

# Policy Analysis

No. 720

February 5, 2013

## *Liberalizing Cross-Border Trade in Higher Education The Coming Revolution of Online Universities*

by Simon Lester

### Executive Summary

Recent developments in higher education, with leading institutions starting to offer courses online, suggest that the Internet is going to disrupt this industry, just as it has already disrupted the music and book industries and many others. We are entering a period of experimentation with new business models for higher education, with MOOCs (massive open online courses) the most prominent among these. At this early stage, it is not clear what the final product will look like. But regardless of the specific form the new industry will take, there is likely to be more competition, lower costs, and higher quality. This is great news for consumers of higher education.

However, some existing institutions may fare badly in this transition and are likely to call for government support. This would happen even if higher education were exclusively a national market. But demands for government protection will be even stronger where foreign online competition is hurting traditional domestic institutions. With education now moving online, it has become tradable across borders like never before. Until now, trade in education was fairly small in scope, limited mostly to students

studying abroad and a few foreign branch campuses. The growth of online education will make international trade in higher education services far more common. And in response to this increasing trade, there are likely to be complaints about the impact of foreign competition on domestic institutions.

We must resist these calls for protection. The great beneficiaries of the coming online revolution in higher education are people all around the world looking for access to better educational opportunities. We should embrace this new period of innovation in higher education, not try to hold it off.

One way to promote free trade in higher education is with international trade agreements. Through these agreements, governments can make commitments not to discriminate against foreign online higher education programs. The past few decades have seen great progress in bringing down tariffs and other protectionist trade barriers through trade agreements. In order to bring the benefits of international competition to an important sector of the global economy, we should apply that same model to trade in higher education services.

---

*Simon Lester is a trade policy analyst at the Cato Institute's Herbert A. Stiefel Center for Trade Policy Studies.*

**After centuries of being mainly a domestic service, education is now tradable across borders in a way that it never has been before.**

## **Introduction**

In recent years, higher education has become increasingly globalized. More and more, students obtain degrees from foreign universities, professors teach outside of their home countries, and universities open branch campuses abroad.<sup>1</sup> In many ways, the education system is beginning to look like other industries, in which transnational companies are the norm. Nevertheless, higher education continues to be significantly national in character, as most students still attend local colleges and universities in their home countries, often fairly close to where they were raised.<sup>2</sup> For the most part, despite recent trends toward more internationalism, supply and consumption of higher education services is a national affair, with domestic provision of education services dwarfing any international trade in these services.

Online education is likely to change this. Many top universities have begun to offer their courses for free over the Internet, and the day when high-quality degrees can be obtained online at reasonable prices, from both domestic and foreign providers, seems to be drawing nearer. After centuries of being mainly a domestic service, education is now tradable across borders in a way that it never has been before.

All of this is great news for consumers of education. The lack of international competition in this sector has almost certainly led to higher prices and lower quality than would be seen in a more competitive industry.<sup>3</sup> As a comparison, there is little doubt that U.S. consumers of automobiles are much better off as a result of the influx of cars from Europe, Japan, and Korea over the years.

But there is a lurking problem: This new trade will be extremely disruptive, and as foreign competition with traditionally domestic institutions grows, the conditions are ripe for protectionism. Experience in other industries suggests that one response to online education is likely to be calls for “protection” from new foreign competitors. And given the extensive regulation and governmental role

in the education sector, it may be relatively easy for governments to interfere with foreign online universities under the guise of normal regulation.<sup>4</sup>

This paper argues that the coming revolution of cross-border trade in education has enormous benefits, and governments should resist protectionist demands that will slow progress. The emergence of more opportunities for trade in higher education should not be undermined by protectionist trade barriers. In this regard, international trade law can help to ensure that there is free trade in higher education: Governments should agree now on international rules to liberalize trade in online higher education services in order to prevent protection from rising up even before the online education industry has a chance to start.

Previous efforts to liberalize higher education were undertaken at the start of the Doha Round of negotiations at the World Trade Organization (WTO). But little progress was made, and the Round itself eventually went dormant. However, trade talks on services are currently underway as part of the Trans Pacific Partnership talks and through a new initiative at the WTO. Given the important changes going on in online education, this is the perfect time to push for free trade rules in this area.

## **The Traditional Higher Education Model**

Most people reading this paper have some experience with higher education. They have almost certainly been to college and probably have a graduate degree of some kind (and possibly multiple degrees). As a result, readers will have a good sense of what this experience involves.

During the middle ages, the higher education sector enjoyed a relatively high level of international mobility. This was due to a number of factors: There were only a few universities, so aspiring scholars had to travel in order to attend; there were special privileges for traveling scholars; and finan-

cial assistance was available, sometimes in the form of food and lodging.<sup>5</sup>

Over time, though, as educational opportunities expanded and university attendance became more common, certain patterns and habits developed. For many, if not most, people, college became simply another step in the development and learning process. It was usually done nearby, and it “bundled” several different features together: (1) the curriculum, involving “mastery of specific knowledge and development of more general reasoning, analytical, and communication skills”; (2) a network of friends, contacts, and experience gained from various activities; (3) the “signaling process” of attending a prestigious college; and (4) the “college experience.”<sup>6</sup> Together, this bundle of components is what college students (and their parents) pay for.

This experience takes place in a “bricks and mortar” setting. The particular character of the buildings may vary. It may be near a bucolic countryside, or it may be in an urban high-rise. But higher education usually means spending considerable time in a specific location, in close physical proximity to fellow students and professors.

One characteristic of this traditional model is that it is not easily tradable across borders. To be sure, students can study abroad, teachers can teach abroad, and colleges can set up foreign campuses. But these possibilities remain the exception, rather than the norm. The higher education experience is primarily national in nature. This is largely due to language and cultural barriers, as well as a desire to maintain physical proximity to family and friends.

The lack of international trade in these services has some unfortunate consequences, including rising prices and lower quality than would otherwise be the case. Comparing the price levels of tradable goods and nontradable services offers a stark contrast. Over the past 10 years, easily tradable goods have seen prices fall considerably. By contrast, for difficult-to-trade services, prices have gone up a lot. For example, television prices have fallen by 74 percent and toys by 36.8 percent. But hospital ser-

vices have gone up by 68 percent and college tuition and fees by 73.2 percent.<sup>7</sup> The absence of trade is not the only cause of higher prices, of course, but it is almost certainly a factor. Unlike in many industries, higher education institutions have not faced significant competition from foreign entities, and this lack of competition has had a clear impact on prices.

Quality is harder to measure than price, but our experience with goods indicates that trade improves quality as well. An obvious example is the auto industry, in which imports to the United States have long set the standard for quality and pushed the domestic industry to improve. There are many reports that American college graduates are not receiving adequate training through higher education.<sup>8</sup> More international competition would almost certainly lead to higher quality in the education sector.

The traditional model has also come under increasing criticism in recent years. In 2006, then-U.S. secretary of education Margaret Spellings said the following:

American higher education has become what, in the business world, would be called a mature enterprise: increasingly risk-averse, at times self-satisfied, and unduly expensive. It is an enterprise that has yet to address the fundamental issues of how academic programs and institutions must be transformed to serve the changing educational needs of a knowledge economy. It has yet to successfully confront the impact of globalization, rapidly evolving technologies, an increasingly diverse and aging population, and an evolving marketplace characterized by new needs and paradigms.

History is littered with examples of industries that, at their peril, failed to respond—or even to notice—changes in the world around them, from railroads to steel manufacturers. Without serious self-examination and reform, institutions of higher education risk falling into the same trap, seeing their

**More international competition would almost certainly lead to higher quality in the education sector.**

market share substantially reduced and their services increasingly characterized by obsolescence.<sup>9</sup>

Secretary Spellings was approaching this problem from the perspective of a government official, and her recommendations mainly involved federal government action. But beyond the federal government's role, there is the role of the educational institutions themselves. In that regard, one of the biggest problems with higher education is its slow response to the emergence of the Internet. That may be about to change.

## The Beginnings of an Online Higher Education Boom

While the potential of the Internet to transform higher education was recognized many years ago,<sup>10</sup> the full impact is only just starting to be realized. Recently, there has been a push by many top universities, as well as some new entrants, to make high-quality online education a reality.

Many traditional colleges have offered Web-based courses for years now, and a number of for-profit institutions offer online degrees. The rise of the "virtual university" was described by the WTO secretariat as far back as 1998.<sup>11</sup> But so far, the traditional higher education model has not been greatly affected by this "potentially disruptive online technology,"<sup>12</sup> as "many young college students still seek the assurance of traditional university names and the benefits of campus life."<sup>13</sup>

But recently, top-tier research universities have begun to enter the field with great fanfare, in collaboration with several for-profit and nonprofit companies. The massive open online courses (MOOCs) they are offering are free and are expected to be used by millions of people around the world. This development could bring credibility to a service that some might previously have looked at with skepticism. U.S. universities such as Stanford,

Harvard, and MIT are at the forefront of this movement, but foreign universities are involved as well.

For now, taking MOOCs does not confer an actual degree. You cannot simply enroll in Stanford's online free courses and receive a Stanford diploma. But some in the industry predict that eventually students may be able to earn a certificate that serves the same function as a traditional diploma.<sup>14</sup> Some schools already say they will offer college credit for these courses.<sup>15</sup> Stanford's president notes that one day students may be able to use these courses to get actual degrees from Stanford without having to pay for it.<sup>16</sup> And the American Council on Education and Coursera, a leading provider of MOOCs, recently announced a "pilot project" to determine whether some free online courses should be eligible for credit.<sup>17</sup>

In addition, some people are beginning to experiment with new models. One example is the Minerva Project, which aims to provide Ivy League-quality education at significantly lower prices. Both the students' and professors' experiences will be much different than today's norm. Students will be encouraged to live in "dorm clusters" around the world, moving between cities during their studies. This will allow students to experience some of the traditional aspects of a college education that would not be available through purely online studies done from home. As for professors, rather than a full-time faculty, top academics will be "borrowed" from universities around the world to create courses. Students will be assessed in live online tutorials and study groups.<sup>18</sup>

Recalling the description of the various "bundled" features of higher education, we can see how different aspects will be affected differently by the arrival of online learning. The curriculum is the most vulnerable to disruption from the Internet. Offering lectures, practice problems, and assessment online is fairly easy. By contrast, the other features are affected differently, as much of the college experience comes from friendships and other connections.<sup>19</sup> The Minerva Project seems to

**One of the biggest problems with higher education is its slow response to the emergence of the Internet. That may be about to change.**

be attempting to replicate these other parts by offering students opportunities to live and study together in groups. Other universities are likely to develop a variety of alternative approaches.

Within the curriculum, there are also two separate functions of a college course: the transfer of knowledge, and evaluation and feedback. With MOOCs, the transfer of knowledge has undergone a “great leap forward.” Evaluation and feedback has not progressed as much. That is not likely to last, however, as new methods are being developed to provide them, and online education may soon surpass what can be done in the traditional model in many ways. Online interaction offers advantages over face-to-face contact, in terms of ease of access, convenience, and technical tools.<sup>20</sup>

It is even possible that some day obtaining a “degree” will no longer be important. Students could take classes from various institutions and present their educational experience to potential employers as simply the conglomeration of their coursework. If a student has studied advanced mathematics through courses from MIT, economics through Stanford, and computer science at the online startup Udacity, and can demonstrate that knowledge, obtaining a job might be possible on that basis alone.

It is too early to tell which models will work best. We are in a period of experimentation, and these and other models will be tested. We have all become accustomed to a certain way of doing things, and thus it is hard to imagine a different way. Education entrepreneurs and future generations of students will figure out what is most desirable, as sellers and buyers in the higher education market.

As has been the case with other Internet services, we are likely to see many successes and failures within the field’s overall evolution. The winners will be determined by the market. High quality, low price, and innovation will be rewarded with consumer demand.

But regardless of which models and which entities come out on top, the impact on existing institutions will be significant. Arnold

Kling writes, “Traditional colleges seem poised to be the Borders Books of the next round of technological change.”<sup>21</sup> And David Brooks notes, “What happened to the newspaper and magazine business is about to happen to higher education: a rescrambling around the Web.”<sup>22</sup> Many longstanding, well-respected colleges and universities may eventually disappear from the education map. This will not happen overnight, but eventually the ability to experience a top-quality education at an extremely low price could fundamentally change the current system.

### **Free Trade in Online Education and the Lurking Threat of Protectionism**

Beyond the general impact on traditional higher education, the growth of online courses will transform trade in education. Until now, there have been high natural barriers to trade in education services. As a result, most people studied near where they grew up.

But now the barriers have fallen. Education from foreign suppliers will be as accessible as that from traditional domestic suppliers: you can study from home. Moreover, people will have access to higher-quality services. Instead of being stuck with the local college, students will be able to choose from the best education suppliers around the world. Education will become tradable like never before.

One company that is at the forefront of the recent online education initiatives, Coursera, reports that two thirds of those taking its classes are from outside the United States.<sup>23</sup> The appeal is obvious. As one Indian engineering student put it, “I never imagined that I would be taught by professors from MIT, let alone for free.”<sup>24</sup> While we are only at the beginning stages, and the industry structure has yet to develop, it is easy to imagine a world in the not-so-distant future where online higher education is the norm, and large numbers of people consume

**Instead of being stuck with the local college, students will be able to choose from the best education suppliers around the world.**

**There is a lurking problem: This new trade will be extremely disruptive, and as foreign competition with traditionally domestic institutions grows, the conditions will be ripe for protectionism.**

education services supplied from abroad. It may take a little time before online education can match what traditional education offers, but that time is coming soon, especially with top U.S. universities entering the field and talk of students being able to earn certificates or actual degrees online.

All of this is great news for consumers of education. But there is a lurking problem: This new trade will be extremely disruptive, and as foreign competition with traditionally domestic institutions grows, the conditions will be ripe for protectionism. Many institutions will be troubled by competition from online *domestic* sources as well, but the existence of *foreign* online competition will be an even more sensitive issue politically. This will almost certainly lead to calls for protection.<sup>25</sup>

What might trade barriers in this area look like? While we are at an early stage, and any discussion is necessarily a bit speculative, there are already some concrete examples. First, Coursera has already faced obstacles *within the United States*. The state of Minnesota recently informed Coursera that it could not provide free online courses without first obtaining government permission and paying a fee.<sup>26</sup> In response to a backlash, Minnesota quickly clarified that this rule does not apply to free, not-for-credit courses,<sup>27</sup> but such a restriction still applies to courses that go toward a degree. If an online university operating worldwide is required to get permission from all of the subnational government entities around the world, the administrative cost would be quite high—significantly higher than that of a traditional institution serving one area only.

A second example comes from the area of legal education. In Singapore, with regard to sitting for the bar, only a limited number of foreign law schools have been officially recognized. Singaporeans can study at any foreign law school, of course, but only a degree from the eligible schools will allow someone to be admitted to the bar.<sup>28</sup> Accreditation bodies in other fields present similar barriers to foreign online education.

Speaking more generally, Aik Hoe Lim and Raymond Saner cite a number of possible examples of barriers to trade in education services: “restrictions on the electronic transmission of course material,” restrictions on “the use/import of educational materials,” “non-recognition of qualifications obtained through distance learning,” “quotas or economic needs tests restricting the number of suppliers,” “restrictions on payments and transfer of funds abroad,” “discriminatory local accreditation and recognition requirements,” “restrictions on the types of courses that may be offered,” and “measures requiring the use of a local partner or the physical presence of the foreign institution.”<sup>29</sup> They also note:

Arguably, more important than these formal trade barriers are recognition issues. In some economies, cross-border distance education programmes cannot obtain formal approval to grant degrees or other qualifications that are locally recognized without local presence.<sup>30</sup>

## **The Existing International Legal Framework for Trade in Services**

To combat trade barriers like these, it is worth talking now about establishing international rules to limit protectionism in this area. The legal framework for international trade in higher education services is complicated by a number of factors:

- There are multiple international agreements, some multilateral, some regional, some bilateral.
- There are two competing approaches to making commitments to liberalize trade in services—“positive list” and “negative list” (see below).
- Barriers to trade in services are often regulatory in nature, unlike trade in goods, where border measures are the most common barriers.

- Trade in services is more complex than trade in goods, as it is carried out through four “modes of supply.”

This section explores each of these issues.

### **The International Agreements That Cover Trade in Services**

The liberalization of international trade in services is governed by the services chapters of international trade agreements. The most comprehensive global set of rules is set out in the General Agreement on Trade in Services (or GATS, one of the WTO agreements).

There are also a growing number of bilateral and regional trade agreements that address services issues. As WTO talks have stalled, international trade negotiations have focused on smaller groupings of countries. Whether this approach makes sense in terms of economics is questionable, but political forces have pushed in this direction.

### **Positive and Negative List Approaches to Making Services Liberalization Commitments**

Trade in services rules take one of two approaches. If based on a “positive” list, only those service sectors where governments make explicit commitments to liberalize are covered. A schedule of commitments is annexed to the agreement. The GATS follows this model.

By contrast, if based on a “negative” list, all services will be liberalized unless specifically carved out. The general rule is that all sectors are liberalized, but “nonconforming measures” are set out in special annexes, describing limitations on liberalization of specific sectors. Recent U.S. bilateral free trade agreements (FTAs) use this approach.

The different types of commitments can be illustrated as follows. As noted, GATS commitments are made on a sector-by-sector basis, based on offers made by governments. Liberalization only takes place if governments agree to it (the “positive” list approach). One of these sectors is education services. Thus, the existing GATS rules apply to education

services, but only to the extent that commitments have been made. If countries have made no commitments, they can be as protectionist as they choose to be. Some governments made GATS commitments to liberalize trade in higher education services as part of the Uruguay Round of trade negotiations, which ran from 1986 to 1993. According to a 1998 WTO secretariat study, 21 countries had made commitments to liberalize higher education.<sup>31</sup> Since then, 21 more countries made commitments when they acceded to the WTO, for a total of 42.<sup>32</sup>

In FTAs, the commitments on education services vary. Reviewing the commitments that pertain to cross-border trade in these services can be a challenge. Uncertainty remains in some cases as to just what has been committed.

To provide a sample of what has been negotiated, I examine a few of the commitments in FTAs signed by Australia, New Zealand, and the United States—three countries that have pushed for liberalization in this area.

Starting with Australia and New Zealand, one FTA these two nations have in common is an agreement with the countries belonging to the Association of Southeast Asian Nations. In this agreement, which is based on the positive list approach, Australia and New Zealand both made a full liberalization commitment. By contrast, most of their FTA counterparts have not done so: The Philippines, Singapore, Thailand, and Vietnam have not made a commitment; and Malaysia has made only a partial commitment.

Similarly, in the New Zealand-China FTA, New Zealand has made a full commitment, while China has made no commitment.

In the Australia-Chile FTA, where a negative list was used, a side letter on education services makes clear that Australian educational institutions are to maintain “autonomy in admissions policies,” may use nondiscriminatory accreditation procedures, and can continue the practice of government subsidies and grants. The Australia-U.S. FTA includes an exchange of side letters along these lines as well.

**The liberalization of international trade in services is governed by the services chapters of international trade agreements.**

**The substantive obligations of the GATS can be more complicated than those for trade in goods.**

Many of these commitments leave some doubt as to exactly how they apply to the complexities of the regulation of higher education services. While the impact of having no commitment is clear, partial and even full commitments do not answer all the questions that may arise about whether specific government actions in the sector comply with the rules.

**Addressing the Regulatory Barriers to Trade in Services**

Liberalizing trade in goods is easier than dealing with trade in services. Goods often face border measures, such as tariffs and quotas, which are simpler to track and to control. By contrast, the services sector faces regulations that are often extremely complex. As a result, the substantive obligations of the GATS can be more complicated than those for trade in goods.

In terms of the rules of the GATS and other FTAs, the key obligations are as follows. First, in the GATS, there are two types of commitments that members may make: market access (Article XVI) and national treatment (XVII). National treatment is a basic nondiscrimination requirement and does not differ considerably from the similar requirement in trade in goods. In essence, it covers discrimination against foreign suppliers and services that is explicit in a law or regulation, as well as discrimination that is implicit (i.e., the treatment is formally identical, but nevertheless “modifies the conditions of competition” in favor of domestic services or service suppliers).

Market access is more complex. The term is defined in the GATS with reference to specific types of measures, such as “limitations on the number of service suppliers whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirements of an economic needs test.”<sup>33</sup> In a sense, the provision simply defines “market access” through the examples it sets out; it does not provide a general definition or standard for the term. In the education sector, government dictated accreditation policies could be implicated under several of the items listed. For example, such measures may limit the number of suppliers.

Beyond these liberalization commitments, there are also some general rules that apply regardless of whether countries have made commitments. In this regard, Article VI of the GATS covers “Domestic Regulation.” Unlike trade in goods, where tariffs and quotas are the dominant form of protectionism, barriers to trade in services usually come from regulatory measures. Thus, domestic regulations are of particular importance in service sectors, and trade liberalization in services needs to take this into account.

The full scope of Article VI is not clear, as there is limited jurisprudence, but it has potentially broad implications. Paragraph 1 states: “In sectors where specific commitments are undertaken, each Member shall ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner.” Terms such as “reasonable, objective and impartial” lead to a potentially wide scope for international disciplines on measures in the services sector.

In addition, paragraph 4 says that certain types of services regulations should be subject to more general disciplines to be developed by the Council for Trade in Services:

With a view to ensuring that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services, the Council for Trade in Services shall, through appropriate bodies it may establish, develop any necessary disciplines. Such disciplines shall aim to ensure that such requirements are, inter alia:

- (a) based on objective and transparent criteria, such as competence and the ability to supply the service;
- (b) not more burdensome than necessary to ensure the quality of the service;
- (c) in the case of licensing procedures, not in themselves a restriction on the supply of the service.



So far, such disciplines have only been developed in the accounting sector, and these standards have not really been tested. But these obligations—for example, that services regulations not be “more burdensome than necessary to ensure the quality of the service”—could have an impact on the extensive domestic regulation in the education sector.

### **Trade in Services: Modes of Supply**

Due to the nature of services, international trade in services is very different from trade in goods. All trade in goods crosses borders; this is not always the case for trade in services. As a result, trade in services is conceptually more difficult to understand than trade in goods. GATS Article I:2 sets out four modes of supply for trade in services. To explain more precisely how trade rules in services work, let’s look at the ways trade in education services might occur under these four modes.<sup>34</sup>

As noted, there has always been some small amount of trade in education services. Studying abroad for a semester or two is a fairly common practice, and some people attend foreign universities for all of their higher education. In the language of international trade in services rules, this is known as the supply of a service “in the territory of one Member to the service consumer of any other Member,” or “consumption abroad.” This is the second of the four supply modes described in the GATS. Currently, this represents the largest share of international trade in education services.

In addition, a number of universities have set up facilities in foreign countries to offer education services to foreign customers. This can be done through local branch or satellite campuses, “twinning” partnerships, or franchising arrangements with local institutions. The services rules refer to this as the supply of a service “by a service supplier of one Member, through commercial presence in the territory of any other Member.” This is mode three.

Trade through online education, the focus of this paper, will take place in a more traditional way (i.e., the way goods are traded), through cross-border supply. This is mode one. The services rules describe this as “from

the territory of one Member into the territory of any other Member.” There have long been forms of “distance learning,” but the Internet has expanded the possibilities considerably. In terms of the commitments made under this mode, 27 of 42 of the WTO schedules where commitments on higher education were made contain a full commitment under this mode. Eleven others have partial commitments.<sup>35</sup>

Finally, trade can also be carried out “by a service supplier of one Member, through presence of natural persons of a Member in the territory of any other Member.” This is mode four. This type of trade is sort of like a limited version of the “commercial presence” mode, where teachers or schools offer short-term courses in foreign countries (e.g., by running a summer program in a foreign country).

## **Negotiating New Services Commitments for Cross-Border Trade in Higher Education**

There are two problems with the existing GATS rules on trade in education services. First, most countries have no commitments. Thus, actual liberalization in this sector is minimal. And second, the commitments and rules were developed in the late 1980s and early 1990s. At that time, there was little if any thought given to how the internet would change the supply of certain services. The *U.S.–Gambling* WTO dispute illustrates the difficulty of applying 1980s treaty language to online issues. Governments now need to develop clear rules and commitments related specifically to cross-border trade in online higher education services.

In this regard, a basic, full commitment may only be a start. Due to the complexity of the sector, what is really needed is something along the lines of a Higher Education Services Annex to set out special rules for the sector. In large part, this need arises due to the extensive role of the government in this area, as discussed in the next section. Simply

**Governments now need to develop clear rules and commitments related specifically to cross-border trade in online higher education services.**

**There is great potential for new trade liberalization in education services that goes beyond existing commitments.**

making a full commitment would leave a great deal of uncertainty as to whether particular government actions in the higher education sector constitute a protectionist trade barrier.

With regard to existing FTA commitments, as with the GATS, many countries have made no commitments yet. And for some commitments that have been made, the full scope in relation to cross-border supply of education is somewhat unclear.

As a result of these deficiencies, there is great potential for new trade liberalization in education services that goes beyond existing commitments. Several past and present efforts in this regard are worth noting.

In 2001 the WTO membership formally launched the Doha Round of negotiations, but talks had been going on even before that. With regard to education services, in December 2000, the United States submitted a communication on higher education, adult education, and training, in which it explained:

The purpose of this proposal is to help create conditions favorable to suppliers of higher education, adult education, and training services by removing and reducing obstacles to the transmission of such services across national borders through electronic or physical means, or to the establishment and operation of facilities (schools, classrooms or offices) to provide services to students in their home country or abroad.<sup>36</sup>

In June 2001, October 2001, and March 2002, New Zealand,<sup>37</sup> Australia,<sup>38</sup> and Japan<sup>39</sup> respectively made negotiating proposals on education services. The United States then made an initial offer to liberalize its own market in March of 2003 and revised it in 2005.<sup>40</sup> However, the Doha Round stalled soon after, and no further progress was made.<sup>41</sup>

At the bilateral and regional level, as noted, U.S. FTAs use a negative list approach to services liberalization, under which services sectors are liberalized unless there is an explicit carve-out. The focus of U.S. FTA negotiations

right now is the Trans Pacific Partnership. While the full details of the negotiations have not been made public, certain countries are pushing for liberalization in the higher education sector.

There is also a recent effort underway among a number of WTO Members to complete a plurilateral “International Services Agreement” within the WTO framework. But discussions are at an early stage; basic principles, such as whether a negative or positive list approach will be used, have not been fully settled, and liberalization offers have not been made yet.<sup>42</sup>

Liberalization of education services could be part of either the WTO or FTA negotiations, or both. The debate over whether to prefer multilateral or bilateral liberalization is an important one, but I do not weigh in on it here. Rather, my argument is simply that cross-border trade in higher education is important and should be pursued.

Before making specific proposals, however, it is necessary to discuss one particular characteristic of higher education: the extensive role of government.

## **The Role of Government in Education Services**

As noted above, the education sector is one in which the government plays a fairly extensive role.<sup>43</sup> This is particularly true at the primary and secondary levels, but it is also the case for higher education. Government involvement, which can take many forms, complicates the goal of trade liberalization.

The strongest form of government involvement comes when the government operates higher education institutions directly. In effect, such entities are state-owned enterprises. Generally speaking, they receive taxpayer funding, maintain low tuition rates for local students (in essence, subsidized by the taxpayer), and give preference in admissions to students from within their territory.

Beyond these state institutions, government involvement can also be seen in subsidies

for education. These subsidies are more likely to exist in a system with expensive, private education, as the money provided is used to offset the high tuition costs of private universities for poor and middle-income students.

And finally, there is the complex role of accreditation. Accreditation is intended to certify the competence of educational institutions and signal a certain level of quality. In the current system, a failure to achieve accreditation makes it difficult for an institution to succeed. Governments are an important player in the process of accreditation, with government agencies sometimes running the accreditation process directly. This process can be questioned on the grounds that the market itself will sort out the high- and low-quality institutions, rewarding high performers and forcing low performers to shut down. Accreditation also has great potential to act as a barrier itself. As will be discussed later, any trade rules in this area need to address this possibility. However, at least in the near future, accreditation is likely to remain an important issue for traditional colleges, and therefore any proposal for liberalized trade in education must take it into account. It remains to be seen how the new online world of education will affect the role of accreditation.

To develop new trade-in-services rules for online education, the governmental role in traditional higher education needs to be taken into account. There are arguments that these aspects of the existing education sector are themselves in need of reform, but such issues are outside the scope of this paper.

As a final point, the extensive role of the government raises an important general question: Are higher education services even covered by the trade-in-services rules? Article I:3(b) of the GATS excludes certain services provided by the government, as follows: services “includes any service in any sector except services supplied in the exercise of governmental authority.” However, Article I:3(c) then states, “a service supplied in the exercise of governmental authority” means any service which is supplied neither on a commercial basis nor in competition with one or more service suppliers.

In most countries, the government is not the sole provider of higher education. There is some private competition, and it is usually provided on somewhat of a commercial basis. Therefore it is reasonable to interpret these provisions as not excluding government-provided higher education.<sup>44</sup>

## A Proposal for Liberalizing Trade in Education Services

With these considerations in mind, here are a few preliminary suggestions on how to develop international trade rules that can help prevent discrimination against foreign online education providers and thus contribute to the liberalization of trade in higher education services:

1. *Treat foreign and domestic online programs alike in accreditation.* One of the keys to allowing online education to grow is to make sure that governments do not undermine foreign online educational offerings by restricting accreditation possibilities for foreign programs. Accrediting agencies, whether public or private, must not discriminate, explicitly or in a disguised manner, against foreign entities. Online education from different countries must be treated in a nondiscriminatory manner, with open transparent regulation. It is fine to have certain general rules that all entities must follow, such as for financial solvency, qualifications of the faculty, or transparency of financial fees. But these criteria cannot be used to favor domestic entities.
2. *Online degrees should be recognized all over the world.* There are great benefits to having online degrees be valid anywhere in the world, both for employment and admission to graduate programs, and the industry should work to make sure this is possible. Accreditation may interfere with this, for example if only accredited universities are recognized for certain purposes. Certain professions—such as

**Online education from different countries must be treated in a nondiscriminatory manner, with open and transparent regulation.**

**Governments can treat online and traditional programs differently. But they cannot use these differences as an excuse to discriminate against foreign competitors.**

law—are particularly likely to see barriers of this sort. Harmonized standards and mutual recognition could be of great value in this regard, and international agreements may help with this process to some extent.<sup>45</sup>

3. *Treat online, traditional, and hybrid programs fairly.* There is no question that traditional higher education and online education differ in important ways. Critics of online education are sure to point out aspects that do not measure up to traditional programs. At the same time, online education offers many things that traditional programs cannot. The differences in these programs may mean that separate processes are used for accreditation of each.

When online education programs begin to offer certificates or degrees that compete with the degrees offered by traditional education, it will be useful to have in place international rules that prevent governments from discriminating against foreign online rivals in favor of traditional domestic institutions. There will be a temptation to discriminate in this way, as some state-run universities will have trouble competing with foreign online rivals.

Governments can treat online and traditional programs differently, of course. But they cannot use these differences as an excuse to discriminate against foreign competitors. To achieve this, standards can be developed that set out clearly how the different types of education should be treated under domestic laws. Any differences cannot be used as a means of disguised protectionism. There may be real concerns with online education. But restrictions on such programs must have a legitimate basis. Some of the GATS Article VI, paragraph 4, rules may be of use in this context.

4. *Subsidies should be for students, not for domestic educational institutions.* It is common for governments to give financial aid to students from lower- and middle-income

families. However, these subsidies should not be used to discriminate against foreign online universities. If the purpose of these programs is to help students, they should be granted regardless of the institution, provided it is a legitimate one.

In its initial negotiating offer as part of the Doha Round, the United States said: “Scholarships and grants may be limited to U.S. citizens and/or U.S. residents of particular states. Tuition rates may vary for in-state and out-of-state residents.”<sup>46</sup> These policies are designed to help students directly, not educational institutions themselves, and are therefore acceptable. The offer further states: “To participate in the U.S. student loan program, foreign institutions established in the United States would need to meet the same requirements as U.S. institutions.” This principle is also fine, if applied equally to foreign and domestic online institutions.

5. *Government-operated online universities.* Government-run educational institutions have traditionally discriminated in favor of state/local residents, through lower tuition rates and preference in admissions. Should this practice continue in the online world?

The notion of educational institutions designed to support local residents may have made sense when they were first created. Mobility was low, so having a nearby college to serve local residents was a reasonable approach. And while it was possible for some students to come from further away, it would have undermined the purpose if nonresidents crowded out local residents, so preference was given to locals. But in the online world, the business model is different. Space limitations are likely to be much less of a concern. The operation is scalable to a greater extent. If student demand grows, offerings can be expanded as well. Thus there is less of a need for local preferences, and perhaps these preferences no longer make sense. However, for political reasons, this may be a difficult change to make.

6. *Autonomy for admissions, tuition, and curriculum policies.* The initial U.S. Doha services offer states: “Nothing in this agreement will interfere with the ability of individual U.S. institutions to maintain autonomy in admissions policies, in setting tuition rates, and in the development of curriculum or course content.” Without taking any position on the merits of these policies, it is important that trade rules do not interfere in these areas. Admissions, curriculum, and tuition policies are not likely to involve discrimination against foreign institutions, and they pursue goals unrelated to trade policy concerns.

As a final point, as noted above, it may be difficult to achieve these goals solely through liberalization commitments. In certain other sectors, special rules have been developed to deal with complex issues (e.g., financial services and telecoms). The particular issues surrounding education may merit similar efforts through an annex devoted to these issues or through a model draft text to be incorporated in members’ schedules.

## Conclusions

A new world of transnational higher education may be upon us. As with many other industries, education is becoming increasingly unmoored from its domestic roots. Education providers already have multiple national affiliations, employ professors of various nationalities, have mini-campuses in multiple cities, and serve students from all over the world. They do so with a mix of having branches in foreign countries; enrolling students from abroad at their various campuses; and, increasingly, through the online provision of education. Although these developments have been underway for a while, universities are now rapidly becoming transnational institutions.

The growth of online higher education is going to be extremely disruptive to the existing industry structure. There will be many

complaints from those with a vested interest in the current system.<sup>47</sup> But just as the music, book, and movie industries have had to do, traditional higher education institutions need to adapt to the online world.

The education sector that emerges will probably be much more diverse in terms of its structure than it is now. Online higher education will involve competition between government-run entities, nonprofit entities, and for-profit entities. It is quite possible that the new market structure will reduce the role of government and lead to significant growth in the presence of for-profit companies.

But those questions are beyond the scope of this paper, which is focused on how to make sure international trade in these services remains free from barriers. With regard to trade, we must not let protectionism hinder what is almost certainly one of the greatest developments in history for education consumers, especially the poor. Hopefully, access to high-quality education will soon be available at reasonable prices to almost everyone in the world. That is not something we need protection from; it is something to celebrate.

## Notes

1. See generally, Ben Wildavsky, *The Great Brain Race* (Princeton, NJ: Princeton University Press, 2010). See also, Aik Hoe Lim and Raymond Saner, “Rethinking Trade in Education Services: A Wake-Up Call for Trade Negotiators,” *Journal of World Trade* 45, no. 5 (2011): 993.

2. It is difficult to find comparable data on the issue, but for some rough numbers, the Organisation of Economic Co-operation and Development (OECD) estimates that in 2009, 3.7 million tertiary students were enrolled outside their country of citizenship (up from 2.1 million in 2000). OECD, “Education at a Glance 2011,” p. 320. The *Chronicle of Higher Education* puts the total number of tertiary students worldwide at about 150 million in 2007. “Data Points: More College Students around the World,” *The Chronicle of Higher Education*, September 18, 2009, <http://chronicle.com/article/Chart-More-College-Students/48516/>.

3. Daniel J. Ikenson, “How Imports Raise Real Incomes,” *Cato at Liberty*, June 9, 2010, <http://www.cato-at-liberty.org/how-imports-raise-real-incomes/>.

**We must not let protectionism hinder what is almost certainly one of the greatest developments in history for education consumers, especially the poor.**

4. As discussed below, the state of Minnesota has already threatened action against free online courses offered by out-of-state universities.
5. Wildavsky, pp. 17–18.
6. Benjamin Lima, “Massive Online Learning and the Unbundling of Undergraduate Education,” *Art Research and Writing*, July 12, 2012, <http://benjaminlima.wordpress.com/2012/07/17/massive-online-learning-and-the-unbundling-of-undergraduate-education/>; Alex Tabarrok, “Why Online Education Works,” *Cato Unbound*, November 12, 2012.
7. Ikenson.
8. “Restoration Drama,” *The Economist*, April 28, 2012, <http://www.economist.com/node/21553476>. (“America’s problem with training was laid bare in a report published last year by Deloitte, a consultancy firm, and the Manufacturing Institute. It identified 600,000 positions that were going unfilled because there were too few qualified skilled workers. Too many colleges, it seems, still fail to align themselves with the needs of local employers, a mismatch that is bad both for the employers and for potential employees, though arguably universities are even worse at doing this.”) “The College-Cost Calamity,” *The Economist*, August 4, 2012, <http://www.economist.com/node/21559936>. (“Jeff Denneen, a Bain consultant, puts it more cautiously. Higher education has not delivered extra value to match the extra costs, he says. Indeed, the average student is studying for fewer hours and learning less than in the past. Grade inflation only partially masks these trends.”)
9. Quoted in Clayton M. Christensen and Henry J. Eyring, *The Innovative University: Changing the DNA of Higher Education from the Inside Out* (John Wiley and Sons, 2011). Kindle Edition, locations 810–12.
10. See, e.g., World Trade Organization (WTO), “Background Note on Education Services,” WTO Document S/C/W/49, September 23, 1998, p. 4.
11. *Ibid.*, pp. 4–5.
12. Christensen and Eyring, Kindle locations 942–43.
13. *Ibid.*, Kindle locations 940–41.
14. Tamar Lewin, “Universities Reshaping Education on the Web,” *New York Times*, July 17, 2012, <http://www.nytimes.com/2012/07/17/education/consortium-of-colleges-takes-online-education-to-new-level.html>.
15. Terence Chea, “MIT for the Masses? Elite Universities Transform Online Education with Free Cyber Courses,” Associated Press, August 10, 2012, <http://finance.yahoo.com/news/elite-colleges-transform-online-higher-124855202.html>.
16. National Public Radio, “Stanford’s Next Lesson: Free Online Courses for Credit and Degrees?” July 20, 2012, <http://www.npr.org/blogs/alltechconsidered/2012/07/23/157132291/stanfords-next-lesson-free-online-courses-for-credit-and-degrees>.
17. Tamar Lewin, “Free Online Courses to Be Evaluated for Possible College Credit,” *New York Times*, November 13, 2012, <http://www.nytimes.com/2012/11/14/education/moocs-to-be-evaluated-for-possible-college-credit.html>.
18. Alex Dickinson, “IVY.COM: Elite Education Is Coming to the Web, Asking Considerably Less in Tuition,” *The Daily*, May 7, 2012, <http://www.thedaily.com/page/2012/05/07/050712-news-online-ivy-1-4/>.
19. Lima; Tabarrok.
20. *Ibid.*
21. Arnold Kling, “The Education Revolution,” *EconLog*, January 31, 2012, [http://econlog.econlib.org/archives/2012/01/the\\_education\\_r.html](http://econlog.econlib.org/archives/2012/01/the_education_r.html).
22. David Brooks, “The Campus Tsunami,” *New York Times*, May 3, 2012, <http://www.nytimes.com/2012/05/04/opinion/brooks-the-campus-tsunami.html>.
23. Tamar Lewin, “Education Site Expands Slate of Universities and Courses,” *New York Times*, September 19, 2012, <http://www.nytimes.com/2012/09/19/education/coursera-adds-more-ivy-league-partner-universities.html>.
24. Chea.
25. Lim and Saner discuss some of the reasons for this: “Tensions over trade in education services, at risk of oversimplification, are typically between private suppliers and public providers, especially in non-English-speaking European countries. For most of these countries, education is a public good that should not be supplied on a commercial basis in order to guarantee equal access to education for all citizens of a country, no matter what their background or financial means are. Along with this view goes the expectation that the quality of the education provided should be comparable for all students independent of their origin and endowment. Stakeholders like teachers and student unions to a large majority reject trade in education services in general fearing that market access commitments under a trade agreement would open the backdoor to privatization and deregulation and eventually lead to the dis-

mantling of education as a public service.” Lim and Saner, pp. 1025–26.

26. Katherine Mangan, “Minnesota Gives Coursera the Boot, Citing a Decades-Old Law,” *Chronicle of Higher Education*, October 18, 2012, <http://chronicle.com/blogs/wiredcampus/minnesota-gives-coursera-the-boot-citing-a-decades-old-law/40542>.

27. Will Oremus, “In Victory for Common Sense, Minnesota Will Allow Free Online Courses After All,” *Slate*, October 19, 2012, [http://www.slate.com/blogs/future\\_tense/2012/10/19/minnesota\\_coursera\\_ban\\_state\\_won\\_t\\_crack\\_down\\_on\\_free\\_online\\_courses\\_after.html](http://www.slate.com/blogs/future_tense/2012/10/19/minnesota_coursera_ban_state_won_t_crack_down_on_free_online_courses_after.html).

28. Singapore Ministry of Law, “Approved Universities,” <http://app2.mlaw.gov.sg/UsefulInfo/PracticeoflawinSingapore/ApprovedUniversities/tabid/264/Default.aspx>. There are 10 Australian universities on the list; 2 New Zealand; and 4 American.

29. Lim and Saner, p. 1021.

30. *Ibid.*

31. WTO Document S/C/W/49, p. 10.

32. WTO, “Services Trade,” [http://www.wto.org/english/tratop\\_e/serv\\_e/serv\\_e.htm](http://www.wto.org/english/tratop_e/serv_e/serv_e.htm); Lim and Saner, p. 1017.

33. The full provision reads as follows:

2. In sectors where market-access commitments are undertaken, the measures which a Member shall not maintain or adopt either on the basis of a regional subdivision or on the basis of its entire territory, unless otherwise specified in its Schedule, are defined as:

- (a) limitations on the number of service suppliers whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirements of an economic needs test;
- (b) limitations on the total value of service transactions or assets in the form of numerical quotas or the requirement of an economic needs test;
- (c) limitations on the total number of service operations or on the total quantity of service output expressed in terms of designated numerical units in the form of quotas or the requirement of an economic needs test;

- (d) limitations on the total number of natural persons that may be employed in a particular service sector or that a service supplier may employ and who are necessary for, and directly related to, the supply of a specific service in the form of numerical quotas or the requirement of an economic needs test;
- (e) measures which restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service; and
- (f) limitations on the participation of foreign capital in terms of maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment.

General Agreement on Trade in Services, “Marrakesh Agreement Establishing the World Trade Organization,” April 15, 1994, Annex 1B, *The Legal Texts: The Results of the Uruguay Round of Multilateral Trade Negotiations* 284 (1999), 1869 U.N.T.S. 183, 33 I.L.M. 1167 (1994).

34. Jane Knight, “Higher Education Crossing Borders: A Guide to the Implications of the General Agreement on Trade in Services (GATS) for Cross-Border Education,” *Commonwealth of Learning/UNESCO* (2006), p. 30; WTO Document S/C/W/49, pp. 7–8; Lim and Saner, pp. 1001–1003.

35. WTO, “Services Trade.” Based on author’s review of members services schedules.

36. “Communication from the United States, Higher (Tertiary) Education, Adult Education, and Training,” WTO Document S/CSS/W/23, 2000.

37. “Communication from New Zealand, Negotiating Proposal for Education Services,” WTO Document S/CSS/W/93, June 26, 2001.

38. “Communication from Australia, Negotiating Proposal for Education Services,” WTO Document S/CSS/W/110, October 1, 2001.

39. “Communication from New Zealand, Negotiating Proposal on Education Services,” WTO Document S/CSS/W/137.

40. “Communication from the United States, Initial Offer,” TN/S/O/USA, April 9, 2003, p. 61; “Communication from the United States, Revised Services Offer,” TN/S/O/USA/Rev.1, June 28, 2005, p. 68.

41. There was also a collective, plurilateral re-

quest on education services, coordinated by New Zealand. See Government of India, Ministry of Commerce and Industry, Department of Commerce, “International Trade,” [http://commerce.nic.in/trade/international\\_trade\\_tis\\_gaitis\\_requests\\_pr.asp](http://commerce.nic.in/trade/international_trade_tis_gaitis_requests_pr.asp).

42. “WTO Members Discuss Services Deal Elements Linked to Potential Expansion,” *Inside U.S. Trade*, October 4, 2012, <http://insidetrade.com/Inside-US-Trade/Inside-U.S.-Trade10/05/2012/wto-members-discuss-servicesdeal-elements-linked-to-potential-expansion/menu-id-172.html>. There is talk of using positive list for market access, and a negative list for national treatment. See “Compromise ‘Hybrid’ Approach for Services Deal Largely Follows GATS,” *Inside U.S. Trade*, October 9, 2012, <http://insidetrade.com/201210092412372/WTO-Daily-News/Daily-News/compromise-hybrid-approach-for-services-deal-largely-follows-gats/menu-id-948.html>.

43. See paragraph 1 of U.S. communication from 2000; paragraph 3 of New Zealand’s nego-

tiating proposal; and paragraph 2 of Australia’s negotiating proposal. Lim and Saner put it as follows: “Government policies play a dominant role in this sector,” p. 993.

44. As Lim and Saner note, however, “the coverage of the carve-out will . . . have to be determined on a case-by-case basis,” p. 1018.

45. Lim and Saner discuss specific proposals and developments in this area. Lim and Saner, pp. 1024–25.

46. WTO Document TN/S/O/USA.

47. The American Council for Higher Education Accreditation wrote to the U.S. Trade Representative in 2007 to request that the U.S. position in services trade talks should “exclude services offered by accredited, degree-granting, postsecondary institutions and accrediting organizations.” Letter to U.S. Trade Representative’s Office, March 6, 2007. This position may change now that U.S. institutions are at the forefront of offering trade in education services.