

PUBLIC LAW, HIGHER EDUCATION, AND THE *EX ANTE* REMOVAL OF THE CAUSES OF INEQUALITY

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Abstract

Globalized markets, digital economies, robotization, artificial intelligence and their impact on social inclusion have recently received increasing scholarly attention in economics, law, sociology, philosophy and development studies. Super-fast economic changes spurred by world-widely integrated markets and related explosive social inequality represent one of the most triggering questions of the modern world. One that can even rival the fatal issue of the global climate change. This paper seeks to address the role of public law as an ex ante mechanism designed to remove the causes of inequality in the first place and not to treat its consequences. This paper, while employing an example of the optimal regulatory intervention in the field of public law, particularly its regulation of public education, joints critical debate and expresses the view that legal system might indeed be in certain circumstances superior to the classic ex post interventions (e.g. tax-and transfer system or all-encompassing subsidies) at reducing income inequality. The paper is an attempt to find out what new light the legal theory can shed on the issues of social exclusion, inequality, public law regulation of higher education, optimal governmental intervention and of their possible success or failure in order to help to clarify it.

Résumé

Les marchés mondialisés, les économies numériques, la robotisation, l'intelligence artificielle et leur impact sur l'inclusion sociale ont récemment reçu une attention croissante de la part des chercheurs en économie, en droit, en sociologie, en philosophie et en études du développement. Les changements économiques ultra-rapides provoqués par l'intégration mondiale des marchés et les inégalités sociales explosives qui y sont liées représentent l'une des questions les plus déclenchantes du monde moderne. Une question qui peut même rivaliser avec la question fatale du changement climatique mondial. Cet article cherche à aborder le rôle du droit public en tant que mécanisme ex ante conçu pour éliminer les causes de l'inégalité en premier lieu et non pour traiter ses conséquences. Le présent article, tout en utilisant un exemple d'intervention réglementaire optimale dans le domaine du droit public, en particulier sa réglementation de l'éducation publique, suscite un débat critique conjoint et exprime l'opinion que le système juridique pourrait effectivement, dans certaines circonstances, être supérieur aux interventions ex post classiques (par exemple, système d'imposition et de transfert ou subventions globales) pour réduire l'inégalité des revenus. Cet article est une

tentative pour découvrir sous quelle nouvelle lumière la théorie juridique peut apporter sur les questions d'exclusion sociale, d'inégalité, de régulation de l'enseignement supérieur par le droit public, d'intervention gouvernementale optimale et de leur succès ou échec possible afin d'aider à la clarifier.

INTRODUCTION

The importance of poverty and inequality on the existence and stability of social fabric can hardly be overstated. Super-fast economic changes spurred by world-widely integrated markets and related explosive social inequality represent one of the most triggering questions of the modern world. Namely, in last thirty years, the gap between rich and poor has reached its highest level¹. Today, in OECD countries, the richest 10% of the population earn 9.6 times the income of the poorest 10%². In emerging economies, particularly in Latin America, income inequality has narrowed, when income gaps remain generally high³. Moreover, also the frontier of economic development is not immune to the growing inequality and to even more troublesome wage-stagnation below the high-earner level⁴. Domhoff for example reports that between 1997 and 2016 median US household income fell by 6% after the adjustment for inflation and that is still stagnating⁵. Income inequality continued to increase during the period of crisis and is accompanied with a ruinous fall in employment rates which, accompanied with economic depression, form a vicious cycle. Such a vicious cycle then represents a heaven-like environment for all sorts of populisms, extremisms, demand for trade protection, restriction on immigration, union protectionism, numerous anticompetitive measures, useless government subsidies and represent an outmost threat to, as history witnessed numerous times, fragile social fabric⁶. In other words, identified high inequality slows down economic growth, destroys social fabric, adversely affects social mobility, hampers social wealth and opens “Pandora’s box” of the apocalyptic, evil forces of Sauron.

What should then be done about this rising inequality? What would the optimal policy intervention and what should be done at the EU level? In this respect, traditional economic literature offers *ex post* tax-and transfer system (*ex post* redistribution) and direct transfers as the exclusive institutional mechanisms that should regulate inequality and social exclusion⁷.

¹ OECD, *OECD Science, Technology and Innovation Outlook 2016*, OECD Publishing, 2016, available online: http://dx.doi.org/10.1787/sti_in_outlook-2016-en (visited February 11, 2018).

² OECD, “Chapter 5: And the Twain Shall Meet: Cross-Market Effects of Labour and Product Market Policies”, *Employment Outlook*, OECD, 2002.

³ *Ibid.*

⁴ See e.g. K. Phillips, *Wealth and democracy: a political history of the American rich*, Broadway Books, 2002.

⁵ W. Domhoff, “Wealth, Income and Power” 2018, available online: <https://www2.ucsc.edu/whorulesamerica/power/wealth.html> (visited March 17, 2018).

⁶ It should be also emphasized that in the countries that experienced the most severe economic depression real household incomes decreased more substantially at the lower end of the income distribution.

⁷ See e.g. S. Shavell, “A note on efficiency vs. distributional equity in legal rulemaking: should distributional equity matter given optimal income taxation?”, *American Economic Review Papers & Proceedings*, 1981, vol. 71, pp. 414-418; L. Kaplow, S. Shavell, “Why the legal system is less efficient than the income tax in redistributing income”, *Journal of Legal Studies*, 1994, vol. 23, issue 2, pp. 667-681; L. Kaplow, S. Shavell, “Should legal rules

Moreover, it is widely accepted that measures to reduce income inequality could increase economic efficiency by reducing political pressures for inefficient policies. Bismarck's programmes of governmental health, accident and disability insurance, and old-age pensions have effectively reduced such political pressures and have *de facto* decreased inequality⁸. However, such extensive social safety nets might be just too expensive to be expanded further without jeopardizing the solvency of EU member states and produce an explosive, ruinous and growing public debt which in the end resort in complete economic and social collapse⁹.

However, one may wonder whether such an *ex post* tax-and-transfer system should be indeed employed as an exclusive tool to address inequality. Should perhaps also legal rules do something about this dismal situation? In other words, is the tax-and-transfer system a superior, exclusive remedy and should the attempts in legal science to address the issue of inequality also via legal rules be declared as futile? Conventional economic wisdom provides a clear-cut answer and suggests that legal system should focus only on efficiency and that efficiency-equity tradeoffs should be made only in the tax system and inequality arguments should be irrelevant in property law, contract law, public and administrative law or any field of law except tax law¹⁰. The main reason advanced in the literature is the so-called "double-distortion" argument under which any legal rule that redistributes income only adds to the economic distortions already present in the tax system¹¹. This double-distortion argument launched by Louis Kaplow and Steven Shavell¹² has been a subject of extensive debate and recent cataclysmically growth of inequality has amplified the media-political-scholarly interest in their argument¹³. However, it should be emphasized that several law and economics scholars seem to challenge Kaplow and Shavell's decisive argument advocating formation of the equity-distributive-informed legal rules¹⁴. Dimick for example argues that there is no reason to believe that legal rules that have

favour the poor? Clarifying the role of legal rules and the income tax in redistributing income", *Journal of Legal Studies*, 2000, vol. 29, issue 2, pp. 821-835..

⁸ R. Posner, *Economic Analysis of Law*, Wolters Kluwer, 8th ed., 2011, p. 635.

⁹ For example, the vast social expenditures in EU MS in last economic depression

¹⁰ See e.g. L. Kaplow, S. Shavell, *op. cit.*, 1994.

¹¹ Hence, traditional law and economics literature suggests that it would be better for everyone, and especially for the poor, to instead adopt a more efficient, non-redistributive rule, and then increase transfers to the poor or reduce everyone's taxes. Thus, as argument goes, the law should concern itself only with the efficiency-making the pie bigger-and not with distribution-how to divide the pie; D. Weisbach, "Should legal rules be used to redistribute income?", *University of Chicago Law Review*, 2003, vol. 70, p. 439. See also A. Alstott, "Work v. Freedom: A liberal challenge to employment subsidies", 1999, *Yale Law Journal*, vol. 108, issue 5, pp. 967-1058, p. 972.

¹² L. Kaplow, S. Shavell, *op. cit.*

¹³ See e.g. Z. Liscow, "Reducing inequality on the cheap: when legal rule design should incorporate equity as well as efficiency," *Yale Law Journal*, 2014, vol. 123, issue 7, pp. 2478-2509, p. 2480.

¹⁴ See e.g. R. Avraham, D. Fortus, K. Logue, "Revisiting the roles of legal rules and tax rules in income redistribution: a response to Kaplow and Shavell", *Iowa Law Review*, 2004, vol. 89, p. 1125; R. Kaplan, "Economic Inequality and the role of law," *Michigan Law Review*, 2003, vol. 101, issue 6, pp. 1197-2006; T.

redistributive effects will always reduce efficiency and that legal rules are likely to be more attractive than taxation precisely in cases where inequality itself or normative concerns about inequality are high¹⁵. He suggests that a mix of legal rules and taxation, rather than taxation exclusively, might be the best way to address economic inequality¹⁶.

This paper, while employing an example of the optimal regulatory intervention in the field of public law, particularly administrative law and its regulation of public education, joins this critical debate and challenges the classical viewpoint and expresses the view that legal system might indeed be intrinsically superior to the classic *ex post* interventions (e.g. tax-and transfer system or all-encompassing subsidies) at reducing income inequality. Moreover, this paper argues that the policy maker should focus on the policies that prevent inequality from occurring *ex ante* and that a priority should be given to the *ex ante* policies that do not induce moral hazard and opportunism, are fiscally sustainable, economize on transaction costs, and that do not distort dynamic efficiency (preserve incentives for productive, entrepreneurial social-wealth increasing behavior). Namely, Kenneth Arrow, the Nobel prize laureate for economics, proved that not only are all perfect markets efficient but also that all efficient outcomes can be achieved employing a competitive market, by adjusting the starting position¹⁷. He actually argues that when one is trying to balance the excesses of competitive markets she should not interfere with the markets themselves but should adjust the starting block by making lump-sum payments and levying onetime taxes. As it is in practice due to the asymmetric information problem unfeasible one should hence via public education put everyone on an equal footing. Afterwards perfect markets then find every possible opportunity to make everybody better off from their revised starting points.

Moreover, professor De Geest in his recent groundbreaking article on removing rents introduces a pathbreaking differentiation between different sources of inequality and related, until now overlooked, phenomena of rents as a source of inequality. De Geest observes that

Blumkin, M. Yoram, "On the limits of redistribution taxation: establishing a case for equity-informed legal rules", *Virginia Tax Review*, 2005, vol. 25, issue 1 and A. Fennell, R. McAdams, "The distributive deficit in law and economics", *Minnesota Law Review*, 2016, vol. 100, p. 1051.

¹⁵ M. Dimick, "Should the law do anything about economic inequality?", *Cornell Journal of Law and Public Policy*, 2016, vol. 26, issue 1.

¹⁶ Dimick emphasizes that since legal rules can sometimes be both more efficient and redistributive, policy makes must consider each situation, case-by-case, to determine whether legal rules should or should not be used to redistribute income. He states that the double-distortion argument does not save us from the hard work of comparative and institutional analysis. *ibid.*, p. 67.

¹⁷ K. Arrow, "General Economic Equilibrium: Purpose, Analytic Techniques, Collective Choice", *The American Economic Review*, 1974, vol. 64, issue 3, pp. 253-272. See also K. Arrow, G. Debreu, "Existence of an equilibrium for a competitive economy", *Econometrica, The Econometric Society*, 1954, vol. 22, issue 3, pp. 265–290.

there are two fundamental ways to correct income inequality¹⁸. The first one advocated by Shavell and Kaplow is the so-called *ex post* approach that intervenes after income inequality has occurred and the second one coined by De Geest as the “*ex ante* approach” which tries to prevent income inequality from occurring in the first place. De Geest also argues that if the inequality is not caused by the differences in efforts or talents but by rent-seeking behavior (rents)¹⁹, then the *ex ante* legal intervention is superior because it prevents income inequalities from occurring in the first place – this is what he calls an *ex ante* approach²⁰. Identified rents are in reality enabled by a variety of market failures such as network externalities, prohibitive transaction costs, various asymmetric information problems, cartels, behavioral biases and their exploitation, lock-in effects, temporary market powers and decreasing economies of scale.

While opening an unprecedented avenue for potential further research, De Geest convincingly shows that legal rules that prevent rents from occurring are intrinsically better at correcting these market failures and that preventing them *ex ante* is intrinsically superior to correcting them *ex post*²¹. Hence, as argument goes, legal rules that prevent rents therefore reduce labor and price distortion and that the trade-offs between equity and efficiency should be made in the legal system whenever legal rules generate or reduce rents²².

In line with De Geest’s argument public law and related legal regulation of education appears as one of the most important legal areas which can *ex ante* cure market failures, deter rents, reduce information asymmetries, and hence remove the causes of income inequality in first place. This paper offers *ex ante* investments in education (human capital) and related regulatory intervention as one of the most significant measures that will address/prevent wage stagnation without increasing EU MS public indebtedness. Furthermore, due to the utmost importance of education as an *ex ante* mechanism for rent prevention and for removing the causes of ruinous inequality paper calls for an EU-wide regulatory policy intervention. In addition, the shift of the law-maker’s (policy-maker) regulatory attention from the *ex post*

¹⁸ G. De Geest, “Removing Rents: Why the legal system is superior to the income tax at reducing income inequality”, *Washington University in St. Louis School of Law Legal Studies Research Paper Series*, October 2013, paper n. 13-10-02, available online http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2337720.

¹⁹ He defined rents as profits that would not have been earned in a perfectly competitive and transparent economy, *ibid.*

²⁰ Although this is a largely untested hypothesis at this point it may well be that prevention of rents might be the most understated, overlooked function of legal systems from ancient Roman law onwards.

²¹ G. De Geest, *op. cit.*

²² *Ibid.* He also emphasizes that rents are from analytical perspective implicit commodity taxes causing labor and price distortions.

policy intervention which merely treats the inequality's symptoms towards the *ex ante* focus on removal of its causes appears as one of the main arguments of our paper.

In relation to suggested *ex ante* focus on removal of inequality's causes one should note several EU and global initiatives that emphasize the role of education as one of the most significant tools to tackle the issues of inequality. For example, European Commission recently launched an initiative on the development of higher education policies in EU MS (formation of inclusive and connected education systems and supporting effective and efficient higher education systems), whereas World Economic Forum (hereinafter as WEF) in its recent study on how to tackle the sources of inequality emphasizes the importance of the *ex ante* measures²³. Moreover, United Nations in 2015 launched the "2030 Agenda for Sustainable Development" which among other 17 goals that should ensure global sustainable development (which should end poverty) has as its fourth goal the assurance of the inclusive and equitable quality education²⁴.

This paper attempts at contributing to the existing literature in several ways. First, it emphasizes the *ex ante* role of law as one of the main inequality preventive mechanisms. Second, it shows that public law and its regulation of public education might feature as one of the most important *ex ante* mechanisms for removing the causes of inequality. Third, it argues that the shift of the EU law-maker's regulatory attention from the *ex post* policy intervention which merely treats the inequality's symptoms towards the *ex ante* focus on removal of its causes is of vital importance.

Having said all that, it should be emphasized that proposed *ex ante* education mechanism should not be regarded as a sole or the only possible regulatory tool to tackle the income inequality. Namely, we argue that an effective policy maker should, while tackling the inequality problem, design its policy in line with the golden Tinbergen rule – N problems requires N solutions. This rule, employed in natural sciences as a general research maxim, was

²³ Namely, WEF correctly advocates reforms that promote strong, inclusive growth that by its nature reduces inequality. Their approach focuses on *ex ante* reducing inequalities of opportunity and broadening the base of participants in the growth process, thereby ensuring that more people benefit from it. WEF's range of policies that can stimulate inclusive growth is indeed very broad, yet they emphasize education is a key instrument for tackling the notorious inequality. Improving the availability and quality of education expands the talent pool in the labor force and upgrades and broadens its skills base. Early childhood development programs, for example, have been demonstrated to provide lifelong educational benefits and the foundation for success in the workplace; World Economic Forum, *What's the best way of tackling inequality*, 2015, available online <https://www.weforum.org/agenda/2015/09/whats-the-best-way-of-tackling-inequality/> (visited March 17, 2018).

²⁴ United Nations, *Transforming our world: the 2030 Agenda for Sustainable Development*, 2015, available online <https://sustainabledevelopment.un.org/post2015/transformingourworld> (visited March 18, 2018).

formulated by the Dutch economics Nobel laureate, Jan Tinbergen in 1952 and is generally stated as “for each policy objective, at least one policy instrument is needed - there should be at least the same number of instruments as there are targets”²⁵. Hence, a smart, enlighten policy maker should identify different sources of market failures/rents/inequality and apply for each of them its specific, *ex ante* or *ex post* (or combination of both) instrument²⁶.

However, several caveats should be stated. Namely, this paper omits discussion on whether statistics on income inequality provide a clear-cut guidance for social policy or even a clear picture of income inequality²⁷ and instead takes the problem of inequality as an undisputable one. Moreover, paper does not discuss the perplexing issue of whether inequality is at all inefficient and what might be an “optimal” amount of inequality in a given society. Moreover, due to the limited scope of the paper we focus merely upon the EU Member States. Moreover, the analytical approach employs interdisciplinary dynamic²⁸ analysis and enriches it with the concepts used in the economic analysis of law²⁹.

This paper is structured as follows. First part recapitulates current findings on the inequality, redistribution and its consequences. In the second part, the rationale behind the *ex post* tax-and-transfer system is presented. This is also a widely used view which argues that only tax system should be used to redistribute income and to mitigate current explosive inequality. The third part challenges this widely accepted premise and offers arguments in support of *ex ante* intervention. In this part paper offers a set of arguments that public law and its regulation of public education might feature as one of the most important *ex ante* mechanisms for removing the causes of inequality and might be superior in reducing income inequality. In fourth part paper particularly focus on WEO’s initiatives, on the regulation of

²⁵ J. Tinbergen, *On the Theory of Economic Policy*, North-Holland, 1952.

²⁶ Numerous rules in contract law might be interpreted exactly in that way. For example, doctrines of mistake, fraud, duress, misrepresentation, unjustified enrichment, *culpa in contrahendo*, antitrust rules, good faith can also have such an *ex ante* function. However, this does not imply that legal rules should not be, while drafted, *ex ante* primarily concerned with redistribution goals. On contrary, legal rules should still be designed in line with economic suggestions – such rules would actually than maximize social wealth and *ex ante* tackle the notorious rents and inequality problems.

²⁷ Posner for example argues that by taking a snapshot of incomes for one year, scholars misleadingly compare people in different stages of their life cycle. For example, he emphasizes that the statistics places a young lawyer who has just joined the a firm and a senior partner in the same firm in different income classes, yet both may earn the same amounts in their lifetimes (or the young lawyers might probably earn even more); R. Posner, *op. cit.*, p. 627.

²⁸ Dynamic part of analysis employs recent behavioral insights that offer a novel assessment of how will parties react in their daily behavior upon different set of rules and norms.

²⁹ For a synthesis of law and economics scholarship, see G. De Geest, *Contract Law and Economics – Encyclopaedia of Law and Economics, Volume 6*, Edward Elgar Cheltenham, 2nd ed., 2011. Also see R. A. Posner, *op. cit.*

education as an *ex ante* legal remedy and call for an EU-wide harmonization of legislation in the field of education and critically examines the proposed 2030 Agenda for Sustainable Development. Finally, some conclusions will be presented.

I. WEALTH INEQUALITY AND ITS CONSEQUENCES: A SYNTHESIS

This part summarizes the main findings from economic literature on the wealth inequality and on its consequences.

I.A. Inter-generational social mobility

An important channel through which public policies could influence intergenerational social mobility is by affecting intra-generational inequality³⁰. Galbraith and Kum (2005) argue that inequality has risen with globalization in most parts of the world³¹. Further, the household income inequality is distributed more consistently across the world that one would believe³². According to Gottschalk and Danziger increased family income inequality primarily reflects increased inequality of wage rates which in turn reflects differences in returns to education³³.

I.B. Institutional framework

Differences in wage distribution across countries are also influenced by the institutional environment. In the 1996 and 2003 studies by Blau and Kahn emphasize an important role of institutions affecting wage inequality through resource allocation was identified³⁴. Contrary to the expected Blau and Khan study found that the low-skilled workers have higher employment rations compared to higher-skilled workers in the US than in other countries. To some extent through labor market policies (government employment, training programs and subsidies) governments are trying to diminish negative effects of wage-setting institutions. In OECD countries wage leveling policies are encouraged by the government, on the one hand, to achieve desired level of wage inequality and, on the other hand, to provide safety net for low-wage

³⁰ O. Causa, Å. Johansson, "Intergenerational Social Mobility in OECD Countries", *OECD Journal: Economic Studies*, 2010, vol. 2010.

³¹ J. Galbraith, H. Kum, "Estimating the Inequality of Household Incomes: A Statistical Approach to the Creation of a Dense and Consistent Global Data Set", *Review of Income and Wealth*, 2005, vol. 51.

³² *Ibid.*

³³ P. Gottschalk, S. Danziger, "Inequality of Wage Rates, Earnings and Family Income in the United States, 1975-2002", *Review of Income and Wealth*, vol. 51..

³⁴ Even though an adverse impact of resource allocation would be expected. We would expect that this reallocation will have positive impact on employment and productivity. F. Blau, L. Kahn, "International Differences in Male Wage Inequality: Institutions Versus Market Forces", *Journal of Political Economy*, 1996, vol. 104; F. Blau, L. Kahn, "Understanding International Differences in the Gender Pay Gap", *Journal of Labor Economics*, 2003, vol. 21.

workers. Acemoglu (2003) developed a theory where labor market institutions creating wage compression in Europe also encourage more investment in technologies increasing the productivity of less-skilled workers, thus implying less skill-biased³⁵ technical change in Europe than in the US³⁶. If we believe that SBTC indeed causes higher wage inequality than this is good news for Europe. However, it is far from the entire story of inequality.

In OECD (2002) study a number of policies and institutional factors affecting the labor market, anti-competitive product market regulations (e.g. establishing entry barriers in potentially competitive markets or restricting price competition) were found to have significant negative effects on the non-agricultural employment rates of OECD countries³⁷. The evidence also points to significant effects of employment protection legislation³⁸ and industrial relations regimes³⁹ (e.g. bargaining arrangements, business associations, business codes of conduct, etc.) on innovation activity in manufacturing. Across OECD countries, wage dispersion is lower in countries where institutions compress the distribution of wages (e.g. the Nordic countries). However, recent OECD studies showed that such institutions likewise reduce employment among older workers and therefore reduce the overall share of wage-earners in the economy. Bassanini and Duval (2006) study found institutional effect on employment not only through their impact on aggregate unemployment but also through their effects on labor market participation⁴⁰. In the average OECD country, high unemployment benefits and high tax

³⁵ Shift in the production technology that favors skilled over unskilled labor by increasing its relative productivity and its relative demand. Many discussions were held about whether technological change is the primary source of wage inequality or not (as opposed to policy and institutions).

³⁶ If we believe that SBTC indeed causes higher wage inequality than this is good news for Europe, however it is far from the entire story of inequality. D. Acemoglu, "Cross-Country Inequality Trends", *Economic Journal*, 2003, vol. 113.

³⁷ OECD, *op. cit.*, 2002.

³⁸ Countries where product market regulations and employment protection legislation are relatively strict also tend to specialize in industries characterized by low wage premia. Features of the institutional and regulatory environment affecting the functioning of labor markets, indicators of the strictness of Employment Protection Legislation (EPL) based on institutional procedures regarding dismissal practices for regular workers and legislation on fixed-term and temporary work agency contracts, may reflect differences in the innovation process across industries, see OECD (2002).

³⁹ Can have independent effects on innovation activity, but the intensity of this effect is likely to depend on the way these policies and institutions interact with each other. Restrictive EPL and highly coordinated industrial relations regimes generally encourage firms to resort to internal labor reallocations and undertake firm-sponsored training. Industrial relations regimes raise job turnover and tend to increase wage dispersion and skill premia, see OECD (2002).

⁴⁰ Particularly for those groups at the margin of the labor market, group-specific employment rate equations are also estimated. These effects are high and long-lasting unemployment benefits, high tax wedges and stringent anticompetitive product market regulation which increase aggregate unemployment, when coordinated wage bargaining systems are estimated to reduce unemployment. A. Bassanini, R. Duval, "Employment Patterns in OECD Countries: Reassessing the Role of Policies and Institutions", *OECD Economics Department Working Papers*, 2006, n. 486.

wedges are found to be associated with lower employment prospects for all groups studied, namely prime-age males, females, older workers and youths⁴¹.

I.C. Sources of inequality – education and social fabric

The relationship between wage inequality and intergenerational income persistence is not straightforward, as a range of factors might influence observed results, sometimes in opposite directions, as the countries with a wide distribution of income are also likely to be those where the returns to education are relatively high⁴². On the one hand, countries with a wide distribution of income are also likely to be those where the returns to education are relatively high. As discussed above, if parental background affects access to investment in education through credit or other constraints, then the ability to take advantage of the high returns from education is limited to the offspring of relatively advantaged parents. After the crisis we observed inequality grow at an alarming rate, therefore a need to develop tools for gauging inequality had risen⁴³. According to Corak almost one half of children in the US born to low income parents become low income adults. The fraction is also high in the United Kingdom at four in ten⁴⁴, and Canada where about one third of low income children do not escape low income in adulthood⁴⁵. In the Nordic countries⁴⁶, where overall child poverty rates are noticeably lower, it is also the case that a disproportionate fraction of low income children become low income adults⁴⁷.

In this respect d'Addio provides clear evidence of relative immobility across generations in many fields such as income, occupations and education, showing that children largely "inherit" their parents' socio-economic status⁴⁸. Resources can be inherited from the

⁴¹ *Ibid.*

⁴² Countries with a wide distribution of income are also likely to be those where the returns to education are relatively high. S. Mat, M. Harun, N. Bakar, "Determinants of Social-economic Mobility in the Northern Region of Malaysia", *International Journal of Economics and Financial Issues*, 2016, 6 (7S), pp. 109-114. Retrieved online <http://dergipark.gov.tr/ijefi/issue/32000/353038>.

⁴³ F. Chang, Felix, "Asymmetries in the Generation and Transmission of Wealth", *Ohio State Law Journal, Forthcoming*, 26 April 2017, available online SSRN: <https://ssrn.com/abstract=2939878>.

⁴⁴ M. Corak, "Do Poor Children Become Poor Adults? Lessons from a Cross Country Comparison of Generational Earnings Mobility", *IZA Discussion Papers*, 2006, No. 1993.

⁴⁵ *Ibid.*

⁴⁶ Denmark, Finland, Norway, and Sweden.

⁴⁷ M. Corak, *op. cit.*

⁴⁸ While education is a major contributor to intergenerational income mobility, several studies suggest that a large portion of the mechanisms governing the transmission of income across generations is unexplained by it (for example see J. Blanden, *Essays on Intergenerational Mobility and Its Variation over Time, Place and Family Structure*, PhD Thesis, University of London, 2005; J. Blanden, P. Gregg, L. Macmillan, "Explaining Intergenerational Income Persistence: Noncognitive Skills, Ability and Education", *Centre for Market and Public Organisation*, 2006, Working Paper n. 06/146; S. Bowles, H. Gintis, "The inheritance of inequality", *Journal of Economic Perspectives*, 2002, vol. 16, issue 3, pp. 3-30; S. Bowles, H. Gintis, "Schooling in Capitalist America

parents either directly through genes and wealth, or indirectly when children learn behaviors and attitudes⁴⁹. These resources interact with the cognitive and non-cognitive⁵⁰ abilities of children in ways that can work together to strongly influence their future life chances and to strengthen the transmission of inequality⁵¹. Literature also suggests that the family should be regarded as an important social policy institution. There is the need to understand all the aspects of family background, which are correlated or uncorrelated with parental earnings or incomes, and that are important in explaining the influence of the family on intergenerational mobility⁵². Among these, the mechanisms that contribute to transmitting parental education, occupations, values, beliefs and attitudes across generations seem to be critical. Burtless and Jencks suggest that it makes sense to evaluate policies aimed at changing the distribution of income by asking whether they are consistent with widely held norms about justice⁵³. The political impact of changes in economic inequality could be reduced by designing a political system that minimizes the influence of money and further by mobilize less affluent voters around distributional issues. However, the US does not provide such political system, as both major political parties have become dependent on large contributions from the wealthy citizens. They argue that within the range of rich democracies, inequality does not have large and obvious effects on growth, mobility, and longevity. Furthermore, rich countries have relatively similar living standards⁵⁴. The difference among wealthy democracies is the relative political influence of different economic and ideological groups, which further explain higher equality within such democracies. According to several studies higher cross-sectional inequality tends to be

Revisited", *Sociology of Education*, 2002, vol. 75, issue 1, pp. 1-18; S. Bowles, H. Gintis, M. Osborne Groves, "Introduction" in S. Bowles, H. Gintis, M. Osborne Groves (eds.), *Unequal Chances: Family Background and Economic Success*, Russell Sage, pp. 1-22; A. D'Addio, "Intergenerational Transmission of Disadvantage: Mobility or Immobility Across Generations? A Review of the Evidence for OECD countries", *OECD Social, Employment and Migration Working Papers*, 2007, n. 52.

⁴⁹ *Ibid.*

⁵⁰ Non-cognitive skills may moderate the effect of genetic components on socio-economic outcomes and affect the extent of income mobility across generations. J. Blanden P. Gregg, L. Macmillan, *op. cit.*, consider a range of non-cognitive and cognitive factors and argue that the former account for 19% of intergenerational earnings correlation and the latter for 27%.

⁵¹ Genetics allow inherited traits, and more particularly genetic endowments, to influence income transmission across generations and are largely unexplained. See A. D'Addio, *op. cit.*

⁵² G. Solon, "Chapter 29 - Intergenerational Mobility in the Labor Market" in O. Ashelfenter, D. Card (eds.), *Handbook of Labor Economics*, Elsevier, 1999, vol. 3, part A.

⁵³ G. Burtless, C. Jencks, "American Inequality and its Consequences" in H. Aaron, J. Lindsay, P. Nivola (eds.), *Agenda for the Nation*, 2003.

⁵⁴ Living standard is most directly influenced by long-run permanent income, such as household disposable income. L. Chadwick, G. Solon, "Intergenerational Income Mobility among Daughters", *American Economic Review*, 2000, vol. 92; G. Solon, "A Model of Intergenerational Mobility Variation over Time and Place" in M. Corak (ed.), *Generational Income Mobility in North America and Europe*, Cambridge University Press, 2004, pp. 38-47; C.-I. Lee, G. Solon, "Trends in Intergenerational Income Mobility", *National Bureau of Economic Research Working Papers*, 2008, n. 12007, available online.

associated with lower mobility⁵⁵. In reality, this association⁵⁶ is positive in European OECD⁵⁷. Similarly, there is a positive association across European OECD countries between intergenerational persistence in wages and poverty rates, although weaker than the association between persistence and inequality⁵⁸.

I.D. Redistribution and its effects

Redistributive policies are generally perceived as a main mechanism that should enable disadvantaged families to invest in their children's human capital. Moreover, social and redistributive policies might, as argument goes, narrow the gap between current incomes of parents, so that the incomes of their offspring could regress to the mean more quickly⁵⁹. Therefore, such well-targeted redistributive policies could reduce inequalities. However, such redistributive policies are concerned solely with the static efficiency but disregard the issues of dynamic efficiency its incentive for productive behavior and for related entrepreneurial creation of new social wealth. may have detrimental effects upon dynamic efficiency. Namely, such policies may also lower incentives to undertake effort and invest in human capital, deter entrepreneurial activity and innovation as the net returns from these investments are reduced⁶⁰. One measure of the redistribution of the taxes is the progressivity in the personal income tax schedule, which varies significantly across OECD countries and over time⁶¹. Cross-country estimates suggest that higher tax progressivity correlates across countries with a lower influence of parental background on their offspring's cognitive achievement in secondary education, as well as on their wages⁶². One interpretation of the positive correlation between student performance and wages is that redistributive policies allow disadvantaged parents to provide children with a better environment, more time and resources for their education. However, it should be emphasized that correlation is not causation and that omitted bias variable problem makes such studies poisoned.

⁵⁵ See D. Andrews, A. Leigh, "More Inequality, Less Social Mobility", *Applied Economics Letters*, 2009, vol. 16; A. Björklund, M. Jäntti, "Intergenerational Income Mobility in Sweden Compared with the United States", *American Economic Review*, 1997, vol. 87, issue 5, pp. 1009-1018; M. Corak, 2006, *op. cit.*; A. D'Addio, *op. cit.*; G. Solon, *op. cit.*, 2004.

⁵⁶ Measured by the Gini coefficient of household disposable income.

⁵⁷ O. Causa, C. Chapuis, "Equity in Student Achievement across OECD Countries: An Investigation of the Role of Policies", *OECD Economics Department Working Papers*, 2009, n. 708.

⁵⁸ O. Causa, S. Dantan, Å. Johansson, "Intergenerational Social Mobility in European OECD countries", *OECD Economics Department Working Papers*, 2009, n. 709.

⁵⁹ M. Corak, 2006, *op. cit.*

⁶⁰ O. Causa, Å. Johansson, *op. cit.*; O. Causa, S. Dantan, Å. Johansson, *op. cit.*

⁶¹ J. Arnold, B. Brys, C. Heady, A. Johansson, L. Vartia, "Tax and Economic Growth", *OECD Economics Department Working Papers*, 2008, n. 620.

⁶² O. Causa, C. Chapuis, *op. cit.*; O. Causa, S. Dantan, Å. Johansson, *op. cit.*

The unemployment benefits policy implications are not clear, because empirical evidence suggests that the presence of transfer income among parents is associated with lower wage prospects for their offspring⁶³. Furthermore, a substantial degree of intergenerational persistence in reliance on welfare could imply sustained cycles of welfare dependency⁶⁴. Therefore, income support programs are more likely to remove obstacles to intergenerational mobility if they are designed to encourage labor market participation and self-sufficiency across generations, while at the same time providing adequate income support during job search.

II. THE RATIONALE BEHIND THE *EX POST* TAX-AND-TRANSFER SYSTEM

This section provides a synthesis of general arguments advanced in the economic literature that favors the *ex post tax-and-transfer system* as an optimal inequality remedy.

II.A. Conventional economic wisdom

Conventional economic literature offers tax system and not the legal system as the optimal mechanism for income redistribution and as a superior tool to address the notorious inequality problem. Shavell and Kaplow in their seminal, widely cited article, coined the double distortion argument where they argue that although *ex post tax-and-transfer system* might cause certain economic distortions using the legal system in order to address inequality would produce the same distortions and also undermine other social functions of an effective legal system⁶⁵. Their basic claim is that “using legal rules to redistribute income distorts work incentives fully as much as the income tax system and also creates inefficiencies in the activities regulated by the legal rules”⁶⁶.

Consequently, “redistribution through legal rules offers no advantage over redistribution through the income tax system and typically is less efficient”⁶⁷. From this analysis they also draw the more general conclusion that “it is appropriate for economic analysis of legal rules to focus on efficiency and to ignore the distribution of income in offering normative judgments”⁶⁸. Thus, effective and smart legal system should not focus on inequality and should instead focus merely on efficiency. Moreover, the efficiency versus equity tradeoffs should be made only in

⁶³ M. Corak, 2006, *op. cit.*

⁶⁴ M. Page, “New Evidence on the Intergenerational Correlation in Welfare Participation” in M. Corak (ed), 2004, *op. cit.*

⁶⁵ L. Kaplow, S. Shavell, 1994, *op. cit.*

⁶⁶ *Ibid.*, p. 668.

⁶⁷ *Ibid.*, p. 667.

⁶⁸ *Ibid.*, p. 677.

the *ex post* tax-and-transfer system⁶⁹. Hence, the argument goes inequality arguments should not be part of public or administrative law-making procedure and the correction of income inequality should not be its goal. To sum up, current leading law and economics textbooks offer Kaplow and Shavell's argument as the main, leading policy-law-making principle⁷⁰.

II.B. *Ex post* instruments: progressive taxation and social welfare programs

Traditionally economists argue that progressive taxation and *ex post* social welfare programs are the most effective mechanisms to pursue redistributive goals and mitigate the inequality problem. As the argument goes, pursuing redistributive goals is an exceptional use of law that special circumstances may justify but that ought not be the usual use of for example private law⁷¹. Cooter and Ulen for example offer several different reasons supporting the supremacy of *ex post*-tax-and-transfer mechanisms⁷². They argue that a) income tax precisely targets inequality, whereas redistribution by private legal rules relies on crude averages; b) the distributive effects of reshuffling private rights are hard to predict; c) the transaction costs of redistribution through private legal rules are typically high; and d) redistribution by private law distorts the economy (incentives) more than progressive taxation does⁷³. Thus the general principles of private law cannot rest on wealth redistribution⁷⁴.

III. PUBLIC LAW, PUBLIC HIGHER EDUCATION AS AN OPTIMAL *EX ANTE* INTERVENTION AT REDUCING INCOME INEQUALITY

This part presents a set of recent law and economics arguments for why the legal system might be more efficient than the income tax system for redistributing income and why public law's regulation of higher education might be instrumental in removing the causes of rents and inequality.

III.A. Superiority of *ex ante* legal intervention

Generations of lawyers from Roman times onwards⁷⁵ have intrinsically always felt that legal rules, despite economists' objections, are the right way to pursue distributive justice and

⁶⁹ *Ibid.* See also L. Kaplow, S. Shavell, 2000, *op. cit.*

⁷⁰ See e.g. R. Cooter, T. Ulen, *Law and Economics*, Pearson, 2008; R. Posner, *op. cit.*

⁷¹ *Ibid.*, p. 8.

⁷² *Ibid.*, p. 9. See also R. Posner, *op. cit.*, p. 15 onward.

⁷³ *Ibid.*, p. 9 onward.

⁷⁴ It should be emphasized that Cooter and Ulen focus merely upon the *ex post* role of law and that they do not address the potential *ex ante* capacity of legal rules to remove the sources of inequality and rents in first place.

⁷⁵ See e.g. Cicero M. Tullius, *De Officiis*, (transl. A. Peabody, Little Brown and Co., 1887).

to tackle the ruinous inequality problems. However, their analytical justification remained tautological or based on general standards of morality, good faith and ethical behavior. The contradicting economic arguments were, at least for last decades, the prevailing ones. Yet, recent legal scholarship managed to make a first revolutionary step in refuting traditional economic wisdom. Namely, De Geest in his recent groundbreaking article on removing rents introduces a pathbreaking differentiation between different sources of inequality and related, until now overlooked, phenomena of rents as a source of inequality. De Geest observes that there are two fundamental ways to correct income inequality⁷⁶. The first previously discussed Shavell and Kaplow's article (the general economic one) that intervenes after income inequality has occurred and the second one coined by De Geest as the "*ex ante* approach" which tries to prevent income inequality from occurring in the first place. De Geest also argues that if the inequality is not caused by the differences in efforts or talents but by rent-seeking behavior (rents)⁷⁷, then the *ex ante* legal intervention is superior because it prevents income inequalities from occurring in the first place – this is what he calls an *ex ante* approach⁷⁸. Namely, legal system has an information advantage combating ruinous inequality in comparison to the *ex post tax-and-transfer system* since it needs less information than the later⁷⁹.

Moreover, the *ex post tax-and-transfer system* leaves the source of inequality and the price distortions associated with rents unaffected. In other words, *ex post tax-and-transfer system* cannot observe the causes of inequality and cannot in line with Kenneth Arrow's insight by adjusting the starting position achieve perfect markets and their efficient outcomes⁸⁰. Arrow shows that when one is trying to balance the excesses of competitive markets then she should not interfere with the markets themselves but should adjust the starting block. As it is in practice due to the asymmetric information problem unfeasible one should hence via public education put everyone on an equal footing. Afterwards perfect markets then find every possible opportunity to make everybody better off from their revised starting points. Furthermore, De Geest convincingly shows that legal rules that prevent rents from occurring are intrinsically

⁷⁶ G. De Geest, *op. cit.*

⁷⁷ He defined rents as profits that would not have been earned in a perfectly competitive and transparent economy; *ibid.*

⁷⁸ Although this is a largely untested hypothesis at this point it may well be that prevention of rents might be the most understated, overlooked function of legal systems from ancient Roman law onwards.

⁷⁹ De Geest shows that legal system needs less information than the tax system since it intervenes at an *ex ante* stage where there is less information required than at an *ex post* stage, where the symptoms have to be removed. In order to effectively address inequality and rents problem legal system need merely information on the total amount of rents and not on individually received rents and consequent inequality; G. De Geest, *op. cit.*, p. 10 onward.

⁸⁰ K. Arrow, *op. cit.* See also K. Arrow, G. Debreu, *op. cit.*

better at correcting these market failures and that preventing them *ex ante* is intrinsically superior to correcting them *ex post*⁸¹. Hence, as argument goes, legal rules that prevent rents therefore reduce labor and price distortion and that the trade-offs between equity and efficiency should be made in the legal system whenever legal rules generate or reduce rents⁸². Thus, one should make an analytical distinction between different sources of rents and consequential income inequality and design legal rules accordingly.

III.B. Public law and public higher education

Previous section emphasizes the potential advantage of an *ex ante* regulatory intervention in comparison to the *ex post* one in instances where the inequality is not caused by the differences in efforts or talents but by rent-seeking behavior (rents). However, if indeed such approach is the most efficient one, the issue of what kind of such an *ex ante* approach should be employed becomes the second most important questions that triggers the attention of legal scholars. Should a policy maker then introduce an *ex ante* lump sum individual taxation that would depend on future income or shall a law-maker, while designing regulation, pursue redistribution goals and neglect the other social objectives of law?

We argue that an effective law-maker should, while tackling the inequality problem, design its policy in line with the golden Tinbergen rule – N problems requires N solutions. This rule, employed in natural sciences as a general research maxim, was formulated by the Dutch economics Nobel laureate, Jan Tinbergen in 1952 and is generally stated as “for each policy objective, at least one policy instrument is needed - there should be at least the same number of instruments as there are targets”⁸³. Hence, an informed law-maker should identify multiple sources/causes of inequality (rents) and for each of them design its own *ex ante* regulatory instrument. Legal rules should be designed to *ex ante* deter/prevent formation of inequality that is caused by rent-seeking behavior (rents). If, however, inequality is caused by the differences in efforts or talents then such an inequality should be allowed and might be eventually, according to specific, efficiently justified, normative preferences of a national law-maker, tackled only with the economically suggested *ex post tax-and-transfer system* of redistribution. We argue that the potential *ex post* intervention should only be done in line with previously emphasized economic principles. In other words, *ex post* pursuit of distributive justice should

⁸¹ G. De Geest, *op. cit.*

⁸² G. De Geest, *op. cit.* He also emphasizes that rents are from analytical perspective implicit commodity taxes causing labor and price distortions.

⁸³ J. Tinbergen, *On the Theory of Economic Policy*, North-Holland, 1952.

not be done via modifying or reshuffling private legal rights but only via progressive taxation and social welfare programs.

Following this line of reasoning public law and related legal regulation of higher education appear as one of the most important legal areas/disciplines which fits into this *ex ante* framework of instances where the inequality is not caused by the differences in efforts or talents but by rent-seeking behavior (rents)⁸⁴.

According to the still dominant legal scholarship, public law is a coherent set of rules, ordered by some general principles, like the rule of law, impartiality, transparency, and proportionality, and characterized by its own specific features, such as the existence of public law entities, the special prerogatives of the Executive and its related branches, the decision-making procedure, and the judicial review⁸⁵. On the other hand, the law and economics literature has traditionally paid very little attention to public and administrative law and their rules⁸⁶. Notwithstanding its great expansion also in nonmarket fields, it is still an “unexpected guest” in the public law context⁸⁷. Modern law and economics analysis of public law divides into two strings of work. One dealing with causes and consequences of bureaucratic action inside bureaucracies and the other focusing on external interaction, such as between legislators and the bureaucratic institutions comprising executive branch, between the latter institutions and the citizens and enterprises⁸⁸. Surprisingly, the potential employment of public law as an *ex ante* mechanism to tackle the sources of inequality has received very little attention in law and economics scholarship.

This paper argues that the public law and its regulation of higher education is one of the most important mechanisms for an *ex ante* efficient curing of market failures, deterring rents, reducing information asymmetries, and hence facilitating the removal of the causes of income inequality in first place.

The importance of higher education for removing the causes of inequality and for adjusting the starting positions can hardly be overstated. In economic terminology higher

⁸⁴ For an excellent synthesis of public law regulation of education see D. Tyack, T. James, A. Benavot, *Law and the Shaping of Public Education, 1785-1954*, The University of Wisconsin Press, 1987.

⁸⁵ See e.g. M. Elliot, R. Thomas, *Public Law*, Oxford University Press, 2017; A. Le Sueur M. Sunkin, J. Khushal Murken (eds.), “Public Law Text, Cases, and Materials”, Oxford University Press, 3rd ed., 2016.

⁸⁶ G. Napolitano, “Administrative law” in A. Marciano, G. Rammello (eds.), *Encyclopedia of Law and Economics*, Springer, 2014, available online: DOI 10.1007/978-1-4614-7883-6_526-1.

⁸⁷ T. Ulen, “The unexpected guset: law and economics, law and other cognate disciplines, and the future of legal scholarship”, *Chicago-Kent Law Review*, 2004, vol. 79, issue 2, pp. 403-429.

⁸⁸ W. Weigel, “Why Promote the Economic Analysis of Public Law?”, 2006, *Homo Economicus*, vol. 23, issue 2, pp. 195-216.

education is generally regarded as a public good with extensive, significant positive externalities⁸⁹. For example, research and teaching at universities are a major source of production and dissemination of knowledge. Knowledge is a public good, with an open access, and when embedded by entrepreneurs in new investments, it increases the quantity and quality of goods and services (including public services) offered to all higher education feeds the labor market and the society with highly skilled manpower, which allows for increases in workforce productivity and favors professional mobility⁹⁰. The positive impact of education and human skills on economic growth and development is also a widely recognized externality⁹¹. In other words, the social benefits of higher education are higher than individual benefits and hence in the absence of the state intervention (pure market situation – market provided higher education), higher education would be under-produced and under-consumed⁹². In addition, the benefits of tackling the disastrous effects of inequality should be accounted for on the benefit side of such an equation. In such instance, the arguments for publicly provided higher education became even more persuasive.

However, it should be emphasized that current EU MS public law provisions and its regulatory framework in the field of higher education differs substantially. Analysis reveals that current EU MS public law regimes could be classified into three broad groups: a) EU MS with no or low tuition fees and generous student support systems in the form of student loans/vouchers or grants (governed by public law in The Netherlands, Denmark, Sweden, Finland and Norway); b) EU MS with low tuition fees and less-developed student support systems (Austria, Belgium, Czech Republic, France, Germany, Ireland, Italy, Poland, Portugal, Switzerland, Slovenia and Spain); and c) EU MS with high tuition fees and well-developed student support systems (United Kingdom)⁹³. The discussion on which of these systems is a more effective one, although a very substantive one, exceeds the limits of this paper and can be

⁸⁹ However, one might also argue that higher education should not be regarded as a public good, since it can be appropriable and excludable.

⁹⁰ P.-B. Ruffini, “Economic Models of Higher Education: An International Perspective”, *International Dialogues on Education: Past and Present*, 2015, vol. 2, issue 2.

⁹¹ See e.g. M. Gradstein, M. Justman, “Education, Social Cohesion and Economic Growth”, *The American Economic Review*, 2002, vol. 92, issue 4, pp. 1192-1204; J. Tilak, “Higher education: a public good or a commodity for trade?”, *Prospects*, 2008, vol. 38, issue 4, pp. 449-466; D. Cecchi, *The Economics of Education: Human Capital, Family Background and Inequality*, Cambridge University Press, 2006; Z. Griliches, “Education, Human Capital, and Growth: A Personal Perspective”, *Journal of Labor Economics*, 1997, vol. 15, issue 1, part 2; G. Becker, *Human Capital: A Theoretical and Empirical Analysis with Special Reference to Education*, The University of Chicago Press, 3rd ed., 1994; and T. Schultz, *Investment in Human Capital. The Role of Education and of Research*, Free Press, 1971.

⁹² *Ibid.*

⁹³ OECD, *Education at a Glance: OECD Indicators*, OECD Publishing, 2016.

found elsewhere⁹⁴. However, one should note that the quality of provided education, the obtained results, high levels of innovation, low levels of inequality, high human development indexes offer a broad scope of evidence in support of a “Nordic model”⁹⁵. Moreover, the OECD report shows that the most successful EU MS The Netherlands, Norway, Sweden and Denmark actually combine grants and loans⁹⁶. For example, The Netherlands employs the so-called participation system which is publicly governed/provided higher education scheme but which is actually designed to mimic the market⁹⁷. Such a system induces universities to provide high-quality higher education and also induces citizens with incentives to make rational choice decisions, to invest and make efforts and consequently allocating economic and human resources to their best effective use. This system also derives its operational mode from the so-called “protestant doubt-full scientific approach” and from the early works of the Erasmus of Rotterdam. Namely, his seminal statement, motto that “*de enige manier om beter te worden is je eigen werk afkeuren*” (“the only way to get better is to reject your own work”)⁹⁸ can be employed as an illustration of such a higher education model.

In relation to this discussion, government-provided public higher education could be taken as an example of a free non-market service. However, such a system conceals the fact that the poor do not get the same quality of education that the rich do. Namely, the real information on values, quality, costs and benefits are in such a “free” system very often blurred. In a market system, where one would have to pay out-of-pocket directly for his education, the information on how much it costs to provide good, high quality higher education and who would be willing to pay for such an education would emerge immediately. On the other hand, the existing non-market *free-for-all* public higher education struggles with these basic questions. Moreover, such a system is prone to low-quality-education service (and consequent poor performance of graduates) since it, in general, disincentivizes providers of education (reduces its quality) and triggers benevolent, free-riding attitude on the side of students/citizens.

Would than a public subsidization of higher education as well as for example the introduction of mortgage interest deduction schemes for home ownership represent the correct

⁹⁴ For an excellent assessment and overview see: EU Commission, *Education and Training Monitor*, 2017 available online: https://ec.europa.eu/education/policy/strategic-framework/et-monitor_en.

⁹⁵ *Ibid.*

⁹⁶ OECD, *op. cit.*

⁹⁷ The Netherlands actually experienced the transition from a partly grant-based system to low-interest loans, enrolments initially dropped in higher education but recovered in 2016; see EU Commission, *Education and Training Monitor 2017 Netherlands*, Luxembourg: Publications Office of the European Union, 2017.

⁹⁸ Erasmus Desiderius, *De correspondentie van Desiderius Erasmus. Deel 7: Brieven 993-1121*, (trad. István Bejczy en John Piolon, 2010), Donker Rotterdam.

public regulatory intervention? The basic insight is that subsidization of higher education is effective insofar as it cannot be tracked down to the individual recipient. For example, if the bank knows that you receive an income tax deduction, it will adjust its interest rate accordingly. In similar, but slightly different vein the loans to students might result in a similar outcome: admission fees will be such that a large part of the benefit to the student will end up in the accounts of the University. This, of course, forms a substantive problem for the welfare state and for the effective removal of causes of inequality. Direct income transfers must either be so small that it doesn't pay for commercial parties to adjust their pricing to recoup the subsidization or be distributed in such a way that it is very difficult or impossible to determine whether or not an individual customer belongs to the group of recipients. In short information asymmetry must be conserved. To sum up, the so-called Nordic system might be taken as raw model for potential EU-wide regulatory intervention.

IV. TOWARDS THE OPTIMAL EU *EX ANTE* REGULATION OF HIGHER EDUCATION AND CREATION OF SOCIAL FABRIC

Addressed *ex ante* investments in education (human capital) and related public law intervention features as one of the most significant measures in deterring rents, removing the causes of inequality, simultaneously addressing/preventing wage stagnation without increasing EU MS public indebtedness. Identified regulation of higher education as one of the core *ex ante* mechanism for removing the causes of ruinous inequality generated by rent-seeking behavior paper calls for an EU-wide regulatory policy intervention. In addition, the shift of the law-maker's (policy-maker) regulatory attention from the *ex post* policy intervention which merely treats the inequality's symptoms towards the *ex ante* focus on removal of its causes appears as one of the main arguments of our paper.

However, it should be stated that the EU has recently in the field of higher education launched several, outmost promising, initiatives that represent long-awaited steps towards fully harmonized public law framework of higher education⁹⁹. Paper argues that such a policy should be fully supported and designed to tackle the disastrous problem of inequality and related

⁹⁹ At a general level EU has in place the "EU promotion of equity, social cohesion and active citizenship" program that aims at fostering the education of disadvantaged children and young people, by ensuring that EU MS education and training systems address their needs. Moreover, policy framework on promoting inclusion and fundamental values through education, as well as an online compendium of good practices are also launched. See http://ec.europa.eu/education/policy/strategic-framework/social-inclusion_en.

destruction of social fabric and cohesion that threatens/undermines the sole existence of our European project.

IV.A. EU development of higher education policies

Through its Erasmus+ and Horizon 2020 programs, the EU indeed supports international exchanges for students, academic staff and researchers, as well as structured cooperation between higher education institutions and public authorities in different countries. The stated objective is to create new opportunities for people in higher education to learn from one another across national borders and to work together on joint projects to develop good learning and teaching, undertake excellent research and promote innovation¹⁰⁰.

Moreover, the EU Commission works closely with MS policy-makers to support the development of higher education policies in EU countries in line with the Education and Training 2020 strategy (ET2020)¹⁰¹. This renewed EU agenda for higher education, which should also academic credits, adopted by the Commission in May 2017, identifies four key goals for European cooperation in higher education: a) tackling future skills mismatches and promoting excellence in skills development; b) building inclusive and connected higher education systems; c) ensuring higher education institutions contribute to innovation; and d) supporting effective and efficient higher education systems¹⁰². To achieve each of these ambitious, and long-awaited goals, the EU Commission proposes a set of specific actions at EU-level, primarily supported by different strands of the Erasmus+ and Horizon 2020 programmes. In order to ensure that these aims are met the EU Commission is also developing and supporting tools to promote mobility (such as ECTS and the Diploma Supplement), increase the recognition of skills and qualifications, and provide better information about higher education in Europe. In addition, the EU Commission also provides support to the Bologna Process, designed to promote higher education reform with a view to establishing a European

¹⁰⁰ See EU Commission, *Education and training: Supporting education and training in Europe and beyond*, 2017.

¹⁰¹ Under this ET2020 strategy each EU country is responsible for its own education and training systems. EU policy is designed to support national action and help address common challenges, such as ageing societies, skills deficits in the workforce, technological developments and global competition. Education and training 2020 (ET 2020) is the framework for cooperation in education and training. Moreover, it is also a forum for exchanges of best practices, mutual learning, gathering and dissemination of information and evidence of what works, as well as advice and support for policy reforms. In order to ensure the successful implementation of ET 2020, Working Groups composed of experts nominated by member countries and other key stakeholders work on common EU-level tools and policy guidance; see https://ec.europa.eu/education/policy/strategic-framework_en.

¹⁰² *Ibid.*

Higher Education Area, and promotes the exchange of good policy practices between different countries through the ET2020 higher education working group¹⁰³.

Obviously, considering previous discussion the Education and Training 2020 strategy (ET2020) should be applauded for and is actually designed in line with our suggestions as an *ex ante* mechanism that should remove the causes of inequality and that tackles the part of ruinous income inequality that is caused/enabled by unjustified rents and rent-seeking behavior.

IV.B. 2030 Agenda for Sustainable Development

While addressing EU initiatives one should briefly mention also the 2030 Agenda for Sustainable Development and its 17 goals to transform our world. The very first goal of this Agenda is to end poverty in all its form everywhere, and even though poverty rates have been cut by fifty percent in the last three decades without increasing social mobility many people risk slipping back into poverty. The term poverty refers not only to the lack of resources (income or wage), but include limited possibilities to education, social discrimination and exclusion as well as hunger in extreme cases. Economic growth must be inclusive to provide sustainable jobs and promote equality¹⁰⁴. One of the goals is also to ensure equal right to economic resources¹⁰⁵ and to reduce exposure and vulnerability to economic, social and environmental shocks and disasters. Agenda also suggests a creation of a sound policy framework at the national, regional and international levels, based on pro-poor and gender-sensitive development strategies, to support accelerated investment in poverty eradication actions. Another goal closely connected to social challenges is ensuring inclusive and quality education for all and promote lifelong learning, as obtaining a quality education is the foundation to improving people's lives and sustainable development.

CONCLUSIONS

¹⁰³ In addition ET2020 sets the following outstanding EU education benchmarks for 2020: a) at least 95% of children (from 4 to compulsory school age) should participate in early childhood education; b) fewer than 15% of 15-year-olds should be under-skilled in reading, mathematics and science; c) the rate of early leavers from education and training aged 18-24 should be below 10%; d) at least 40% of people aged 30-34 should have completed some form of higher education; e) at least 15% of adults should participate in lifelong learning; f) at least 20% of higher education graduates and 6% of 18-34 year-olds with an initial vocational qualification should have spent some time studying or training abroad; and g) the share of employed graduates (aged 20-34 with at least upper secondary education attainment and having left education 1-3 years ago) should be at least 82%; *ibid.*

¹⁰⁴ UN, *op. cit.*

¹⁰⁵ Including basic services, ownership and control over land and other forms of property, inheritance, natural resources, appropriate new technology and financial services, including microfinance.

Traditional economic literature offers *ex post* tax-and transfer system (*ex post* redistribution) and direct social transfers as the exclusive institutional mechanisms that should regulate inequality and social exclusion. This paper, while following De Geest ground-breaking insights, employs an example of the optimal regulatory intervention in the field of public law and its regulation of public higher education, supports the view that legal system might indeed be intrinsically superior to the classic *ex post* interventions (e.g. tax-and transfer system or all-encompassing subsidies) at reducing income inequality that has been caused by the rent-seeking behavior (and not by the differences).

This paper offers *ex ante* investments in higher education (human capital) and related regulatory public law intervention as one of the most significant measures that will in long run address wage stagnation without increasing EU MS public indebtedness. Furthermore, due to the utmost importance of education as an *ex ante* mechanism for rent prevention and for removing the causes of ruinous inequality paper calls for an EU-wide regulatory policy intervention. In addition, legal rules should be designed to *ex ante* deter/prevent formation of inequality that is caused by rent-seeking behavior (rents). If, however, inequality is caused by the differences in efforts or talents then such an inequality should be allowed and might be eventually, according to specific, efficiently justified, normative preferences of a national lawmaker, tackled only with the economically suggested *ex post tax-and-transfer system* of redistribution. We argue that the potential *ex post* intervention should only be done in line with previously emphasized economic principles. In other words, *ex post* pursuit of distributive justice should not be done via modifying or reshuffling private legal rights but only via progressive taxation and social welfare programs.