The Australian

Don't just throw cash at universities

- **by: Henry Ergas**
- From: **The Australian**
- January 04, 2012 12:00AM

THE report of the Higher Education Base Funding Review has important things to say: things every university student now basking at the beach should know. And it contains many sensible recommendations. But it concentrates too heavily on increasing funding rather than on incentives for resources to be used efficiently. As a result, its approach cannot durably resolve our universities' problems.

The review provides a sobering assessment of those problems. Such comparisons are fraught but, per student, Australian universities receive less than half the total funding of their US counterparts. As for government outlays, the publicly funded University of Michigan, ranked 18th in the Times Higher Education World University Rankings, receives nearly twice as much government funding per student as Melbourne, which, at 37th place, is our most highly ranked university.

Little wonder Michigan's student-to-staff ratio is half that of Australia's universities.

Nor do the contrasts end with funding. Teaching quality is difficult to measure, but surveys find Australian students' satisfaction with the teaching they receive is well below that of students in Britain.

And while 65 per cent of American students say they get timely performance feedback from staff and 50 per cent discuss their grades with their teachers, the proportions for Australia are barely 40 and 20 per cent, respectively.

These indicators suggest our publicly funded universities, which have a de facto monopoly over higher education, are unable to provide it efficiently. That failure is a serious distortion preventing our economy and society from performing as well as they should, and hence ought to be of vital concern.

The review argues the solution lies in greater funding, finding, for example, that "base funding for medicine, dentistry, veterinary science and agriculture should be increased by as much as 25 per cent". The key issue is how those increases should be financed, in terms of the balance between fees and government subsidies.

Setting this balance, the report rightly argues, is not a matter of equity. Although Australian students' contributions to universities' costs are relatively high in international terms, most students still earn high lifetime returns on their investment. And our income-contingent loans, which defer undergraduates' fees until their earnings exceed a threshold, ensure fees are not an obstacle to participation.

In theory, fees could therefore be put on a user-pays basis. However, the report argues fees should be set at 40 per cent of tuition costs, with government contributing the remainder. It also recommends the 60:40 ratio apply to all fields, unlike the present situation, where government's share varies from 16 per cent in law and accounting to 81 per cent in science.

Those recommendations are based on two claims. The first is that the 60:40 split reflects the balance between the lifetime returns from higher education to the individual student and the wider benefits to society as a whole. This is based on how much additional tax society collects from graduates, and the share of that attributable to a university education. This amount turns out to be reasonably close to 60 per cent of average tuition costs. The second claim, justifying the split's uniform application, is that "there is no evidence that public benefits differ across disciplines".

However, the tax take, on which the review's analysis relies, is a poor basis for setting subsidy rates. After all, we tax returns on utes, shares and super; that doesn't mean they should be subsidised. Rather, the question is whether higher education is taxed more heavily than other investments; if so, there is an efficiency case for offsetting that burden. But the review pays no attention to this issue.

Even more important, the tax take at best measures society's benefit on average from graduates. But it is not the average benefit that matters.

Rather, it is society's gain from increasing the number of graduates, beyond those who would study anyway. The first basket-weaving graduate may yield large social gains; the 100,000th is unlikely to. And while the first is likely to be well-qualified and motivated, the review's data suggests the 100,000th will have low admission scores, with substantial costs to educate and a high chance of dropping out. If even without subsidies society will be awash with basket-weavers, taxpayer subsidies will do more harm than good.

Indeed, the review argues that because of income-contingent loans, student fees have little impact on enrolments. But if that is true student numbers, and public benefits, will be the same regardless of the government contribution, so there is no efficiency case for a taxpayer subsidy.

The review's 60:40 split therefore lacks a strong basis. But even if that split were accepted, it would be rash to simply promise the universities 60 per cent of whatever their costs per student proved to be. That would invite gouging by the tertiary unions, while those most ruthless of rent-seekers, the vice-chancellors, would soon acquire even larger yachts.

A better approach would have two components. First, the subsidy would be determined as a fixed-dollar amount payable to any accredited institution, public or private. Second, universities would, over time, be allowed to set their own fees. Students would therefore pay any surcharge a university imposed above the standard rate: if that reflected higher quality, they might accept it; if not, they would take their voucher elsewhere. Thus, better universities would secure higher incomes.

This assumes our universities operate in a reasonably competitive market and have incentives to act efficiently. The review dismisses that assumption and, as matters stand, it may be right to do so. But its analysis in this respect is extremely slight and it says nothing about how the situation could be improved. Rather, it takes that situation as given and pins its faith entirely on central controls to ensure good use is made of added funding, without any explanation of why they would work better in future than they have in the past.

That risks repeating the error this government has made in so many parts of the public sector: throwing money at problems without addressing underlying issues of governance.

So long as the dollars flow, spending without reform can work; when they dry up, as they eventually must, all the difficulties resurface.

The review's recommendations are therefore only a first step. They need to be accompanied by changes that expose universities to the disciplines and freedoms, the rewards and constraints, of a truly competitive market. Until that happens, greater funding will merely paper over the cracks.