Professional cartels and scale fees: chiselling on the celtic fringe?

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1. Introduction

Economists have been, traditionally, highly critical of many aspects of professional self-regulation [see, for example, Friedman and Kuznets (1945), Friedman (1962), Faure et al. (1993), Benham and Benham (1975), Arnauld (1972), Arnauld and Friedland (1977), Lees (1966), Kessel (1958), Leffler (1978)]. More recently there has been a greater awareness of the informational asymmetry inherent in professional markets which demand some protection for the (infrequent) consumer of personal professional services [see, for example, Dingwall and Fenn (1987)]. Nevertheless, there has been a gradual shift in the policy debate against self-regulation which has quickened in pace, particularly in the UK, in recent years [MMC (1970, 1976a, 1976b), FTC (1984), DTI (1989), HMSO (1990)]. Commentators have identified three principal instruments of self-regulators which work against the public interest: (i) restrictions on entry; (ii) restrictions on fee competition; and (iii) restrictions on advertising and other means of promoting a competitive process within the profession. The economics literature on the self-regulation of the legal profession is surveyed in Stephen and Love (2000).

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The present paper is concerned, in particular, with empirical evidence on the effectiveness of restrictions on fee competition. It presents tests of the view widely held by policy-makers and academic commentators that the existence of a recommended scale of fees drawn up by a profession’s self-regulatory body will result in such recommended fees actually being charged.

The paper is structured as follows. In the remainder of this section we review briefly what economists have had to say on professional self-regulation, in general, and in particular on the use of fee scales, contrasting the views expressed on fee scales with those expressed more generally on price fixing by cartels. The next section examines the applicability of these arguments to the market for conveyancing services and presents empirical evidence from two jurisdictions at two points in time: Scotland in 1984 prior to the liberalization of conveyancing markets in 1985 and the Republic of Ireland in 1994. In both cases the solicitors’ self-regulatory body published a Table of Recommended Fees for Conveyancing. The third section of the paper assesses the view that self-regulatory bodies act as professional cartels using data from Scotland and Ireland. A final section concludes the paper.

Self-regulation is characterized by many economists as, potentially, having the effect of a cartel: by controlling entry to the market and setting an agreed price above the competitive price members of the profession earn economic rents. Restrictions on advertising and prohibitions on using fee-levels to attract business are used to restrain competition from ‘breaking out’ between existing suppliers. Restrictions on entry to a profession or restrictions on providing a particular service by persons not recognized by a particular professional body have been the subject of criticism by economists [see, for example, Friedman and Kuznets (1945), Leffler (1978)]. This can undoubtedly lead to supply shortages and hence the earning of substantial economic rents by members of the profession. However, restrictions on entry to the profession in general do not necessarily imply an absence of competition in specific service markets. Professional service markets, particularly of a personal nature, tend to be spatially localized. General controls on entry do not necessarily, therefore, imply barriers to entry into specific service markets for existing members of the profession. Other restrictions on behavior such as prohibiting advertising may raise the cost of entry (through an inability to quickly generate good will) and thus constitute a barrier to entering a specific spatial market. Alternatively prohibitions on ‘undercutting’ or ‘supplanting’ existing suppliers may reduce the incentive to enter a local market where rents are being earned.

The literature on professional advertising and competition is reviewed in Stephen and Love (2000). The extensive empirical evidence on the restriction of advertising of professional services and what happens to fee levels when such restrictions are relaxed is assessed in Love and Stephen (1996). The general thrust of the evidence from this literature is that restrictions on advertising increase the fees charged for the profession’s services and that the more advertising there is the lower are fees.

It has been argued that restricting fee competition, particularly by publishing mandatory or recommended fee scales reduces competition and innovation and is against the public interest [MMC (1970), Arnauld (1972), Arnauld and Friedland (1977), Domberger and Sherr (1989), Van den Bergh and Faure (1991)].

In contrast to the considerable empirical research on the role of advertising (as discussed above) there would appear to have been little on the effectiveness of recommended fee
scales. This is somewhat surprising. Observers of professional self-regulation are highly critical of scale fees:

In general, we regard a collective obligation not to compete in price, or a restriction collectively imposed which discourages such competition, as being one of the most effective restraints on competition. The introduction of price competition in the supply of a professional service where it is not at present permitted is likely to be the most effective single stimulant to greater efficiency and to innovation and variety of service and price that could be applied to that profession. [MMC (1970), p 78]1

In professional markets, although some scale fees have been described as mandatory or having the backing of the State, in many cases they are ‘recommended’ charges [MMC (1970) pp. 21–22, Arnauld (1972) p. 498]. Even where they are ‘mere’ recommendations it has been argued that they have the effect of raising fees:

There appears to us to be little difference between so-called mandatory and recommended scales in their practical effect . . . although disciplinary action could not be taken specifically for breach of a recommended scale, the fact that the fees charged were not in accordance with the scale might in some circumstances be quoted in support of a charge of breach of some other rule . . . such that the established practitioner would not depart more readily from a ‘recommended’ scale than from a mandatory scale. [MMC (1970) p. 22] 2

Similarly, the Fair Trade Commission in the Republic of Ireland argued against mandatory scale fees and considered that recommended and maximum fees will tend to be considered as fixed fees:

... there may be little practical difference between mandatory and recommended scales . . . . . . recommended fees will tend to assume the character of fixed charges. . . . [fixed fees are] likely to lead to higher charges than would otherwise occur [and are] a serious detriment to competition, without compensating advantages [FTC (1990) p. 218–20]

However, economists are skeptical, in general, of the ability of cartels to avoid members of the cartel selling output at prices below that agreed by the cartel. This practice has become known in the economics literature as ‘chiselling’ [see, for example, Cohen and Cyert (1965, pp. 245–6)]. Where a cartel sets price above marginal cost each firm in the cartel has an incentive to increase its profits by selling more than its quota by reducing price below the cartel price (Stigler, 1964). A number of factors have been identified as being important in determining the likelihood of such chiselling and consequently the stability of cartels because they effect the ease of detection and policing of chiselling and the ability of the cartel to enforce its price.

2. The empirical context

There have been very few published studies of fee restrictions imposed by professional regulatory bodies. One such study is Arnauld and Friedland (1977) where the relationship between the incomes of a sample of lawyers and minimum recommended fees for a simple transaction was estimated. A positive relationship was found between minimum recom-
mended fee and lawyer income. If demand for the simple transaction is inelastic this implies that fees charged rise as the minimum fee rises. Although the general thrust of this paper is critical of the setting of minimum fees the authors point out that there may be widespread cheating on the recommended fee schedule.

The present paper brings together further unpublished evidence on the pricing of professional services in the presence of recommended fee scales in order to test the proposition that ‘recommended’ fee scales will inhibit competition and help enforce the ‘professional cartel’. The evidence is drawn from the area of conveyancing which is a relatively standard legal service and hence might be thought susceptible to control through scale fees. Two jurisdictions provide the context:

2.1. Scotland in 1984. The behavior of solicitors in Scotland is regulated by the Law Society of Scotland, their professional body. Subject to approval by Scotland’s senior judge, their rules of professional conduct have been given the force of law under delegated legislation. In 1984 these practice rules prohibited advertising by individual solicitors or firms of solicitors and the Law Society of Scotland published a Table of Recommended Fees for conveyancing transactions.3

The so-called scale fee for conveyancing published by the Law Society of Scotland was not a mandatory scale. It provided ‘what the Society considers to be reasonable charges which may be recommended for the average transaction’ [Law Society of Scotland (1977), p155]. Such fees have been interpreted by some as maxima [MMC (1970) p29] but, as pointed out above, it has been argued that they are likely to become the normal charge. Indeed that was the conclusion reached by the Monopolies Commission itself [MMC (1970, p22)]. The Law Society of Scotland’s scale fee for conveyancing was a function of the value of the property involved.

2.2. Republic of Ireland in 1994. In Ireland, the Incorporated Law Society recommends a conveyancing scale fee for the purchase of a property of one and a half percent of the property value and one percent plus £100 on the sale of the property. These scale fees are calculated to make allowance for solicitor’s time and for overheads, including staff costs (FTC, 1990). The solicitor and the client are permitted to come to an alternative agreement on the level of remuneration and the scale fee was originally intended to be the maximum fee a solicitor could charge if they could not reach an agreement on fees. Following the introduction of the Competition Act 1991, the Law Society in Ireland is prohibited from publishing compulsory scale fees in relation to conveyancing. Instead the Society “recommends” that solicitors charge the scale fees.

The situations with regard to scale fees for lawyers in the two jurisdictions and some summary data are presented in subsequent sections. Subsequently more formal statistical evidence is presented. Before turning to this, however, these two contexts are assessed in terms of the conditions required for effective enforcement of cartel prices.4

2.3. Legal environment. Co-ordination of pricing policy through a well disciplined cartel will be difficult in jurisdictions which outlaw cartels and/or price co-ordination (e.g., United States). Sanctions against ‘chiselaers’ would be unenforceable by law and thus would have to
be informal in nature. Thus the legal status of the ‘cartel’ will determine the ability of its members to punish ‘chiselers’ and hence the incentive to chisel.

The legal environment in the two jurisdictions at the relevant times was one which exempted each of these professional bodies from that country’s legislation prohibiting restrictive practices. The professional bodies were also invested with the power to make regulations governing the behavior of their members and powers to discipline members in breach of such regulations. The disciplinary powers extended as far as withdrawing a solicitor’s right to practice. Thus these professional ‘cartels’ would seem to meet the first test for exercising cartel discipline.

2.4. Nature of demand. The more homogeneous the product or service produced, the easier it will be for a cartel to judge whether a member is chiselling, that is whether deviations from the cartel price ‘genuinely’ arise from these differences or contain an element of chiselling. In addition, other factors such as rapid technological change, unstable demand and elastic demand are less likely to be able to sustain a cartel, ceteris paribus.

Conveyancing is seen by many as a relatively routine legal service well within the competence of any qualified solicitor. Both professional bodies would argue that every practitioner carries out conveyances to the same high professional standard. However, the work involved in a conveyance is as varied as the location and ownership history of the property determines. Furthermore, different consumers may demand a different service in terms of number of meetings with the solicitor, speed of completion and the physical environment in which they meet the solicitor. In other words, although the formal conveyancing work for two clients might be identical the ancillary services they require may be different and vary in cost. Hence, demand may well be heterogeneous and pose problems for cartel discipline.

The demand for conveyancing is a derived demand. It is determined by house purchase activity which in turn will be related to the economic cycle. However, housing activity will be related to local economic circumstances and thus will vary from region to region. Thus it will be difficult to monitor adherence to a national scale. However, firms in a given locality may be more attuned to local variations in demand. Thus local collusion may be more likely than adherence to a national scale. The existence of a cycle makes discipline even at a local level problematic.

Although professional services may not appear to be likely candidates for high rates of technological change in one respect the routine service of conveyancing is: computerization makes possible greater routinisation of the work and thus may disrupt the homogeneity required for cartel discipline. On the other hand, because the demand for conveyancing is derived from the demand for house purchases and represents a relatively small proportion of the cost of purchase it may be thought that the demand for conveyancing is relatively price inelastic. This suggests less incentive to cheat on the cartel price.

2.5. Cost conditions. Differences in costs between cartel members will affect the ease with which the cartel can agree on price and in the ability to use sales as an indicator of chiselling. In addition, a high level of fixed costs relative to marginal cost also encourages chiselling on price to increase the sales over which the fixed costs may be spread.
Firms of solicitors of the same size and mix of work are likely to have similar cost structures. In both jurisdictions there are a large number of very small firms doing mostly work for household and small business clients. For these firms costs will be homogeneous suggesting, \( \textit{ceteris paribus} \), greater cartel discipline. On the other hand, the larger firms are more likely to be involved in more commercial business and thus have a higher opportunity cost of their time and hence a different cost structure. This may interfere with cartel discipline. However, in both jurisdictions such large firms will tend to be located in the larger cities suggesting that cartel discipline will vary between such markets and the more rural and small town markets. The position with respect to fixed costs is less clear cut than it might at first seem. Law firms have low physical capital suggesting less incentive to chisel, but they are human capital intensive organizations. Solicitors have made a relatively large investment in their own training which has to be recovered through fees. This provides the incentive to chisel in order to keep business coming in to ‘pay back’ the investment in human capital.

2.6. Transparency of prices. Industries where contract prices are subject to negotiation (e.g., contracting, second-hand car sales) have greater scope for hidden price cuts. Conveyancing prices are nontransparent. Only the solicitor and the client know the fee charged for a particular transaction. This is particularly the case for these two jurisdictions at the relevant times since fee advertising by solicitors was not permitted. This suggests a greater likelihood of chiselling.

2.7. Number of firms, market concentration and relative firm size. The fewer the number of firms the more interdependent is the demand for each firm and the more obvious, \( \textit{ceteris paribus} \), the effect of chiselling. It may also affect the ability of cartel to punish chiselers. Clarke (1985) argues that the argument with respect to number of firms generalizes to market concentration in that high levels of concentration are associated with low levels of price cutting. George, Joll and Lynk (1992) argue that relative firm size is important in that where one firm is much larger than the others it may tolerate price cutting by the smaller firms. On the other hand, a dominant firm may have a credible threat of punishment over the smaller firms.

Although in both jurisdictions the number of firms is relatively high suggesting more likelihood of chiselling on the scale fee, the fact that the firms are geographically dispersed across local service markets (many of which were highly concentrated) suggests that chiselling on local (tacit or explicit) agreements on fees is less likely. The relative size of largest firms involved in conveyancing compared to most firms is quite low suggesting a low ability to discipline chiselers in the market. This applies both nationally and locally.

2.8. Smaller customers and repeat purchasers. These two factors are likely to make it more difficult to detect cheating. In the market for domestic conveyancing individual customers are small relative to both the national and local markets. Furthermore, they are only likely to be repeat purchasers over relatively long time spans. This suggests a low ability to perceive chiselling.

2.9. Nonmembers of the cartel and barriers to entry. This factor limits the ability of a cartel
to enforce its prices and thereby provide an incentive for members to cheat. Barriers to the entry of new firms in the industry are necessary to maintain discipline among cartel members.

At the relevant time periods in both jurisdictions there were no suppliers of conveyancing services who were outside the jurisdiction of each Law Society. It was illegal for a nonsolicitor to supply conveyancing services. While it was possible for a solicitor from outside a locality to operate outside any co-operative agreement on pricing between local firms there were barriers to entry (particularly given the prohibition at that time on advertising in Scotland and price advertising in Ireland) in the form of the need to generate goodwill locally and a client base. This suggests an ability to discourage chiselling.

On balance all of this suggests that in the field of conveyancing although the two professional bodies operated in a legal environment which made it possible to enforce scale fees, their ability to observe chiselling was limited. However, the conditions do seem to suggest a greater ability of firms in each geographical locality to observe deviations from local tacit or explicit agreements on fees as well as the incentives to enter into such agreements. As such the legal profession in both countries merit an investigation in terms of their potential ability to control prices.

In the next section we test the proposition that recommended fees will ‘tend to be considered as fixed fees’ by considering empirical evidence from these two instances where recommended scale fees were published by a profession’s self regulatory body.

3. Empirical tests

3.1. Scotland, 1984

The data analyzed here come from a sample of Fee Notes (bills) for carrying out conveyancing transactions rendered to clients by 55 firms of solicitors in 1984. Because the 55 respondents represented a low response rate from the original sample they cannot be considered representative of all Scottish solicitors’ firms. However, the selection of each firm’s Fee Notes was random. Thus, although the firm’s cannot be treated as an unbiased sample of Scottish firms, the fee notes can be treated as a random sample of fee notes of these 55 firms. Consequently inferences can be drawn about the behavior of these firms but not about Scottish solicitors’ firms in general. Nevertheless, evidence that firms in the sample deviate from the recommended scale fee refutes the view that there is ‘little difference between so-called mandatory and recommended scales in their practical effect’.

There are two broad categories of conveyancing transaction covered by the fee notes: those for sales of property and those for purchases of property. The nature of the legal work involved differs between the two types. Furthermore, the sale of a property often permits the seller to withdraw part of his/her equity in the property’s value thereby increasing his/her disposable income and perhaps increasing his/her ability to pay a higher fee. Such considerations do not apply to a purchase. There is also evidence from England (Domberger and Sherr, 1989) that the introduction of greater competition reduced fees for sales by more than those for purchases in that jurisdiction. Therefore, we analyze sales and purchases separately.

A large number of the sample of fee notes gave two fees. The first (and higher) was often
indicated as ‘Fee for professional services as per Law Society of Scotland Scale’. The lower fee was simply described: ‘Fee restricted to . . . ’. The practice of restricting fees was quite open and is legitimized by the fact that the Table of Fees indicates that conveyancing should be charged at the scale or ‘according to circumstances’. The Table of Fees provided guidance on what factors (seven in total) should be considered when charging ‘according to circumstances’. These are all related to the nature of the work carried out, not the circumstances of the client or market factors. Guidance was also given on how each factor should be treated. There was also an over-riding requirement that whatever basis was used to arrive at the fee it should be ‘fair and reasonable’. The practice rules of the Law Society of Scotland also had a prohibition on touting for business and attracting business ‘unfairly’. Holding oneself out to charge below the scale would have been seen as ‘attracting business unfairly’. The existence of the scale should perhaps be seen as an indication of the appropriate fee for firms to charge but not a rigid requirement.

The practice of quoting two fees (restricted and unrestricted) in a fee note was very common among the 55 firms in 1984. The proportion of bills for sale transactions where the fee was declared as restricted was just over 40% while that for purchases was just under 45%. In addition, other fee notes showed a fee charged which was below the scale fee for the property value involved. This suggests that some solicitors who were restricting fees below the scale fee did not declare so on the fee note. Furthermore, because the fee note sometimes covered other services in addition to conveyancing, a total fee, which appeared to be above the scale fee, might incorporate a fee for conveyancing which was below the scale fee but was not separately identified.

An estimate was made of what the full fee for these composite bills would be. This was done separately for sale and purchase transactions by regressing the observed ‘fee as per Law Society of Scotland scale . . . ’ for bills showing two fees on a constant, the scale fee for the property value, dummy variables for the local market in which the firm operated and separate dummy variables where the fee note indicated that (i) a mortgage contract had been drawn up (MOR), (ii) estate agency services had been provided (EA), (iii) insurance services had been provided (INS), (iv) where the property was being registered for the first time (FREG) and (v) other services had been provided (OTH). The size of the law firm (measured by number of qualified solicitors) is also included as an explanatory variable since previous work (Stephen, 1994) has shown that conveyancing fees are sensitive to firm size. Where there was only one transaction in a given market in the sample of transactions indicating two fees that market was dropped from the analysis. This reduced the sample to 43 firms and 10 local markets for sales transactions and 47 firms and 11 local markets for purchase transactions. The resulting regression equations (88 observations on sales, 183 on purchases) were used to predict the ‘total fee as per Law Society of Scotland scale . . . ’ for those fee notes showing only the fee actually charged. Full details of these regressions are available from the authors. Where this predicted total fee exceeded the fee actually shown on the fee note, this fee was classified as restricted. The percentages of observed restricted fees and ‘predicted restricted fees’ for this subset of transactions are shown in Table 1. When the percentage of ‘predicted restricted fees’ is added to the percentage of observed restricted fees it suggests that 82.2% of sale fees and 83% of purchase fees had been restricted below the scale fee. The
mean proportionate reduction in fees for those which were reduced was 19.61% for sale transactions and 12.93% for purchase transactions.

Thus for the firms in the subsample there is substantial *prima facie* evidence that the recommended scale fee had not become the standard fee in Scotland. Even if only the observed restricted fees are considered the evidence still points to considerable variation from the recommended scale fee.

### 3.2. Ireland, 1994

Shinnick (1998) conducted a telephone survey of 604 solicitor firms in Ireland in 1994. Firms were asked the conveyancing fee they would charge on three hypothetical house purchases, *excluding* V.A.T., stamp duty, registration and search fees. A response rate of 80% was achieved. The three transactions were houses valued at:

- £35,000 with a mortgage\(^{12}\) of £20,000 (designated Lowfee)
- £50,000 with a mortgage of £30,000 (designated Midfee)
- £80,000 with a mortgage of £50,000 (designated Highfee)

The £50,000 property transaction represented the average national house price in Ireland in 1994. Table 2 provides summary statistics for the three different house values.

The mean value of £473 for Lowfee has a standard deviation of £62 and ranges from £325 to £550. For Midfee the mean is £643 with a standard deviation of £94 and ranges from £400 to £1125. Highfee has a mean of £946 with a standard deviation of £152 and ranges from £500 to £1800.

In each case the mean value is less than the scale fee. However it should also be noted that for each property value there were some solicitors who charged a fee above the recom-

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<th>Table 1</th>
<th>Restricted fees, Scottish firms 1984 (sub-sample)</th>
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<tr>
<td></td>
<td>Percentage of fees declared restricted</td>
</tr>
<tr>
<td>Purchases</td>
<td>50.01</td>
</tr>
<tr>
<td>Sales</td>
<td>46.07</td>
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<tr>
<th>Table 2</th>
<th>Irish conveyancing fees for purchase (£’s), 1994</th>
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<tbody>
<tr>
<td></td>
<td>Lowfee</td>
</tr>
<tr>
<td>Scale fee</td>
<td>525</td>
</tr>
<tr>
<td>Mean</td>
<td>473</td>
</tr>
<tr>
<td>St. dev. of mean</td>
<td>62</td>
</tr>
<tr>
<td>Median</td>
<td>463</td>
</tr>
<tr>
<td>Minimum</td>
<td>325</td>
</tr>
<tr>
<td>Maximum</td>
<td>800</td>
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mended scale fee. At this aggregate level, F-tests indicate that the mean fees are statistically
different from the recommended scale fee for purchase transactions (i.e., 1.5% of house
price), at the 5% level of significance. This would indicate that over Ireland as a whole the
scale fee is not the determinant of conveyancing fees.13

3.3. Statistical analysis

The previous two subsections have presented evidence which suggests that the existence
of recommended fees for conveyancing in Scotland in 1984 and Ireland in 1994 did not have
the effects predicted by those who argue that professional bodies act as cartels or by public
bodies such as the UK Monopolies and Mergers Commission and the Irish Fair Trade
Commission who have argued that recommended fees become ‘fixed’ fees. The present
section reports statistical analysis designed to test the robustness of these findings.

Systematic variations in fees due to local market conditions are inconsistent with the view
that national recommended scale fees determine the fees actually charged. Consideration of
the nature of conveyancing markets with respect to the conditions for successful policing of
cartels points to local collusive agreements being easier to police than national cartels. In this
section the data from Scotland and Ireland are analyzed to test whether such systematic local
variations existed in the presence of a recommended scale fee. The dependent variable in
each case is PRDISC, the percentage discount on the scale fee (or predicted scale fee). For
the Scottish sample the subsample containing observed and predicted scale fees is used and
separate regressions run for sale and purchase transactions. Because the Scottish fees include
fees for other services, the service dummy variables are included as is firm size. Local market
variations in fees are captured by including dummy variables for all but one of the local
markets in each of the regressions. The estimated coefficients on these dummy variables
measure the deviations, ceteris paribus, of fees in each market from that in the base market.14
For the Irish data which covers fees for hypothetical purchase transactions, only local market
dummies are included as explanatory variables. Again, the statistical significance of the
coefficient on a local market dummy indicates that local market forces affect fees.

The maximum value which PRDISC can take in each of these regressions is one. Where
the fee charged is above the scale fee (or predicted scale fee) PRDISC can take negative
values. Observations on the dependent variable are thus censored and OLS is an inappro-
priate regression technique. Tobit regressions are carried out with the upper limit set at one
and the lower limit set just below the lowest observed value of the dependent variable.

For the Scottish sale transactions observations were drawn from ten Travel-to-Work
Areas, thus a constant and nine locational dummy variables were included along with
transaction dummies and firm size. A χ² test was carried out to test for the exclusion of
insignificant explanatory variables. The value of the test statistic indicates that the exclusion
restrictions are valid. Table 3 shows the estimated coefficients when the exclusion restric-
tions are imposed. These suggest that when no mortgage is involved the rate of discount on
the scale fee is around 9%. The presence of a mortgage leads to a further discount of 11%.
However, the significant coefficient on one market dummy indicates that fees in that market
are, ceteris paribus, discounted by a further 8.7% beyond the discount in other markets. Thus
while there is some evidence of local market factors affecting the size of the discount it is relatively marginal.

In the case of purchase transactions observations were drawn from eleven TTWAs. Consequently one further locational dummy was used in addition to those explanatory variables used in the sale regression. A $\chi^2$ test of 11 exclusion restrictions showed the restrictions to be valid. Table 4 summarizes the results of a regression with the valid

<table>
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<td>Purchase transactions, Scottish sub-sample, 1984</td>
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<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>St. Error</th>
<th>Coefficient</th>
<th>St. Error</th>
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<tbody>
<tr>
<td>Constant</td>
<td>0.151**</td>
<td>3.70E-02</td>
<td>0.15097**</td>
<td>3.70E-02</td>
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<tr>
<td>MOR</td>
<td>0.10861**</td>
<td>3.32E-02</td>
<td>0.10859**</td>
<td>3.32E-02</td>
</tr>
<tr>
<td>LN(SIZE)</td>
<td>-7.40E-02**</td>
<td>1.41E-02</td>
<td>-7.39E-02**</td>
<td>1.41E-02</td>
</tr>
<tr>
<td>DUM65</td>
<td>0.25325**</td>
<td>0.1005</td>
<td>0.25321**</td>
<td>0.10046</td>
</tr>
<tr>
<td>DUM54</td>
<td>-0.18597**</td>
<td>6.41E-02</td>
<td>-0.18594**</td>
<td>6.40E-02</td>
</tr>
<tr>
<td>$\sigma^2$</td>
<td>0.23751**</td>
<td>8.79E-03</td>
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Notes: * Statistically significant at 5% level. ** Statistically significant at 1% level.
restrictions imposed. In the absence of a mortgage the base markets show a discount of 15%. Two statistically significant market dummies indicate that one market involved a discount of a further 25% while a second market had a premium over the scale of just under 4%. When a mortgage transaction is involved a discount of 11% is found. The discount over the scale is reduced as the size of the firm rises.

The Scottish regressions suggest that, in general, fees were discounted on the scale but there was only marginal evidence of variation in discount between markets. In the case of Ireland the data are only available for administrative areas which consist of 26 counties and three cities. Since the data had been gathered from solicitors on standardized conveyancing transactions there is no need to take account of nonconveyancing characteristics of the transaction. Thus PRDISC, the rate of discount on the recommended scale fee, is the dependent variable and the explanatory variables are a constant and 28 locational dummies.

For the observations on Lowfee a χ² test was carried out on the validity of excluding 27 apparently insignificant dummy variables but this rejected excluding them all. However, a similar test showed that it was valid to exclude 26 of them. The results of the restricted regression are shown in Table 5. This reveals that 26 locations have discounts of around 10% and one has a small premium over the scale fee.

The MidFee transaction coincides with the average Irish property price of £50,000 in 1994. A total of sixteen locational dummies were validly excluded according to the χ² test. The results of the restricted regression presented in Table 6 suggests 17 markets with a discount of around 9% and the other 12 having discounts varying from 15% to 21%. This not only suggests widespread discounting of the scale but that the size of the discount varies across local markets reflecting the conditions in the local market.

At the higher end of the market the level of discounting is greater although there is less systematic variation. Similar tests of exclusion restrictions as before were carried out. Twenty-five dummies could be validly excluded. Thus for 26 markets the discount was around 22% while for the other three it was around 10%. The results for HighFee are given in Table 7.

Overall the Irish data suggests that the recommended scale fee was far from the standard
fee. There is evidence of the discount being sensitive to the location of the transaction (as indicated by the significant coefficients on 12 of the 26 market dummies) particularly for properties priced around the average value of £50,000.

The statistical analysis confirms that for the Scottish firms in the sample and for the Irish firms in general there was significant discounting on the recommended scale fees for conveyancing transactions. While the Scottish data shows only limited variation across

Table 6
Discount on midfee

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>9.08E-02**</td>
<td>8.04E-03</td>
</tr>
<tr>
<td>MRK3</td>
<td>0.10394**</td>
<td>2.80E-02</td>
</tr>
<tr>
<td>MRK11</td>
<td>8.48E-02**</td>
<td>3.12E-02</td>
</tr>
<tr>
<td>MRK15</td>
<td>7.38E-02*</td>
<td>3.34E-02</td>
</tr>
<tr>
<td>MRK16</td>
<td>9.25E-02**</td>
<td>3.46E-02</td>
</tr>
<tr>
<td>MRK17</td>
<td>9.59E-02*</td>
<td>3.78E-02</td>
</tr>
<tr>
<td>MRK18</td>
<td>0.12435**</td>
<td>3.61E-02</td>
</tr>
<tr>
<td>MRK19</td>
<td>0.12658**</td>
<td>2.56E-02</td>
</tr>
<tr>
<td>MRK20</td>
<td>9.21E-02**</td>
<td>1.40E-02</td>
</tr>
<tr>
<td>MRK21</td>
<td>6.79E-02*</td>
<td>2.67E-02</td>
</tr>
<tr>
<td>MRK22</td>
<td>9.67E-02*</td>
<td>4.20E-02</td>
</tr>
<tr>
<td>MRK23</td>
<td>8.50E-02*</td>
<td>3.61E-02</td>
</tr>
<tr>
<td>MRK24</td>
<td>7.96E-02</td>
<td>2.39E-02</td>
</tr>
</tbody>
</table>

Notes: * Statistically significant at 5% level.
** Statistically significant at 1% level.

Table 7
Discount on highfee

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>0.22391***</td>
<td>5.86E-03</td>
</tr>
<tr>
<td>MRK4</td>
<td>-0.11224***</td>
<td>2.51E-02</td>
</tr>
<tr>
<td>MRK21</td>
<td>-0.11082***</td>
<td>0.0309</td>
</tr>
<tr>
<td>MRK24</td>
<td>-0.12134***</td>
<td>3.43E-02</td>
</tr>
<tr>
<td>(\sigma^2)</td>
<td>0.12185***</td>
<td>3.91E-03</td>
</tr>
</tbody>
</table>

Notes: *** Statistically significant at the 0.1% level.
markets in the level of discounting the Irish regressions confirm that local market conditions can affect the level of discounting. In particular, for MidFee (which related to the average house price in Ireland at the time) there was wide variation in the level of discounting across local markets.

These Irish regressions indicate that there was considerable variation in discounting across markets, refuting the existence of a single cartel-like price. They do not, however, allow us to judge whether these variations were the result of variations in local-market supply and demand conditions or due to different local cartel determined fees.

4. Conclusions

The economic literature on professional self regulation largely views the professions as producers’ cartels, arguing that scale fees are analogous to cartel prices. These prices are seen as subsidizing inefficient producers and generating economic rents for others. In contrast, microtheorists are generally critical of cartel stability unless fairly stringent conditions effecting the ability of members of the cartel to detect cheating are met. Policy makers have been critical of scale fees for professional services arguing that even when the scale is merely a recommendation it will become the norm. Examination of conveyancing markets suggests that they do not meet the conditions for successful detection of deviations from a national cartel price but do meet the conditions necessary for successful detection of deviations from local collusive agreements.

This paper has sought to use data on conveyancing prices in Scotland and Ireland at points in time where there was a recommended scale fee to assess the validity of these competing claims. Although the Scottish data does not represent a random sample of all Scottish firms it does suggest that for the firms concerned discounting was widespread. The Irish data, which is representative of all Irish solicitors firms, also shows discounting to be widespread.

Both sets of data were analyzed to test whether discounting was a random occurrence or varied by local market. The Scottish data provided only slight evidence of local differences and is probably insufficient to support the claim that there were systematic local deviations from the scale. This may be due to the poor quality of the Scottish data or an insensitivity to local conditions. For the Irish data there does seem to be a greater degree of sensitivity to local markets and systematic deviations from the recommended scale.

The evidence casts doubt on the strongly expressed view of policy-makers that recommended fees are tantamount to mandatory fees. It is clear from the data that for the Scottish sample firms and Irish firms in general the recommended fee was not seen as mandatory. However, this does not necessarily mean that fees were determined competitively. While the data rejects a ‘national cartel’ in both jurisdictions that for Ireland is consistent with, at least, two other explanations: (1) fees are determined competitively in local markets by local forces of supply and demand; (2) fees are determined by local cartels. Differentiating between these two explanations would require data which can relate variations (or lack of variations) of fees in a local market to the conditions required for effective policing of a cartel as discussed above. Neither does it mean that scale fees do not influence actual fees. The national recommended fee may provide a focal point against which solicitors discount. Interviews
with Irish solicitors provide some support for this view (Shinnick, 1998). Many used the recommended scale fee for a sale transaction in setting their purchase transaction fees because it was lower and ‘more appropriate’ in their local market.

The use of the scale fee as a focal point from which to discount may provide an anchor to ensure that firms do not engage in ‘destructive’ competition.

This research cautions against sweeping generalizations based on the view that professional self-regulation generates cartel-like behavior. The conditions in the markets involved will determine whether such ‘cartels’ can successfully police ‘chiselling’. These conditions may be such that only more localized collusive agreements can be successfully policed. It also suggests that the often expressed view of policy-makers that ‘recommended scales are tantamount to mandatory scales’ is too strong.

Notes

1. See also Arnauld (1972), Arnauld and Friedland (1977) and Domberger and Sherr (1989, 1992).
2. See also Arnauld (1972) p498.
3. In 1985 under pressure from the government the practice rules were amended to permit advertising and the Table of Recommended Fees was withdrawn.
4. For a more detailed discussion see, for example, Stigler (1964), Clarke (1985) and George, Joll and Lynk (1992), Carlton and Perloff (1994).
5. In the UK the professions were excluded from the provisions of the Restrictive Trade Practices Act, 1976 which outlawed collusive agreements between firms. In Ireland the professions are excluded from provisions in the Competition Act 1991.
6. The regulations governing the conduct of solicitors are made by the Law Society of Scotland under various Solicitors (Scotland) Acts subject to the approval of Scotland’s senior judge. In Ireland the principal Acts governing the profession are the Solicitor Act, 1954 and 1960, which empowers the Incorporated Law Society of Ireland to make regulations, which in turn are brought before each House of Parliament.
7. In Scotland in the mean firm size was 5.1 solicitors. In 1994 in Ireland the mean firm size was 1.9 solicitors, 37% of firms were sole practitioners.
8. In Scotland in 1984 there were 896 firms of solicitors, while in Ireland in 1994 there were 1712 firms of solicitors.
9. For example in the UK the average length of ownership of a house is about eight years. Research in Ireland suggests that the average person changes house three times during their lifetime.
10. Firms in the sample were drawn from a stratified sample of geographical markets in Scotland but because of low response rates repeated sampling was used. A fuller discussion of the sampling method is given in the Appendix in Stephen (1993).
11. Just over 13.5% sale bills showed a fee below the scale fee for the property value concerned. The corresponding figure for purchases was just under 9.5%.
12. The presence or otherwise of a mortgage is important because some solicitors base a proportion of their fee on the size of the mortgage.
13. The mean fees in each of the 29 administrative regions were also compared to the recommended scale fee. F-tests reveal that for LOWFEE 19 out of 29 regions had fees that were statistically significantly different from the purchase scale fee. For MIDFEE and HIGHFEE the corresponding number of regions were 24 and 29 (i.e., all regions) respectively. See below.
14. That is, the market for which no dummy is included and whose local market effect is captured by the constant term in the estimated equation.
15. It should be remembered that because of the bias in the Scottish data discussed in the text at fn 8 these conclusions can relate only to the fee practices of the firms in the data set and not to Scottish solicitors in general.

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