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## Graduates don't try to dodge HECS

Bernard Lane  
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SURPRISINGLY few graduates massage their incomes to defer HECS repayments, according to a study involving Bruce Chapman, the architect of the income-contingent loan system.

Only 9 per cent of those with a HECS debt adjusted their incomes in this way even though the repayment threshold represents an effective marginal tax rate as high as 19,300 per cent.

Their deferral of repayments cost the budget about \$1.5 million, less than 1/300th of the amount collected via HECS every year.

The study could help Britain in its attempt to adapt Australia's innovative use of the tax system, Professor Chapman and his Australian National University colleague Andrew Leigh suggested in a discussion paper.

In September Britain is to put into practice a reformed system of income-contingent student loans. "A critical issue in the design of such programs is the repayment structure," they said.

There were two designs: a repayment threshold at a low income level with repayments based only on earnings above the threshold, or a higher income threshold with repayments based on a percentage of total earnings.

The second system, pioneered by HECS, spared low-income earners and ensured reasonably quick repayment.

But there had been fears that the HECS repayment design, creating what the authors believe may be the highest effective marginal tax rate in the world, would lead to graduates engaging in avoidance, and thereby deprive the Government of tax revenue and HECS repayments.

In 2003-04 a graduate earning just on the repayment threshold of \$25,348 had \$760 less disposable income than a graduate earning \$1 per year under the threshold.

"[But this] extremely high marginal tax rate seems to have a surprisingly small impact on behaviour," Professor Chapman and Dr Leigh said.

They said their study pointed to a better system for Britain than the options being debated at present.

A parliamentary committee had urged that the repayment threshold be lifted to match average weekly earnings but the Government had protested this would increase the overall cost of the loans and the time over which they would be repaid.

"Neither side appeared to acknowledge a third option, that the threshold could be raised to average earnings, but with repayments based on total income [rather than income above the threshold, as in the current system]," Professor Chapman and Dr Leigh said.

"Our results from Australia, upon which the UK income-contingent loans scheme has been modelled, suggests that such a reform in the UK might strike a better balance between equity and efficiency."

The Chapman-Leigh study assumed that graduates would defer repayments for only one year and analysed data from a random sample of 15,000 taxpayers, divided into those with and without a HECS debt.

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