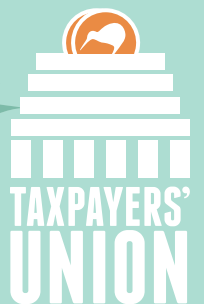


ROBIN HOOD REVERSED

How Free Tertiary Education Robs
Today's Poor for Tomorrow's Rich



SUMMARY

The idea of free tertiary education is politically appealing. People like to vote themselves “free” stuff, and politicians like to claim something is “free” - when in fact they are just shifting costs. But the implementation of such a system in New Zealand would lead to job shortages in crucial areas and poorer quality education, while the country’s poor will be subsidising the future’s rich.

We should strive to ensure that everyone has the opportunity to pursue higher education, but currently the up-front costs of tertiary education are already covered by a generous student loan scheme. Removing fees only serves to transfer any private cost to the taxpayer – most of whom won’t benefit.

The cost of tertiary education is already subsidised by approximately 84 percent. Taxpayers contribute \$4.235 billion per year to higher education. Per household, that’s \$2,456 in tax.

Imposing modest financial costs of obtaining a tertiary qualification helps to discourage individuals from pursuing unsuitable degrees, and aids their ability to identify individual pathways that offer the greatest return for their future. Tertiary fees are an incentive to maximise opportunities that study provides.

Offering three years of higher education disrupts the industry pathways into other jobs that do not currently require a tertiary qualification. The Labour party’s just announced proposal, including the significant cuts to immigration, threaten to reduce the already declining trades and skilled labour work force in New Zealand. With more incentive to pursue a university degree, jobs that do not currently require a tertiary qualification could well become even harder to staff in the future.

Free tertiary education significantly reduces the value students put on the qualifications. A significant influx of students would also result in lower quality education from providers. More bums-on-seat type courses, where quality is low and job prospects even lower, will be encouraged.

On the other hand, if the Government began capping entrance numbers, as is another likely consequence, the number of individuals from lower income households obtaining tertiary qualifications would fall.

Scotland’s zero fees scheme illustrates the unfair financial advantage that the wealthy have over those with lower incomes in pursuing higher education, and in setting up their opportunities for higher future incomes. Its zero fees scheme sees it having

fewer disadvantaged students accepted into tertiary education than England.

Currently, tertiary students are required to pay back some of the cost of their higher education. This is fair, as tertiary qualifications give them private privileges, including the opportunity to earn 43 percent more on average than those without a degree within five years.

Labour’s tertiary education policy sees the poor subsidising the rich, reaching into the pockets of the disadvantaged and lining the wallets of the future’s wealthy.

“Imposing modest financial costs of obtaining a tertiary qualification helps to discourage individuals from pursuing unsuitable degrees”

INTRODUCTION

With the General Election less than a month away, and the government's books in good shape, political parties from across the political spectrum are offering expensive election bribes.

As expected, new Labour Party leader Jacinda Ardern announced that if elected to power on 23 September, Labour will deliver three years of free tertiary education, being phased in from 2018. Along with the promise to increase student allowances, Labour's policy will cost \$610 million per year from 2018-2024, and \$1.47 billion per year from 2024, when it is fully implemented. That's the equivalent to \$852.57 per New Zealand household in additional taxes to fund student's ambitions.

Any perception that central government currently forgets students is misguided. As of 2010, the government subsidises approximately 84 percent of the cost of tertiary education. It spends \$4.235 billion of taxpayers' money per annum on tertiary education. Per household, this amounts to \$2,456 in taxes per year.

The spend is made up of \$2.463 billion in tuition (\$1,428 per household), \$486 million in student allowances (\$282 per household), \$799 million in student loans (\$463 per

household), and \$487 million on other tertiary related areas (\$282 per household). In 2016, 732,000 people had a student loan, making up a nominal value of \$15.3 billion. No interest is charged on student loans for people living in New Zealand nor are balances adjusted for inflation.

This paper identifies the key impacts of a "free" (i.e. taxpayer-funded) tertiary education policy in New Zealand.

In short, the economic rationale for such a policy is weak, with the political rationale much stronger. Helen Clark won the election in 2005 on the promise of the interest free student loan policy described above.

First, we show that shifting the cost of tertiary education from (partly) user pays, to 100 percent taxpayer subsidised, would be regressive. Current middle and low-income earners would effectively subsidise the future's wealthy.

Second, we explain why a zero fees policy would result in students undertaking pathways they are not suited for, resulting in even further shortages in trades and other skilled labour.

Thirdly, we argue that there is no real need for a zero fees policy, because the current system provides a way to meet the upfront costs of tertiary

education, whilst also assisting those from disadvantaged backgrounds. In fact, international evidence shows that free tertiary education is regressive because it may reduce the number of students that obtain a tertiary education from low-income backgrounds, reducing social mobility and entrenching income inequality.

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SECTION 1: THE POOR SUBSIDING THE RICH

There is no such thing as ‘free’ tertiary education. Only politicians and special interest groups (Labour-affiliated student unions, for example) claim otherwise. The key distinction is not what tertiary education costs, but rather who bears the burden of that cost. Providing ‘free’ tertiary education to those who reap its rewards only means that someone else must pay for it. Under a zero fees policy, this will be the taxpayer.

Fully taxpayer-funded tertiary education would see the least well-off subsidise people who will go on to earn comparatively higher incomes.

**On average,
university
graduates
go on to earn
significantly
higher incomes
than non-
graduates.**

Five years after finishing study, the median earnings of those with a bachelor’s degree are 43 percent higher than those with just an NCEA Level 1-3 certificate.

While Labour’s tertiary education policy extends zero fees to training outside of universities, it would be irrational for an individual not to take advantage of three years’ free money for something as valuable as a university degree.

Median annual earnings are \$64,600 for bachelor’s degree graduates ten years after completing a qualification. This is compared to \$45,000 for those with only NCEA Level 1-4 certificates (also ten years after leaving study). Graduates who complete a postgraduate qualification have median earnings ranging between \$73,000 and \$76,200, depending on the type of qualification. Doctoral graduates have much higher median earnings of \$88,400.¹

Tertiary education, therefore, provides a private benefit to the individual in the form of much higher earnings.

The argument often put forward by advocates of zero tertiary

fees is that there are societal benefits from having a larger proportion of the population with a tertiary education. This is true, but not usually to the extent claimed by advocates. To justify fully taxpayer-funded tertiary education, the benefits would need to entirely accrue to society, and not at all to individuals. This is not the case, as is shown by the earnings disparity above.

It is hard to argue that society receives more than 84 percent of the return - equivalent to the current rate of subsidisation - on tertiary education. In fact, if there were a case to be made to fundamentally overhaul the existing funding structure, then the evidence would lend itself to a higher fees and user pays system - the opposite of the Labour Party’s policy. At the very least, New Zealand should retain the status quo and refrain from further socialisation of the cost of tertiary study.

Prices play the key role in determining what society (as an aggregation of individual choices) value most. Wages are no different. Higher wages go to occupations that are more highly valued. When the government intervenes in this

¹ http://www.educationcounts.govt.nz/__data/assets/pdf_file/0004/181777/Young-graduate-outcomes-earnings-factsheet-June-2017.pdf

market process, they skew the costs and returns. Individuals are the single largest beneficiaries of higher education, so the incentives are already there.

This is the argument we often put forward against corporate welfare. The public, through their taxes, should not be coerced into paying for an activity that ultimately yields private returns.

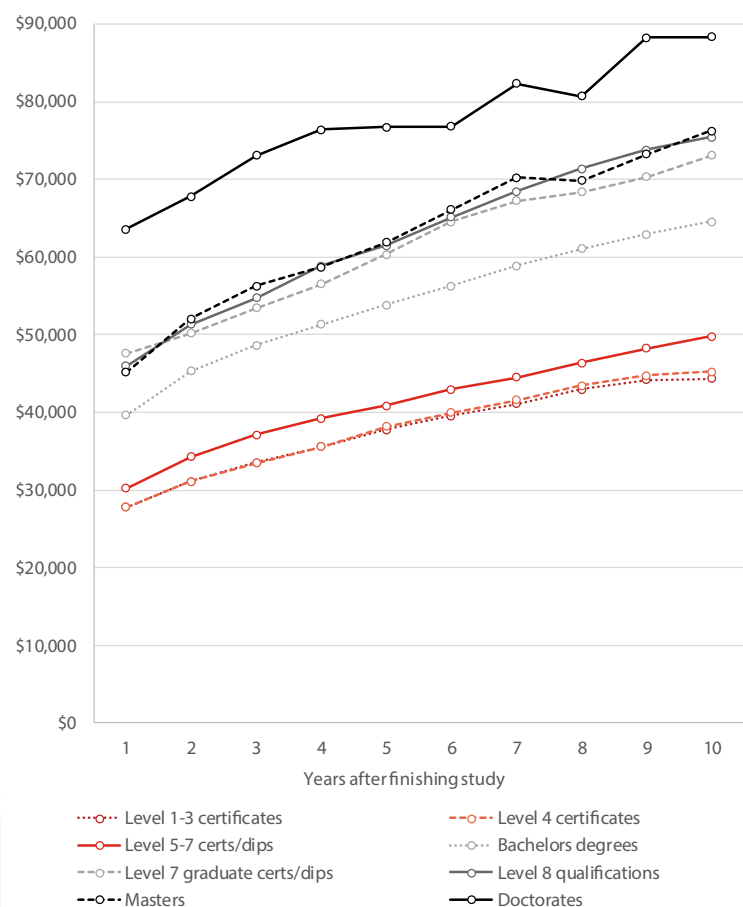
The bulk of the government's tax take is from those earning less than \$90,000.

Since zero tertiary fees would be funded from consolidated taxpayer funds, and not targeted rates on higher earners, there is a cross-subsidisation where, unlike almost any other government subsidy, it is the poor subsidising the rich. Economists call these sorts of policies regressive.

The current tax system, along with the welfare state,

results in high-income earners contributing higher taxes, and receiving fewer social services. The reverse is true for low-income earners. Instituting a zero fees policy would contradict the broad economic consensus (both domestically and globally) for progressive economic policies.

It is odd, therefore, that the push for free tertiary education has come from the centre-left Labour Party, and the sometimes hard-left Green Party. Zero tertiary fees will punish low-income earners and allow high-income earners to increase and entrench their existing prosperity.



Source: Statistics New Zealand, Integrated Data Infrastructure, Ministry of Education interpretation. Note that earnings are annual, gross and in 2015 dollars.

SECTION 2: FEWER TRADESPEOPLE, MORE FREE RIDERS

Requiring individuals to pay for their own tertiary qualifications discourages people from undertaking an education pathway they are not suited for.

Bearing some degree of the cost encourages students to pursue qualifications that provide them with the highest expected return on their investment over their lifetime.

Prices reflect the value society attributes to given occupations, therefore when individuals maximise their own lifetime earnings, they also maximise their contribution to society.

People are more likely to care about the value for money of something they are paying for. Where an individual bears no, or very little cost for tertiary education, the price signal is weakened. The inefficient choices that will result from this policy may do more harm than good to economic growth.

As stated in the previous section, while Labour's policy also applies to polytechnics and other training centres, it would be irrational for an individual not to take advantage of three years' free money for something as valuable as a university degree, even if they would otherwise be best suited to some other field.

When there is no cost to the user, it is harder to establish a distinction between who is, and who isn't, suitable for higher education (i.e. those who would generate the highest earnings

from their tertiary qualification).

Distorting this occupational decision process, by reducing the cost of some occupations over others, distorts the allocative efficiency of the labour market.

A zero fees policy will disrupt pathways into jobs where higher education is not required, and will further dry up New Zealand's drought of people in trades and other occupations that do not require tertiary study. Labour's policy would be detrimental to the construction industry for example, particularly if coupled

SECTION 3: AFFORDABILITY ALREADY SOLVED BY GENEROUS LOAN SCHEME

Tertiary education has an upfront cost, with the benefit coming later. The issue is timing, not the ability to pay. This is known as the 'liquidity' barrier.

The current education funding system supports the liquidity constraints of students by providing a loan to cover most of the upfront costs of education, while heavily subsidising the rest of it. There is a case to be made that the government could ease this liquidity constraint further, by increasing the living costs available to students, which they must ultimately repay.

But the removal of tuition fees will not solve liquidity constraints.

Zero tertiary fees removes the long-term cost of education, but does not address the short term cost, which is the more pressing concern. This paper has already established that the long term costs are not an issue as tertiary educated individuals earn much higher returns in the labour market and have the ability to pay back accrued debt over their working life. Zero fees will

not address the short-term or immediate costs associated with study.

Furthermore, the current system provides support for those who come from less wealthy backgrounds by offering a non-repayable student allowance. Those academically able, but from disadvantaged backgrounds should not be prevented from attending university by the upfront cost of tuition. Their future higher earnings will more than cover this initial expense.

We accept that there are considerable problems with the current student allowance framework. The targeting is poor, with many families able to use family trusts to income split, reducing the parental income to a level where the university aged children become eligible for the student allowance. This is an argument for better targeting of the student allowance – such as assessing all family income – not an argument for zero fees.



SECTION 4: LOWER QUALITY TERTIARY SYSTEM AND FEWER ENTRANTS



Providing three years of zero fees tertiary education will eventually force the government to reconsider the number of placements in New Zealand universities. The policy will impose large fiscal pressure on the Crown's finances for two reasons. Firstly, increasing the subsidisation of current students will have a large cost. Secondly, lower fees will incentivise larger tertiary enrolment, increasing total costs.

The government may be able to ease this second constraint by capping the number of students. But this would undermine the intent of the entire policy - to increase tertiary education attainment. If numbers are capped then it will likely be by secondary education results. Currently, students from lower socioeconomic backgrounds achieve poorer results, and would therefore be the most likely to not be accepted into university.

Under the current system, with a relatively relaxed acceptance threshold, the individual is able to choose to pursue further education, and they bear some of the cost. When individuals bear the cost, they are free to make their own choices.

Alternatively, if future governments do not cap student numbers, then the cost to taxpayers will be enormous - and the quality of education is likely to deteriorate.

New Zealanders with lower incomes are currently given the opportunity to pursue a course of study without the burden of finding the funds to cover upfront costs. The Studylink scheme gives everyone the equal opportunity to better their education. Labour's new policy threatens this by increasing the likelihood that future governments will need to further restrict the number of students accepted into universities. This will mean only those with the top grades at secondary school, statistically from more advantaged backgrounds, are the ones more likely to pursue higher education.

The comparison between England and Scotland shows how a zero fees policy impacts those least advantaged. In England, tuition fees are capped at £9,000 (equivalent to \$15,891 NZD). Scotland has zero tertiary fees.

In Scotland, there are 3.5 advantaged students (from households in the top quintile of income earners) for every one disadvantaged student (from the

bottom quintile). In England, the advantaged to disadvantaged ratio is 2.4 to one. This suggests that having a zero fees policy is regressive in effect - despite being marketed as progressive by centre-left politicians.

There is a double-edged sword to a zero tertiary fees policy. Firstly, as established in section one, low-income taxpayers inevitably subsidise high-income earners, with funding coming from consolidated taxpayer funds. Secondly, as seen in Scotland, students from low socioeconomic groups are the first to be shut out of the education system, effectively entrenching their social status. Once again, this contradicts the political claims ideology of those who advocate such a policy.

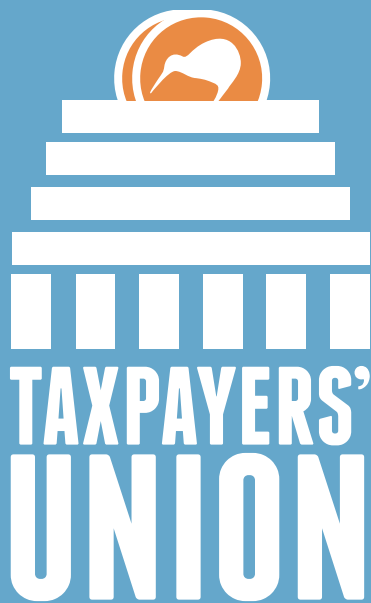
The result of a zero fees policy, would likely be a hampering of social mobility, and entrenched income inequality.

CONCLUSION

Public policies should be assessed against likely results, not intentions. Costs must be weighed against benefits. Offering zero fee university schemes is likely to result in:

1. low and middle-income earners subsidising tomorrow's rich;
2. job shortages in crucial skills-based areas;
3. lower quality tertiary education;
4. less access to education for disadvantaged students.
5. a hampering of social mobility and entrenched income inequality.





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