

Hamilton East Rotary Club

**Zero Fees and a Universal Student Allowance for
New Zealand?**

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Zero Fees and a Universal Student Allowance for New Zealand?

Thank you for the opportunity to address the Hamilton East Rotary Club.

New Zealand student unions protesting the student debt 'explosion' and demanding lower tuition fees (if not free tertiary education) and a universal student allowance. Concerns from some about Asian immigration. Competing promises of tax cuts. More money for front-line police officers. Promises of reduced hospital waiting lists.

Promises to the left of me and promises to the right.

It must be election year!

Tonight I want to talk about tuition fees and student support. This is particularly relevant in Hamilton, a city that hosts a major university and institute of technology, as well as several private training establishments.

I will begin my talk with a brief overview of tertiary education financing in New Zealand, including tuition fees, student loans and student allowances. Several features of the system are worth highlighting:

- The government funds tertiary education institutions (TEIs) directly through a system of tuition subsidies;
- TEIs receive other forms of direct government funding, including Performance-based Research Funding (PBRF), a competitive research funding programme that provides funding on the basis of the quality of researchers, research degree completions and external research income;
- TEIs are able to charge tuition fees (within government-determined maxima) and raise other forms of revenue to supplement their government income, including undertaking consulting work, carrying out contract research and providing other services;

- All full-time and some part-time students in tertiary education (who are citizens, residents or refugees) are able to borrow money from the government under the student loan scheme to help offset the cost of tuition fees, living costs and other expenses. In 2006, there were some 167,000 students with a student loan; and
- A sizeable proportion of tertiary education students are also eligible for non-repayable student allowances to help cover living costs. In 2006, there were nearly 60,000 students in receipt of a student allowance. The student loan and allowance systems are integrated so that eligibility for allowances affects eligibility for the living cost component of student loans.

While there have been some major shifts in policy since the early 1990s, the broad outlines of the tertiary education system were developed as part of the *Learning for Life* reforms of the late 1980s and introduced as part of a comprehensive reform package that included changes to the governance of TEIs, the introduction of tertiary tuition fees, the establishment of the student loan scheme, targeting of student allowances and measures aimed at promoting the expansion of private tertiary education.

Taxpayer spending on tertiary education is significant. In 2008, the government is expected to spend some \$3.25 billion on tertiary education. As shown in Table 1, almost two-thirds of this spending is on tuition subsidies, followed by student loans, student allowances and other tertiary education spending. In 2008, taxpayers will spend an average of around \$13,800 per equivalent full time student on tertiary education.

Table 1: Tertiary Education Expenses, 2008

| <i>Spending Area</i> | <i>Expense (\$ Millions)</i> | <i>%</i> |
|-------------------------------|----------------------------------|----------|
| Tuition | 2,106 | 64.7 |
| Other Tertiary | 183 | 5.6 |
| Tertiary Student Allowances | 402 | 12.4 |
| Student Loans | 562 | 17.3 |
| Total | 3,253 | 100.0 |
| | | |
| Equivalent Full Time Students | 235,451 | |

Source: *The Treasury*

According to the Organisation for Economic Cooperation and Development (OECD), spending on tertiary education in New Zealand in 2004 amounted to 1.5% of Gross Domestic Product (GDP) – below levels for the Nordic countries (2.1% to 2.5%), but above levels in ‘Anglo’ countries such as the United States, Australia and the United Kingdom (1 to 1.3%) and above the OECD average of 1.3%. In that same year, public spending on tertiary education amounted to 4.9% of total public spending – second only to Norway (5.3%) and well above other countries including the US, UK and Sweden and above the OECD average of 3.1%.

As you can see from these statistics, New Zealand financial support for tertiary education is significant, both in absolute terms, relative to overall government spending in New Zealand and relative to the country’s ‘ability to pay’, as measured by GDP.

One would not be left with this impression from much of the current debate on tertiary education in New Zealand. While television footage of students in makeshift soup kitchens, in cardboard box ‘cities’ and in student loan debt ‘shackles’ makes for great theatre, it does far less for advancing serious debate on the issue of tertiary education financing in New Zealand.

There is much evidence that good policies matter for a country’s economic performance. I have no doubt the same is true in education generally, and in tertiary education more specifically. In my view, there are serious issues to be debated in respect of the tertiary education system – including how it is funded and regulated.

This is particularly true given the continuing march of globalisation, the rise of economic powers such as China and the need for New Zealand to continue to foster a knowledge economy. While phrases such as globalisation and knowledge economy may be over-used, their effects are real. For example, the rise of cross-border tertiary education places new and challenging demands on tertiary institution quality assurance systems, while the advent of a global labour market means there is increased competition for academic staff and graduate students.

Two initiatives that, in my view, should be low on the list of tertiary education policy priorities have been front and centre in the news this past week – a reduction in tuition fees (zero fees for some) and the introduction of a universal student living allowance.

As I have written elsewhere, and on several occasions over the past 6 years, the case for zero or reduced tuition fees at the tertiary education level is weak. Indeed, any move to further curtail the ability of TEIs to charge tuition fees could have adverse consequences – particularly if any economic downturn puts pressure on government spending. The payment of tuition fees – aka private responsibility for the costs of tertiary education – is justified on several grounds. Let me mention just three.

First, they reflect the fact that tertiary education should be seen as an investment that will benefit those who undertake that education. Many studies – including from New Zealand – provide ample evidence that graduates enjoy a significant payoff from undertaking tertiary education. Second, tuition fees are equitable – it is only fair that those who benefit from the investment pay for at least part of it. Finally, tuition fees provide an important and decentralised revenue stream for TEIs that is essential to the maintenance of quality in the tertiary education sector.

While many arguments are raised against tuition fees, these are generally wrong. For example, those who argue that fees deter students from attending tertiary education institutions ignore the fact that it is an investment and that the system of subsidies and student loans in place provide an important buffer against this. While significant tuition fees on their own might deter access to tertiary education, the combination of tuition fees and significant public subsidies (as exists in New Zealand) does not.

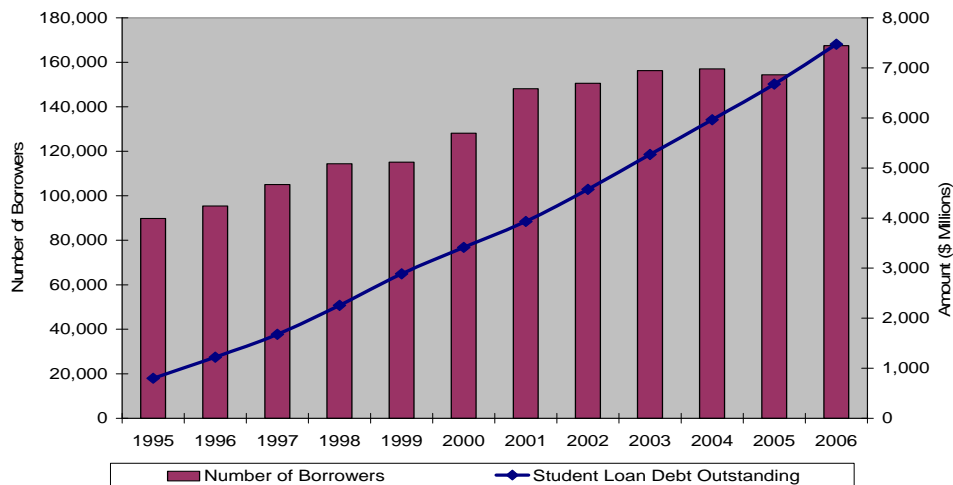
Indeed, OECD data show that two countries – New Zealand and Australia – with a combination of ‘high’ tuition fees and significant public subsidies have among the highest entry rates into tertiary ‘Type A’ (advanced) education. Other similar countries, including the USA, the Netherlands and the UK are all around or above the OECD average for entry rates into tertiary ‘Type A’ education.

The call for the introduction of a universal student allowance is even less justified in my view – particularly given the extremely generous provisions of the student loan scheme in New Zealand. The student loan scheme is both comprehensive and generous and would be the envy of any entrepreneur borrowing funds to finance an investment:

- eligibility is not means-tested and there is no duration limit on receipt;
- students can borrow to cover tuition fees, living costs, course-related costs and student association fees;
- interest is written off for all students while in study and for graduates who remain in New Zealand; and
- the current student loan interest rate – 6.7% – is well below mortgage and personal lending rates.

The ‘two-step’ abolition of student loan interest (in 2000 and then again in 2006), has been, in my view, a policy failure – if a political success story. Critics’ predictions of the impact of the policy change have proven correct. As shown in Figure 1, the number of borrowers under the scheme rose by 8.4% and the value of loans outstanding (the so-called debt mountain) grew by nearly 12% between 2005 and 2006. Both occurred despite a decline in the number of government-funded students.

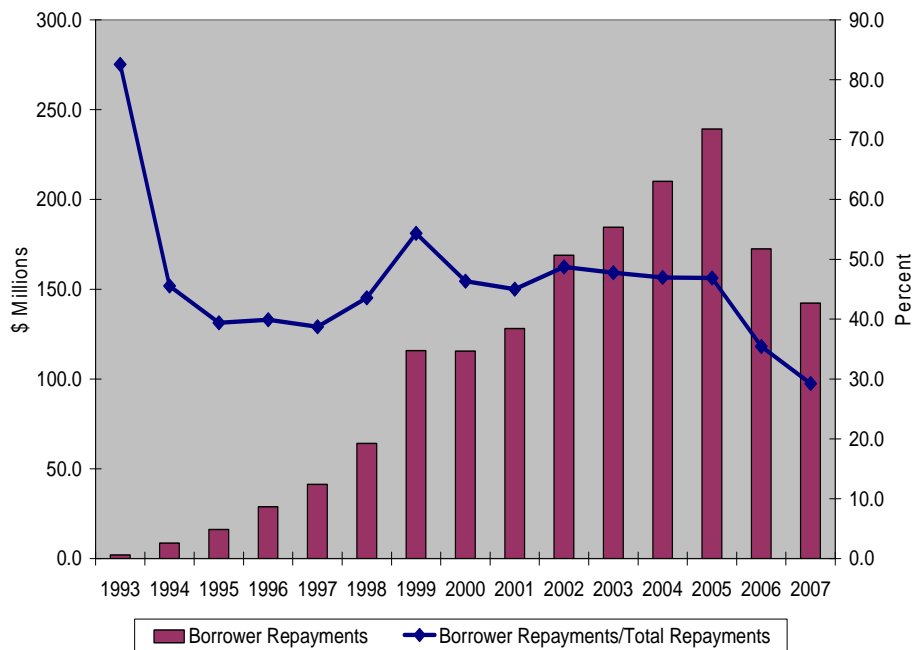
Figure 1: Annual number of student loan borrowers and student loan debt outstanding, 1995 - 2006



Source: Ministry of Education, Inland Revenue Department and Ministry of Social Development (2007) Student Loan Scheme Annual Report.

The abolition of interest has also led to a sizeable drop in borrower loan repayments (ie. those made directly by borrowers, rather than through employer deductions). As shown in Figure 2, borrower repayments dropped sharply from \$239 million in 2004/05 to \$173 million 2005/06 and \$142 million in 2006/07.

Figure 2: Borrower repayments and borrower repayments as a proportion of total repayments, 1993-2007

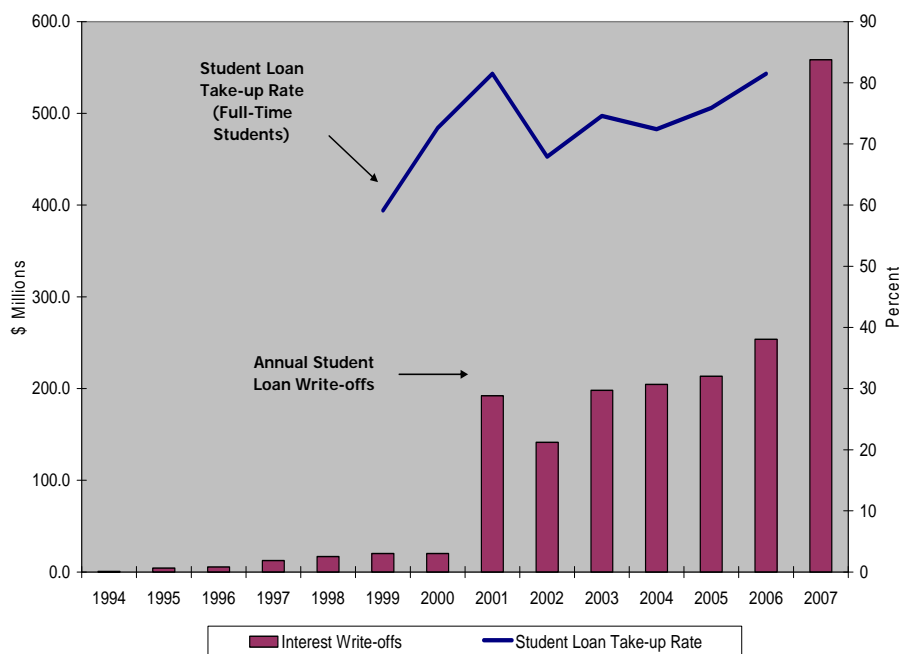


Source: Ministry of Education

Moves to make the student loan scheme more generous have lifted the 'economic cost' of the loan scheme to the Crown – which takes into account factors such as loan write-offs, doubtful debts and the timing of repayments – and by a significant amount. Throughout the 1990s, the economic cost of the scheme was estimated at around ten cents per dollar of loans drawn down. The decision in 2000 to write-off the interest of students who were studying led to a more than doubling of the economic cost of the scheme – to an estimated 23 cents per loan dollar drawn down. The 2006 policy change will have increased this significantly.

According to the Treasury, student loan interest-write-offs totalled \$558 million in 2006/07, up from just \$20 million in 1999/00 (see Figure 3). That is a significant annual cost and could have nearly financed the equivalent of the newly announced *Fast Forward* research fund *every year*.

Figure 3: Interest write-offs and student loan take-up rate, 1994 - 2007



Source: Ministry of Education

Money spent on student loans is money that would have been available to finance other government priorities – including building New Zealand's research base, financing quality improvements and attracting and retaining top flight academic staff. And the gains from the interest rate abolition – ie. increased access to tertiary education – are likely to be minimal.

The end of January 2008 National Party announcement that, if elected, it would not reverse the student loan 'no interest' student loan policy was a disappointment, but not unexpected. It does, however, mean the continuation of the policy, whatever the election result. Such expensive in-built subsidies have no place in a student loan scheme, whose role is to give students the money they need to pay the up-front costs of their investment in tertiary education – fees and living costs. It should not be a

mechanism for providing subsidies on top of those delivered as part of the tuition subsidy scheme.

The growing debt ‘problem’ that has been created by the removal of interest is now being used as a justification for the supposed ‘cure’ – namely the introduction of a universal student allowance.

The government has been right to resist the calls for the introduction of a universal living allowance, with the Tertiary Education Minister the Hon Pete Hodgson saying it was government policy not to move to a universal allowance, but to make progress towards it. It is difficult to see the policy imperative for moving toward a universal student allowance given the generosity of the student loan scheme. The loan scheme is a very good deal for students if there ever was one. A universal student allowance would do nothing to correct the current system’s failings. Although subsidies under such a scheme might be more transparent, they would also cost considerably more given they would be non-repayable.

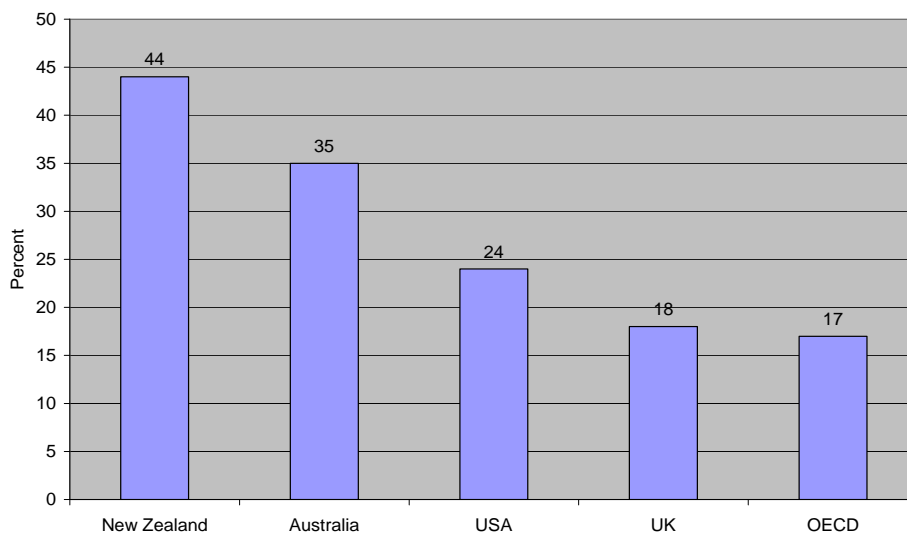
A recent OECD study argues in favour of a policy framework much like the one New Zealand has had since the early 1990s, including charging tuition fees and introducing a universal student support system with two major components: an income-contingent loan system complemented with a scheme of means-tested grants.¹

Rather than debating whether or not to spend more on tertiary education by moving to a universal student allowance, the focus in the first instance should be on whether we are spending the current tertiary education budget in the right way. There is good reason to believe we are not. According to a 2006 New Zealand Vice Chancellors’ Committee report, New Zealand stands out compared to other countries in terms of the high proportion of the tertiary education budget that was spent on student support in 2002: 44% in New Zealand versus 35% in Australia, 24% in the US, 18% in the UK and 17% for the OECD as a whole (see Figure 4). They

¹ OECD (2008) *Tertiary Education for the Knowledge Society: OECD Thematic Review of Tertiary Education*, Paris, p. 16.

further estimate that the New Zealand figure is likely to rise to 55% due to the introduction of interest free student loans.² A universal student allowance would further skew spending in New Zealand away from direct support to institutions toward student support. These figures suggest we should be looking at ways of shifting the balance of assistance away from student support, not towards it.

Figure 4: Share of tertiary education budget spent on student support, various countries, 2002



I have no illusions – such a move would be politically difficult. It seems to me it cannot happen without groups such as the NZVCC and the Association of University Staff (AUS) – both of whom directly bear the consequences of current policies – taking on this contentious issue. There is little hope of this happening in the short term. Indeed, the AUS has supported the introduction of a universal living allowance. For its part, the NZVCC did raise concerns about this issue in a 2006 submission to the government, but it seems to accept that the situation is unlikely to change in the current political climate.

One can only hope that, at some stage, we experience some ‘climate change’ of the policy variety and that the opportunity cost of the no interest

² New Zealand Vice Chancellors' Committee (2006) *An Investment Approach to Public Support of New Zealand's Universities*, Wellington, pp. 6-7.

student loan policy becomes such that student support reform – the ‘elephant in the room’ – can no longer be ignored.