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Ulrich van Lith

Europe and Education



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Europe and Education

Harmonisation versus competition

Ulrich van Lith

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We need competing education and training systems to make the Member States strong, and to European capital market for investment in human capital to make Europe competitive and grow together

Ulrich van Lith

Introduction: The individual as owner of knowledge, skills and competencies

It is the individual person who invests in his/her education and training, it is he or she who decides to use or not to use the knowledge, skills and competencies acquired. He or she also decides when and how to use them. He or she gets the benefits of his/her education, but also has to bear the costs and to take the risks of false investment in time, effort and money spent on education. Since we have good reasons to believe that the individual knows best what he can, what his potentials are, what he/she should learn and how he or she can make the best use of knowledge and skills acquired, he/she normally cannot be forced to be educated and trained in a special way or to be forced to make use of what he or she has learnt. Such compulsory action would be inefficient.

Difficulties individuals have to finance their education and training

For this reason, individuals (students, trainees) and their families who do not have the money to be educated or trained could have difficulties to get this money from a private bank, with the exception, they can offer a collateral or a guarantee that someone else will pay the money back, if he or she is unable to do so. This is one of the main reasons why schools and universities in Europe are nowadays mainly financed by the state. Knowing about the importance of education and training and their growing importance in a globalising and rapidly changing economy, we do not want that individuals and young citizens are either unable to pay for their education or start their professional career with high amounts of individual debts. We do not want the first, because the individual would suffer a loss in welfare and personal fulfilment when he or she cannot make the best of his or her natural endowments and also, because other members of our society loose welfare, since the individual cannot offer his/her qualified services to them. Finally, we all, Europe as a whole, would loose if this would happen too often. We would loose our competitiveness and, after some time, even social cohesion and peace.

The characteristics of European education systems: institutional unity of finance, production and control of education

The problem, however, is that most of the systems of public financing of education in Europe have characteristics that generally increase the demand for (school-based) education and training above an efficient level and distort its structure, because the individual himself does neither know what the teaching and training services cost he receives nor does he have to bear these costs individually.¹ They are not an item of his personal cost-benefit-estimate. His behaviour is more like someone who has only to bear the costs of his personal effort and time spent on education or the lost alternative use of both. The second point is, teachers and teachers' unions are interested in increasing the education supply and can more easily raise wages above those of competitive markets. The third point is that financing of education and provision of education are mixed up.² Mostly the nation state itself provides education and finances it institutionally. In sum, this creates problems of monopoly power, deficiencies in incentives to detect the natural gifts and potentials of individuals, to identify the changing as well as the relative stable demands for special and basic skills and competencies and to match both cost-effectively by screening and educational programmes and training. It strengthens teachers' union power and forms state and teachers into one institution which finances, produces and controls education and is highly efficient in protecting itself against competition from outside, be it private or international. Co-determination of parents and students is for several reasons not effective to destroy this monopoly.³ Thus, the production of information about gifted individuals, required basic attitudes and key qualifications, about expert knowledge and skills needed, about cost-minimising solutions in the production process of multiple educational goods is reduced, the flexibility and innovational power of the education system and its parts lowered.

1 See Buchanan, J. M., and N. E. Devletoglou: *Academia in Anarchy*, New York 1970, Chapter 2.

2 Lith, Ulrich van: *Der Markt als Ordnungsprinzip des Bildungsbereichs*, in: *Zukunftsprobleme der Sozialen Marktwirtschaft, Verhandlungen auf der Jahrestagung des Vereins für Socialpolitik, Gesellschaft für Wirtschafts- und Sozialwissenschaften in Nürnberg* 1980, p. 383, and *Der Markt als Ordnungsprinzip des Bildungsbereichs - Verfügungsrechte, ökonomische Effizienz und die Finanzierung schulischer und akademischer Bildung*, Munich 1985, pp. 127 sub. Most recently see also Lith, Ulrich van: *Die Ordnung des Bildungswesens, Problemzonen seiner ordnungsökonomischen Gestaltung, Argumente der Freiheit*, Bd. 14, Liberales Institut der Friedrich-Naumann-Stiftung, Berlin 2005, pp. 11 sub.

3 Watrin, C.: *Studenten, Professoren und Steuerzahler, Die Gruppenuniversität in ökonomischer Sicht*, and van Lith, U.: *Gruppenuniversität: Den Beweis schuldig geblieben*, both in: *Bildungspolitische Studien Nr. 3*, Institut für Bildungs- und Forschungspolitik, Cologne 1984.

The potential role of the European Union

This is the point where the European Union, the Commission, could come in to find its productive and value adding role: not to harmonise, not to reduce the competency of national governments or to distribute still more money through education programmes or a European Educational Opportunity Bank. Though the latter might produce additional value to the Community as a whole and to its members when it is an independent body. Instead, the main point is to show what national governments and their citizens and taxpayers will gain, if they allow their education systems and parts of them (educational tracks, schools, faculties and universities, training companies) to compete freely for individual European citizens whatever their nationality may be. The political philosophy, the guideline must be to put them into competition for the best of those who want to learn, to be educated, to be trained and retrained.

The costs of educational protectionism and the gains of an open education and training market

Practically speaking, the first step would be that the European Union⁴, the Commission, shows what national governments, taxpayers and, last but not least, the individual student or trainee will gain through open competing education systems. It has to demonstrate what gains can be achieved through productivity increases and reduction of costs, through better education decision-relevant (ex ante) information available to parents, students, trainees, employers, schools and universities, through increased flexibility and innovation and, finally, through a better matching of produced competencies and their demand on labour markets.

It must be shown that a European Education Market does not only give a chance to those who can pay for their education and training abroad - in addition to taxes paid at home -, and reduce the others to the chance of the very limited number of students and trainees who are 'exchanged' across national borders as goods are exchanged when there is no money. It means to enable students and trainees to choose their high school, their university and faculty or their training institution inside and outside national borders and to enable them to pay for it. There is no need any more to balance incoming and outgoing numbers of students, to have

4 In the shape of mercantilism it is even of concern to the US. See e. g. Stephen Joel Trachtenberg: *The future and the present-day problems of education: An American perspective*, in: *Wissen wozu? Erbe und Zukunft der Erziehung*, Europäisches Forum Alpbach 1997, ed. by Heinrich Pfusterschmid-Hardtstein, Vienna 1998, pp. 121-130.

special programmes for exchange, etc. The market and its participants would do it, if nation states learn to distinguish between their function they exercise as providers of school and university education and their function as financiers of the individual's investment in it.

National education systems, their parts and elements would be put under a sound pressure to act and to react, to be student- and trainee-oriented, to look more precisely at what the labour market, what employers need, what position the individual can attain. It makes it possible to them to compete for students from all parts of Europe and to be rewarded by funds that come with the student or trainee. Why should English and French universities not take German students just after they have completed their 12th grade to make them start their undergraduate studies, not waiting until they have passed their Abitur. Why should these universities not set up subsidiaries to recruit students beyond national borders, why not take advantage of a beautiful landscape and healthy climate to attract students from less favourable regions? Should this be restricted to those who can pay both, taxes at home and fees abroad, or those whose parents can afford it? Why should the others be compelled to attend their school or university at home where costs may be higher? Why should schools and universities not reduce their costs by recruiting cheaper but equally or even better qualified teachers from 'abroad', to teach English or French or Italian as a foreign language, or to promote the understanding of different cultures and ways in which people think and live in various European regions?

Why don't we take this secular chance in Europe to respond to the global challenge by turning our national monopolies into competing systems for the best of our young generation, a generation which has to cope with enormous structural and technical change under conditions that make new scientific knowledge available at nearly any location on earth, under conditions that no longer protect it from competition from emerging countries, countries that have set up their own education and research systems and which have highly motivated young people. We owe our young generation increased competence and quality orientation in our schools and universities instead of distributing rents to the established parties (teachers' and professors' union) within the existing national systems. We have to take Karel van Miert as an example, to fight against monopolistic power and mercantile thinking, we have to tear down protectionist walls.

To initiate a shift to demand-side finance of education and training

An effective way to do it – and this is the second much more difficult step – is (1) to switch the system of education finance to a demand-side financed system and (2) to distinguish between *financing* education (i. e. to solve the problem of so-called capital market deficiencies in financing investment in education) and state *subsidies* to education. The latter are state interventions into the education and training market to reduce deficiencies of this market, i. e. deficiencies in the provision of special, socially desirable educational goods the production of which is for what reason so ever too low, crime reducing educational measures in certain suburban areas, for example. These interventions have nothing to do with the finance of education and training, i. e. finance of investment in human capital and the functioning of the capital market.

The guideline of thinking and action must be: All Governments should be more interested in the best education of their citizens than in running their education systems themselves. It means they have to set up rules, supervise the market and competition on it, to be on the side of parents, students and trainees to protect them against false information, fraud and market power on an European education and training market. It means further to make provisions that citizens can finance their education and training on this European wide market or even abroad according to their individual choice.

What measures should be taken to do this?

A potential starting point: facilitate the use of the capital market for investment in education and training

A potential point of departure could be what we observe already in certain countries within the European Union and outside when investment in training has to be financed: Quit often companies not only train and retrain their employees at their costs, but also pre-finance these costs when training costs exceed benefits (returns from productive work) during the training or contract period. They do this because they expect pre-financed costs including calculated interests to be covered and exceeded by future (hard and soft) benefits they gain from their skilled and qualified employees. In other words, companies are willing to pre-finance training, to give unqualified 'hidden' loans to their trainees. Banks would not do this, give loans to trainees except to their own ones. Companies do it, because they know more about the personal characteristics of their trainees than banks.

They know what skills and competencies they need to be successful on the product market, they can judge quite well whether a trainee will fit into the company or not, whether he will be able and willing to acquire the skills and competencies required and to use them. This is why companies are willing to play the role of banks to trainees. And this is why banks and other suppliers on the capital market do not go into this business. Companies use their informational advantage to take over this original banking function. Sometimes companies even go on the capital market to borrow extra money to lend it to their employees for human capital investment, or they increase their equity for this purpose. Eventually, investment in high skilled labour is more and more important in times of rapid technological and structural change and less costly than high wages caused by shortages in skilled and highly qualified labour.

In Germany, e. g., the volume of pre-financed costs or ‚hidden loans‘ of companies to their trainees (apprentices only) is estimated to average at about Euro 8 700 per year and trainee, i. e. Euro 14.7 billion for the economy as a whole (2000 estimate)⁵.

It is said that this informational advantage used for steering and controlling investment in vocational education and training is what Germany makes so successful in training and qualifying its labour force – take aside the disadvantages it has through its highly state-regulated dual vocational training system making it difficult to be flexible enough for rapidly altering demands of skills and changes in required competencies. If the trained employee wants to leave the company to work with another one, the new employer takes over the loan from the former and reimburses him. The trainee now owes repayment to his new employer, if he is not willing to cancel his debt.

National states or agencies just have to protect the individual against certain risks of unemployment, sickness, invalidity, death. And the measure the European Union has to take is to give guarantees in those cases where individuals chose schools and faculties across EU-internal borders or move from one company to another across these borders. They could do this in co-operation with national and international institutions which are or might be interested to be part of a European wide guarantee system, like public and private banks and insurance companies.

5 Beicht, U., u. Walden, G.: Wirtschaftliche Durchführung der Berufsausbildung, Untersuchungsergebnisse zu den Ausbildungskosten der Betriebe, in: Berufsbildung in Wissenschaft und Praxis, 6/2002, p. 42. See further information in: Berufsbildungsbericht 2004, Bundesministerium für Bildung und Forschung, Berlin 2004, pp. 107 sub.

The same idea can apply to schools and universities and their faculties who know their students quite well. But while companies are interested in good training, since their competitiveness depends mainly on their qualified employees, state-owned schools and universities are mostly not, since they do not depend on their students and what they will become, whether they will be successful and the investment in them profitable for them and at the same time for society in the sense that costs are at least covered by tangible and intangible benefits. This changes immediately, when schools and universities are run as independent profit or non-profit-institutions under competitive conditions, depending on the money they earn when parents or students choose them and being obliged to report on their activities and on what happens to their students when they have left school or university. Though the Netherlands have already moved in this direction and a number of German Länder finance a citizen's school education by an earmarked amount of money per capita and school year when he or she attends a private school, this needs general consent between national states to finance the educational demand of the individual instead of the institution and to do this without regard of the territory (administrative boundaries) on which the school or faculty is situated. The financial function of the state must be regarded as separate from the state's ownership of schools and universities and be separated from it institutionally. It would be advantageous if the financing system is not (direct) part of the state budget, but a function exercised by a parafiscus or a consortium of banks in the name of the state. It is necessary that those who want to attend a school or an institution of higher education abroad are able to transfer an amount of money averaging the costs per capita to the school or university of their choice through a drawing right on a parafiscus, a voucher, a „Kindergeld-“ or „Bildungsgeld“ or a payment which is fully deductible of the citizen's or his/her parent's tax bill or even reimbursed if this amount is higher than the income tax to be paid, a negative income tax or „Bürgergeld“⁶.

6 Werner, Horst: ‚Bürgerge‘, hP er



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