

Submission

to

Senate Employment, Workplace Relations and Education
References Committee

Inquiry into student income support

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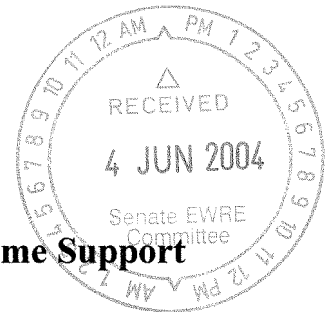
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Submission to Senate Committee Inquiry into Student Income Support

This submission considers a range of possible funding options for student income support. The submission considers the following options:

- (i) Self funding
- (ii) Family funding
- (iii) Commercial loan arrangements
- (iv) Income contingent loans
- (v) University funding
- (vi) Government funding

In some options developments in capital markets that may be needed are also discussed.

(i) Self Funding

Under this option individuals would be responsible for their own income support. Given wealth constraints it is unlikely that individuals could earn sufficient returns from investment of available funds. As such one would expect to observe greater part-time labour market participation of full-time students and the available statistics (see *inter alia* McInnis and Hartley (2002)) are consistent with this view. Government can impact the value of these earnings through the treatment under the tax and welfare system and this issue is taken up in the section on government funding.

A discussion of the self funding option is typically constrained by the stereotype of who is a student. The stereotypical student is a school leaver who moves straight from secondary school to university and as such has only had limited participation in the full time labour market. In a world where lifelong learning is becoming more important it is reasonable to expect a greater number of students will participate in the full-time labour market and then return to study. These type of students are often not explicitly considered in the student income support debate because it is implicitly assumed that they will remain working full-time and study part-time in either a campus or workforce delivery mode. However addressing student income support in a comprehensive manner also requires consideration of how to handle those who return to full-time study between episodes of full-time employment.

There is nothing to prevent individuals utilising regular investment vehicles (managed funds, unit trusts) to save while in full-time employment to create a provision for income support on a return to full-time study. However it is reasonable to conjecture that existing superannuation contributions and the costs of involvement in housing markets (both owner occupied and rental) limit the amount of funds available for such investment. As such there is a possible role for government in providing incentives and leverage. These could be in the form of concessional tax treatment and government co-payment linked to investment contributions. These co-payment options are already utilized in a superannuation context.

(ii) Family Funding

Under this option families would be responsible for providing income support. The typical and stylized example here is parents providing income support to their school leaver children on entry to university. This would typically be facilitated by parents making medium term investments (15 – 20 years) in the early childhood years and these investments providing an income stream to the student. This type of investment is well covered in existing capital markets through products tied specifically to education (for example see the range of products offered by the Australian Scholarships Group on their website, <http://www.asg.com.au>) or in more vanilla products (managed funds, unit trusts). There is again a possible role for government in concessional tax treatment and exploration of co-payment options.

(iii) Commercial Loan Arrangements

Under this option individuals would borrow from commercial providers to fund income support. In a conceptual sense it is possible to outline such a model, however there are numerous practical challenges. These include:

- (a) merit / public good arguments that would support subsidies to interest rates charged.
- (b) lack of fixed / tangible assets to be used to provide security over the loans.
- (c) equity arguments that credit providers would probably screen out certain low status groups from participation in these markets.
- (d) lack of benefit arguments, in that some groups of graduates may not obtain significantly higher salaries post-graduation to be used for loan repayment.

These issues and others are discussed in greater detail in Chapman (2003). However, there is a private version of the HECS style arrangements in the US running through My Rich Uncle (<http://myrichuncle.com>) where students take out educational investments (effectively income contingent loans) that are repaid as a percentage of future earnings for a fixed period of time.

(iv) Income Contingent Loans

In the context of student fees HECS has proven to be a system that overcomes many of the problems associated with commercial loan arrangements. The HECS system has been extensively evaluated and discussed and for a flavour of this discussion see *inter alia* Chapman (1997, 2003), Chapman and Ryan (2002). Existing government policy appears to be based on the premise that HECS type arrangements overcome the majority of access and equity problems associated with higher education. As such one could argue for extending HECS style arrangements to student income support provision. Chapman (2002) has made this argument and has also supported the extension of HECS style arrangements to a wider set of contexts including drought relief (see Chapman, Botterill and Egan (2004)).

A possible concern in this regard is the debt level of students and any associated debt aversion behaviour. Previous work has raised issues around the possible impact of student debt levels on participation in other capital markets, (see *inter alia* Brooks (2003)). Possible options in this regard could include building greater debt relief options into HECS style arrangements.

A possible means of providing debt relief is to use it to provide incentives for certain types of further study or employment. Concerns around ability to recruit future teachers and nurses have led to their HECS levels being set lower than other disciplines. Incentives could also be provided by retiring HECS debt for each year of employment in teaching or nursing post-graduation. Similar arrangements could apply to those who undertake postgraduate research study (Masters by research, PhD) with some HECS debt relief on successful completion. These types of arrangements might go some way towards addressing debt aversion issues. It is worth noting that the My Rich Uncle educational investments do contain debt relief in that they only require repayment for a fixed period of time. This feature could possibly be considered if HECS style arrangements were to be extended to the provision of student income support.

(v) University Funding

A possible way to provide student income support would be through the universities. One could argue that as universities are close to their individual students they may be well placed to tailor appropriate student income support. A key challenge would be around how universities could access the funds to provide this support. There are two possible options in this regard. One would be via an increase in operating grants. This would allow for both scholarships (no need to be repaid) and income contingent loans (which could be repaid through HECS style arrangements). However in the current government funding environment increases in operating grants are unlikely.

The other option would be to allow the universities to raise funds either from philanthropic sources (government could provide additional tax concessions) or bonds. The philanthropic source could be used to fund scholarships while the bonds could be used to fund income contingent loans repaid on a HECS style basis. The use of bond issues would raise a number of challenges. First it might produce more diversity in the university sector. While the government sought to encourage diversity in the Crossroads process, it is not clear that this would represent the type of diversity intended. Second, there may be issues around the enabling acts of certain universities that may constrain their ability to undertake this activity.

The final set of issues relate to bond markets and rating assignments. The Commonwealth Treasury (2002) released a discussion paper on the issues and possible options around the significant reduction in the government debt market. The majority of submissions to this inquiry (for details of the submissions see <http://www.debtreview.treasury.gov.au/public-sub.asp>) argued that the government should maintain a Commonwealth bond market on the public good basis that this

provides a risk free asset that underlies and assists the pricing of risky assets in Australian capital markets. In their submission Diggle, Brooks and Tucker (2002) argued for a possible alternative of a wider set of state government and semi-government issues which were credit wrapped by the Commonwealth. Brooks, Diggle and Stewart (2003) argue for a similar arrangement to be explored around local government infrastructure bonds. A set of university bond issues with credit wrapping would be another possibility. As regards credit ratings for individual Australian universities these have been recently introduced by Standard and Poor's who see the potential for a larger market in this regard.

(vi) Government Funding

The provision of government funding can be made from a variety of sources. The most immediate is direct income support provided to students through the social welfare system. There will be some arguments as regards the levels of these payments.

Beyond direct income support the government is also able to influence the level of student income support through the operation of the tax and social welfare system. The areas of interest are:

- Appropriate treatment of other income (labour market, scholarships) under the tax / social welfare system.
- Tax concessions to philanthropy and investment vehicles being used to provide student income support.

Summary and Conclusions

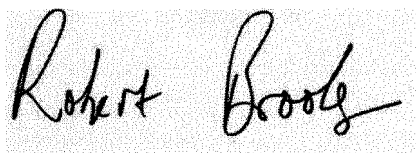
This submission has covered a number of issues relating to the provision of student income support. It would seem that comprehensive provision of student income support needs the following elements:

- Direct payments to students at appropriate levels through the social welfare system.
- Concessional treatment of other income earned by students under both the tax and social welfare systems. This other income needs to include both scholarships and that which is derived from part-time participation in the labour market.
- Concessional tax treatment of investment vehicles used by individuals and families to provide for student income support in the future. For certain groups this could also extend to co-payment options similar to those used in the superannuation area.
- Concessional tax treatment of philanthropic donations to provide student income support.

- Wider availability of HECS style income contingent loans for student income support.
- Appropriate debt retirement options built into HECS and other income contingent loan schemes.
- Greater provision of support from universities through increases in operating grants and / or capital raising (both philanthropic and bonds).

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Note: The views in this submission represent the personal opinion of the author and should not be taken to represent the views of RMIT and RMIT Business.