HEPI

Debate

49

Time to Reconsider a Graduate Tax?: Why 20 years of student loans change the case for reform

Bahram Bekhradnia



About the author

Bahram Bekhradnia established the Higher Education Policy Institute in 2002, and was its Director until December 2013 following which he became HEPI's First President. Before establishing HEPI he had been the Director of Policy of the Higher Education Funding Council for England (HEFCE) since its formation in 1992, and prior to that was a senior civil servant in the Department of Education and Science.

Foreword

Rose Stephenson, Director of Policy and Strategy, HEPI

The issues with higher education finance in England are widely recognised. The value of tuition fees has fallen sharply in real terms since 2012, leaving higher education providers in financially precarious positions. Graduates feel they are saddled with a debt they did not sign up for, and taxpayers and policymakers place universities at the bottom of a list of spending priorities within the education system.[1] It can feel like an unsolvable problem.

HEPI has published several reports seeking to add ideas and evidence to the public debate on higher education funding. This has included:

- *How should undergraduate degrees be funded?* (A collection of different funding ideas, modelled for economic impact by London Economics and tested with potential higher education applications.)[2]
- *An examination of higher education fees and funding across the United Kingdom.*[3]
- *Undergraduate fees revisited.* (A proposed model developed by the economist Lord Tim Leunig).[4]
- *Understanding the Plan 2 repayment system* (A cost-neutral alternative model to the current Plan 2).[5]

This HEPI Debate Paper, authored by HEPI's founder and President, Bahram Bekhradnia, argues another idea deserves reconsideration: the graduate tax. A tax on graduates is a recurring idea in higher education policy debates. One major reason it has been rejected previously is that a graduate tax would generate no revenue for years (as students and recent graduates would not pay it, or would pay only at a low rate), yet universities require funding to function now. As such, government would face a lengthy and expensive transition before seeing any

return. Further, the treatment of loans in the national accounts – once considered a decisive matter in favour of the present loan scheme – has changed dramatically.

The paper suggests that time has undermined these arguments. More than 20 cohorts of graduates have now passed through the fee-and-loan system. Many are already making income-contingent repayments through PAYE. However, moving these graduates to a tax-based system would require further – potentially very controversial – changes to the current repayment system. But detailed economic models for a graduate tax would add to this debate. (If you are interested in funding work along these lines, please do reach out to HEPI.)

HEPI does not take a position on which funding model is the right answer; we seek to add ideas and evidence to inform and stimulate debate – and I have no doubt that this paper will do just that.

1 Michael Crowhurst, 'Polling on Education Priorities' in the spending review', Public First, February 2025 **https://www.publicfirst.co.uk/polling-on-education-priorities-in-the-spending-review**

2 Rose Stephenson, 'How should undergraduate degrees be funded?', HEPI, April 2024 **https://www.hepi.ac.uk/reports/undergraduate-fees-revisited-2/**

3 Dr Gavan Conlon and Maike Halterbeck 'An examination of higher education fees and funding across the United Kingdom', HEPI, February 2024 **https://www.hepi.ac.uk/reports/new-reports-shed-light-on-differences-in-higher-education-fees-and-funding-systems-across-the-uk/**

4 Tim Leunig, 'Undergraduate fees revisited', HEPI, September 2024 **https://www.hepi.ac.uk/reports/undergraduate-fees-revisited-2/**

5 Dr Gavan Conlon et al, 'Understanding the Plan 2 repayment system', HEPI, April 2026 **https://www.hepi.ac.uk/reports/understanding-the-plan-2-loan-repayment-system/**

Contents

Executive summary 7

Introduction 9

Why graduate taxes were rejected 11

The student loan system today 14

A graduate tax with the benefit of hindsight: the arguments revisited 20 years later 18

A possible graduate tax 31

Conclusion 36

Executive summary

For over half a century, proposals for a graduate tax have appeared periodically in debates on the funding of higher education. Each time, they have been rejected in favour of alternative approaches, most recently the tuition fee and loan system introduced in stages from 2006.

Among the other objections to a graduate tax listed below, the principal objection has never been that it is inherently unfair or economically unsound. Rather, it has been that universities require funding immediately while a graduate tax would generate revenue only many years later. Governments would therefore have to bear substantial transitional costs before receiving any return, and even then, as a tax going to the Exchequer, it would not guarantee income for universities.

This paper argues that circumstances have changed fundamentally.

Over 20 cohorts of graduates have made use of the tuition fee and student loan system. Most are readily identifiable through records held by the Student Loans Company. Many are already making income-contingent repayments through the tax system. The principal obstacle that prevented adoption of a graduate tax has therefore substantially reduced.

At the same time, the existing student loan system has evolved into something that increasingly resembles a graduate tax (though it is to be noted that the Treasury Select Committee argues that the loans should look more like loans and less like a tax).[1] Repayments are collected through PAYE, depend on earnings rather than debt, and often continue for decades, until the debt is extinguished or wiped out: many graduates never repay their loans in full and taxpayers remain responsible for a substantial proportion of the costs through subsidy and write-offs.

1 **https://committees.parliament.uk/publications/54019/standard/pdf/**

This paper argues that:

- many of the traditional objections to a graduate tax have weakened;
- universities remain heavily dependent upon government, despite the existence of tuition fees;
- the real value of tuition fees has fallen significantly since 2012, demonstrating the limits of institutional financial autonomy;
- objections to retrospective taxation are weaker than often assumed, as taxation arrangements and student loan conditions are regularly changed after individuals have made long-term decisions;
- a graduate tax could potentially provide a simpler, more transparent and more sustainable basis for funding higher education; and
- the existence of more than 20 cohorts of loan-funded graduates means that the principal Treasury objection to a graduate tax – the cost of transition – has been substantially reduced, if not eliminated.

The paper concludes that a graduate tax deserves reconsideration and that the existence of more than 20 years of loan-funded graduates changes the terms of the debate.

Introduction

The funding of higher education has been one of the most contentious areas of public policy in England this century. Since the reintroduction of tuition fees in 1998, governments have sought to balance three competing objectives: maintaining access to higher education; protecting resources for institutions; and controlling public spending.[2]

The solution eventually adopted was a system of tuition fees, later supported by income-contingent student loans. This arrangement has evolved through several reforms, most notably in 2006 and 2012, but its basic structure since 2006 has remained intact. Students borrow to finance tuition fees (as well as maintenance costs). Graduates subsequently make repayments through the tax system once their earnings exceed a specified threshold.

At various points, alternative approaches have been proposed, including a graduate tax. Before he was Prime Minister, even Andy Burnham backed a graduate tax and, since taking on the top job in mid-2026, he has heavily criticised the current loan-based system.[3] Under a graduate tax, rather than accumulating debt and repaying loans for a defined period, graduates would, after graduation, pay a tax, calculated as a proportion of their earnings. Those contributions would help finance the higher education system.

While a graduate tax has attracted much support, those in charge have consistently rejected it. Their view has tended to be that, whatever its theoretical attractions, a graduate tax is impractical. A generation

2 Many, including the author, take the view that a preferable outcome would be a greater public contribution to the costs of higher education and a reduced financial burden on graduates. This paper, however, takes as its starting point the political reality that public expenditure is likely to remain under sustained pressure and that a significant increase in direct taxpayer funding of higher education is unlikely in the foreseeable future. The analysis proceeds on that basis.

3 **https://www.timeshighereducation.com/news/burnham-pledges-replace-tuition-fees-graduate-tax**

on, however, the assumptions underlying that judgement deserve re-examination.

The student loan system has become more complex. Graduates routinely leave university with debts exceeding £50,000. Repayment periods have lengthened for subsequent cohorts and taxpayers have borne substantial costs via loan write-offs. Universities remain dependent on government decisions, despite the existence of fees. At the same time, millions of people have gone through the fees-and-loans system. The main objection to a graduate tax – that revenue would take years to accrue – is less compelling than it was.

The purpose of this paper is not to say a graduate tax is a silver bullet. Important questions remain regarding fairness, implementation and institutions' funding. Rather, the papoer seeks to examine whether 20 years of experience with tuition fees and student loans have changed the facts on which earlier decisions to reject graduate tax proposals were based.

The issue is politically timely: Wes Streeting, now Defence Secretary, was for some years the most prominent advocate of a graduate tax and James Purnell, the Chief of Staff at Number 10 Downing Street, argued for moving the existing loan model closer to a tax during his time as Vice-Chancellor of the University of the Arts London (2021 to 2024). The political climate in which this paper is written is therefore more receptive to the idea than has sometimes been the case.

Why graduate taxes were rejected

Graduate taxes have a long history in British higher education policy debates. The concept is straightforward. Rather than charging home students tuition fees and then lending them the money to pay them, under a graduate tax people would repay a proportion of their earnings once they enter employment.

The attractions of a graduate tax rest on the idea that graduates who benefit financially from higher education should contribute towards the costs. Those who earn more pay more; those who earn less pay less. Payments would be linked to people's ability to pay (which also means those who would pay more than they do under today's system may be hostile).

Yet despite its apparent simplicity, and despite the similarity of its principal features to the current fee and loan repayment system, graduate tax proposals have repeatedly failed to secure political support.

The transition problem

The most important objection concerns timing. Universities incur costs today. Lecturers must be employed, laboratories maintained and students taught. A graduate tax, however, generates income only after graduates enter employment. A government introducing a graduate tax would therefore face a prolonged period during which it continued funding universities but received little or no revenue in return.

This problem appeared particularly acute during periods of rapid expansion in student numbers. Governments would have to finance increasing participation while simultaneously waiting many years before the first significant revenues emerged. For the Treasury, this has always seemed a powerful argument against adoption.

Concerns about graduate mobility

A second concern is that graduates might leave the country, since

a graduate tax imposed only on those remaining in the United Kingdom might encourage emigration and prove difficult to enforce internationally.

This concern was especially significant when proposals were being debated within the framework of free movement across the European Union. People could potentially study in Britain and subsequently work elsewhere.

Fear of increased government control

Although many institutions disliked the political controversy surrounding tuition fees, they also valued the apparent link between student recruitment and institutional income, and so were often ambivalent about graduate tax proposals.

A graduate tax appeared likely to increase dependence upon government. Universities feared becoming more vulnerable to spending reviews and changing political priorities. There would be no necessary link between the money raised through the tax and the money available to universities and, while it would be possible to create such a link, the Treasury were generally opposed to hypothecated taxation.

Concerns about fairness

Critics also asked whether a graduate tax was fair, since a highly successful graduate might pay many times the cost of his or her own education. In contrast, a graduate with modest earnings might pay little or nothing. Opponents said the relationship between the cost of someone's education and the amount they repaid would become increasingly tenuous.

The attraction of loans

Against this background, student loans appeared to offer a compromise:

- universities would receive funding immediately;

- students would not face upfront charges;
- repayments would depend on earnings; and
- public spending would be reduced, or at least look like it had been reduced.

For many policymakers, student loans therefore seemed to provide the advantages of a graduate tax without the perceived disadvantages. Whether that judgement remains persuasive is the subject of the next section.

The student loan system today

The distinction between an income-contingent loan and a graduate tax has been set out most clearly by Professor Nicholas Barr, the LSE economist who is widely credited as one of the architects of the income-contingent loan system introduced in 2006.[4]

Barr's framework helpfully distinguishes between an income-contingent loan, which is repaid as a percentage of earnings but stops once the amount borrowed, plus any interest, has been cleared, and a graduate tax which is likely to continue for as long as the graduate remains in employment, with no link to a specific borrowed amount.

The student finance system that exists today differs in important respects from the system introduced in the early 2000s. Originally, tuition fees were relatively modest and debt levels were limited. It was assumed that a large proportion of graduates would repay their loans in full. As the system was changed, those assumptions have waxed and waned.

Increasing debt levels

Tuition fees increased from £1,000 in 1998 to £3,000 in 2006 and then to £9,000 in 2012 (currently £9,790).[5] As a consequence, the debts accumulated by graduates increased dramatically. For many individual students, their total borrowing now exceeds £50,000, including maintenance loans.[6] The size of such debts has transformed public perceptions of student finance.

4 See for example **https://www.hepi.ac.uk/wp-content/uploads/2014/03/Financing-of-HE-Nick-Barr.pdf**

5 The 1998 system is mentioned here for completeness but involved means-tested payments of up to £1,000 per year, with no loans available.

6 **https://explore-education-statistics.service.gov.uk/find-statistics/student-loan-forecasts-for-england/2024-25**

Repayment and reality

Despite the language of debt, student loan repayments differ significantly from conventional borrowing. For example:

- the size of each month's repayment is linked to earnings rather than to the total amount owed;
- collection takes place via the Pay As You Earn arrangements (PAYE);
- those with low earnings pay little or nothing, and take longer to extinguish their loans if they ever do; and
- people on higher earnings repay their loans more quickly.

For many graduates, the experience is less like repaying a bank loan and more like paying an additional earnings-related tax. But the language of debt and the size of the debt that many students accrue has entered public discourse.

The weakening link between borrowing and repayment

The relationship between the amount borrowed and the amount repaid has become increasingly weak:

- some graduates repay little or nothing before balances are written off;
- others repay approximately the amount borrowed (plus interest); and
- a minority (mainly a subset of those on Plan 2 loans) repay substantially more because of the application of a real rate of interest.

The amount repaid depends not on the cost of education but on lifetime earnings patterns, repayment thresholds, interest rates and government policy changes. The system therefore already incorporates significant redistribution among graduates and, at the margins, not

always in the direction that might be assumed: as interest accrues on outstanding balances, some graduates can end up repaying more than the best-paid graduates, who can repay quickly because they earn more. Analysis by the Institute for Fiscal Studies (IFS) suggests, for later Plan 2 cohorts, the cost to the public purse might actually be negative, an outcome that sits awkwardly alongside claims that the present system is more equitable than the alternatives.[7]

The relevant policy question is not whether every graduate repays exactly the cost of his or her own education. That objective has never been a core feature of the policy. The more important question is whether graduates as a group make an appropriate contribution towards a system from which they have benefited.

Government remains heavily involved

One argument historically advanced in favour of tuition fees was that they would reduce dependence upon government, yet the experience of the past decade suggests otherwise.

The maximum tuition fee has remained frozen for long periods of time. As inflation has eroded its value, universities have experienced a substantial reduction in the real resources available per student. The real value of the fee that was set at £9,000 in 2012 has fallen by something like 25 per cent to 30 per cent, depending on the measure of inflation used in the calculation.

This illustrates an important point. Universities remain highly dependent upon government decisions. The existence of tuition fees has not insulated them from political intervention, nor has it eliminated public subsidy. Government continues to bear substantial costs through loan write-offs and other support mechanisms.[8]

7 **https://ifs.org.uk/sites/default/files/output_url_files/BN341-Student-loans-reform-is-a-leap-into-the-unknown.pdf**

8 Loans are written off after 40 years under current rules – it is that, together with the earnings threshold below which graduates are not obliged to make repayments, that leads to such a high non-repayment rate.

Debt aversion and widening participation

Concerns persist that the prospect of graduating with debts exceeding £50,000 may discourage some potential applicants, particularly from families with limited experience of higher education. However, the evidence that student debt deters participation remains contested, at least in respect of full-time young undergraduates. UCAS data show application rates have not collapsed and participation among disadvantaged groups has continued to increase. However, while the argument that the present fee and loan system discourages participation cannot be sustained in fact, nevertheless whether these concerns are fully justified is in some respects less important than the fact that they continue to shape behaviour and political debate. A graduate tax would remove the language of debt from graduates' experience, and that is a substantive change regardless of whether the underlying economic burden is identical: in other policy contexts, it is clearly understood that labelling and framing can affect behaviour.

A graduate tax with the benefit of hindsight: the arguments revisited 20 years later

The arguments that once appeared decisive against a graduate tax deserve to be revisited in light of the experience of the past two decades. Not every objection has disappeared but the force of the various arguments has changed.

Past graduate cohorts: the transition problem weakens

The most important development since the reintroduction of tuition fees has received surprisingly little attention in discussions of graduate taxes. England now possesses a large population of graduates who have studied under the tuition fee and student loan system. This changes the terms of the debate.

Historically, advocates of graduate taxes faced an obvious question. If students no longer paid fees and instead made graduate contributions, where would the money come from during the decades before sufficient graduates entered the workforce and started making substantial repayments? There was no satisfactory answer.

Universities require funding every year, whereas graduate tax revenues would emerge only gradually. A graduate tax would have required government to finance universities for many years before receiving significant revenues in return. From the Treasury's perspective, this represented a large and unattractive commitment, and the transition problem became the principal objection to graduate tax proposals. Loan-based systems have a similar shortfall, or would have done had they scored similarly in the national accounts (of which more later).

Today, however, the position is very different. More than 20 cohorts of graduates have passed through the tuition fee and student loan system. Most are identifiable through records held by the Student Loans

Company. Many are already making income-contingent repayments through the tax system. For these individuals, the practical difference between loan repayments and a graduate tax is modest.

More importantly, these people constitute an immediately available contribution base. Rather than waiting 20 years for revenues to emerge, government could begin collecting payments from a large existing graduate population. In effect, 20 years of tuition fees and student loans may inadvertently have solved the principal problem that previously prevented adoption of a graduate tax. A graduate tax could begin generating revenue almost immediately. The lengthy period during which government would have been required to fund higher education without receiving corresponding graduate contributions has largely disappeared.

Moreover, the current student loan system already imposes substantial fiscal costs on government. Large sums are lent upfront, many graduates never repay their loans in full, and government ultimately bears a significant proportion of the cost through subsidy and write-offs. The notion that the present system shields the public finances from higher education expenditure is for the birds.

From a Treasury perspective, a graduate tax should therefore be seen not as a wholly new expenditure commitment but as an alternative mechanism for financing obligations that government already carries.

A question sometimes raised at this point is whether a graduate tax would require the same money to be spent twice: using what graduates pay today both to fund new students' education and to service the government debt incurred when making loans to past students. The concern is understandable, but the reform proposed in this paper does not in fact create that problem: it does not change how universities are funded at the front end. What changes is the back end: instead of graduates repaying a named loan balance, they make an income-contingent tax payment. Government would continue to receive broadly the same stream of graduate income and the debt originally incurred to fund the loans would continue to be serviced from the general public

finances, exactly as it is now. The two obligations do not collide because they were never being met from a single ring-fenced pot in the first place.

Whether the Treasury would ultimately support such a reform is uncertain. Governments may continue to prefer the accounting treatment associated with student loans or may remain concerned about hypothecation and fiscal flexibility. Nevertheless, the principal objection that dominated earlier debates-the need to finance a lengthy transition period has been substantially weakened by the passage of time itself.

The transition problem has not disappeared entirely. However, it is no longer the insurmountable obstacle that once justified rejecting graduate tax proposals. The existence of a large, identifiable and already-contributing graduate population means that the fiscal and administrative circumstances are fundamentally different from those that prevailed when the issue was last seriously debated.

The burden of proof has consequently shifted. It is no longer sufficient simply to repeat the arguments that led policymakers to reject graduate tax proposals 20 years ago. The relevant question today is whether those arguments remain persuasive in the light of 20 years of experience with tuition fees and student loans. Nor is the political objection as potent as it once was, since most graduates of the last 20 years are already accustomed to having their pay reduced by loan repayments. They may well object to a new deduction in place of the old, especially one that is set to apply for longer, but it would not be an unfamiliar experience.

Administrative feasibility

The administrative barriers of introducing a graduate tax have also diminished. The Student Loans Company already holds extensive records relating to graduates who have borrowed under the system, while HM Revenue and Customs already collects income-contingent repayments through PAYE. Much of the administrative architecture required for

a graduate tax therefore exists. Implementation would undoubtedly require careful planning, but the practical challenges are considerably lower than they would have been 20 years ago.

The hypothecation objection

One objection frequently raised against graduate taxes has little to do with higher education and much to do with the traditions of British public finance.

The Treasury historically disliked hypothecation: the practice of earmarking particular taxes for particular purposes. They argue that spending requirements and tax revenues rarely move in parallel. Governments must therefore retain the ability to supplement or reduce spending from other sources. More fundamentally, money is fungible. Even where a tax is formally earmarked, governments may simply reduce funding from general taxation, leaving overall expenditure unchanged.

These are serious arguments and should not be dismissed but they are not decisive. The United Kingdom already operates a number of taxes and levies that are wholly or partly associated with specific purposes, including:

- the TV Licence;
- the Growth and Skills Levy;
- local authority precepts for policing and social care; and
- historically, National Insurance contributions, which were explicitly linked to pensions and social security benefits.

While not all of these are taxes in the strict sense, and none represents perfect hypothecation, they are all examples of revenues collected and then used for a specific purpose, and they demonstrate that the principle is not alien to the British system.

More importantly, the success of a graduate tax does not necessarily depend upon strict legal hypothecation. What matters is the existence

of a transparent and durable relationship between graduate payments and the funding of higher education.

If graduate payments were introduced as a replacement for tuition fees and the associated student loan system, there would be a strong political expectation that the proceeds would be used to support higher education institutions. It would be difficult for any government to argue that graduates should make a dedicated contribution towards higher education while simultaneously diverting the proceeds entirely to unrelated areas of expenditure.

The key requirement is not necessarily strict hypothecation in the Treasury sense. It is that universities, students and graduates can see a clear and credible connection between the payments graduates make and the resources available to support higher education. The sceptic will object that no such connection can be trusted in practice: any government might over time reduce the general Department for Education allocation to universities by approximately the extra amount raised through the graduate tax, leaving them no better off, or might redirect receipts to entirely different priorities. This is a legitimate concern, but it is not a definitive one. The current system provides no firmer guarantee: currently, government already sets the fee level, controls the terms on which loans are issued and has repeatedly altered those terms retrospectively. If the existing arrangement does not protect universities from political interference, it is not obvious that its retention is preferable on those grounds to an alternative.

The ONS reclassification of loans – Why the Treasury's calculation may change

A separate development, largely unconnected to the above considerations, has materially altered the public finance context in which any future graduate tax proposal would be assessed. Since September 2019, the Office for National Statistics has partitioned student loans into two components for the purposes of the public finances: the portion expected eventually to be repaid, which continues to be treated as a financial asset with no immediate effect on public sector net

borrowing; and the portion expected never to be repaid, which is now treated as government spending at the point the loan is issued, rather than decades later when the balance is formally written off.[9] That is a material change, considering that official forecasts suggest only 56 per cent of the 2024/25 entry cohort are projected to repay their loans in full.[10]

The practical effect of this reclassification has been to remove much of the fiscal advantage that loans were once claimed to hold over direct grant funding. Before 2019, I described the fiscal treatment of loans and the benefits they were supposed to convey as 'smoke and mirrors'.[11] The Institute for Fiscal Studies, among others, rather more prosaically described the previous treatment as creating a 'fiscal illusion', since none of the eventual cost of non-repayment appeared in the public finances until the loan was written off, decades after issuance.[12] But since 2019, a meaningful proportion of new lending has already been accounted for at the point of issue.

Again, the argument is not straightforward but the gap that the Treasury was historically concerned to protect, between the immediate fiscal cost of grants and the deferred cost of loans, has narrowed considerably. Consequently, a graduate tax ought to appear more attractive – or at least less unattractive – to the Treasury.

9 **https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/articles/newtreatmentofstudentloansinthepublicsectorfinancesandnationalaccounts/2018-12-17**

10 **https://explore-education-statistics.service.gov.uk/find-statistics/student-loan-forecasts-for-england/2024-25**

11 **https://www.hepi.ac.uk/reports/the-governments-proposals-for-higher-education-funding-and-student-finance-an-analysis/**

12 **https://ifs.org.uk/articles/better-accounting-student-loans-increase-headline-measure-governments-deficit-around-ps12**

The emigration objection

Concerns about graduate mobility also appear weaker than they once did. The current student loan system already faces the challenge of collecting repayments from graduates living overseas and a graduate tax would therefore confront a problem that already exists to some extent, rather than creating an entirely new one – a problem to address precisely which administrative systems have been developed. The scale of the challenge should not be overstated: of the higher education borrowers currently liable to repay, fewer than one in 20 are recorded by the Student Loans Company as living overseas.[13]

Moreover, one aspect of the original concern has diminished. During the period when graduate taxes were most actively debated, policymakers were concerned that students from other European countries might study in England, then return home and become lost from the loan repayment system. Following the UK's departure from the European Union, people coming from an EU member state to the UK can no longer access tuition fee loans (or the lower fees on offer to home students), so these concerns are less significant.

Graduate mobility remains a practical challenge, but it is no more than the challenge already faced, and is no longer a compelling reason to reject a graduate tax outright.

The government-control objection

Universities have long feared excessive dependence upon government. This is understandable. Academic institutions value autonomy and are naturally wary of funding systems that seem to increase political influence – they are distrustful of politicians and whether they can be relied upon to make decisions in universities' interests. Yet experience suggests that tuition fees have not provided the insulation from political interference many expected:

13 **https://questions-statements.parliament.uk/written-questions/detail/2025-12-08/98200**

- the maximum fee level remains determined by ministers;
- changes to immigration policy directly affect institutional finances;
- regulatory requirements have expanded; and
- inflation has substantially eroded the maximum tuition fees that the government permits universities to charge for undergraduates, with the real value of the £9,000 fee cap introduced in 2012 declining markedly.

The argument that tuition fees guarantee institutional independence is difficult to sustain, as universities are heavily dependent upon political decisions. The question is therefore not whether government influence exists, but whether it can be managed effectively.

The fairness objection

Perhaps the most persistent criticism of graduate taxes is that some graduates may pay substantially more than the cost of their own education – a criticism that carries less force than is often assumed.

The maximum tuition fee allowed by the government in England, like the limits in Northern Ireland and Wales, does not vary according to the subject studied. Nor does the system require each graduate to repay precisely what he or she borrowed. Some repay little or nothing. Others repay substantially more. The amount ultimately repaid depends upon earnings patterns, repayment thresholds, interest rates and government policy. Indeed, the present arrangements mean those who benefit less from higher education (because they earn less after graduation) can end up paying back much more than those who benefit more – a system feature which turns the fairness argument on its head.[14]

The connection between educational cost and graduate repayment has long fluctuated, and the relevant question is therefore not whether each individual repays the exact cost of their degree or even the amount borrowed. Rather, it is whether graduates collectively make

14 Because interest is added annually to their outstanding loan

an appropriate contribution towards a system from which they have benefited.

Once the debate is framed in those terms, the distinction between a graduate tax and the current system becomes considerably narrower.

Retrospection and existing loan holders

One of the strongest objections that is likely to be raised concerns retrospection. How can it be fair to impose a graduate contribution on individuals who completed their education many years ago? The answer depends largely on the population concerned.

Graduates with existing loan liabilities

The objection is weakest for graduates who currently hold student loan liabilities, as they already face repayment obligations and they already make income-contingent contributions through the tax system.

Replacing those obligations with a graduate contribution does not create an entirely new burden. It changes the announced mechanism through which an existing obligation is discharged, even though careful consideration would be needed – for example in relation to people who have have just, or are about to, extinguish their loan repayments or to reach the end of their original repayment term.

Precedents for retrospective change

Governments routinely alter tax arrangements originally settled made many years earlier. For example:

- pension taxation has changed repeatedly;
- capital gains taxation has changed repeatedly;
- Inheritance tax rules have changed repeatedly; and
- business taxation has changed repeatedly.

In each case, individuals made long-term decisions under one set of assumptions only to find the rules subsequently altered.

Student finance itself provides an important precedent. For example, successive governments have modified elements such as expected repayment thresholds after students had already entered into borrowing and repayment arrangements.

The principle that financial arrangements cannot be altered retrospectively has therefore not been observed consistently in practice and would not be entirely novel.

Avoiding double payment

A more serious concern is the possibility of double payment: graduates who have already repaid substantial amounts under the loan system may reasonably object to being required to pay more. Any reform would therefore need to recognise previous repayments.

Several approaches are possible:

- payment credits;
- shorter payment periods;
- reduced payment rates;
- exemptions for graduates who have fully discharged their obligations.

These issues are important, but they are problems of policy design rather than fundamental objections to reform. Another is the treatment of graduates who never took out a loan, either because they studied before loans were introduced or because they found other ways to pay their fees.

Political and public perception challenges

The arguments considered so far have been largely analytical. But there are significant political challenges that deserve equal honesty. These are likely to be decisive in any reform of the present system.

The most obvious is the public reaction to a permanent tax. Whatever its economic similarities to the present system, a graduate tax would be viewed and experienced differently. Today, graduates incur a debt and repay it – in full or in part – and, at some point, the obligation ends. A graduate tax would not end. For graduates who have already repaid, or who are close to doing so, the prospect of continuing to pay will feel unfair.

Student finance policy has a particular history of proving politically difficult once it reaches the public domain. Fee increases, the application of a real interest rate to student loans and policy changes on repayment thresholds have caused serious controversy, however defensible on economic grounds. A graduate tax proposal would find similar scrutiny, and any proponents need to be ready for it.

None of this is a reason to abandon the idea. National Insurance is also a permanent levy on earnings with no precise relationship to individual benefits – and it has survived for decades. But it has survived because it is embedded and because its purpose is understood. A graduate tax would need to establish its own legitimacy: it would need to be framed and communicated as a contribution to a system from which graduates have benefited and distinguished from an open-ended additional burden on a group that considers itself already to have paid its way.

The economics of a graduate tax

The central economic question is not whether a graduate tax could fund the whole of higher education, but whether it could generate revenues comparable to those collected from graduates through the student loan repayment system.

In 2024/25, higher education borrowers in England repaid approximately £5 billion (a sum that will increase in coming years). This is the relevant

comparator for a graduate tax: it is the amount graduates themselves pay, not the larger sum universities receive in tuition fee income (and students receive in maintenance support), which is funded upfront through the loan system and only partly recovered from graduates over time. A graduate tax needs to replace what graduates pay, not what universities receive; government would continue funding the remainder either way.

A crucial point follows directly from this. If a graduate tax were applied at 9 per cent to the same population currently making loan repayments, collected through the same PAYE mechanism, it would by definition produce the same £5 billion as the present system – since that is precisely how the current £5 billion is generated. Nine per cent is therefore a ceiling, not a floor: the rate required under a graduate tax to match current graduate payments can never exceed 9 per cent. The only question is how far below 9 per cent it could fall.

A graduate tax could operate on a wider base in three distinct ways, each of which would reduce the required rate.

- First, abolishing the maximum repayment period, meaning graduates currently in the repayment system who would otherwise have their balances written off would continue contributing, extending the duration of existing payments. The effect on the rate is modest in a single-year snapshot but would compound over time.
- Secondly, graduates who have already repaid their loans in full currently pay nothing more. Under a graduate tax, they could resume contributing – and with no cutoff would continue doing so for the remainder of their working lives. This group is likely to contain many higher earners, since clearing a substantial loan within a working career suggests higher lifetime earnings.
- Thirdly, future graduates who under the present system would repay quickly and then stop would end up contributing indefinitely, further expanding the base over time.

These three mechanisms all point in the same direction: each reduces the rate required to raise the same amount of revenue. On conservative assumptions about the earnings and earnings trajectories of the newly-included groups, widening the base to include other groups is likely to reduce the required rate to somewhere in the region of 4 to 6 per cent.[15] As the cancellation of a clear cut-off date (other than leaving the labour market) reaches full maturity and the payment base grows, the rate could fall further still.

These figures are illustrative rather than definitive. Their purpose is to demonstrate that the required payment rate depends critically on the scope of the contributing population and the duration of payments, and that on any reasonable widening of the base it falls meaningfully below today's 9 per cent repayment rate. A precise estimate would require modelling using earnings data held by HMRC and the Student Loans Company.

15 The range of 4 to 6 per cent reflects different assumptions about the earnings of graduates who have already repaid their loans in full. The upper end (around 6 per cent) assumes this group earns, on average, the same above the repayment threshold as the current repaying population. The lower end (around 4 per cent) assumes they earn approximately twice as much above the threshold – a reasonable inference given that clearing a substantial loan balance within a working career requires sustained earnings well above the threshold. The Student Loans Company does not publish the earnings of fully-repaid borrowers, so the precise multiple cannot be verified from published data; the range is intended to bracket plausible outcomes rather than to assert a single figure.

A possible graduate tax

A possible scheme would have the following broad characteristics.

Core principles

A successful graduate tax should satisfy the following objectives:

- Institutions should receive stable and predictable funding;
- payments should depend upon people's ability to pay:
- administration should be straightforward;
- existing, as well as future, graduates should be treated fairly; and
- the system should be transparent and publicly understandable.

Payments

Payments could be collected through PAYE in much the same way as current student loan repayments, and an earnings threshold would protect graduates with modest incomes.

Payment rates could be set at levels sufficient to support the higher education system while avoiding excessive burdens on individual graduates.

Duration

Traditional graduate tax proposals often envisaged fixed payment periods but the circumstances considered in this paper suggest a different approach.

Because more than 20 cohorts of students have been through the current student fee / loan system, a tax could potentially operate across a much larger population while maintaining relatively modest payment rates. There is therefore no compelling reason to limit payments to a

stated period. The longer the payment periods, potentially extending across much of a graduate's working life, the broader the potential tax base and the lower the annual payment rates.

University income

Funding allocations could continue to reflect student recruitment and institutional performance. If the revenue is collected centrally (as it will almost certainly need to be), then some central mechanism will be required to distribute it.

This would be unwelcome to some, but the introduction of a graduate tax need not imply a return to detailed central planning. It would not be difficult to devise a scheme in which university funding followed student recruitment, and preserving institutional autonomy should remain an important objective. The Office for Students distributes block grants for high-cost subjects and other purposes, so the principle of central allocation of higher education funding remains embedded.

Scope and exemptions

Any scheme must define its scope clearly. The natural affected population is graduates who received publicly-funded teaching in England, whether or not they originally took out a student loan.

Several boundary questions would arise in practice: whether graduates who studied at wholly private institutions or abroad should be included; whether those who paid fees upfront and took no loan would nonetheless be subject to the tax; and how to handle graduates who have retired or are no longer in paid employment. On the last point, if the tax were collected through income tax rather than National Insurance, retired graduates with income above the relevant threshold would in principle be within scope, since income tax applies to pension income as it does to earned income. Whether that outcome is desirable is a question of policy. These are questions of design rather than objections in principle, but they would need resolution before any scheme could be legislated into being.

Maintenance support

This paper focuses on the graduate tax as a replacement for tuition fees and loans. It does not directly address maintenance support, which covers students' living costs during study. That is a deliberate limitation: the arguments for and against a graduate tax are distinct from the separate question of how student living costs should be funded.[16] A graduate tax confined to replacing tuition-related payments could leave the current maintenance loan system untouched, at least in the first instance, thought care would need to be given to the total quantum of money being removed from people's pay packets through a combination of the new graduate tax and the existing maintenance loan repayments.

Transparency

Arguably, perhaps the greatest advantage of a graduate tax would be transparency, as graduates would know:

- when payments begin;
- how payments are calculated; and
- the circumstances in which payments cease.

The complexity associated with nominal debt balances, interest rates and write-off arrangements would largely disappear, at least for the costs of tuition if not for maintenance. However, as with any scheme of taxation, the rate of tax could be subject to change at major fiscal events.

The arguments that once justified rejecting a graduate tax were formed in circumstances that no longer hold. At the time, higher education participation was expanding rapidly, tuition fees were a recent innovation and the prospect of collecting graduate payments immediately, rather than waiting decades for a first cohort to enter employment, appeared remote. More than 20 cohorts of loan-funded graduates have since passed through the system, and millions are

16 And indeed the arrangements for maintenance support have, over the years, varied.

already making income-contingent repayments through PAYE. The objection that once dominated the debate, that government would have to fund universities for years before receiving anything back, no longer describes the position with anything like its former force.

At the same time, the present system has drifted toward resembling the thing it was designed to avoid. Repayments depend more on earnings and less on the amount borrowed, government continues to bear a substantial share of the cost through subsidy and write-off and universities remain as exposed to political decisions as they would be under a tax-funded alternative. So the distinction between today's arrangements and a graduate tax has become one of presentation more than substance.

This paper has gone beyond restating that the principal objections have weakened to set out, as far as the available data allow, what a reformed arrangement might actually look like. The relevant comparison is not whether a graduate tax can replace the gross income universities currently receive, but whether it can replace what graduates themselves already pay, since government would continue funding the remainder either way. On that basis, and combining a wider contributing population, with the removal of the cutoff that currently lets higher earners stop paying early, a workable scheme could plausibly collect the same sum from graduates that the present system already collects, at a rate below – and perhaps well below – today's figure of 9 per cent. The accounting treatment of student loans has changed in the past decade, narrowing much of the fiscal advantage loans were once claimed to hold.

None of this is to suggest implementation would be straightforward. Real questions remain about the precise payment rate, the treatment of graduates partway through an existing loan, the position of those living overseas, how university funding would be allocated if revenue were collected centrally and the treatment of students from and studying in the devolved administrations. These are questions of design, to be worked through by the Department for Education and HM Treasury.

The case against a graduate tax has historically rested on the practical difficulty of the transition and on doubts that the proceeds would reliably reach universities. Both objections were formed before tuition fees were introduced, when no contributing graduates therefore existed, and when loans appeared to carry an unambiguous fiscal advantage over the alternative. Neither assumption now holds in the form it once did. It is no longer enough to explain why a graduate tax was rejected in 2004 or 2010; the question is whether the same arguments remain persuasive given what has changed since. This paper has argued that, on the evidence available that they do not, and that a graduate tax deserves to be reconsidered on its current merits rather than dismissed on the strength of a calculation that the passage of time has overtaken.

Conclusion

This paper notes that the past case against a graduate tax – while well-founded and sincerely made – rested on circumstances that have changed. The transition problem has receded. The administrative infrastructure largely exists. The present system has come to resemble a graduate tax in most respects other than its name, while the accounting treatment of student loans has narrowed the fiscal advantage that loans were once thought to hold. But this report does not pretend to have settled the question. It is a contribution to a debate that needs to be had, not a blueprint.

Several things need to happen before a graduate tax could be seriously considered for adoption. The economics need proper modelling. The illustrative figures in this paper are based on publicly-available data and are sufficient to demonstrate that the required rate of payment could rest meaningfully below 9 per cent under a range of plausible assumptions, but these are not a substitute for detailed analysis using individual earnings and repayment data held by HMRC and the Student Loans Company. Other organisations are better placed than the author to do that work.

The fiscal scoring question also needs independent examination. A graduate tax would bring in tax revenue, but the upfront outlay would no longer generate a matching loan asset, as it would just count as public spending. However, if the government is meeting some costs upfront and expecting individuals to contribute later in life, the borrowing consequences of loans versus a graduate tax are the same. The real change, some might say opportunity, of a graduate tax is the ability to increase the number of people making payments.

Design questions remain: how to treat graduates currently partway through existing loans; how to handle graduates living overseas; how to allocate revenue to universities; how to deal with the devolved administrations; the relationship between a tuition-focused graduate tax and the continuing maintenance loan system; and what to do about

graduates of private institutions or those who paid their fees upfront (some of whome faced real disadvantage in doing so but did so because interest-bearing loans breached their religious convictions). These are not objections in principle, but they are not trivial, and so they need working through.

Finally, the political challenge is real. A graduate tax would need a clear and honest public narrative – one that addresses directly why a permanent contribution is preferable to a finite debt, and why it represents a fair settlement rather than a retrospective imposition. That argument can be made, but it will not be easy to make and will need to be made well.

This paper is intended as a contributon and invitation to that wider debate. The question of whether a graduate tax would serve students, higher education institutions and the public better than the present arrangements deserves serious examination, which it has not recently received in recent times.

President

Bahram Bekhradnia

Trustees

Professor Dame Sally Mapstone (Chair)

Mary Curnock Cook CBE

Professor Dame Julia Goodfellow

Professor Sir Chris Husbands

Professor Nick Pearce

Chief Executive

Nick Hillman OBE

Advisory Board

Alison Allden OBE

Professor Sir Nishan Canagarajah

Anne-Marie Canning MBE

Andy Forbes

Professor Julie Sanders

Professor David Sweeney CBE

Partners

Advance HE

Browne Jacobson

Cambridge University Press & Assessment

Duolingo

Ellucian

Elsevier

Huron

iQ Student Accommodation

Instructure

Interpath

Jisc

JS Group

Kaplan

Kortext

Lloyds

Pearson UK

Research England

Studiosity

Taylor & Francis

TechnologyOne

Times Higher Education

Unite Students

UPP Foundation

HEPI

Debate

49

Bahram Bekhradnia, HEPI's founder and President, takes a look at the case for a graduate tax to fund higher education. He argues that circumstances in the UK, and especially England, have changed so much in the past 20 years that the arguments against the idea have weakened significantly. So has the time arrived to take another look at the idea?

HEPI was established in 2002 to influence the higher education debate with evidence. We are UK-wide, independent and non-partisan.

November 2026
978-1-915744-72-2
Higher Education Policy Institute
99 Banbury Road,
Oxford OX2 6JX
www.hepi.ac.uk

Printed by Holywell Press Ltd, Oxford
Typesetting:
Steve Billington,
jarmanassociates.co.uk