Public versus Private University Systems

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In the higher education world today, private versus public is a moot distinction. It is certainly very hard to find a purely public or purely private university. According to the OECD's glossary, an institution is classified as public if it is controlled and managed directly by a public education authority, or by a governing body most of whose members are appointed by a public authority. Conversely, a private institution is one that is controlled by a non-governmental organization, or if its governing board consists mostly of members not selected by a government agency (OECD 2003, 441-442). Such a definition is very close to the heart of the matter regarding institutional comparisons of university systems, i.e. who makes the critical decisions regarding the operations of a university: Is it the center, e.g., a bureaucrat in the Ministry of Education? Or is it the university senate and, why not, the student-user of university services?

Table 1 lists what I believe to be the most critical decisions a university has to make in order to function and excel. In a public university system, as it is typical in continental Europe, all critical decisions are ultimately made by the center. The amount of resources available each year to the university is a line in the state budget – usually what it was last year adjusted for inflation. Universities cannot raise additional resources by charging even moderate fees. The Minister of Education has to approve the appointment of professors, who are civil servants paid on public sector pay scales regardless of their performance. The university does not have a say on how many students it admits, nor does it select the candidates. And of course the students may end up studying subjects they are least interested in, provided they have a place in a numerus clausus system. Such an institutional polar case of a public university system is found in Greece where, by explicit constitutional provision, all universities are public, private universities are prohibited, tuition is zero, professors are civil servants and cannot be dismissed (Psacharopoulos 2003).

By contrast, in a private university system, the size of an institution's budget largely depends on its own efforts and quality of services offered. Students react with their feet regarding the tuition charged by a given institution, crowding centers of excellence and penalizing mediocre institutions. If not rendering what students want, private universities close down, whereas public universities carry on never closing. Private universities can attract star professors by offering market salaries well above civil service pay scales. Most important, private universities have a say on their admission policy, and students can choose what subject to study in what university.

Figure 1 illustrates in another way the essential difference between public and private university systems. In a public system, the financier and the producer overlap, keeping the user (student) out of

Table 1

Critical decisions pertaining to universities, and decision makers in public and private university systems

Decision	Main decision maker in a	
	public univ. system	private univ. system
University budget level	State	University, students
University budget allocation	State	University
Tuition fees	State	University, students
Hiring professors	State	University
Professorial pay	State	University
Professorial promotion and tenure	State	University
Admissions policy	State	University
University entry choice	State	Students

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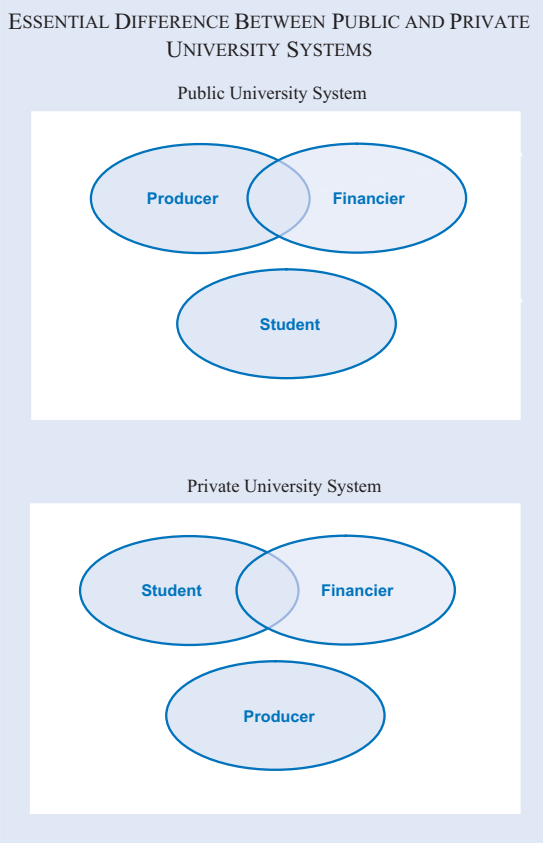
Figure 1



the loop. Such separation of user control over what is produced has detrimental incentive effects on the quality of public universities. At least there is wide agreement today that the public sector is not the best for producing services offered more efficiently by the private sector. By contrast, in a private system the student has control over the services offered by virtue of directly financing the university by the tuition, and thus being able to choose among different producers.

Where between the two polar cases?

Notwithstanding the classification difficulties expressed above, the world today is divided in four distinct clusters regarding the degree of privatization of universities:

- Continental Europe: mostly public university systems
- The UK, Ireland and Spain: outliers in Europe regarding private systems
- Australia and Japan: leaders in privatization
- North America: United States mostly privatized

Table 2 (col. 2) presents evidence for this division based on the private share of the GDP devoted to tertiary education. This information is matched to the number of universities listed in the World Top 100 (Table 2, col. 3). The criteria for the academic ranking of universities are mainly based on a combination of the number of alumni and staff winning Nobel prizes, and publications and citations in 21 broad subjects, all adjusted for the size of the institution (Liu 2004). The leader in privatization (US) accounts for more than half of the top 100 universities. The first time a continental EU-15 country appears in the list is the Netherlands (Utrecht) at rank 39, followed by Germany (Munich Technical) at rank 49.

Until the middle of the last century, Europe was the center of excellence in global learning. But in the last 50 years the trend has been reversed, at least as judged by the number of Nobel prizes won on the two sides of the Atlantic (Psacharopoulos 1999). Although it is very difficult to establish a cause-effect, the prima facie evidence points to a clear correlation between privatization of tertiary education and academic excellence.

Even in the UK, where tuition fees are the highest in Europe, universities struggle to retain the best staff and continue to fall further behind their American counterparts (The Economist, October 4, 2004, quoting the Vice-chancellor of London University).

Table 2

Private resources to tertiary education and number of universities in the World Top 100

Country	Private share of GDP to tertiary education (%)	Number of universities in Top 100
(1)	(2)	(3)
Austria	0.0	1
Denmark	0.0	1
Finland	0.0	1
Greece	0.0	0
Norway	0.0	1
Belgium	7.7	0
France	9.1	4
Portugal	9.1	0
Germany	10.0	7
Italy	11.1	1
Sweden	11.8	4
Netherlands	16.7	2
Ireland	20.0	2
Spain	25.0	0
UK	30.0	11
Australia	43.8	2
Japan	54.5	5
Canada	38.5	4
USA	66.7	51

Source: Col. (2) based on OECD (2003), p. 208; Col. (3) based on Liu (2004).

Why public systems dominate

If a dose of privatization helps academic performance, why are most university systems in today's world (and not only continental Europe) public? There are four popular technocratic arguments in favor of tertiary education being public, based on equity and market failure. But having recently served a stint in politics, my favorite key phrase in this respect is "cherchez les votes".

Equity

If good universities were private, the poor would be excluded because they could not afford the tuition. This is one of the biggest popular fallacies ever. It has been fully documented in all countries that have cost-benefit incidence studies, (i.e. who really pays and who really benefits from higher education) that public financing is regressive (Castro-Leal, Dayton and Mehra 1999; Tsakloglou and Antoninis 1999). Even in a "free" higher education system it is the poorer segments of the population who finance (through general taxation) the university studies of the rich (Blondal, Field and Girouard 2002). And even where higher education is proclaimed to be "free", the incidental costs of attending university can amount to 20 percent of family income among farmers and manual workers. This is in contrast to the nearly 10 percent of such expenditure among families in the top quintile (Psacharopoulos and Papakonstantinou 2005).

Those who attend higher education come without exception from the wealthier segments of any society. After they obtain their degree, they will have a considerable earnings advantage over those who did not attend higher education. Actually, the more privatized the higher education system, the higher the earnings advantage of the graduates and the private returns they realize on their investment (Table 3, col. 3). Zero tuition for all, irrespective of family income, goes against the grain of the equity it is supposed to serve. Charging selective tuition, in direct proportion to family income would, paradoxically, be more equitable.

Capital market imperfections

What if the poor wanted to borrow the necessary funds to reap the benefits reported in Table 3, but they cannot because human capital does not have collateral? This is not a real argument against private universities as student loans do exist in several countries (DICE 2004b), and several new funding schemes have been developed in theory and practice, such as individual learning accounts (DICE 2004a) and human capital contracts (Palacios 2004). Student loans are equitable, because it is those who benefit who will ultimately pay. They are also efficient, in the sense that students may make wiser choices on the subjects they study and, certainly, will graduate faster.

Externalities

This is the argument par excellence in favor of public universities. What if the university graduate spills over to society benefits that are not privately captured? In such a case the social returns to education would be higher than the "narrow" social rates reported in Table 3, col.3. Regretfully, it is also the argument for which there exists no solid evidence whatsoever (Venniker 2001). Surely, university education, as other levels of education and many other activities in life must have positive external effects, and some would argue that it even has negative external effects (LaRocque 2003; Veder 2004). But to base the subsidization of higher education on externalities, one should have evidence on the relative value of such externalities between sectoral activities – a luxury not yet available in empirical economics.

Table 3

Earnings advantage and returns to investment in tertiary education circa 2000

Country	Relative earnings (tertiary / secondary graduate = 100)	Rate of return (%)	
		Private	Social
(1)	(2)	(3)	(4)
Denmark	128	7.9	6.3
France	163	13.3	13.2
Germany	141	7.1	6.5
Italy	142	6.7	7.0
Netherlands	132	11.7	10.0
Sweden	140	9.4	7.5
UK	151	18.1	15.2
USA	190	18.9	13.7

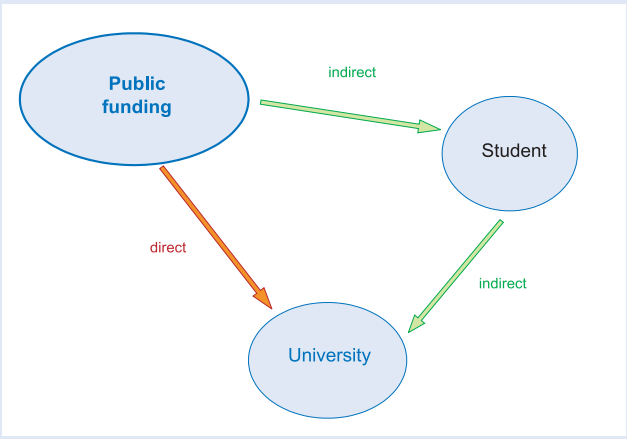
Source: OECD (2003), pp. 165 and 167.

Information

Public universities have also been defended on the basis of student protection against unscrupulous entrepreneurs offering bogus degrees. But in today's world, students themselves may know better than the central Ministry of Education which universities are best and what subject to study where. Public universities tend to offer outdated subjects out of inertia, leading to graduate unemployment. An example in case is Greece, where in 2001 there were 21,000 applications to study computer science in the public (and only) university system, yet there were only 125 available places.

Figure 2

DIRECT VS. INDIRECT UNIVERSITY FUNDING



Political votes

This is the most persuasive explanation on why public university systems still dominate worldwide. Telling the electorate that in the name of equity higher education is free generates votes. Alas, it is only the highly educated (still a minority) who understand the fallacy of the argument. But they also tacitly accept that populist argument because it is in their interest to have their children study free in a state university system. And given the fact that a university degree is a passport to civil service jobs, the question of quality of the degree is swept under the carpet.

Towards a new institution

Throwing more public money to universities will not necessarily lead to academic excellence under the dominant finance model (red arrow in Figure 2). But if the same money were channeled through the hands of the students (green arrows in Figure 2), the efficiency and equity of higher education would be enhanced. This major institutional change would mean that the state would stop paying university salaries and the like, and each university would survive based on the willingness of the students to enroll and pay tuition. Some universities would close down, while others would excel.

The state could continue financing higher education, although it would not be a producer of university services. What the state spends on education today could be given to the hands of the students in inverse proportion to family income. Wealthier students would receive nothing from the state and would have to pay full tuition. Less wealthy students will get vouchers to buy university services from a producer of their choice.

Of course such institutional change cannot happen overnight, but in my opinion this is the direction we must go to achieve better higher education in Europe.

Where is Europe heading?

It was not until some time in the 1990s that Europe realized it was falling academically behind the United States. Some countries like the United Kingdom adopted politically unpalatable measures to try to correct the situation by injecting a degree of privatization in the university system – raising tuition fees (Dearing Committee 1997). Yet, according to The Economist (January 22, 2004) "the price and quantity of courses are state-controlled, in a system more suited to Soviet central planning than a modern democracy".

Most countries in the continent stuck to traditionally free and low-quality mass higher education. Current debate in continental Europe focuses on the amount of resources the state devotes to higher education, without questioning how the resources

would be used. There is a move towards a three versus four years of the first higher education cycle, without asking what would be taught during any number of years (Bologna-European Council 1999).

Recently, the European Commission has shown interest in the subject and is asking good questions (European Commission 2003). But the Commission is handicapped in its actions because, according to the Treaty of Rome, education policy is in the hands of individual countries. The EU Education Ministers met in Prague in May 2001 to discuss a possible European Higher Education Area. In their communiqué they "supported the idea that higher education should be considered a public good (sic) and is and will remain a public responsibility (regulations etc.) …" (European Commission 2001). Beyond the wrong use of the term "public good", such thinking among Education Ministers does not augur well for a radical institutional change in Europe regarding higher education.

The degree of privatization of a university system is a major institutional arrangement that affects academic quality. What matters is not the legal status of the institution – rather who has control over university functions and quality control. Without exaggeration, many European universities today resemble nationalized industries that are on the way out in other sectors of the economy.

Today in Europe there is a divide between the protected non-competitive higher education area, and the drive for the internal market and international competitiveness (Lisbon, EU 1999). Unless there is a radical institutional shake-up away from direct state finance and control of universities, academic excellence in the old continent will keep slipping away to more progressive parts of the World.

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