

Profitable Universities

University students will get a better education if they pay very high tuition fees.

By Edwin G. West

Frustration with the inadequate performance of higher-education institutions is centuries old. In 1776, Adam Smith wrote: "In general, the richest and best endowed universities have been the slowest in adopting ... improvements." Having attended the particularly heavily-endowed Oxford University, he spoke from bitter experience.

Smith makes almost exactly the same complaint as the 1985 Macdonald Commission, namely that innovative ideas and initiatives tend to come from outside the university sector. But Smith goes further.

He offers what can be interpreted as a testable hypothesis: beyond some point, the higher the level of endowment (subsidy) to any university, the lower its efficiency. This hypothesis can reasonably be reworded as follows: The greater the share of the student/customers' tuition fees in the total revenues of a university, the greater its efficiency.

Smith's reasoning can best be understood by considering the consequences of introducing a policy of supplying groceries free of charge to customers while the grocers receive payment from the taxpayers via government.

Families in such circumstances are not likely to receive their accustomed quality of service from their grocer/suppliers since the latter's incomes are now derived independently of their efforts.

According to Smith, "The endowments of schools and colleges have diminished more or less the necessity of application in the teachers. Their subsistence, so far as it arises from their salaries, is evidently derived from a fund altogether independent of their success and reputation in their particular professions."

From such remarks and others in Smith's *Wealth of Nations*, we shall assume the following 'Adam Smith test': the threshold of tolerable efficiency is reached when the share of student fees in the total operating costs of universities rises to at least 50%.

As long as tuition fees remain well below one-half of total costs, the threat that a student may withdraw his or her custom from a university will not create enormous injury to the university. This means that only relatively weak attempts will be made to meet the preferences of the student consumers.

The absence of adequate incentives to meet the ongoing and changing preferences of students is of more consequence than would appear at first sight.

This consideration is one source of the inefficiency and high cost in the university system, namely the excessive length of time that many students are often forced to take to obtain first degrees or diplomas. The problem is widespread, not only in Canada, but throughout the world.

Since the main cost of education is that of students' foregone earnings, it might be predicted that private universities would be especially motivated to economize on students' time. Casual support for this proposition appears in Britain where the new private University of Buckingham now operates four terms a year and offers two-year degrees.

More systematic evidence of the better incentive of private universities to economize on students' time has been available for some time. In 1981, a comparison of 20 private and 21 public universities revealed that, for example, it takes nearly 50% more time for PhDs to graduate in public than in private universities.

And when we notice that Canadian PhD graduates require a median of five years to complete and social science students take six years, the scope for improvement in productivity bears very careful consideration.

The fact is, after all, that if changes can be made to enable students to complete their degree in 50% to 75% of the usual time, costs will be dramatically lowered, especially when we take into account the reduction of the students' foregone earnings while at university.

The DeVry Institutes are a striking example of a for-profit organization in higher education. About 27,000 high school graduates are now attending one of DeVry's 23 campuses in the US and Canada, pursuing associate and bachelor of science degrees. (Ontario students must take the last four months of degree programs outside the province.)

Operating in Ontario for more than 45 years, throughout this time DeVry has been entirely independent of tax subsidies and private donors. It clearly passes the Adam Smith test since student tuition fees amount to over 90% of total revenues.

DeVry has an edge over other institutions in its excellent record of job placement. Employers like TD Canada Trust, Celestica Inc., Motorola Cellular, AT&T Canada, and Bell Canada work closely with DeVry faculty to help shape the curriculum. Ninety per cent of DeVry graduates have jobs in their field within six months of graduation.

Far from resisting innovation, DeVry makes a concerted effort to help its students prepare for careers by keeping pace with the rapid changes continually taking place.

DeVry's director of graduate placement in Toronto explains: "We are continuously trying to stay abreast of emerging industries and their technologies. This is to ensure that our graduates are hired by leading-edge organizations where they can utilize the technical skills acquired during their studies at DeVry."

The evidence shows that for-profit higher education institutions can deliver better courses at much less cost than public institutions. It is easy to predict that this sector will play an important part in the future.

(Adapted with permission from "Reforming the Universities," a much longer paper published by the Atlantic Institute for Market Studies. www.aims.ca. The late Dr. West was Professor Emeritus at Carleton University.)