

Tertiary Funding Policy at an Impasse

A fundamental law of economics is that you can control the price of something or the quantity supplied, but not both.

We saw that law in operation in the old Soviet system, with rationing and queues, and during the Muldoon wage and price freeze.

Governments impose controls on prices to court short-term political popularity. The problem is getting rid of them as pressures and distortions mount.

The Muldoon government was struggling in vain to solve this problem when it was ousted in 1984.

The same dynamic has been at work in tertiary education in recent years.

The last government imposed a cap on university fees. It also made student loans interest-free while students were studying and then, in a blatant bribe at the 2005 election, across the board.

By doing so it left a poisoned chalice for the current government.

New Zealand now directs a higher proportion of tertiary funding to students than any other OECD country. Inevitably, institutions are being squeezed for resources, given the need for fiscal restraint, and are struggling to maintain quality and international competitiveness. With price controls, quality deteriorates.

Next, we are seeing the equivalent of rationing. Victoria University is not accepting any new domestic applications for undergraduate programmes for the remainder of 2010. Because the government is limiting funded places, universities are having to turn away students, and to favour students over age 20 (who have open entry) rather than better qualified school leavers.

These are worrying developments for a country that wants to increase human capital and living standards, and more broadly encourage individual flourishing. The government is hamstrung in dealing with them, however,

given its enormously costly 2008 election commitment to retain interest-free student loans (now costing \$1.3 billion a year).

It is trying to nibble away at the problem around the edges. The 'fees maxima' policy is to be dropped and course fees can be increased by up to 4% next year. The government is also cutting loans for failing students and applying a \$40 annual administrative fee, among other measures.

Other stop-gap measures would be possible. Domestic students excluded by intake restrictions could be allowed to pay full fees provided they meet entry standards, just as international students do.

And while it's good that some thousands of older (65+) people enrol in university courses, it's hard to see why their study should be subsidised by taxpayers.

Two separate aspects of tertiary funding have become confused.

Debate about taxpayer subsidies should be focused on fee policy, not the loans scheme. Research reported by the 2025 Taskforce concluded that the benefits from tertiary education were about three-quarters private and one-quarter public. Current policy assumes that the proportions are the other way round.

Whatever the proportion, fee subsidies are justified by public benefits – benefits that accrue to the wider society rather than students themselves. They will differ across courses – perhaps higher for humanities and lower for dentistry education, for example.

The loans scheme has a different justification. Its rationale is to ensure that students, including students from low-income families, are not denied the opportunity of higher education because of an inability to borrow.

But subsidies for loans are unjustified. They encourage a culture of over-borrowing, indebtedness and slow or non repayment of loans. As the 2025 Taskforce recommended, the terms of loans should be as close to market-based interest rates as possible.

Moreover, fee subsidies and the loans scheme should not be regarded as the sole means of student support. Personal savings, part-time work, vacation employment and parental support all have a role to play.

Fees and loans are connected and the government faces a diabolical problem: simply cutting fee subsidies would lead to more taxpayer-subsidised borrowing.

Policy should recognise that most, though not all, university students come from better-off backgrounds and enjoy higher than average incomes in later life. Excessive taxpayer funding of higher education is a subsidy from poorer to richer people.

As financial realities bite, many governments are lifting fee caps and cutting student funding. David Willetts, universities minister in the new British government, recently stated that the cost of subsidising degrees was a “burden on the taxpayers that has to be tackled”.

The case for doing so in the interests of social equity, sensible decisions by students, sound public finances and economic growth is compelling. Vice-Chancellors and others who care about higher education should be making their voices heard.

In the overall public interest the government could seek an election mandate to make changes, political parties could agree on them among themselves, or a future fiscal and economic crisis like those in Europe could force changes upon us.

It is hard to see other options.

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