THE CONVERSATION

University fees: how to structure a system that benefits poor students

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South African students campaigning for lower university fees during a sit-in protest on the steps of Jameson Hall at the University of Cape Town. Reuters/Mark Wessels

Students across South African universities have embarked on protests against planned fee increases and are also demanding free education. Business and Economy editor Andile Makholwa put questions to Nicholas Barr*, Professor of Public Economics at the London School of Economics and Political Science, about the best ways to fund university education.*

Since the mid-1980s Barr has been involved in the debates about the financing of higher education. In the UK, he argued for many years that tuition fees should be fully covered by income-contingent loans. He and his colleague Iain Crawford have been described as the architects of the 2006 reforms in England. He led the team that designed the student loan system in Hungary and has advised governments in Australia, New Zealand and Chile.

What is the best form of funding university education for a developing country with high inequality levels such as South Africa?

"Free" is just another word for "some other sucker pays". The more unequal a country, the more likely it is that university students are from better-off families. Financing higher education from taxation means that poorer people are paying for richer people to get degrees that will help to keep them richer and thus perpetuate inequalities.

In a good system, university is free for students while they are studying but they then pay part of the cost of their higher education once they have graduated. Thus, a good system would have tuition fees, but initially paid for the student by the student loans administration. Students would repay part of the cost once they start earning.

Thus, what is needed is a good system of student loans, where “good” means a loan designed so as not to deter people from poor backgrounds from going to university. I talk below about how to design such a system.

Why does this matter? It matters for two strategic reasons. Technological advance continues to drive up the demand for skills; thus a large, high-quality university system (alongside its other purposes) is necessary for economic growth.

Also, expansion of higher education is central to increasing social mobility. By assisting expansion, a good system of fees and loans does not pull up the drawbridge – it widens the staircase.

Which countries have successfully implemented systems where students don’t pay fees when they go to university? How have those systems worked?

There are two approaches. Some countries have no tuition fees. In Scandinavia this approach works reasonably well because (a) those countries are rich and (b) their electorate is prepared to pay high taxes. But, in most countries, public finance for universities has failed to keep up with student numbers, creating downward pressure on quality (more below).

Other countries (Australia, New Zealand, the UK) take a different approach. They have tuition fees, but fully covered by a well-designed student loan. Thus students do not pay when they go to university but contribute afterwards.

You’ve suggested that a progressive system needs to start with income-contingent student loans. Could you please explain how this would work?

Loans like mortgages or bank overdrafts have fixed monthly repayments. If a person’s earnings fall, or disappear, he or she cannot afford to make repayments, leading to default, and possible bankruptcy and loss of home. This is clearly a terrible way to organise student loans because most people from poor backgrounds (and many from middle-income backgrounds) would not be prepared to take the risk.

In an income-contingent system, monthly repayments are not a fixed amount, but a fraction of a person’s earnings. As an example, repayments in the UK system are 9% of earnings above GBP21,000 per year.

As Table 1 shows, in this system, student loans are another payroll deduction like income tax or social security contributions:

Table 1 Pay slips, UK 2015-16

	Bill	Tariq	Richard	Jane
Annual earnings	£21,000	£25,000	£30,000	£50,000
Income tax (monthly)	£173	£240	£323	£784
SS contributions (monthly)	£129	£169	£219	£356
Total IT and SS (monthly)	**£302**	**£409**	**£542**	**£1,140**
Loan repayments (monthly)	**£0**	**£30**	**£87.50**	**£217.50**

Loan repayments: own calculations: repayment = 9% of earnings above £21,000 per year

Source: Nicholas Barr October 2015

Low earners make low or no repayments;

Repayments automatically track changes in earnings; and

Loan repayments for all but the highest earners are considerably smaller than the other deductions.

Another highly desirable feature of the UK system is that any loan that has not been repaid after 30 years is forgiven. Thus income-contingent repayments protect graduates with low monthly earnings and forgiveness after 30 years those with low lifetime earnings.

In short, the system is very different from credit card debt: no unaffordable repayments, no default, no bankruptcy.

There is much misinformation (and disinformation) about loans in the UK. For an excellent account of reality see the article here on a leading website masterminded by Martin Lewis, a former student of mine and a leading and passionate campaigner for social justice and for protecting consumers from misbehaviour by banks etc.

In South Africa there have been concerns that “free education” would cause the quality to drop. Has this been the case with other countries that have introduced free education?

The short answer is yes. In the UK in 1960 about 5% of 18-year-olds went to university. With such small numbers it was possible for the taxpayer to finance a high-quality system.

But as student numbers grew (an essential element in widening participation) funding per student fell by nearly half, with consequent ill-effects on quality. With less money per student, class sizes get larger; it becomes harder to see teachers; the cafeteria gets over-crowded; and library resources are stretched.

Tuition fees were introduced explicitly to make it possible both (a) to continue to expand the system while (b) maintaining quality. In the UK today, nearly 45% of 18-30-year-olds now go to university.

You’ve argued that fees that have to be paid upfront are bad because many students cannot afford them. Could you elaborate?

Most students are broke. They cannot afford to pay fees. Both for economic growth and to increase social mobility it is imperative that bright people from all backgrounds can go to university. Thus making people pay fees at the time that they enter university is a dreadful system.

But graduate contributions are very different from upfront fees. Graduates contribute (a) only once they start earning and (b) only if they earn enough.

A truly progressive system would reduce taxpayer subsidies to university students and instead spend the money earlier in the system. The evidence is enormously powerful that what stops people going to university is not fees or loans but not getting good high school grades (including not getting anywhere near to graduating high school).

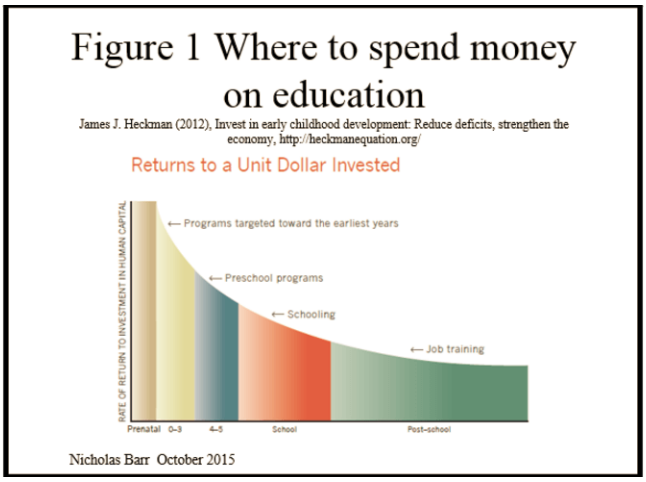

Figure 1 shows that the biggest payoff to public spending is in infancy and during early school years.

As a Labour education minister put it (somewhat losing his temper at a debate with students):

> *If I were a real socialist, I wouldn't spend a penny on higher education. I'd spend it all on nursery education.*

So maybe the next campaign should be to spend more on the under-fives.

Nicholas Barr discusses financing higher education for quality access.

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