

Economics

Question 2: What will be the effect on socio-economic mobility of the UK government's plan to impose value added tax on school fees?

Access to quality education remains one of the most influential determinants of an individual's capacity to advance socially and economically. Across the UK, approximately 10.63 million students are enrolled in schools. Students are enrolled in both public and private schools. Private schools host 5.9% of all pupils and are characterised by offering smaller class sizes with superior facilities and resources. In contrast, public schools accommodate 94.1% of all pupils, but are associated with dilapidated infrastructure with inadequate teachers and resources. The UK government has aimed to improve socio-economic mobility, the ability of individuals or groups to move up the socio-economic ladder, as measured by changes in income and occupation, by investing in education, a recognised macroeconomic objective, thereby helping reduce societal inequity. With public finances already strained, and about 4.1% of GDP already being spent on education, it is imperative for the government to find new sources of funding, one of which is to tax those who can afford. Thus, the question remains: Will the government's proposed 20% VAT on private school fees truly advance socio-economic mobility?

Objectives of the Policy:

The government aims to shore up its resources for public education from the imposition of this 20% VAT, the highest rate, on private school fees. While some may argue that the government could raise these funds through borrowing, the economic impact of COVID-19 has constrained funding options, which is depicted by Figure 1 below, showing minimal increases in GDP. With a renewed focus on self-sufficiency, the government views this VAT as a necessary measure to support sustained investment in education and, in turn, drive growth in both GDP and GDP per capita, which is currently stagnant or declining as observed in the graphs below.

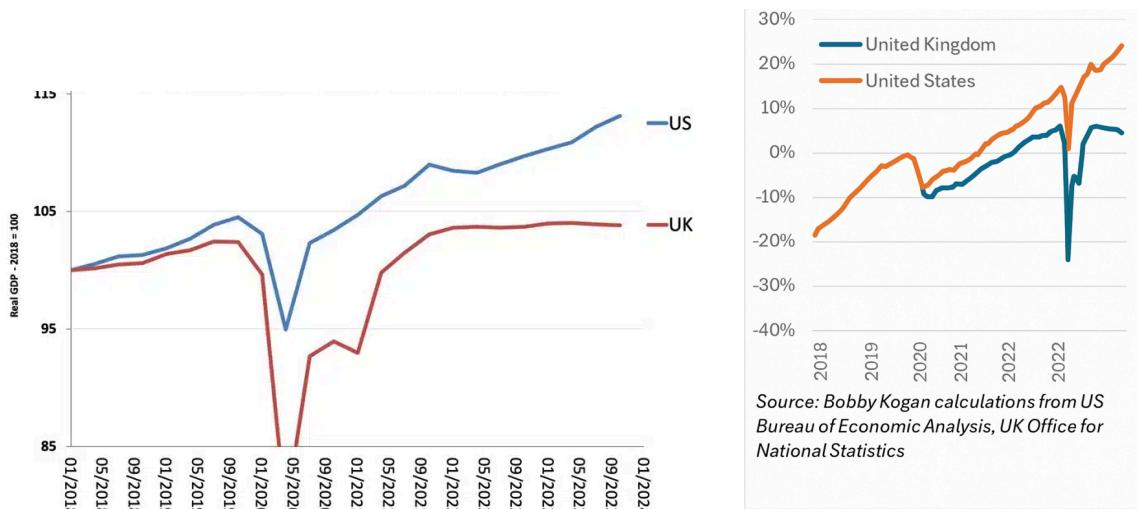


Figure 1: Comparison of UK and US economic growth and Real GDP per capita over the years.

Likely Advantages of this VAT:

One may argue in favour of the tax by noting that the projected revenue of £1.6–£1.8 billion is meaningful and could be redirected toward more equitable public investment in public schools. The socio economic mobility will be more equitable with this VAT, given the likely increased prevalence of public sector schools in many regions due to the decline of private sector schools. And only around 35,000 pupils are expected to transition to the public schools, a number unlikely to destabilise the system at a national level.

Likely Disadvantages of this VAT:

However, I believe the imposition of 20% VAT on private school fees will not be helpful. This VAT is counterintuitive, given that education is considered a merit good and education should, therefore, be promoted both in public/private schools. This policy may fail to achieve its intended outcomes:

- It could impose unintended strain on public-schools and productivity challenges;
- This strain is likely to be geographically uneven - creating skew;
- The VAT will increase bureaucracy and there is significant uncertainty to the amount that can be collected; and
- A degree of elitism is arguably inherent in stratified societies like UK and the so called educational elitism of private schools is not so elite and it can be made to work in system's favour.

Unintended Strain on Public-Schools and Productivity Challenges:

With the imposition of VAT, private school fees are set to rise significantly, placing pressure particularly on middle-income families, which will make up about 20-30% of the students going to private schools, who will view private education as a key for mobility for their children. However, due to affordability, some families are likely to move their children from private to public schools.

The public education sector, already under considerable strain, is ill-equipped to absorb this sudden influx of students. Compounding this issue, over 83% of headteachers report difficulties in recruiting sufficient staff. The current student-teacher ratio in UK public schools stands at about 18:1. Lower student-teacher ratios are recommended as it improves the individualised attention a student receives, thereby allowing them to build efficiency in academic and social capital necessary for change in their socio-economic mobility.

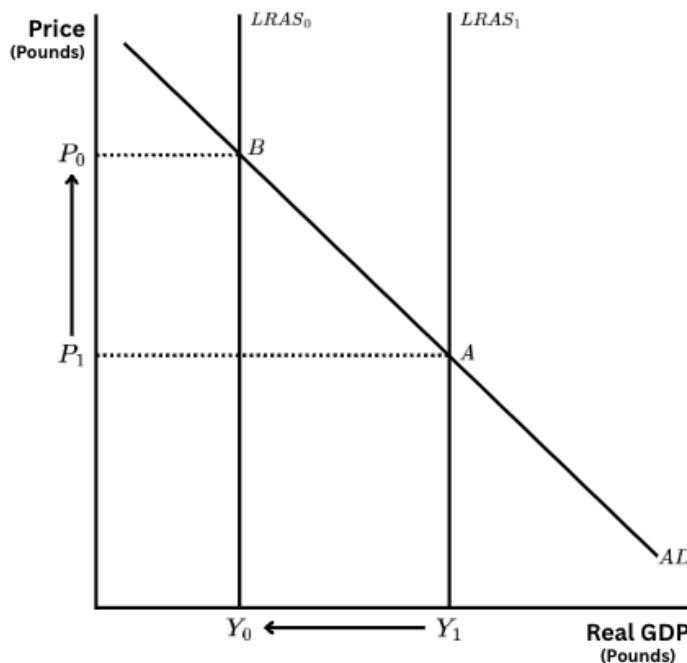


Figure 2: LRAS Framework showing decline in Real Output over time due to the imposition of VAT

In the long run, if more students are pushed into already overstretched public schools due to rising private school fees, the overall quality of education may decline. This can lead to a reduction in human-capital formation - that is, the development of essential skills, knowledge, and abilities within the workforce. With larger class sizes, reduced teacher attention, and limited resources, students may leave school less prepared for higher education or skilled employment.

This decline in education weakens the productivity of future workers, ultimately reducing the economy's capacity to produce G&S efficiently. The government may ultimately need to invest more in the future workforce, indicated by the increase in price from P_1 to P_0 and with per capita already stagnant or declining, it cannot afford a further decline in labour productivity. This is illustrated by Figure 2 by a leftward shift in the LRAS curve, from $LRAS_1$ to $LRAS_0$. As a result, output falls from Y_1 to Y_0 .

Uneven Geographical Strain:

The impact of this migration of students will be felt unevenly, concentrated in specific geographies. This impact may be mitigated in part by the nature of the UK's education system, where public school quality is strongly tied to local income demographics. In many areas where private schools are prevalent, local public schools also tend to be relatively well-funded, due to higher council tax revenues. Thus, in some high-income regions, public schools may be better equipped to absorb displaced pupils without significant deterioration in quality. The challenge will be felt across already disadvantaged regions, as illustrated by figure 3, which shows that wealthier areas tend to have top-performing public schools, while less wealthier regions are likely to have middle or bottom performing schools, as indicated by Top Grammar Schools in the country in the chart on next page.

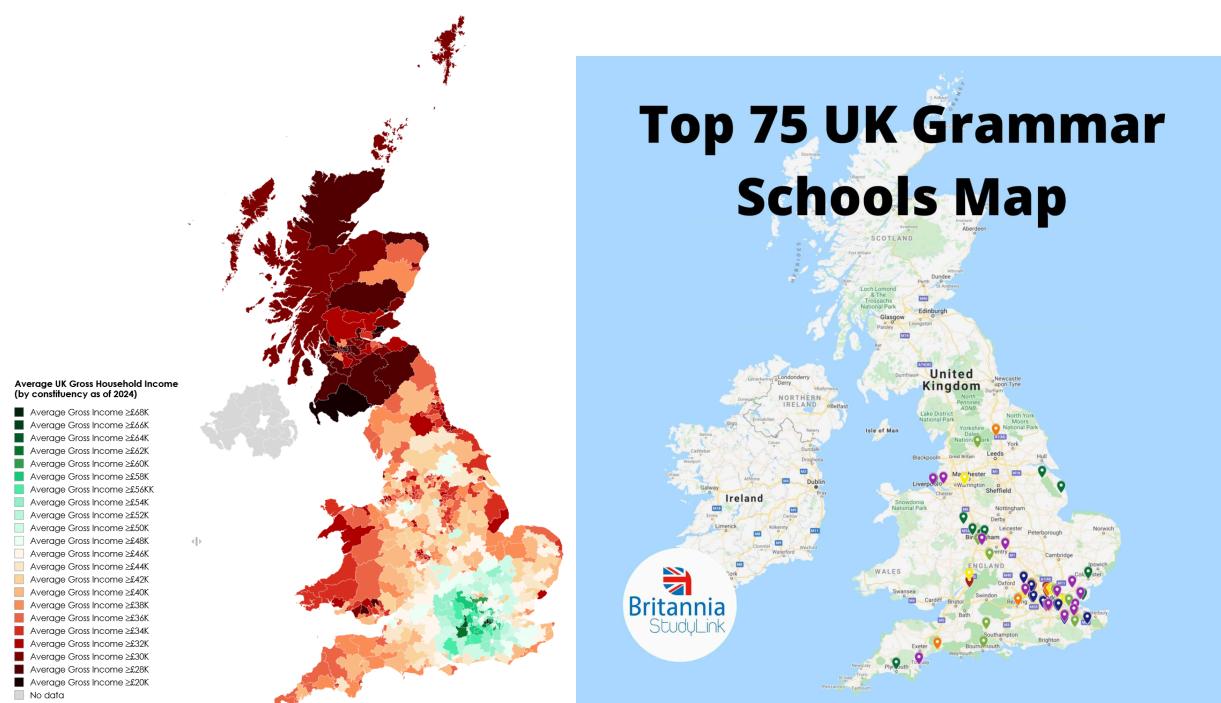


Figure 3: Two comparative maps illustrating the correlation between the rankings of top schools in the UK and regional income levels.

Ballooning Bureaucracy and Uncertain VAT Collection:

Through this new scheme the government expects to raise between GBP 1.6 and GBP 1.8 billion, which is only $\approx 1.4\%$ of the overall education budget of GBP 116 billion. On top of this, the opportunity cost of a relatively modest increase in revenue may be high, as it would require significant implementation effort and ongoing oversight.

VAT applied to specific sectors, especially those involving complex exemptions or restructuring, can result in administrative costs of up to 15%. In this case, the logistical burden would likely include regulatory oversight, monitoring fee structures, and dealing with legal and audit costs, as schools attempt to adapt or contest the policy. Although no official estimate of the administrative burden has been published, a 15% cost is a reasonable projection given the scale and complexity of implementation. Therefore, the actual amount available is about £1.5 billion (at higher end of range). With over 9.5 million students currently enrolled in public schools this revenue would equate to about £150 per student, per year. The government's own COVID-19 education recovery plan proposed up to £1,500 per pupil as the scale of funding required to meaningfully address learning loss. In contrast, this new taxation scheme would generate a figure that is not only significantly lower, but also spread thinly across a wide range of potential needs. Even if used for cost-effective interventions like subsidised tutoring, textbooks, or classroom upgrades, the funding would be too limited to achieve measurable system-wide improvements.

Further, one could argue that if middle income families respond to the tax by sending students to public schools the government's anticipated revenue could decline. A drop in enrollment would shrink the taxable base, further reducing the actual amount raised, limiting per-pupil funding. Historically, similar policies have repeatedly failed, as seen in Greece; and if the government later reverses the decision, it risks revenue loss and disruption from students shifting between private and public schools.

Elitism and Socio Economic Mobility of Disadvantaged Groups:

Elite charitable schools like Eton, Harrow, and Westminster primarily cater to the top 5% of earners, making their students relatively insulated from the effects of VAT on school fees. Their financial edge enables them to attract top teaching talent, offer more individualised support, and maintain low student-teacher ratios. Combined with cutting-edge facilities and rich extracurricular offerings, these advantages help students build both academic excellence and well-rounded personal development.

However, private schools are not necessarily detrimental to society and their impact is much wider than the students enrolled with them, paying high tuition fees. Many elite charitable

schools actively engage in philanthropic initiatives. For example, Eton runs extensive scholarship schemes that offer transformative opportunities to talented students from underprivileged backgrounds. These programmes can provide access to high-quality education, helping recipients develop valuable academic and interpersonal skills that enhance their future employment prospects and enable them to support their families.

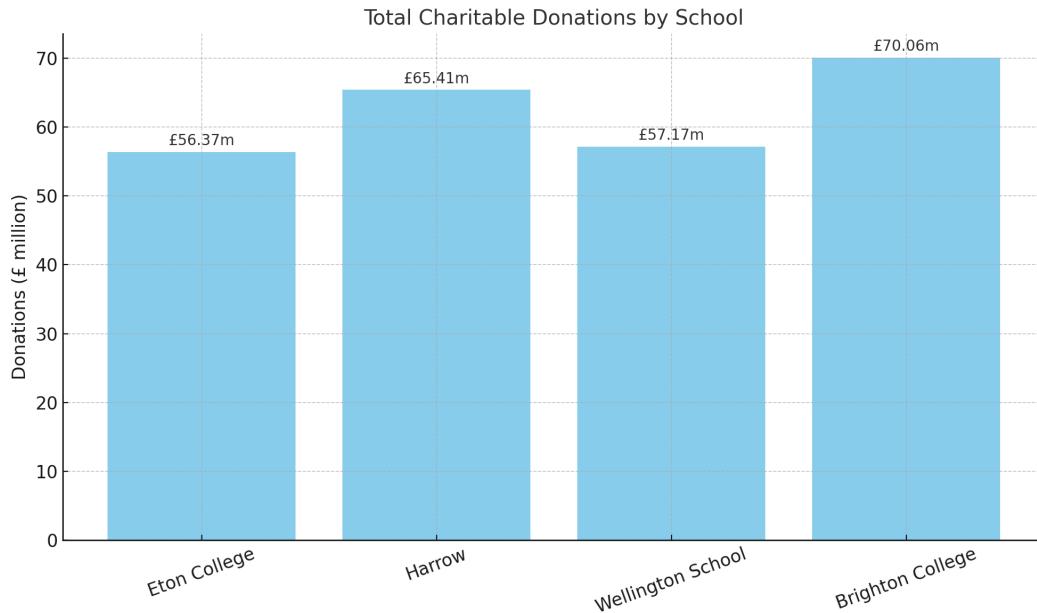


Figure 4: Investment made by Private Schools as part of charitable spends in 2024

Private schools often invest in specialised support programmes tailored to SEN pupils. With access to greater resources, they are able to provide personalised attention, targeted interventions, and a more supportive learning environment that helps SEN students thrive.

Moreover, the operation and maintenance of these schools require a wide range of staff, including teachers, administrative personnel, and service workers. This demand creates numerous employment opportunities, contributing to local job markets. The high standards expected at these institutions can also help raise the overall qualifications and professional development of the teaching workforce, potentially boosting productivity in the education sector and contributing to a stronger economy through increased spending and economic activity.

Alternate Pathways to 20% VAT on Private Schools Fees:

It is well established that education is a key driver of socio-economic mobility, and the government uses it as a policy tool to promote a more equitable and fair society. The government should improve public schools through alternative solutions that promote educational equity without imposing a 20% VAT.

With the vast majority of children attending public schools, these institutions are often attended by families from a range of income levels. Therefore, the government could consider introducing a system of 'voluntary contributions,' where individuals have the option to donate funds to their local public school, providing additional support and resources. Furthermore, the government could incentivise donations by making them fully tax-deductible, only up to a certain level. This is analogous to a system in Australia, where public schools can request voluntary financial contributions from families to help cover educational costs. Figure 5 highlights a positive trend, with the number of teachers and administrative staff increasing at a significantly higher rate than student enrolment, thereby indicating enhanced overall education quality.

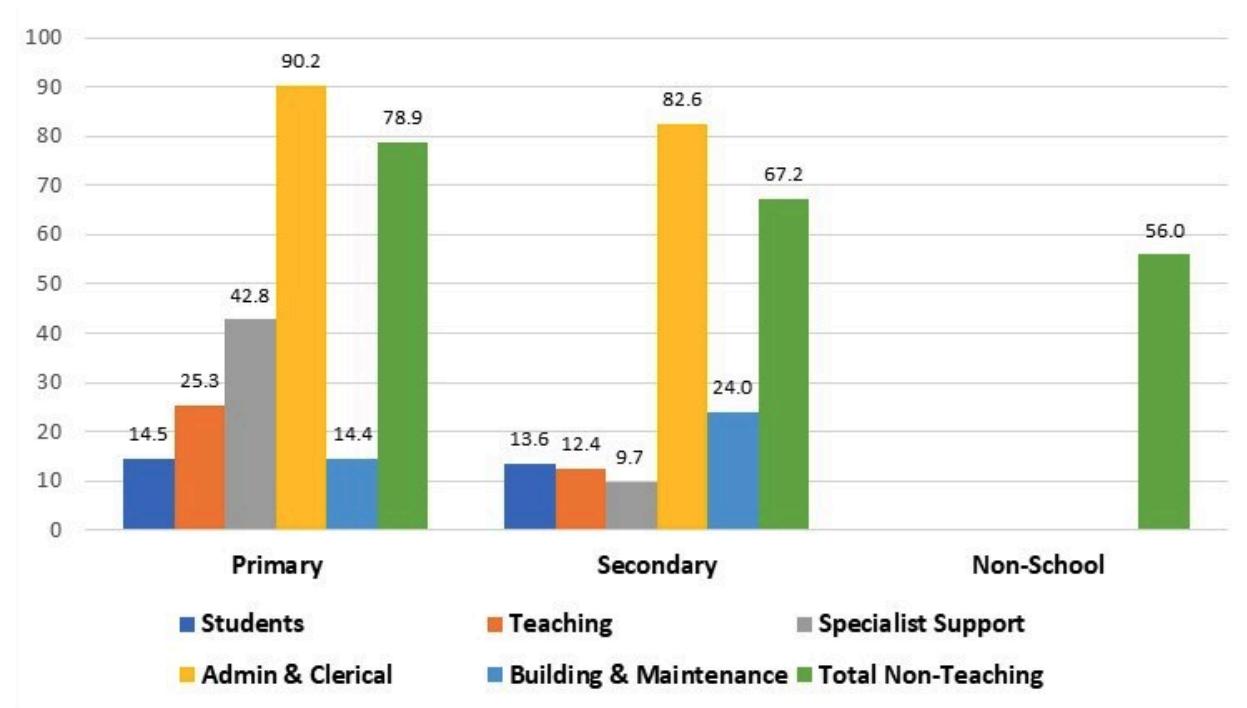


Figure 5: The increase in staff from 2002 to 2019, expressed as a percentage increase, in Australia

In addition, the government could focus on fostering PPP: public-private partnerships. Such collaborations could offer a 'best of both worlds' approach, where students benefit from the high-quality resources of private schools while accessing them at subsidised fees through government support. Germany is one example where private educational institutions operate under public oversight and receive substantial subsidies, resulting in relatively low tuition fees, depending on income levels.

Furthermore, the government could monetise certain aspects of public schools, as they often

occupy valuable land and facilities. These spaces could be rented out for after-school purposes, such as sporting classes or community activities, generating additional revenue.

The government could also consolidate underperforming or struggling schools to pool resources and reduce operational costs in order to concentrate efforts on improving educational outcomes at targeted schools.

Alternatively, the government could consider implementing a reduced VAT rate on private school fees. This approach would ease the financial strain on both public and private schools by preventing a sudden shift in enrolment and maintaining stability across the education sector. While it would generate less revenue than the 20% rate, the funds collected could still be directed toward initiatives that serve the wider public good, such as developing an upskilling platform for students and teachers, similar to Khan Academy or Udemy.

Summary:

Undoubtedly, education in the UK needs to improve. The 20% VAT on private schools is not the best approach. This review has explored the potential consequences of the UK government imposing VAT on private education fees. While private schools are often criticised for promoting elitism, they also offer significant benefits that contribute to societal development, leading to upward socio-economic mobility, and hence need to be encouraged. Additionally, the average revenue generated per child through VAT would likely be small for any meaningful impact. As such, alternative approaches, such as voluntary levies, public-private partnerships, and investment in technology, could offer more effective and equitable solutions.

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