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1

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End the turf war

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The big question in the white paper on higher education expected to be published next week – as Professor Nicholas Barr says – is whether universities are going to be allowed to set their own fees. That is what we need. The extra money needs to go into higher education. If the Treasury sets the fee and treats the money as a graduate tax the universities won't be better off because the money will simply be appropriated by the Exchequer and used as it wishes. This point has been completely missed by commentators who have preferred to see the tussle between Downing Street and the Treasury as a battle between Old Labour (good) and New Labour (bad) when in fact it was probably simply a turf war between Treasury mandarins and the rest.

Nicholas Barr and Iain Crawford: Set universities free to decide their own fees

16 January 2003

There is quite a lot of writing on the wall, much of it by Charles Clarke, the Education Secretary, about the contents of the White Paper on higher education expected next week. He has said that the beneficiaries of higher education should pay more than they have in the past. That is right. As a major ingredient in national economic performance, higher education benefits the country as a whole. Thus taxpayers have contributed, and should continue to contribute, to the cost of higher education.

However, getting a degree also benefits students, so that they too should contribute. But until now, the degrees of people who continue to be among the best-off have been heavily financed by less well-off taxpayers. This is deeply regressive; money that should be spent promoting access is hijacked by the middle class.

But if beneficiaries pay more, what form should that contribution take? Charles Clarke's second statement is also right: that contributions should be made after graduation not before – in the jargon, a deferred contribution.

Though university funding has been a growing problem for all governments for at least 25 years, the present government brought in an important part of the solution in 1998. Since then student loans have had income-contingent repayments, that is, repayments calculated as x per cent of a graduate's earnings, piggy-backed on income tax, until the loan is repaid. The change is fundamental: graduates' loan repayments instantly and automatically track changes in their income; and someone with low earnings makes low (or no) repayments.

The bad news is that the Government has been utterly woeful in explaining the system. Almost nobody understands that student loan repayments are just like an add-on to their income tax. In that sense, we have a form of graduate tax already. Nobody lies awake worrying about their tax debt to the Government (on plausible assumptions close to a million pounds in income tax and national insurance contributions over a 40-year career). Loan repayments are no different.

Where Charles Clarke has kept his cards conspicuously close to his chest is over whether universities will be able to set their own fees. If fees are set by the Government and are the same at all institutions, as in Australia and the UK, rising fee income can be offset by falling taxpayer contributions. That is exactly what has happened in Australia, where fees were introduced in 1989 to resolve a funding crisis. Their system is now back in crisis. For exactly the same reason, the introduction of fees in the UK has not netted any extra money.

In short, when government sets fees, as in Australia and the UK, funding is closed-ended. Flat fees are also fundamentally unfair. Why should a student at a local university pay the same as one at a world-class institution? Again, the system favours the best-off students at the best universities.

A pure graduate tax (repayments for 25 years or until retirement) is little different. Funding remains closed-ended, because the Treasury decides on the volume of resources going to higher education. And this type of graduate tax has its own unfairness, as contributions bear an arbitrary relation to the cost of a person's education.

Deferred flexible fees bring in a different world. Here, universities can set their own fee levels, up to a ceiling. Funding is open ended: if the Government cuts taxpayer funding, each university has the option to raise its fees.

Provided (and the proviso is crucial) fees are fully covered by a loan, higher education is free at the point of use. The Student Loans Company pays a maintenance loan into the student's bank account and his or her tuition fee into the university's bank account. The student repays after graduation, but only to the extent that his or her earnings warrant.

In short, only open-ended funding will solve the crisis and only deferred charges are compatible with access. Deferred flexible fees are the only way to do both. They protect access as repayments are related to people's income; and they free resources to promote access, for example by restoring grants for less well-off students.The third piece of writing on the wall is as critical as the other two.

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