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Prof Nicholas

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With university tuition fees set to rise to up to £9,000 a year from 2012, Nicholas Barr (right), a London School of Economics professor, who brought the current Income Contingent Repayment system to the UK, says governments have done a disastrous job of explaining true costs.



One of the worst features of the debate about paying for universities is that all governments have been woeful beyond belief in explaining how the system of student loans work.

Key Points

- Student fees NOT like credit card debt
- They're simply a payroll deduction
- Deductions lower than tax or NI

They have let the word 'debt' escape, and run round like a rabid ferret. So people think of student loan debts like credit card debts. They are not.

They are a payroll deduction, like income tax and national insurance, but smaller than either. A better way of thinking of the system is as a form of graduate tax, but one that does not last forever.

Before explaining, it's a good idea to answer the 'so what' question, ie, why is going to university a good idea?

So why should I go to university?

The argument the Government gives for going to university is graduates generally earn more than non-graduates.

That is true, but it is only part of the story. When I meet my ex-students they are not all making shed-loads of money (though some are). But what stands out is most of them really enjoy their work.

Because people are living longer they will have to work longer – so you will be working for a long time.

So it's enormously important to have a job where you don't wake up on a Monday morning with a sinking feeling in the pit of your stomach.

Having a degree does not guarantee that – and of course many people without a degree also enjoy their work. But having a degree increases your chances of having a job that pays well and which you enjoy.

I may owe £40,000 when I'm done. Isn't that scary?

If you put it that way, yes. But that is not the way to put it.

Here are the key points:

1. The Government has been a total waste of space in publicising that loans have income-contingent repayments (for students starting in 2012 and after, repayments will be 9% of earnings above £21,000). If you earn £25,000 (about the national average) your repayment will be 9% of £4,000 = £360 per year, or £30 per month.

This year, someone earning £25,000 pays £292 in income tax per month and £177 in national insurance contributions. So loan repayments are like income tax in that low earners make low or no repayments, they are automatically related to the size of your pay packet, but are much smaller than income tax.

The only differences are the tax is paid only by people who have been to university and does not last forever (if you start university in 2012 or later, anything a person has not repaid after 30 years is forgiven). The table shows how this loan system would look under the new system.

Student loan repayments post-2012

ANNUAL EARNINGS	£21,000	£25,000	£3
Tax (monthly)	£225	£292	£3
NI (monthly)	£137	£177	£2
Loan repayments (monthly)	£0	£30	£8
Assumes current tax and NI regime remains the same			



- Thinking of student debt like credit card debt is filing it in the wrong bit of your brain. Repayments are like a capped graduate tax, so the right place to file it is as a payroll deduction like income tax and national insurance.
- Though £40,000 is large, it needs to be seen in proportion. If you think that owing £40,000 is scary, the really bad news is that over a full career, in cash terms, a typical graduate will pay the Government over a million pounds in income tax and national insurance. Any number can be made scary by adding it up over many years; think how much you will spend on food over the next 50 years.

If I want to buy something on credit after my degree, will my student loan be taken into account?

Yes, but that won't be a problem. Lenders (mortgage, car, etc) are normally interested in your take-home pay, net of deductions like income tax, national insurance and loan repayments. The latter will reduce your borrowing capacity, but not by much since your monthly repayments are a relatively small fraction of earnings.

Remember that your income will generally be higher because you have a degree and lenders regard graduates as good risks. So a person's borrowing capacity will generally be higher with a degree than without.

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