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Schools: make a 'club good' better

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 [Joshua Gans](#)

Last week Mark Latham put school funding on the election agenda. What was refreshing about this was that he was not afraid to identify losers. Indeed, my household is fortunate enough in life to be one of them. This is a necessary first step to achieving real reform and, as such, it is timely to take a look at what is really at the heart of the economics of all this.

There are many reasons put forward to justify extensive government regulation and intervention in the education process. These range from the standard claim that private choice and provision would lead to insufficient education levels to achieve social and economic goals to notions of equity and fairness in access to educational attainment. Such factors clearly have an impact on policy. But as Stephen King and I argue in our new book, *Finishing the Job*, what is unique about education is its "production process".

Put simply, education is not a traditional public good; that is, one that is non-rival (all can consume it) or non-excludable (it is hard to stop them anyway). While a classroom and teacher can handle a given number of students, this is only up to a point. So education is only partially non-rival. This stands in contrast to, say, defence, where a significant addition to the population of Australia would not necessarily entail an explosion in our defence budget.

In addition, education is excludable. A school can simultaneously provide education and deny access to its benefits to anyone. For defence, in contrast, protecting some Australians means protecting them all.

The best description of education's production process is that it is a club good. In a classroom, all students (nominally) consume the same product, but that classroom's size can be limited by its membership rules. As such, it involves similarities to movie theatres, sports stadiums and gyms.

So how does the club-good nature of education sit with extensive

government involvement? Why, in a world where students/parents have different preferences over education levels and styles, can't the market

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sort them into schools the way it sorts moviegoers into theatres?

For one, simple equity and efficiency grounds demand that all students have access to education. The market will place a price on anything that is costly to do and, for education, that price may significantly exceed each household's ability to pay. Moreover, because it is a club, the club will set its price based on the demands of its members. If you happen to be in an area where all the schools are costly, you may be out in the cold. For this reason, a school's fees cannot be the guiding instrument of access, as it would be for other club goods.

But herein lies a key issue: without fees to moderate access, free-riding rears its ugly head. So, even if many households want to pay for more educational services in their school, there is no means of making this compulsory. And there is no mechanism to allow those additional services to be provided, even if many households want and are willing to pay for them. Thus, the government faces a conflict: by guaranteeing access it thwarts attempts by school communities to manage schools according to the preferences of their members.

This same tension drives government policy with regard to health care and housing. In those cases it deals with it by subsidising low-income households to a minimum acceptable level, while letting everyone consume more if they choose.

The club-good nature of education prevents this same solution. Consider a direct allowance to all students to ensure they consume the minimum acceptable education level. To be effective, students need to be able to use that allowance to purchase education. However, if their school community decides additional fees need to be paid in order to meet their own educational desires, some students may be left out. Hence, the allowance would need to be combined with restrictions on compulsory fees, whether it be blanket prohibitions, a minimum number of fee-free places or designation of some schools in each area that are fee-free.

While the model differs in many countries, Australian states have gone for a policy whereby government-owned schools are fee-free. But with this has come an additional restriction in terms of standardisation of those schools on the basis of a common curriculum. As such, there is little scope to match school style with diverse preferences.

In a world of clubs, these are very stringent conditions. Why should only government-owned schools be fee-free? Any private school that agreed not to charge additional fees could surely be a candidate for this. Indeed, this occurs in the United Kingdom. Moreover, this would open up the possibility that fee-free schools might choose different educational styles based on the preferences of their local community.

Given this, how might we rethink education funding? For starters, it is useful to remember that our desire for access is at the student level. So any universal allowance would naturally be tied to a student rather than a school. Any registered school - public or private - could receive a student's allowance. This is all one would need to ensure access to minimum educational standards.

This would also allow another possibility: income testing of allowances. At the moment, we achieve this by relying on high-income households to opt out of the public system. However, this same outcome could be more directly achieved by tying the allowance level to income level. Students from higher-income households would be associated with a lower

allowance.

What about the tension between fees and access? After all, if fees exceed the allowance, access will become an issue. One simple option is our present one of having an "opt-out" rule. Schools whose fees exceed the minimum allowance would lose that allowance completely. Such toughness would break the trade-off but at the cost of severely restricting parent/student choice.

A softer approach would be to tie the allowance to the fee policy of schools. A school with no additional fees or with a certain number of fee-free places could receive the full allowance, while those with fees would receive a reduced allowance. This would effectively amount to a tax on the improvements a school may wish to put in place but, compared with the system now, at least schools would have that option.

Surely, if education funding is back on the agenda, it is worth being innovative and rethinking all our current preconceptions.

• *Joshua Gans is professor of management (information economics) at the Melbourne Business School, University of Melbourne. Finishing the Job: Real World Policy Solutions in Housing, Health, Education and Transport is published by Melbourne University Publishing.*

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