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### **States and Markets: Competing Paradigms for the Reform of Higher Education in Europe**

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*Abstract* – The construct of the market is an interesting new element in the discourse on higher education in Europe. It has generated serious initiatives in deregulating higher education, in developing performance-based models of resource allocation, in fostering inter-institutional competition and efficient management structures, and even in considering the "privatization" of higher education. These developments affect particularly the financing of higher education, where new models of resource generation and allocation, institutional steering and controlling, and accountability are being explored. Within this context, and with a view towards the future of higher education in Europe, eight issues are being examined in more detail: The transition from line-item budgets to block grants, formula funding, the role of incentives, the mobilization of external resources, the introduction of tuition fees, the creation of private institutions, alternative strategies of steering and controlling, and the internal distribution of resources.

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## **1. Introduction**

This paper proceeds on the assumption that changes in financing and governance are the key element in the current reform of higher education in Europe, and that there is a very close link between changes in financing and changes in governance. Reviewing a number of critical reform issues in the current debate in Germany and other European systems of higher education will highlight these linkages.

I am drawing most of my evidence from German higher education, but I am also reaching out into the experience of other Western countries (mainly the ones belonging to the OECD), including from time to time the United States, in order to highlight both underlying commonalities and important differences in higher education policy.

I am primarily interested in questions of funding in higher education, but I have learned that there is no way to treat questions of funding as separate from questions of governance and decision-making. I am therefore treating the issue of funding as a key element in the governance of higher education. I will argue, in fact, that the issue of funding can serve as a lens through which the entire issue of structural reform in higher education can be most clearly observed.

In addition to the documentary evidence, I have drawn on my own experience both as a faculty member and administrator at a major private university in the United States – Stanford University – where I worked for nearly thirty years, and as the head of a new institution of higher education – Viadrina European University – which was founded in the Eastern part of Germany in 1991. Both institutions, albeit in very and instructively different ways, have faced and continue to face some of the very issues in financing that have occupied the broader OECD discussion over the past decade (OECD 1990; Williams 1992).

As one of the most prestigious and selective private institutions of higher learning in the United States, Stanford has over the last two decades witnessed the blurring of the distinctions between public and private higher education in the US, has faced growing governmental pressure for

accountability especially in its sponsored research programs, has played a major role in moderating the market forces in higher education through programs of need-blind admissions and affirmative action, and continues to face the increasingly difficult task of reconciling rising cost and limitations to price increases in its tuition and indirect cost rates.

My experience for the past seven years of planning and building a new university in Germany is of a rather different, but I think similarly instructive kind (see Weiler 1994 and forthcoming). As a university built literally and deliberately on the border between Germany and Poland, committed to making a significant contribution to the renewal and strengthening of the relationship between these two countries, and located in one of the more economically deprived areas of what used to be the German Democratic Republic, the Viadrina European University has a good deal in common with both its fellow universities in the rest of Germany – East and West – and some of the newly developing universities in Central and Eastern Europe. With regard to the issue of higher education financing and governance, the Viadrina is right now in a state of transition from less autonomy from the state to more autonomy, from line-item systems of budgeting to more lump-sum and "global" patterns of resource allocation, and from fairly automated systems of internal resource distribution to much more performance-based systems in allocating resources both to individual institutions and within institutions to individual operating units. In addition, there is by now in Germany a debate of unprecedented intensity on both the question of tuition (which thus far does not exist, and which I happen to think should exist) and on the further growth of the (as yet insignificant) private sector in German higher education. Since I have become an active participant in these debates (recently, among other things, as chair of a panel set up to assess a number of projects for new private institutions in higher education), I have developed some first-hand knowledge not only of the issues, but also of the extraordinary level of political conflict that can develop around them.

## **2. The rise of the market in higher education**

There is a new game being played in European higher education. Some call the game "deregulation", some call it a combination of greater autonomy and greater accountability, some call it a shift from input controls to output controls, and some call it simply "passing the buck". Whatever it is called, it certainly is different from the old game, which always looked a little like a state-owned version of "Monopoly". The new game is being played on different stages; it is being played on the stage of governance, on the stage of new programs of study and their accreditation, on the stage of new personnel regulations, and increasingly on the stage of new higher education legislation. Wherever the new game is being played, there are the same three players involved: the university, the state, and the market. And that is what makes it new, because the old game was a pretty simple, straightforward and rather boring affair that was essentially limited to two players: the university and the state. And one always knew the outcome of the game; Both players claimed they won, but it was always the state that kept score.

Now there is a third player in the game, something called "the market". Nobody quite knows what a market is in higher education, but that doesn't keep anybody from talking about it. This construct of the market is an interesting new element in the discourse on higher education in Western Europe, and it is rapidly spreading, with the tender care of the World Bank and the Soros Foundation, to Central and Eastern Europe. It is pretty clear that it won't spread into the United States, because there it has been around already for some time.

For Europe, the interesting question may not be so much why the market has recently moved into such a prominent position in the debate about higher education, but why it took so long. After all, we have known about markets at least since Adam Smith wrote "The Wealth of Nations" over 200 years ago (1776). And we know how exasperated Adam Smith was when he incredulously took Colbert, the minister of Louis XIV, to task for daring "to regulate (industry and commerce of a great country) upon the same model as the departments of a public office" (quoted

in Lindblom 1977, 33). Somewhere along those 200 years, someone might have had the idea that there may be better ways to regulate higher education than "upon the same model as the departments of a public office". But apparently, until very recently, and with the exception of the U.S. and a few of its imitators, nobody did.

But now it seems to have happened. There is not only serious talk, but even some action in the direction of deregulating higher education, of performance-based models of resource allocation, of inter-institutional competition, of efficient management structures, of the development of specialized "products" of higher education, even of "privatization". And the arena of European, and even German, higher education, long a rather sleepy habitat, has all of a sudden become exciting, controversial, and lively.

Of the various stages on which, as I have said, the new game is being played in European higher education, there is one where it is being played with special intensity, and where it is particularly instructive to watch. This is the stage of financing in higher education, and this is the one on which this paper will focus. Because it is with regard to the question of financing that the new higher education discourse of the market becomes most tangible, most controversial, and thus most revealing.

### **3. Developments in governance and financing of higher education**

I propose to organize my review of recent trends and developments in the governance and financing of higher education around a number of key issues that proceed somewhat loosely from a macro to a micro level, and will at the end, in a final section, raise a few broader themes in higher education policy that I regard as worth keeping in mind as one debates different options in financing and governance.

The macro/micro distinction in higher education financing is, by the way, not a particularly neat one, since many developments cut across all levels of the system; take, for example, the case of

formula funding or parameter-based funding, which establishes principles and procedures both for the allocation of public resources to individual institutions and for the distribution of resources within each institution. Nonetheless, it may be useful to start with the broader view and work our way to some of the specifically institutional concerns.

As I see it, the twin goals in the current debate in Germany and among other OECD countries about the financing of higher education (and about the future shape of higher education more generally) have to do with autonomy and accountability. As institutions of higher education seek (or are pushed towards – it is not always clear which) greater autonomy from state control, there is a corresponding preoccupation with questions of accountability and transparency in the ways in which more autonomous institutions deal with their resources. Where once the state, through a tightly woven net of budgetary and other regulations, controlled or preempted a substantial part of a university's internal decision-making, policies of deregulation now confront the university with the task of designing, applying and enforcing its own ground rules for the internal allocation of resources. In the process, there is a transition from a system of control that operates "ex ante", i.e., through a set of rules and regulations set up in advance, to a steering system that works largely "ex post" and is based on allocating resources on the basis of performance. In other words: the overall tendency is from a situation where the resource situation of an institution is dependent on a given set of input parameters to a situation where output parameters are becoming more and more important. Line-item budgets, where a certain amount of money is in advance earmarked for a certain institutional purpose – e.g., the purchase of computers – are a key feature of controlling an institution "ex ante" or through the specification of inputs; by contrast, providing a university with a lump sum budget and specifying the performance criteria by which it will be judged as to whether or not it has spent this budget wisely (and should therefore receive more the next time around) controls an institution "ex post" or through its outputs.

This description may sound like a nicely professional and disinterested treatment of the transfer of responsibility for financial decision-making from the state to the universities. In actual fact, however, this transfer only thinly conceals a considerable state of emergency in the funding of higher education. In Germany and in most of the other OECD countries I know, at least part of the state's motivation for making institutions of higher education more autonomous in dealing with their financial futures has been the serious shrinking of public resources available for expanding systems of higher education. In this situation, it is very tempting for governments to transfer to the universities the increasingly unpleasant (and politically onerous) task of administering scarcity. In a review of changing financial policies in higher education in several Western European countries, the German HIS research service observes, somewhat tongue in cheek, that "the radical transition from a supply-oriented allocation of resources to a competitive allocation occurs in all countries considered against the background of a severe curtailment of funds" (Schnitzer and Kazemzadeh 1995, 9).

Be that as it may, the overall and rather fundamental change in the general pattern of funding higher education has a number of specific facets, of which I consider the following eight as being both the most significant and, from the point of view of the experience of the OECD countries and my own experience, the ones most in need of a critical assessment.

### **3.1. Changing rationales in budgeting and resource allocation: From line-item budgets to block grants**

Of all the changes in higher education financing, none has probably been more consequential than the change from line-item budgets towards global allocations or block grants, for the use of which the universities are to be responsible and accountable in an ex post manner. In the overall move towards greater autonomy by the institutions of higher education, this shift has probably been the single most important factor. Nowhere, however, has this change been

accomplished in one giant and instantaneous step. Typically, this change has been, or is being, accomplished through a gradual series of consecutive steps, such as:

- Allowing universities to use funds from unfilled staff positions for current operating expenditures in teaching and research, or
- Making possible limited transfers between line items, or
- Selecting a limited number of institutions for pilot projects to try out more encompassing schemes of block grants.

Where, as in the Netherlands, the change towards lump sum or block grant allocations has gone the farthest, it has been closely tied to a system of formulae on the basis of which the overall allocation has been determined (see below). Without going into a great deal of technical detail here, I would like to point out a number of considerations that I have found useful as one moves in the direction of block grant funding.

Among the few advantages of line-item funding is the fact that budget reductions on the part of the government become more easily visible and identifiable; budget cuts can be much more easily concealed in the allocation of block grants.

Implicitly or explicitly, block grant allocations are tied to an underlying contractual relationship between funding agency and recipient such that, in exchange for the grant, the recipient institution engages to perform a certain set of tasks in teaching and research, the satisfactory completion of which is the university's responsibility and on the basis of which it will be supported in the next budget cycle. This kind of contract has been one of the more interesting instances of negotiation between government and universities; in current discussions in a number of German states (e.g., Lower Saxony, Berlin), where the key term is "Zielvereinbarung", universities and the state have negotiated a fairly explicit set of development targets which the universities are committed to achieve in return for (reasonably) secure multi-year funding prospects.

In the United States, the National Commission on Responsibilities for Financing Postsecondary Education has a few years ago spelled out a handy set of four conditions for the

success of this kind of an autonomy-accountability relationship between funding agency and recipient institutions:

- Agree on the tasks that need to be accomplished;
- Ensure that the available resources are sufficient to complete the tasks successfully;
- Provide the enterprise (the university) with the authority it needs to be effective, and then let it do the job without interference; and
- Define a set of measurements to indicate how well the enterprise is doing relative to its goals, and follow up by tracking these measurements (as cited in Massy 1994, 6-7).

This set of ground rules already highlights the critical importance of performance measures and evaluation in making the transition to more global means of funding feasible. Here again an instructive debate on the nature and the measurement of desirable outcomes in higher education has begun in Germany, from completion rates in different programs of study to research productivity, and from the employment record of graduates to the number of scholarly awards.

Block grant systems allow for an important facility especially for universities in a state of transition, namely, the achievement of cross-subsidies between programs, where savings in one program can be invested in the strengthening of another.

From the funding agency's point of view, one of the important elements in this reshaped or reshaping world of university funding could well be the retention of a central contingency pool of resources that can be used for such purposes as:

- Special and particularly promising research programs;
- The support of graduate students on a competitive, cross-institutional basis;
- Compensating an institution for overloads in teaching;
- Bridging the time to anticipated retirements of faculty, thus making the early replacement of retiring faculty possible;
- Investments in special teaching facilities, such as PC pools; or
- Support of provisions for underrepresented groups, such as women students or faculty.

### **3.2. Formula funding: New parameters in resource allocation**

As the pre-ordained structure of line-item budgets has begun to disappear, the need arises to find a basis on which to determine the new block grants or lump-sum allocations that universities

are to receive under more open and autonomous funding arrangements. The search for this basis has led to a variety of "formulas" which are used to compute the funds that a university is expected to need. In this development, the Netherlands and Denmark have played the role of pioneers among OECD countries, and anybody interested in the trials and errors encountered in this process should take a close look at their experience. Other countries have taken up the challenge, and my own state, the state of Brandenburg, is now experimenting with a model of formula funding of its own, as are any number of other states in Germany and countries in Europe. In reviewing these efforts, let me emphasize the following points and observations.

Initially and in its strictest sense, the formulae for funding higher education have focused on input factors, i.e. on those indicators that represent the tasks universities are supposed to perform in teaching and research, and their estimated cost. By now, however, many funding formulae have a double face: they estimate input factors, but they also tend to specify performance measures that are considered to be particularly desirable outcomes of university efforts. To give an example: One of the most fundamental elements in any funding formula is the number of students. That is a straightforward input factor. By modifying or weighing this factor in such a way as to only count students within regular graduation time limits (that is, excluding those who take forever to finish their degrees), one adds an outcome or performance measure that reflects the university's ability to provide an effective teaching program.

One of the difficult questions in the business of designing formulae for funding is just how finely to tune them, and whether to concentrate on a few important indicators or include as many as possible. Here, the general wisdom seems to be to focus on the ones that really matter. This is easier on the input side, where one typically limits the formula to such things as:

- The number of students (possibly modified by limiting it to students within regular graduation time), as an indicator of the load and cost of teaching;

- The number of staff (academic and service), as an indicator of the cost incurred by their work; and
- Space, as an indicator of the cost of maintenance.

The important point about these indicators, however, is that they need to be differentially weighed, depending for example on what discipline is involved, engineering and natural science subjects requiring substantially more cost in teaching and research than humanities and social sciences. It also makes sense to weigh the number of students differentially depending on whether the instructional capacity of a given institution (as determined by its staff and space) is underutilized or overutilized; the formula we are working on in Brandenburg envisages a statistical bonus for student numbers under conditions of overutilization, and a malus or discount factor in case of underutilization.

On the output side, the choice of a few key indicators to include in the formula becomes more difficult, especially since this also depends on what a given institution, by the nature of its institutional mission, considers particularly important. A heavily research-oriented university will value and weigh research productivity (as measured, for example, by the elaborate peer review procedures of the UFC in Britain) and the acquisition of research funding from the outside more highly, while a more teaching-oriented school will emphasize the quality of teaching and advising and the institution's success in bringing students to an early and high-quality completion of their degree. One of the important but as yet poorly developed outcome measures would clearly be both the occupational success and the satisfaction of an institution's graduates.

Some funding formulae – including the ones that I am struggling with at my institution right now – have an important and not adequately recognized structural deficit in that they disregard the rather simple management truth that institutions have funding needs that are independent of their size and the volume of their activities. Every university, no matter how small, needs a core admissions staff, a core personnel department, certain basic maintenance services, basic library

resources, etc. The importance of this baseline estimate tends to be often overlooked when the logic of linear relations between size and funding needs prevails.

Funding formulae – and this is perhaps their most important function in shaping systems and institutions of higher education – serve as an important communication device. Their very composition sends a powerful message as to what is and is not considered important in a system or an institution of higher education. The relative weights given to teaching, community service, foreign student enrollment, scholarly awards, student-teacher ratio or number of women faculty all represent important value decisions for the system or the institution, and should be the result of a rather serious process of reflection and discussion.

Since so much controversy has emerged around the question of markets and democracy in higher education, and about their alleged incompatibility, I would like to pursue this question a little further. It is, of course, nonsense that markets and democracy are incompatible, in higher education as elsewhere. What is incompatible with a competitive and market orientation in higher education are the kinds of so-called democratic governance structures in universities that have, at least in German higher education, degenerated into mutual non-aggression pacts for the purpose of conflict-free and performance-independent resource allocation and of seeking and finding lowest common denominators among competing factional interests. In contrast, a rather worthwhile challenge to the internal democracy of academic institutions would be to specify the kinds of institutional priorities that would result in specific funding formulae. Wherever representative bodies of university governance start engaging in this kind of reflection on institutional values and profiles, both the causes of higher education and of democracy would be served well indeed.

### **3.3. Scholars and markets: The role of incentives**

With its increasing emphasis on output or performance criteria, formula funding contains already a substantial element of incentives for contributing to the institution's mission, and of disincentives for not contributing.

I would like to add to this, however, by reporting on a particularly heated debate that is being conducted in Germany right now – a debate in which, not surprisingly, the experience of American higher education serves once again as a controversial benchmark. The issue is the determination of funds that should be placed at an individual faculty member's disposal for teaching and research and, furthermore and even more delicate, the determination of a professor's compensation. At present, both of these decisions are virtually unaffected by what a professor does, what a load he carries, or how he performs his tasks. The financial resources for his professorship are typically settled when he is appointed, and he has a right to receive them annually as long as the budget permits, regardless of load or performance. Similarly, professorial salaries are set by civil service guidelines and increase inexorably on the basis of only one criterion: advancing age – the only exception being a special raise available to counter an offer from another university. The current debate – fueled by a recent resolution of the German Rectors' Conference – over changing this system with regard to both the financial resources at the professor's disposal and his salary in order to make it more incentive-oriented has all the drama of a war of religion, and may end up just as bloody. It highlights both the inherent difficulty of reform in higher education and the problems of bringing a modicum of market principles to bear upon academia.

On a much more minor scale, I wanted to relate an instructive example of making incentives work. I helped introduce this myself in my department at Stanford where we gave faculty members an 8% share in the overhead that the university charges on externally funded projects. Thus, for every \$100,000 in sponsored research funds that a professor raised, he had \$8,000 at his disposal for travel, added assistants, books, or other professional expenses. The effects were considerable.

Lastly, let me point out an important and often overlooked incentive that is entirely non-monetary, but in my experience extraordinarily effective. I am speaking of the devolution of decision-making, including financial decision-making, to lower levels of the organization. Being involved in decisions in such a way that one's voice does make a difference serves as a powerful motivating factor in all organizations, but particularly in a highly professionalized organization such as a university.

### **3.4. The search for new funds: Mobilizing external resources**

The growing shortage of public funds, combined with the desire for getting away from the state as the sole source of a university's funding, has contributed to an unprecedented preoccupation in German higher education with opening up additional and alternative sources of funding. This effort takes the form of seeking support from organized philanthropy through foundations, of a growing volume of contractual research and training programs for outside clients (for the coverage of both direct and indirect costs), of the sale of services such as language teaching or the use of libraries and data networks, the mobilization of private individual and corporate donors to set up endowment funds for special projects (such as endowed chairs), programs of continuing education, and others. Having dealt with, and carefully observed, this process in both the US and Germany, I would like to offer the following observations.

It is important to realize that most externally obtained resources in higher education, with the exception of endowment funding, are of questionable longevity. They typically last for a number of years, and then disappear, leaving a promising program that was funded from these sources destitute or, just as badly, dependent on the institution's regular resources. Commitments by the state to pick up the support for activities that were started with external funds are, at least in my experience, notorious for being evaded (e.g., the experience of externally funded chairs ["Stiftungslehrstühle"] in Germany in comparison with endowed chairs in the US). This situation is

especially serious where, as is often the case today, state funding only covers the basics of institutional cost, while everything dynamic and innovative about an institution comes out of outside funding. As such outside funding tends to disappear over time and may not be fully replaced, the institution is left with its status-quo-oriented basic framework and sees its innovative features disappear in the process.

A related risk has to do with the fact that external funds tend to carry hidden costs that sometimes even the more sophisticated calculation of indirect cost will miss. These hidden costs have to do with the gradual erosion of basic capabilities in libraries, equipment and physical plant. Some of these are opportunity costs for foregoing other valuable activities in favor of an outside contract. A particularly problematic policy is that of the German national science foundation, the Deutsche Forschungsgemeinschaft, which as a matter of policy makes research awards only on the condition that the recipient institution provides all of the basic outlay – space, equipment, basic staff, and adequate library facilities. In stark contrast to this philosophy, I think it is essential that external funds cover the full cost of the services they purchase and support, including both indirect costs and the cost of developing the institution's long-term capabilities, including the training of young researchers.

The most important and consequential problem with outside funding in higher education, however, is the risk it carries for sustaining the institution's mission and intellectual profile. Except in the rarest case, and protestations to the contrary from the involved parties notwithstanding, the seeking of outside support typically entails compromises between the institution's own priorities and the priorities of the outside funding agency. The attempt to balance market forces with the need for institutional coherence remains in most instances imperfect, and its imperfection causes the problem of a "fragmentation of faculty allegiance" (Massy 1994, 32) between promising funding opportunities

and institutional loyalties that is becoming a serious problem for a growing number of institutions of higher education.

### **3.5. Making users pay: Tuition and fees in higher education**

Given the difficulties of not only obtaining outside funds, but also of dealing with their drawbacks once they are obtained, it is not surprising that the notion of charging users for the use of higher education is gaining ground. The number of countries in the OECD where some form of tuition is charged students of higher education is increasing, and the debate about introducing tuition in those countries that do not yet have fees is heating up. This is, once again, particularly true in Germany which has a long social democratic tradition of tuition-free higher education.

The arguments for and against fees are fairly straightforward. At a time of shrinking resources, tuition can be a significant source of new funding. Provided one makes sure that these resources do indeed remain at the university's disposal and do not serve to offset a portion of state funding so as to cure general fiscal ailments (not an easy condition to meet, I should emphasize), substantial financial benefits can accrue from collecting even (in comparison to, say, high-price US institutions) relatively modest fees. In this connection, it seems essential that students, parents and graduates have a major say in decisions about how tuition money is to be spent by the university.

Perhaps even more important in thinking about tuition fees is the prospect of creating more of a supply and demand dynamic in higher education. There is absolutely no question that in systems where there are fees, both universities and students behave differently. Universities tend to be more responsive to the interests and needs of fee-paying students who make a significant contribution to the financial well being of the institution and who also have the option of taking their tuition money elsewhere. By the same token, students and their families tend to pay a good deal more attention (including critical attention) to a university education, which costs them real money.

The main argument against tuition has been that it discriminates against students coming from economically disadvantaged groups, and that it tends to discourage those students from higher education altogether. There is some evidence from the United States that this is to some degree true, but there is also considerable evidence that this effect can be significantly moderated by appropriate programs of financial aid in connection with need-blind admission and affirmative action policies.

Those who argue against introducing tuition into higher education on social grounds also have to confront the argument, however, that there is nothing terribly social about a situation in which non-students who are working subsidize through their taxes the cost of university education for an upwardly mobile population of students who, by all accounts, tend to be rewarded quite generously for their degrees by significantly higher status and lifetime earnings.

In the end, the question of whether or not tuition in higher education can be justified hinges on the adequacy of the system of financial aid and its ability to compensate the effects of market-based tuition rates for students from disadvantaged groups. In this context, there is still much to be said for the original version of the Australian Higher Education Credit Scheme (HECS) – not the somewhat denatured version that has replaced it in the meantime – where needy students would pay both their fees and their living expenses out of a loan that is to be repaid through the tax system only if and when their later income exceeded a specified minimum income. A somewhat modified (and improved) version of this scheme has recently been proposed in Germany as well (Stifterverband und CHE, 1999).

### **3.6. Private initiatives in higher education: Panacea or dead end road?**

All over the world, with the (perhaps overly) enthusiastic leadership of the World Bank, the notion of privatizing higher education has in recent years picked up a momentum of its own. Having spent most of my academic life at a private university, I am following this development with both sympathy and some concern. There is indeed much to be said for challenging the monopoly of

public forms of higher education in the many countries (including Germany) where such a monopoly effectively exists, but some critical remarks are in order to keep things in perspective and to make sure that an essentially good idea does not get defeated by its own exaggerated claims.

In most countries of the world, including the United States though possibly excluding Brunei, higher education institutions that are entirely or even predominantly funded from private sources are simply not feasible. Even the United States that has arguably the most developed and successful system of private higher education has long moved to a hybrid situation where private institutions cover an ever increasing share of their costs from public funds – just as public universities draw increasingly on private sources of funding. Stanford and UC Berkeley provide an instructive pair in this regard.

What may well give the privatization of higher education a bad name is the emergence of two rather peculiar types of institutions. First, there are institutions like the ones that have recently emerged in Germany and other Western European countries that pick for themselves one or two subjects that are particularly marketable among both prospective students and corporate sponsors (usually business management and informatics), then proceed to obtain substantial resources from both corporate sponsorship and tuition fees and, in addition, seek and receive significant state subsidies. If the (excellent) idea of more privatization in higher education is to create more competition between different types of institutions, then there is no way for a fair competition to be held between these institutions and public institutions that can neither charge tuition nor market their much broader instructional spectrum, while having to maintain the full range of academic subjects over and above business and informatics. For competition to be meaningful, a level playing field is a prerequisite.

The other kind of newcomers in the animal kingdom of higher education are for-profit universities, of which one, the University of Phoenix, was very ably and instructively portrayed in an

issue of The New Yorker some time ago (Traub 1997). I am not necessarily saying that there shouldn't be any institutions of higher education that are conducted for profit. What I am saying is that these institutions are unlikely to serve as the kind of catalyst that could help regenerate and mobilize our existing systems of public higher education.

Against the background of these somewhat problematic developments, we are likely to be more successful if we understand privatization not necessarily as an alternative way of funding higher education, but as an organizational and structural alternative. To introduce, even under public or partly public funding arrangements, entrepreneurial or other private management structures into higher education strikes me as an extremely worthwhile project. There are already enough examples within the overall framework of public higher education systems of running research institutes, language labs, or continuing education programs on a modified corporate model to demonstrate how much more flexibility, adaptability and innovation can thus be achieved.

### **3.7. Shaping the institution's profile: Steering and controlling in higher education**

Financing in higher education, as I have said before, is not just about money and accounting. It has a great deal to do with institutional purposes and with how they can be achieved. I happen to think that the sharpening, the cultivation of institutional purposes, the development of more specific and recognizable institutional profiles is one of the major challenges that lies ahead in German higher education. The time of the all-purpose, across-the-board university, where one could find everything but had a hard time finding excellence, is probably coming to an end. Institutions of higher education in Germany in the future will probably have a more limited, more carefully composed set of specialties, and will seek to excel in those. For this strategy to work, financing will have to play an absolutely critical part, especially in a system of allocating resources in which performance is a key determinant for funding decisions. Because if shaping and sustaining the institution's special profile is an important priority, then part of the funding formula needs to be not

only the general quality of a unit's work (a department, an institute, a professor), but also the contribution which that unit makes to enhancing the university's special profile.

Let me illustrate this with the example that I know best, that of my own university. Viadrina European University was set up in 1991 to serve as an academic link between Germany and Poland, as a bridge across a particularly troubled border. It has opened up its programs of study to students from Central and Eastern Europe, mainly Poland, but also Ukraine, Russia, and the Czech Republic, with the result that it now has the largest percentage of foreign students of any German university, including over a thousand students from Poland alone. Building this bridge through teaching and research has become the special mission, the special profile of the Viadrina, and it is imperative that its limited resources be geared to sustaining this profile as much as possible. It does not work perfectly by any means, but those projects that do conform to this profile, and particularly to our cooperation with Poland through the Collegium Polonicum on the other side of the Oder river, have a priority claim on the university's resources, especially those resources that we receive from the European Union (EU).

### **3.8. Funds and fiefdoms: The internal distribution of resources**

In talking earlier about the level where funding decisions are made in the relationship between the state and the individual university, I have spoken of a contractual kind of agreement by which institutional goals and priorities become the basis for a funding formula and a funding commitment by the state. At the next stage of the allocation process, the distribution of resources inside an institution, we face a similar problem, but with somewhat different players (see on this also Johnes 1999). The problem is exacerbated at this level by the existence of what I have called "fiefdoms" inside the university – professorships, institutes, chairs – that have a tendency to insist on the retention of previous funding commitments (invoking the principle of "Besitzstandswahrung" or preservation of acquired property rights), and to watch carefully over the

maintenance of parity in the allocation of resources. Here, as at the level of resource allocation to entire institutions, the only answer to the problem seems to lie in carefully negotiated agreements in which the level of funding is a function of the recipient's responsibilities and performance. Those agreements are not easy to obtain, but they are easier to obtain if the agreement is openly and transparently negotiated so that, for every participant in the process looking at every other participant, the correspondence between performance and load parameters and funding commitments are understandable. Without that kind of transparency, there is very little chance to succeed in the effort to make the allocation of resources more performance-oriented.

#### **4. Conclusion**

Let me conclude by taking up once more the question of what all the talk about a stronger role of the market in higher education really means. Is it just some fashionable rhetoric designed to mobilize the legitimating (or at least fundraising) potential of corporate and managerial jargon? Or do we see, in this invocation of market models, a genuine change in policy in the direction of giving universities greater autonomy so they can compete more freely and aggressively in the markets for good students, good faculty, and good research funding? Or are we indeed on the threshold of a new paradigm of higher education, where Adam Smith finally catches up with Max Weber, and where the virtual monopoly of state authority over higher education is giving way to an accountable, but essentially autonomous model of higher education?

At first sight, one is tempted to conclude from this review of changes in financing: a little of all of the above. If indeed financing can serve as a crucial indicator, a bellwether for how serious systems of higher education are about their transition to market models, then this little review has shown that a beginning has certainly been made, that it's not all rhetoric, but also that there are still some major problems ahead, especially with regard to restructuring patterns of governance in accordance with the new modes of financing.

In one of the early and very influential contributions to thinking about markets in the context of making policy in modern democracies, Charles Lindblom (in his 1977 book on "Politics and Markets") has a number of interesting things to say, including this:

A market is like a tool; designed to do certain jobs but unsuited for others. Not wholly familiar with what it can do, people often leave it in the drawer when they could use it. But then they also use it when they should not, like an amateur craftsman who carelessly uses his chisel as a screwdriver. (76)

That's about where we are in the reform discourse in European higher education: still trying to figure out what exactly to do with this powerful, but also somewhat risky tool, "the market".

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