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Cartels – What are they and how to avoid being part of one: The implications of University fee deregulation

By

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I Introduction

Thank you for inviting me here today to discuss with you how competition law regulates the conduct of universities. Universities supply a range of services to students. These include most obviously, tuition services in relation to undergraduate and postgraduate courses; research supervision services in relation to research degrees; as well as consultancy services in relation to Government and industry work. For the purposes of the CCA, universities are trading corporations. They engage in trade or commerce through the provision of a range of services for reward.

As such Universities are subject to the same rules and regulations that govern the conduct of other trading corporations, such Coles and Woolworths. As senior officers and managers of a trading corporation you need to acquire some basic understanding of the rules that govern competition in the education sector. In other sectors, companies generally undertake a risk assessment of those areas where they are most at risk of contravening the CCA; to ascertain in advance how problems might arise so that they can put in place strategies to mitigate the risk of inadvertent contraventions.

Professional associations like Universities Australia and the Australasian Association for Institutional Research (AAIR) play a useful role in enabling their members to meet and discuss sector-wide issues and to share information. However, their members are generally competitors and this means that the association and its members must take great care to ensure that they do not engage in anti-competitive conduct that may breach the provisions of the *Competition and Consumer Act* 2010 (Cth) (CCA).

The aim of the CCA is to make markets work better. It does this by regulating the conduct of suppliers and the way they interact with each other; and by regulating the way suppliers interact with consumers. On the supply side the aim of the CCA is to promote competition among suppliers and to prohibit conduct that lessens competition. Competition is a process of rivalry, or striving, to win sales and market share. Suppliers of educational services compete on the basis of price (tuition fees), and the quality of their programs and facilities. The markets in which they compete may be regional, State-based or national.

Tuition fees for Commonwealth Supported students at Australian universities have been capped by the Government, although there have been a significant number of full-fee paying international, and fee paying domestic students. If the changes announced in the 2014 Commonwealth Budget are enacted, the upper limit on fees for Commonwealth Supported university students will be removed. This is likely to result in a much greater degree of price competition among universities.

Competition depends on independent decision-making by universities about tuition fees, which courses to offer, the content of the courses, and who will teach them. When university officers and managers from different institutions get together and agree amongst themselves what courses to offer and what tuition fees to charge, they will fall foul of the CCA. My paper today is falls broadly into three parts. First, I will explain the nature of cartel conduct. Secondly, I will outline the sanctions that can be imposed for engaging in cartel conduct. Finally, I will provide some guidance on how to avoid becoming a party to a cartel.

II What is a cartel?

Cartel conduct takes a wide variety of forms – some cartel conduct is inadvertent and not very harmful in terms of its effect on consumers; other cartel conduct is deliberate and can result in consumers paying millions of dollars in higher prices. Division 1 of the CCA is drafted to reflect this range of culpability and provides for two sets of prohibitions that operate concurrently. They are:

- *cartel offences* which are intended to catch deliberate and serious cartel conduct; and
- *civil prohibitions* which are intended to catch inadvertent and less serious cartel conduct.

Both sets of prohibitions separately prohibit *making* a contract, arrangement or understanding that contains a cartel provision and *giving effect* to a contract, arrangement or understanding that contains a cartel provision.

The cartel offences and the civil prohibitions contain identically worded *physical elements*. However, the cartel offences also require proof of the relevant *fault elements* which are

"intention" in relation to creating the contract, arrangement or understanding, and "knowledge or belief" in relation to the requirement that the contract, arrangement or understanding contains a cartel provision.

Contract, arrangement or understanding

The first physical element that must be satisfied is the need for a contract, arrangement or understanding. The terms "arrangement" and "understanding" are not defined. Broadly, they require some form of *communication between at least two parties*, whereby one accepts a *commitment*, to do something. The commitment does not have to be a legally binding commitment; but it must be more than a mere expectation. There is no need for any element of mutual obligation or reciprocity, insofar as the other party or parties to the arrangement are concerned.

Cartel provision

The second physical element that must be satisfied is the need for a *cartel provision*. The term "cartel provision" is defined to catch four different types of conduct between horizontal competitors:

- Price fixing
- Market sharing
- Output restrictions
- Bid rigging or collusive tendering

In this context, two parties to a contract, arrangement or understanding will be horizontal competitors if they are, or would be likely to be, in competition with each other but for the contract, arrangement or understanding. "Competition" for the purposes of the CCA embraces *actual and potential* competition. Insofar as one University's course is regarded by students as a close substitute for another university's equivalent course, both universities compete in the same market. For example, a university in the Group of Eight should not assume that it is not in competition with an ATN university, or one of the Innovative Research Universities, where all three universities operate in Brisbane and all three offer undergraduate courses in law that have been accredited by the Legal Practitioners Admission Board (Queensland) as a recognized qualification for admission as a legal practitioner in Queensland.

Price fixing

The first type of cartel provision is one that has the purpose or effect of price fixing. Price fixing includes any conduct that interferes with the independent determination of a price. In

most cases this will involve an agreement to increase price or to maintain existing prices, or not to compete on price, or not to grant discounts or rebates. The definition of price fixing would also catch the adoption of a formula for calculating price.

Discussions or exchange of data between competing universities about their *future pricing intentions* in relation to particular courses are likely to result in a contravention of the CCA.

Scenario A

> *AAIR members meet at a forum in 2014 before Universities publicly announce their fees or the principles behind the fee structure. Members discuss the budget changes and the Government's proposed 20% reduction in Commonwealth Grant Scheme funding, and the reduction in Research Training Scheme funding, for universities. Members discuss how to make up the shortfall and agree that they will recommend to their Vice Chancellors that they will increase fees for all courses by a minimum required to meet the shortfall.*

The purpose or effect of the provision is to fix the prices for services likely to be supplied by all of the parties to the arrangement. If each university decides *independently* to increase its fees by 20% this will not contravene the CCA. However, given the fact that university representatives have communicated with each other and if, following the meeting prices rise uniformly by 20 %, there is a risk that a court might draw an adverse inference that the price increase was made pursuant to an arrangement or understanding.

Where the purpose or effect of an arrangement to share price information is to stabilise prices and reduce price variations, this may contravene the CCA. Where the exchange of information is capable of removing the uncertainty about the *intended conduct* of the parties in the future it is likely to constitute price fixing.

In 2006, 50 fee paying independent schools in the UK were fined for information sharing about prices, which infringed the equivalent UK competition rules. The matter was investigated by the Office of Fair Trading (OFT), which is the UK regulator responsible for enforcing competition law, in the same way that the Australian Competition and Consumer Commission (ACCC) is responsible for enforcing the CCA. According to a report in *The Guardian* newspaper:

> The OFT investigation focused on fee rises between 2001 and 2004 and found that in each year, schools swapped details of their intended fees. Sevenoaks School in Kent then collated that information and circulated it, in the form of tables, to the schools concerned. The information in the tables was updated and circulated between four and six times each year as schools developed

> their fee-increase proposals in the course of their annual budgetary processes. The investigation was reportedly started by a student who hacked into his school's financial records and leaked the documents to the press. Bursars have freely admitted that they used to meet regularly and talk about fees, but they maintain that this swapping of information did not amount to a concerted plot to push up fees.[1]

In Australia, such an information sharing provision would have had the purpose or effect of fixing the prices for services likely to be supplied by all of the parties to the arrangement.

Parallel prices not the result of collusion

Universities may draw inferences based on the discussions at AAIR meetings and decide to follow the prices of a competitor. Where there are only a small number of competitors in a market and one obvious price leader, this may result in price uniformity. Economists have a number of different terms to describe this kind of behavior, including "conscious parallelism" and "oligopolistic interdependence".

According to a report in *The Telegraph* newspaper, the UK competition regulator is undertaking an investigation into UK universities after allegations of cartel conduct. The report:

> …raises concerns that universities, which nearly all charge £9,000 a year despite widely varying degree quality, are operating a cartel. Figures last year showed that tuition time for physics students at different universities varied between 11 and 25 hours a week, with contact time for social studies students ranging from just nine hours to 16. However, last week vice-chancellors denied any collusion. Steve Smith, vice-chancellor at the University of Exeter and chairman of the Universities and Colleges Admissions Service (UCAS) board, said: "Do universities collude on pricing? The answer is they do not. "If the government allowed universities to charge £10,000, they would all charge £10,000. [2]

[1] Matthew Taylor, Rob Evans and Rebecca Smithers "Top 50 independent schools found guilty of price-fixing to push up fees" The Guardian, 11 November 2005.

Available at: http://www.theguardian.com/money/2005/nov/10/consumernews.publicschools

[2] Nicola Fifield, Price-fixing claims at British universities to be investigated by watchdog, The Telegraph, 23 February 2014.
Available at:http://www.telegraph.co.uk/education/universityeducation/10656408/Price-fixing-claims-at-British-universities-to-be-investigated-by-watchdog.html

Provided that the decision to charge a particular price is made independently, and is not the subject of an arrangement or understanding, this is not illegal. The mere fact that Universities increase tuition fees to similar levels will not, of itself, be enough to constitute cartel conduct.

Market sharing

The second type of cartel provision is one that has the purpose of market sharing. Market sharing or market allocation occurs when corporations agree to divide the market by allocating customers or geographical areas to each other and agreeing not to poach customers (students) from the territories allocated to their competitors.

Scenario B

This scenario is taken from the University of Melbourne Compliance guide:

> *The University enters into an agreement with a range of other Victorian universities who provide courses in the health sciences area that it will only recruit and enrol students from the metropolitan region. This is in order that regional universities will have a better chance of attracting regional students to its health science courses.*[3]

The purpose of this provision is to allocate between all of the parties to the arrangement the geographical areas in which services are supplied or are likely to be supplied. This sort of rationalisation may qualify for an authorisation. Authorisation is a formal process by which the ACCC is empowered to grant an exemption for conduct *before it takes effect*, if the applicants can demonstrate that it gives rise to a net public benefit. That is, it gives rise to some public benefit (such as efficiency cost savings), that outweigh any public detriment arising from a lessening of competition.

Output restriction

The third type of cartel provision is one that has the purpose of output restriction. Output restrictions occur generally in situations of over-supply in a market which causes prices to fall. Suppliers agree to restrict the supply of the goods or services which will have the effect of increasing prices. Discussions or exchange of data between competing universities about their *future intentions about the number of student places* they intend to offer are likely to result in a contravention of the CCA.

[3] See University of Melbourne Compliance guide available at:
https://www.unimelb.edu.au/compliance/misc/Trade%20Practices%20Act%20Compliance%20Guide.pdf
See also the Compliance Manual of the University of Adelaide available at:
http://www.adelaide.edu.au/legalandrisk/docs/resources/CCA_Manual.pdf

Scenario C

> *Universities agree not to offer certain courses where those courses are also provided by other universities. For example, two universities are currently offering language courses in both Chinese and Japanese which are loss-making. Representatives of these institutions meet at a conference. They agree that the Brisbane demographic area will only support one provider of each language. University A agrees to provide only Chinese and University B agrees to provide only Japanese.*

The purpose of this provision is to restrict the supply or likely supply of services to persons or classes of persons. This sort of rationalisation may also qualify for an authorisation.

Bid rigging or collusive tendering

The fourth type of cartel provision is one that has the purpose of bid rigging. This requires little in the way of explanation and is likely to be deliberate rather than inadvertent conduct.

Scenario C

This scenario is taken from the University of Melbourne Compliance guide:

> *The University enters into an agreement with several other leading research providers that it will not submit a tender for a government research contract relating to a particular area in which each of the research providers (including the University) has expertise. This is illegal under the new cartel provisions as it has the purposes of 'rigging' the bid or tender process*.[4]

III What are the sanctions for engaging in cartel conduct?

In my view there is a low risk that university staff would be caught engaging in any of these scenarios. The reason is that the kinds of decisions that are likely to attract liability are being made by a small group of senior managers within the particular institution.

Even though the risk is low the consequences of a breach are so serious that great care needs to be taken to avoid an inadvertent breach.

Individuals can be made liable on two different bases. First, where a corporation is primarily liable for a breach of a criminal offence or civil prohibition, an employee, servant or agent of the corporation may be liable as an accessory based on aiding, abetting, inducing, or being

[4] See University of Melbourne Compliance guide available at: https://www.unimelb.edu.au/compliance/misc/Trade%20Practices%20Act%20Compliance%20Guide.pdf

knowingly concerned in the civil prohibition under the accessorial liability framework in s 79 of the CCA.

Secondly, individuals can be directly liable for a breach of the criminal offences in the Competition Code applied by the *Competition Policy Reform Act* 1995 in their State or Territory. Before taking criminal proceedings the CDPP will require evidence that the individuals concerned had the requisite knowledge or belief that the contract, arrangement or understanding contained a cartel provision.

The fines and jails terms can be imposed on those convicted of committing a cartel offence.

For corporations (universities) the maximum fines are $10 million per criminal offence or civil contravention; or three times the total value of the benefits obtained by one or more persons; or10% of the annual turnover pf the corporation in the preceding twelve months.

For individuals who are found guilty of being involved in a contravention by a corporation, the sanction is imprisonment for up to 10 years and/or a fine up to 2,000 penalty units ($340,000).

Attempts

The CCA provides for the imposition of civil pecuniary penalties for contraventions of the cartel laws is sweeping in its terms: it catches an attempt, inducing, and an attempt to induce a contravention. The CCA also creates a criminal offence where a person attempts to contravene the cartel offence provisions.

For example, on 28 May 2014 the ACCC commenced civil proceedings for an alleged attempt to restrict the production of eggs against the Australian Egg Corporation Limited (AECL), its Managing Director, and two other AEC directors. The directors send emails to members suggesting that they meet to reduce the over-supply of eggs. The ACCC is concerned that the alleged attempt by the directors sought to obtain the agreement of egg producers to reduce supply. If successful it could have raised the price of eggs for consumers.

Scenario E

> *An AAIR member from South East Queensland gives a presentation at an AAIR conference about a range of possible prices that her institution may charge for a particular course, and what the implications will be in terms of student enrolments. Although she does not disclose which price her institution will charge for the course, she intimates that she will be recommending to her Vice Chancellor that her institution raise fees for its law course by 150%, because that is what she thinks the market will bear. Subsequently, when she sees that two of her competitors in South East Queensland have only increased the fees for their law courses by 50% she sends*

them an email to arrange a meeting to discuss with them a possible fee increase for their law courses.

The initial conduct, sometimes referred to as "signalling", is unilateral conduct that does not result in an arrangement or understanding for the purposes of the CCA. It would not constitute an attempt to induce and arrangement containing a price fixing provision. However, her subsequent conduct in sending an email would constitute a step towards the making of an arrangement, which, if successful, would have increased the price of services supplied, by one or more of the parties to the arrangement. It is not necessary that the attempt must have reached an advanced stage before it comes within the attempt provisions; all that is required is the taking of a step towards the commission of a contravention.

IV How do I avoid joining a cartel?

Some universities provide guidance for their staff on the compliance obligations under the CCA.[5] These compliance guides raise levels of awareness about what constitutes cartel conduct so that staff attending inter-institutional meetings, such as AAIR, do not inadvertently breach the CCA. Depending on the level of risk involved at the inter-institutional meeting, where commercially sensitive information is being discussed, it may be prudent to have an independent legal adviser present. It is also advisable to keep formal records such as agendas and minutes of meetings recording what was discussed. This sort of evidence can be critical in rebutting any allegation of price fixing where price uniformity occurs following a meeting.

Each institution must be able to demonstrate that it arrived at its course fees independently. The process adopted for arriving at course fees should be fully documented, and should be readily explicable in terms of prevailing market conditions.

Information sharing

The whole purpose of information exchange is to make markets more transparent and this will reduce uncertainty. *Universities must not disclose commercially sensitive information which reduces uncertainty about their future commercial intentions.* Much depends on the nature of the information exchanged, the level of detail and specificity of the information exchanged. The more detailed and specific the information – for example, talking about particular course offerings – the greater the risk of crossing the line that separates what is legal and what is illegal.

[5] See University of Melbourne Compliance guide available at: https://www.unimelb.edu.au/compliance/misc/Trade%20Practices%20Act%20Compliance%20Guide.pdf

- This is no objection to sharing information that is *publicly available*. The information about where Universities are drawing their students is available through the Tertiary Admission Centre (TAC) for each state territory (QTAC for Queensland). From that information it is possible to determine demographic details for the students that other universities have admitted – by geography, school, gender, and age.
- There is no objection to sharing information about *past events* so long as it does not provide a basis for predicting a future course of conduct. All discussions about future intentions, especially prices, must be avoided.
- There is no objection to sharing *aggregated data* so long it is not possible to disaggregate it and attribute information to a particular institution. This may allow the parties to the information sharing arrangement to read into the data the likely future intentions of a competitor.

Record keeping

When competitors meet to share information there is a risk that if prices rise following the meeting, the ACCC and the court may draw an adverse inference that it was pursuant to an arrangement or understanding reached at the meeting. In order to rebut such an inference being drawn it would be necessary to produce evidence of what was discussed at the meeting to convince the authorities that commercially sensitive information was not disclosed.

Meetings should follow an agenda that has been circulated prior to the meeting. Minutes of the meeting should be taken and filed for future reference. If discussion strays away from the agenda into commercially sensitive areas the attendees should immediately terminate the discussion. If this is not possible they should leave the room and insist that their departure be recorded in the minutes.

V Conclusion

Competition in the university sector is not going away. On the contrary, you must expect it to become more intense. As you may be aware, on 27 March 2014, the Australian Government announced a wide-ranging review of Australia's Competition Policy (the Harper Review). One of its key terms of reference is how to reform the Health and Education sectors and subject them to more competition. Any attempt by Universities to lessen competition is likely to be met with a swift response by the ACCC, especially any evidence of cartel conduct, which is a major enforcement priority of the ACCC.