PAYING YOUR WAY

Why should government pay for university education anyway? asks **Sinclair Davidson.**

EDUCATION IS OFTEN DESCRIBED AS BEING A 'PUBLIC GOOD'. MOST PEOPLE INTERPRET THAT AS MEANING THAT EDUCATION IS GOOD FOR THE PUBLIC WHICH, INDEED, IT IS.

SINCLAIR DAVIDSON
Senior Fellow at the Institute of Public Affairs

In the May 2014 budget, the Abbott government proposed a 'radical' reform package of the Australian university system. If it were implemented, domestic students would have to pay a greater share of the costs of their own education.

Judging from the outraged responses, you might be forgiven for thinking that this represented the end of public higher education as we know it.

Yet it isn't clear that government should be subsidising higher education at all.

Education is often described as being a 'public good'. Most people interpret that as meaning that education is good for the public which, indeed, it is. Education is one of the better investments individuals will ever make in their lives.

Others interpret public goods as being those goods and services provided by 'the public'. This latter definition is certainly closer to the economic definition of what public goods are, yet it still remains very misleading.

In the economists lexicon, public goods are those goods (and services) that are both non-rivalrous and non-excludable. One person's use of the good does not prevent others from using it, and nobody can prevent others from using the good. Rivalry is determined by the nature of the good itself, while excludability is determined by the nature of property rights.

While that sounds all well in theory, the challenge is to come up with practical examples of actual public goods. National security is one such example. Recently Eric Crampton has made a convincing argument that

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pandemic protection is also a public good. After these examples it becomes quite difficult to think of practical examples of public goods.

'Knowledge' is often nominated as being a public good. After all my knowledge in no way diminishes the amount of knowledge you may have. My sharing of knowledge in no way diminishes my knowledge and may enhance your stock of knowledge. Clearly knowledge is non-rivalrous. But, and this is a very big but, knowledge can be excludable.

Intellectual property rights exist to make knowledge excludable. The entire apparatus of copyright, patents and the like have evolved so as to constrain the uses of knowledge. Now we can quibble as to whether intellectual property is over-protected and whether intellectual property rights add value or not. The fact is, they do exist and so knowledge is excludable. It is not a public good.

That insight can be extended from knowledge to higher education. Not only is higher education excludable, the exclusion has a name—entry standards. Many people bemoan the lowering of university entry standards as a decline in quality.

HIGHLY EDUCATED PEOPLE ARE LESS LIKELY TO BE CRIMINALS, LESS LIKELY TO BE ON WELFARE, LEAD HEALTHIER LIFESTYLES, AND ARE MORE ACTIVE IN THE COMMUNITY

So not only is higher education not a public good on the grounds that it is excludable, but many people think that this exclusion is a 'good thing'. However just because it is possible to exclude individuals from a higher education doesn't mean that we should exclude individuals from a higher education. In fact most of the reforms to higher education in the last 30 years have been to exclude fewer individuals from the higher education system.

Generally speaking we have decided as a society that everyone who can benefit from receiving a higher education should be able to receive that education. In practice that means that ability to pay should not be a deterrent from attending university. And hence the rationale for government subsidies for higher education.

This immediately gives rise to an equity problem. People with a higher education tend to have higher life-time earnings compared to those individuals who don't have a higher education. So the government then ends up subsidising 'the rich'—effectively taxing individuals on lower life-time earnings to subsidise the earning capacity of high-income individuals.

The 'solution' to this blatantly unfair outcome is to recast the argument as the government correcting a market failure. Higher education we're told is associated with so-called 'positive externalities'. If the government didn't subsidise higher education then there would be 'too little' of it and society would be worse off.

In the abstract that sounds all well and good. In practice the argument goes something like this: highly educated people are less likely to be criminals, less likely to be on welfare, lead healthier lifestyles, and are more active in the community. Higher education subsidies save the health and welfare budget. If that sounds elitist, it's because it is.

The positive externality argument also suffers from over-reach and confuses correlation with causation.

Yes, there are both public and private benefits of getting an education. Reduced crime and improved health and the like have been shown to be associated with completing high school. Going on to a higher education involves self-selection which implies selection bias when investigating the public benefits of higher education. There may even be reverse causality where the kind of people who choose to get a higher education are less likely to break the law, less likely to be on welfare, and so on. The argument that higher education provides positive externalities then quickly collapses.

There is, however, what economists call an inter-temporal problem. People who will one day be quite well-off due to their education might not be able to pay for their own education when they are young.

This suggests the need for a loans market, or even a human capital equity market, where potential students can raise money in the present to pay for their education out of future earnings. In many countries the banking system provides student loans. Here in Australia the government has a loan scheme in place that effectively provides interest-free loans to students.

To the extent that young people need access to finance to pay for their own education, Australia is well-served by the FEE-HELP system (the technically correct term for HECS). While having an educated population is preferable to an uneducated population, the private benefits of having an education are so high that people will pay to acquire that education.

There's no such thing as a free lunch. Someone always pays.