

## Nature, Changing Perspective's and Financing in Higher Education

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### Abstract

*As India aims to achieve the goal of “Inclusive growth” and “Building a knowledge Society”, higher education will play a potent role. Economic growth models have proved the important linkage between human capital and economic development. Thus, acknowledging knowledge acquisition as the most important determinant of growth. India with stock of 550 million under the age of 25 years is expected to provide the human capital to the world. But to harness this demographic dividend, India needs substantial expansion in educational opportunities, with the special emphasis on inclusion. But government’s dilemma is whether to fulfil social commitments to ensure access to higher education to all? Or treat it as a private good, whose provision could be subject to market forces? To solve this dilemma it is important to understand the nature of higher education and perspective on it. The paper proceeds by explaining the nature of higher education from economic perspective i.e. is it a public good? or a quasi public good or a private good? Second section, discusses different perspective in higher education. Based on nature of higher education and which perspective is important, third section, gives argument in favour and against public financing, followed by profiling of alternate sources of financing higher education*

**Keywords:** Inclusive Growth, Knowledge Society, Finance, Higher Education

### Introduction

As India moves towards achieving the goal of **“inclusive growth”** and **“building a knowledge society”**, higher education will play a very important role in achieving these goals. World economies emphasize on the importance of education in economic development and acknowledge acquisition of knowledge as the most important determinant of growth. Growing need for or importance of education can also be felt from the fact that education is one of the focussed areas of the twelfth and eleventh five year plan. India has a huge demographic dividend, with 550 million people below the age of 25 years and to harness this incredible pool of human resources we need substantial expansion in educational opportunities, with the special emphasis on “inclusion” so that no one is left out of the system. In this context of inclusive higher education, financing in higher education is of prime importance. Financing higher education is central to higher education policy making because it reflects how education is provided to society and at what price (Chattopadhyay, 2007). Further, financing of higher education through public or private sources has been under continuous debate. J.B.G. Tilak (2005), in his article, “Higher Education in Trishanku” says that higher education is hanging between state and market and higher education systems in many countries today are at crossroads. Governments are faced with the dilemma to fulfil its social commitments to ensure

access to higher education to all those who are willing to pursue higher education on one hand, and the tendency to view higher education as a private good, whose provision could be subject to market forces and the financing of which should be done by households themselves.

Although the government has raised budgetary allocation for higher education substantially in the recent budgets, the question of looking for other sources of financing remains in view of the rising demand for higher education and fiscal constraints being faced by the states. As Mehrotra (2014) in one of his recent lectures in J.N.U said that education and health are the soft bellies for government, whenever there is shortage of resources government reduces the expenditure in these two sectors. Thus, for this reason also there is a need for generating more resources. Further, the increasing arguments against subsidization of higher education and increasing favour for privatization complicates the situation. In this continuous debate on how financing of higher education be done, should it be public or private? With these two forces trying to pull higher education on their sides, it is very difficult to say which is good out of public and private financing of higher education? Or is there any third option available i.e. public-private financing together. In the second section, paper explains the nature of higher education i.e. is it a public good or a merit or quasi public good? Section three of the paper tries to look how perspective in today's globalized world is changing from public to private higher education. Next section gives the arguments in favour of public support of higher education and arguments against it. The last section talks about the alternative sources of financing higher education.

### **Nature of Higher Education**

Before we look into the issue of how to finance higher education, that is, whether it should be public or private financing of higher education, it is very important to know how we treat education as a good. The question of public support (i.e. subsidization) or support to private sector very much depends on nature of higher education, i.e., Is it a public good? Or is it a quasi public good or a merit good? Let us start by explaining what is a Public Good? Public goods are those that are non-excludable and non-rivalrous (Musgrave, 1989 Bagchi, 2005). Public goods cannot be provided exclusively to some and you cannot exclude anyone from consuming it. Further, non-rivalrous means that their consumption by some individuals does not diminish the consumption levels of other people of the same goods. Public goods generate large quantum of externalities. Public goods are available to all equally, marginal utility derived from it is equal, and the marginal cost of producing public goods is zero. Public goods that strictly satisfy all the above conditions are pure public goods.

If higher education wants to qualify as a pure public good, then these two conditions of non-rivalry in consumption and non-excludability has to be satisfied. Let us try to see through an example whether these two conditions are satisfied or not. Suppose for example there are 100 students applying for admission in an M.Phil course in a university but only 20 seats are available and certain eligibility conditions are also there (i.e. suppose minimum of 55% in M.A). Here we can clearly see that there is rivalry in admission as students are competing with each other for 20 seats and the exclusion principle is also applicable through number of seats and eligibility conditions. Thus, we can see that the conditions of non-rivalry in consumption and non-excludability in higher education are not satisfied. "Often eligibility requirements are needed to be complied with for admission to institutes of higher learning and credential certificates are given to successful candidates who pass the examination and comply with the

norms of the institutions for being considered as successful candidates” (Chattopadhyay, 2007).

Higher education is also argued to be a **merit good** (Tilak, 2006) and its consumption needs to be promoted. People could be ignorant of the benefits of education, or may not be appreciative of value of education, or may not be able to foresee the implications of their investment decisions in education, and may be unwilling to invest in education. But governments are expected to have better information than individuals or families, and should be wiser and more able to look into the future and accordingly take wise decisions regarding investment in education. The important aspect is that the individual himself benefits to a greater extent than he is aware of. For example, the effect of education on wages may be known, but the likely impact on productivity, family health and nutrition etc., may not be known to him. It is widely held that governments would be wiser than the individuals in understanding the implications of investing in education as collectively we fail and allow government to impose preferences on us. Unfortunately it is not regarded as merit by ministry of finance. Higher education is also argued to be a **quasi-public good** as it has characteristics of both a public and a private good. When a student gets educated he is the prime beneficiary i.e. there are direct benefits like salary and he is also contributing to society in the process of being educated i.e. positive externalities.

However, Marginson (2007) argues that clear dichotomization between public and private is difficult. Core distinction between public and private creates serious problems. Firstly, putting public and private into two different box as A and B, is unhelpful and confusing.

|             |              |   |                 |   |                   |
|-------------|--------------|---|-----------------|---|-------------------|
| A – Public  | = government | = | state-owned     | = | non – market, and |
| B – Private | = business   | = | privately-owned | = | market            |

This clear cut segregation is not possible and we should not them separately as there is duality in definition. For example, Government can set up markets, manage markets, own and conduct business activities and generate profits, i.e. for example, government telling universities to patent their research papers and generate profits. This strict distinction based on ownership is not helpful and rather the focus should be on the social and cultural character of the outcome or the goods produced by higher education. He says it is very much possible for state owned institutions to produce private goods and vice –versa. Secondly, whether a good is a public or private depends on time, space and policy (i.e. policy sensitive). That is, character of a good change over time and it has to be analyzed in the context of society. Thirdly, public and private do not constitute a single, homogenous logical set. In the dualistic framework it becomes a conceptual ‘given’ that the more higher education is private the less it is public, and vice versa. But in the real world, the public and private elements are not necessarily zero sum. Sometimes they are, sometimes not. Where to draw line between public and private depend on policy and there is always a trade of between public and private good and depend on policy and social context. So there is a need to look into social and cultural character of goods produced by higher education.

### **Transition in Perspective on Higher Education**

The value of higher education was recognised in traditional societies perhaps much more than in modern day globalized societies. Education and knowledge were viewed as great wealth in themselves. “Higher education constitutes a public good in itself, and also it produces public goods, benefiting simultaneously the individuals and the larger society. This view has been

prevailing all over for a long period, influencing public policies on higher education” (Tilak, 2005), but there is a gradual shift from higher education being a state responsibility to its privatization. Some of the important reasons are: Firstly, lack of resources is one of the reasons for the growth of private higher education. Secondly, important factor that contributed to the radical shift in the thinking on the nature and role of higher education is the introduction of neo-liberal economic policies. Thirdly, inclusion of education in the negotiations under GATS and WTO, which is an obvious extension of the neo-liberal economic policies, is also found to be highly attractive to many universities and the governments (Tilak, 2007). An equally important reason is the change in attitudes towards higher education, towards private higher education and towards profit making private institutions of higher education. Further, public good nature of higher education is being increasingly ignored and private higher education is projected as more efficient system than public higher education. The purpose of the universities, their ownership, sources of revenue, norms of management, and the role of the government in university development have been changing very fast (See table 1).

**Table 1: Trends towards Private Higher Education**

| Dimension             | High Public ←-----→ High Private<br>(Traditional) (Modern)          |   |  |   |
|-----------------------|---|---|--|---|
| Mission/<br>Purpose   | Serves as a clear public mission as determined by the State/faculty | Mission avowedly both public and private                        | Mainly to respond to students' private interests               | Mission serves private interests of students, clients, and owners |
| Ownership             | Publicly owned  | Public corporation or constitutional entity                     | Private non-profit; clear public accountability                | Private for profit  |
| Sources of Revenue    | Public/tax payers   | Mainly public, but some tuition or cost sharing                 | Mainly private, but some public assistance (to needy students) | All private, mainly tuition                                       |
| Control by Government | High State control  | Some control by the State                                       | High degree of autonomy; State control limited to overseeing   | Almost no control by the State                                    |
| Norms of Management   | Academic norms, shared governance, anti-authoritarianism            | Academic norms, but acceptance of need for effective management | Limited adherence to academic norms, high management control   | Operated like business, norms from business management            |

Source: Johnstone (1999)

Higher education is facing pressures from both domestic and international markets and there is clash of values between traditional versus modern, state versus market and educational versus commercial. The problem is essentially the interests of the market forces and those of the state universities are different (Table 2)

**Table 2: Conflicting Interests of the State and Markets in Higher Education**

|                        | <i>State</i>        | <i>Market</i>                    |
|------------------------|---------------------|----------------------------------|
| Motivation             | Service             | Profit                           |
| Main Concern           | Knowledge           | Skills                           |
| Area of interests      | Generic             | Specific                         |
| Duration of interest   | short term          | long term                        |
| Team effort            | Rarely              | Always                           |
| Research               | Publish/public good | Strict confidential/private good |
| Time Schedule          | Flexible            | Rigid                            |
| Nature of Universities | Diversity           | Uniformity                       |

(Tilak, 2005)

### **Which Perspective is Important?**

In the current scenario, demand for higher education in India is linked to labour market requirements of trained and skilled manpower to fuel the economic growth that is taking place and because of this there is an increase in commercialization and privatization of higher education. Patnaik (2007) also talks about this perspective of higher education. According to this perspective higher education is a transaction between teacher and student which occurs at a specific place called university, where students are expected to acquire certain skills and get better placement in the job market. The problem with this perspective is: when it sees education as a transaction between teachers and students to augment the latter's employment prospects has an inherent tendency towards privatization. Thus, the institutions providing higher education will be nowhere like a true university, where universities will more look like a 'teaching shop', teachers will be treated as entrepreneurs and higher education as a commodity.

Another perspective sees higher education as an activity in which teachers and students are jointly engaged on behalf of the people of the society and the purpose is to produce "organic intellectuals" (Patnaik, 2007). This perspective sees all activities of skill-imparting as being informed by a concern for, and an awareness of, the social ambience within which the skill-imparting is taking place. What this perspective means is that we should not be exclusively preoccupied with marketability; it means inculcating a sense of the society in the minds of children to which they belong and if there is any role to be played by private institutions in the sphere of education then it has to be secondary and major part needs to be played by the public sector.

Privatization turns education into a commodity and treating higher education as a commodity has dangerous implications (Tilak, 2008). If we treat higher education as a commodity then buyer's preference necessarily enters the nature of the commodity produced and it is different from the higher education that is undertaken in the interests of the people. And if education is to be undertaken in the interests of the people, to defend their interests, then it must be publicly financed. By saying this it does not mean that we should not allow for private institutions, but to emphasize the need for a predominantly public educational system, into which the private institutions must fit. Given the dilemma of public or private financing of



higher education it becomes utmost important to look at the arguments in favour and against public financing.

### **Arguments in Favour of Public Financing**

As we know that higher education is not a pure public good but at least a quasi-public good. Some of the arguments in favour of public financing of higher education are as follows:

**Firstly**, higher education produces a wide variety and huge magnitude of externalities (khadria, 1989; Tilak 2005). The externalities include improvement in health, reduction in population growth, reduction in poverty, improvement in income distribution, reduction in crime, rapid adoption of new technologies, strengthening of democracy, ensuring of civil liberties, etc. If left to the market, there could be under investment in higher education.

**Secondly**, the capital markets are imperfect (khadria, 1989; Tilak 2005; and Chattopadhyay, 2007). Due to imperfect nature of the credit market for education loans, the imposition of financial burden on individuals will be unjustified. As education gets embodied in the student itself, there is a problem of offering human capital as collateral. Further, students may not prefer to borrow to invest in education as gestation period is very long, and may not be ready to take risk of investing in education, whose benefits are not certain. Even more importantly, the lenders would be understandably reluctant to accept risk backed only by uncertain future incomes of the reluctant debtors and lenders don't have full knowledge about the ability of student who is applying for loan. Moreover, "High mobility of students, particularly for those going abroad, poses as a difficulty for lenders to trace defaulters and ensure recovery. All this put together makes the lender wary of giving loans to students irrespective of their socio-economic background and choice of streams" (Chattopadhyay, 2007). **Thirdly**, there is uncertainty involved in investment in higher education. There may be the risk of falling market value of the education that the student has acquired i.e. skill becoming obsolete and student may remain unemployed. **Fourthly**, public financing of higher education insures equality of opportunity in education to everyone irrespective of not only social, racial, and cultural background, but also economic background is considered an important function of the modern State. **Fifthly**, higher education is also an "experience good" whose product characteristics such as quality and price and even the benefits is difficult to observe in advance, but can be ascertained only upon consumption. **Sixthly**, privatization turns education into a commodity and treating higher education as a commodity has dangerous implications. Privatization of higher education will result in a rapid extinction of some of the important disciplines of study that serve as a basic foundation for the development of any humane society. Only the marketable and revenue generating courses of study will survive. So, the need for public financing is very important. **Lastly**, the political rationale has to do with commitments to education as a human right, as a key means for social mobility and social cohesion, for the protection of learners and due to the contribution that higher education makes to all levels of education, among others.

### **Arguments against Public Financing**

**Firstly**, one of the arguments neo-liberals have made against the public provision of higher education benefits the upper middle and upper income groups of the population more than the low income groups and thereby accentuates unequal distribution. Though this argument is true to some extent, the situation in developing countries is changing rapidly; access to higher education is no longer confined to upper middle and high income groups; the participation

rates of the low socioeconomic strata are rising. **Secondly**, World Bank argues that primary education yield higher rate of return than higher education. So, the public financing should be withdrawn from higher education. But comparing one level of education against another is not appropriate as this approach obviously ignores the interdependence of various levels of education (Majumdar, 1983). By following this approach we are ignoring the fact that higher education completers acts as inputs in the primary and secondary level, i.e. it provides teachers, administrators and others for school education. It also ignores the fact that growth in primary education would contribute to rapid rise in demand for secondary and higher education and the corresponding need for expansion of secondary and higher education. **Thirdly**, higher education is regarded as a “positional good”, which gives you a social value or a higher status in society. So, its provision will create inequalities in society. But public provision of higher education to larger numbers of the people or what is known as “massification of higher education” will reduce the undesirable nature of higher education as a positional good, while the treatment of higher education as a private commodity, on the other hand, will only fortify it as a positional good, meant for the privileged (Tilak, 2009). **Fouthly**, heavy subsidisation by the state to education institutions makes them vulnerable to government control. This leads to inefficiency and poor governance since they have “no incentives” to allocate the resources efficiently or work efficiently. **Lastly**, neo-liberal argues that if you subsidise student’s i.e. cheap education, students don’t get motivated and do not value education. Here the idea is to make public sector face competition in market and should work like private management, so that they pay and therefore value there education. But the problem is if public institutions to move towards privatization, there is a danger to treating teachers as entrepreneurs and students as investors. Teachers always on their toes to maximize their profits and students will be like real investor i.e. economic agents.

Given these arguments, there are still some doubts about absolute justification about public financing plus there are inter-sectoral constraints for public funds. Further, the justification for allowing public universities and state to explore alternative sources of financing seems to be appropriate as it will release the financial pressure that public universities are facing. By this way universities will be more self dependent and can emphasize more on better governance of their institutions.

### **Alternative Sources of Financing Higher Education**

**Deregulation of fees:** fee structure should be such that it reflects the per capita cost of education to the extent possible as students move up the ladder of education. But can we identify cost items? what items to be included or what not to be included? And measurement problem, etc. Governments usually have expenditure data and not cost. The method of cost recovery through fees ensures equity on one count i.e. when fee is charged only from those who are the direct beneficiaries of the system. A uniform increase in fees may have adverse effects on equity as higher education as composition of students is not homogeneous and it is dominated by privileged students. Instead, a discriminatory fee structure may be preferred, so that rich students pay higher share of costs as fees, and poorer students less (Tilak and Varghese 1991). But it may lead to only market-oriented courses, which have very high fee levels. This can aggravate inequity in the society as only students from the privileged section of society can afford these courses, which presumably promise higher stream of future income for students. So for equal access and opportunities in higher education, there is a need for more

scholarships and financial aid to students. Further, the amount of scholarship is a matter of concern, as it determines whether the student will go for higher studies or will opt for job.

**Graduate tax:** A graduate tax is an education specific tax to be levied from those who use the educated manpower. The basic argument is that the employers who employ higher educated labor force should be required to share the costs of production of this high skilled “human capital.” The sectors which hire these graduates do not contribute to the cost of educating these graduates although they are the direct beneficiaries in terms of the productivity gains on account of their employment of these graduates. Therefore, the cost of education of graduates they employ should be shared by them (Tilak, 1991). Further the tax rate may vary according to field of higher education, an engineer may pay higher rate than an arts graduate. Graduate tax is not free from problems as it may work as a disincentive to employers to employ graduates. Depending upon the elasticity of substitution between several levels/types of graduates, employers may tend to employ a “cheaper” graduate or a secondary school product. All this may aggravate the problem of educated unemployment, unless education-productivity relationship becomes very strong, and the elasticity of substitution between several types of higher education becomes less. Thus employer may focus on physical capital more than human capital.

**Student tax:** is a tax in addition to the general income tax, which is imposed on graduates. Thus, it is an obvious device to secure additional funds from the primary beneficiary of higher education. Like any other tax it needs to be paid only if income exceeds a certain threshold limit. Some arguments against it are: payment to be made by the student remains independent of costs of education (Greenaway and Haynes 2004), it is not conducive to a more flexible and competitive system and if graduates obtained their degrees from private universities with no government support then such a tax is not justified.

**Educational cess:** Educational cess is an earmarked levy to be used for a specific purpose. Usually a cess is levied as a fraction of some other tax. For example, a cess for public financing of education may be attached to urban property tax. Revenue from these sources could be supplementary and not substitute to financing from general tax revenue. Educational cess provides a small fraction of the total requirements and the education sector has to depend upon allocations from general tax revenue, making its role insignificant.

**Education loans:** Since students are argued to be the primary beneficiaries of higher education, they are encouraged to opt for loans to finance their education. The capital market for such loans is inherently imperfect (Hillman, 2003). Problems related to it have been already discussed.

**Income contingent loans:** Income contingent loans have been successful in some developed countries (Greenaway and Haynes 2004). In Income contingent loans, repayment takes the form of x per cent of the individual borrower’s subsequent annual income (Barr, 1993). This scheme helps to avoid up-front payments and ensuring that education remain free at the point of consumption.

**Good governance and self financing:** “doing more with less” should be the policy of every institution i.e. the most efficient use of resources, there should be effective management of the higher education system by improving governance, better utilisation of funds, democratic decision-making. Further, institutions can also patent their research papers and generate



resources. Class size may be increased wherever possible with increasing the number of shifts of the staff. Self financing courses should also be encouraged, therefore, the possibility for cross subsidization.

### **Conclusion**

There is sufficient evidence that suggest that higher education generates large positive externalities for growth and that the level of development of a country and stock of highly educated manpower are related (Srivastava, 2007). Basically, higher education is not a pure public good but is a quasi public good and the traditional way of defining public and private goods needs revision as publicness or privateness of a good is policy sensitive. Given this, there is a shift in the perception of the nature of higher education from a public good to a private one, a commodity that can be traded, and treating it as a commodity for trade have dangerous implications. As discussed, any role that privatization can play has to be secondary to dominant public role. Governments should play major role in higher education financing and should look for different mix of policies that can be on a whole useful for development of the society. "There does exist a large student body that can also afford to pay for their education. There is no reason why both these two categories of students be placed on the same level when it comes to financing their education. Thus, no student should be turned away from an institution for want of funds for education.

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