With the growth in university management, the previous essential role of academic heads in formulating policy has reduced. And the mode of management appropriate to the administration has increasingly been applied to the academic community.

Not only is this procrustean approach inappropriate and damaging to the overall liveliness of the community, it is also demotivating and inefficient. A well-motivated and proud academic department is more than willing to run school visits, field open days, engage with the media and so on, without coercion and without additional funding. Academics do not expect and do not get overtime pay. Satisfied students who identify with the care and concern of the academics and departmental staff are happy to go back to their schools to spread the word. But this requires a hands-off approach which is anathema to the controlled style of management perfectly appropriate for the administration. And the word soon gets out that this is a good place to be and so helps in the recruitment of new staff. It may give a Vice Chancellor sleepless nights wondering how things are going but they have appointed the academic staff and the least they can do is have confidence and let them get on with it.

It follows from this that paying the expanded administrative structure at high, commercial rates of pay is not only wasting public funds, but is demoralising for the institution as a whole. A Vice Chancellor's pay should be constructed relative to that of the university's leading professors, not to hypothetical managers in the banking and finance sector. There is no reason why any Vice Chancellor should be paid more than double the average rate of professors. Other senior academic officers should be fixed-term, part-time posts where the professor holding the assignment (such as Pro-Vice-Chancellor or Dean) goes back to their academic department, or decides to seek to become a Vice Chancellor elsewhere. It is this ability – after a period of additional service to their university – to return to their normal lives that encourages top researchers and teachers to take on administrative tasks and contribute to the strategic direction of the university.

In our view, students and the taxpayer can spend significantly less money and get not only better value, but a strictly better university education offering and academic environment.

Summary

We have taken the view that the current implementation of the market approach to universities, far from encouraging competition, leads to uniformity and top-down regulatory controls which are costly and counter-productive. For the final time in the book, we observe that we would not have gone down the market route at all. However, on its own terms – and we accept that the government of the day remains wedded to the market approach – the current system is inefficient and wasteful. For the purposes of our policy proposals, we have accepted not only the market system as envisaged by Browne, but even a constraint that no new taxpayer funds be added: we believe early years and schools are higher priorities.

Ironically, the 'market' has led to both less competition and more regulation. There has been a continued process of increasing government control over the last decades, from the UGC (University Grants Committee) being replaced by the UFC (Universities

Funding Council) and then HEFCE (Higher Education Funding Council for England) and now the OfS. Contradictions run throughout policy, with the government simultaneously arguing for greater 'academic freedom' and for the 'prevent strategy'. Our view is that universities work when they seek to achieve excellence and diversity, and are centres for vigorous debate and intellectual enquiry. The role of the government is to set up mechanisms and then get out of the way, without the sort of micromanagement and bureaucracy we have seen in the OFFA, NSS, TEF, and so on.

Effective economic mechanisms are simple but robust. We have the following main policy proposals:

1. Return competition to the system, and have real widening participation, by introducing caps on each university, but with uncapped numbers of students from non-traditional backgrounds, possibly with an overall student number multiplier to increase incentives to attract and support widening participation students.
2. Eliminate the rewards to failure in the current contingent-repayment loan scheme by having a mortgage type student funding scheme, but with means-tested fees and maintenance with a zero real rate of interest.
3. Give the Office for Students four main tasks. Restore the external examiner system as the method for ending grade inflation and guaranteeing the value of degrees. Ensure good and strong governance from the governing bodies. Continue to allocate special teaching grants for high cost subjects but extend this to subjects currently out of favour with students but important for the health of the system and the nation, such as, for example at present is the case with Modern Languages. Monitor participation rates and caps on student numbers.
4. Close down the OFFA and abandon the TEF and NSS.
5. Return base fees to a level more consistent with costs, of between £6000–£7500, to avoid wasteful expenditures.
6. Allow universities to set a reduced fee, with some of the differential made up from a block teaching grant.

Successive cohorts of students (often siblings) have been subject to changes in the cost of their education which will persist through their working lives. This is clearly unfair. How this is addressed and how the problem of paying off the existing long-term debt should be faced is a matter for government and beyond the scope of the task we have set ourselves. We feel strongly, however, that current policies have created complications, inefficiencies and unfairness and it is time for Occam's razor to be brought to the issue of university funding and fees.