ABN 92 140 677 792

Property Exchange Australia Ltd

Table of Contents

Introduction

PEXA thanks IPART for the opportunity to respond to its first Issues Paper in connection with its review of Interoperability Pricing for Electronic Lodgment Network Operators (ELNOs).

PEXA recognises IPART's progress towards creating an interoperability model that does not compromise the core objectives of the e-conveyancing system. In particular, we support IPART's preliminary views on two key issues in the Issues Paper in line with these objectives:

- First, a Responsible ELNO bears significantly greater costs and risks than a Participating ELNO. For a significant period after interoperability is introduced, market shares are likely to be asymmetric with PEXA disproportionately playing the Responsible ELNO role (as it has a far more developed network). While this remains the market structure, inter-ELNO fees are essential so that revenues reflect costs.
- Second, the additional costs of establishing and maintaining interoperability increase the total costs of the overall e-conveyancing system. These additional costs imposed by government regulation should be reflected by an appropriate increase in overall subscriber fees in the short-term. Assuming that interoperability results in innovation and efficiency as predicted, any immediate increase in subscriber fees should be transient and should be eroded over the medium to long term via the benefits of competition.

The following document represents PEXA's response to IPART's Issues Paper 1 and focuses on the two questions on which IPART has requested submissions:

1. Whether fees should be charged by the Responsible ELNO to Participating ELNOs for participation in an interoperable transaction, and how such fees should be passed on to subscribers.

2. Determine the form of regulation for any ELNO interoperable transaction fees, that is:

    a. Whether a negotiate-arbitrate model should apply to setting any such fees, or

    b. Whether a regulated method or price for 2023-24 should apply, with a method for reviewing and adjusting the price in the future.

Please note that this is the public version of our submission. In creating this version we have removed a handful of commercial-in-confidence comments and references and provided some other updates to improve readability for a public audience.

We welcome the opportunity to discuss the matters raised in this submission in further detail or to clarify the issues raised.

We look forward to IPART's consideration of our response and the subsequent recommendations in IPART's report.

Simon Smith
Chief Operating Officer

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Executive Summary

IPART is currently undertaking a review of interoperability price setting in the electronic conveyancing (e-conveyancing) industry. The outcome of this review will help to determine whether inter-ELNO fees are justifiable and what categories of cost should be included in a transfer of fees between Responsible and Participating ELNOs as part of an interoperable transaction. It will also help determine the form of regulation to set these prices and the specific methods of price setting.

PEXA as the major e-conveyancing services and network provider in the market supports IPART's review and our response addresses all ten of the questions on which IPART is seeking input in its first Issues Paper.

PEXA believes the critical issue of IPART's review is what costs and risks should be reflected in inter-ELNO fees and how they should be structured between Responsible and Participating ELNOs. IPART must ensure that the pricing model it adopts provides the right economic incentives to ELNOs, as the risk of 'getting it wrong' could compromise the core objectives of the industry. The core objectives of e-conveyancing being to provide a **more secure, reliable, and affordable method of conducting property transactions for all Australians.** Given the crucial role of property in an economy, this risk cannot be taken lightly. The risks of 'getting it wrong' include:

- **Compromising the security and reliability of the existing network** – It is possible that in an attempt to reduce barriers to entry for new entrants, the only established ELNO (PEXA) is forced to re-prioritise investment away from platform security and stability. This creates risks of long-term delays to the ability to execute electronically a significant number of transactions that other ELNOs are unlikely to be able to execute for a number of years.

- **Undermining future private sector investment** – PEXA has invested significant capital in transforming paper conveyancing, creating the processes and relationships that the e-conveyancing industry is built upon. PEXA may be unable to recover this investment if interoperability and inappropriate inter-ELNO fees effectively give new entrant ELNOs access to PEXA's relationship base without paying for it. This outcome is likely to undermine the confidence of investors in e-conveyancing, and other industries (particularly public private partnerships and future privatisation initiatives of government).

- **Stalling further expansion of the e-conveyancing network** – If inter-ELNO fees to the Responsible ELNO are not set in a considered way, perverse incentives could discourage ELNOs from establishing universal e-conveyancing services that would expand the e-conveyancing network to additional jurisdictions and transaction types. E-conveyancing is not currently available in Tasmania and Northern Territory, and is only partially complete in ACT, Queensland, and Western Australia.

- **Compromising universal affordability** – Poorly designed inter-ELNO fees could also create incentives that drive new entrant ELNOs to target high volume and high value jurisdictions and transaction types resulting in significant re-pricing of lower volume jurisdictions and transactions. In such circumstances, retail users in small population jurisdictions or transactions involving uncommon land registry instruments are likely to pay very high prices to justify ELNOs serving them.

- **Distorting the broader digital property transaction ecosystem** – While IPART is specifically focused on interoperability price setting, it should also consider the broader market dynamics, which will be affected by inter-ELNO fees. Sympli is 50 per cent owned by Australian Technology Innovators Global (ATI Global), which has a market-leading position in the adjacent markets of legal and conveyancing practice management software (PMS) and information search and brokering services (Information Search Services). Once interoperability is implemented, ATI Global will emerge as owner/controller of

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the only fully vertically integrated conveyancing workflow technology stack capable of servicing the entire property transaction value chain. As these upstream markets are unregulated, PEXA will not be able to compete with ATI Global/Sympli on an equivalent basis (as it is not vertically integrated and subject to significant regulatory restraints).

PEXA understands that IPART is seeking input on two questions in response to its first Issues Paper. The first question primarily relates to what cost categories should be considered in an interoperable fee and how these costs should be recovered between Responsible and Participating ELNOs. We have identified four categories of cost for IPART to consider:

1. The **marginal cost** of executing the Responsible ELNO role – PEXA agrees with IPARTs preliminary view that under current market conditions an inter-ELNO fee from Participating to Responsible ELNO should reflect the greater marginal costs and risk borne by the Responsible ELNO.

2. The cost of **establishing and maintaining interoperability** – PEXA agrees with IPART's preliminary view that ELNOs should be able to recover the cost of establishing interoperability which has proven to be a more complex and significant financial investment than anticipated at the time of IPART's 2019 review.

3. The cost of the **universal service obligation** to provide full coverage across Australia – IPART should consider how to ensure the core objective of providing affordable e-conveyancing services to Australians in all jurisdictions across all instruments is achieved. To date, e-conveyancing is still incomplete in QLD, WA and the ACT and is yet to be introduced in Tasmania and the NT. PEXA believes that legal requirements for all ELNOs to provide a full suite of services are unlikely to be realised in practice, particularly if inappropriate inter-ELNO fees create incentives for new ELNOs to delay providing comprehensive services.

4. The cost to **create the existing e-conveyancing system** on which interoperability is built – IPART should consider how to recognise the investment by PEXA in transforming paper conveyancing and creating the e-conveyancing industry network (an intangible, but very real, asset). PEXA's total aggregate revenues to date are materially less than those historical costs. PEXA believes that this investment can be appropriately recognised through inter-ELNO fees between Responsible and Participating ELNOs.

The second question of IPART's Issues Paper 1 seeks views on the appropriate form of regulation to determine inter-ELNO fees. PEXA believes that irrespective of the form of regulation, the critical issue is that an economic regulator (such as IPART) should determine the method of interoperability price setting, taking into account broader questions of how its determination will affect the public interest in facilitating secure, reliable, affordable and nationally accessible e-conveyancing. Inter-ELNO fees do not just redistribute profit between ELNOs. Rather, because of their effects on market dynamics, they can affect the public interest much more broadly, which a decision maker needs to be able to take into account. An economic regulator such as IPART is best placed to weigh up and consider these trade-offs.

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1 Establishing a common understanding of e-conveyancing and interoperability

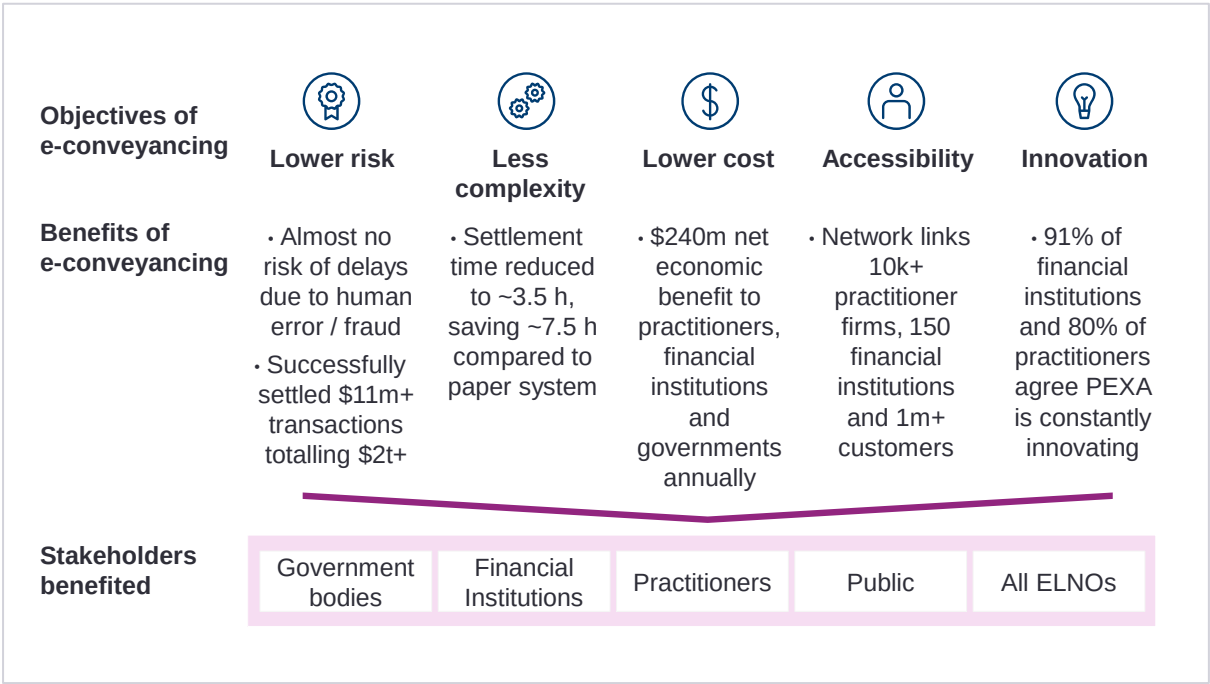
1.1 The objectives and history of the e-conveyancing market

1.1.1 The objectives of e-conveyancing

In transforming paper conveyancing into e-conveyancing, PEXA and its collaborators across Government and the private sector consistently aimed to deliver a **more secure, reliable, and affordable method of conducting property transactions for all Australians**. This is expressed across five objectives (in Exhibit 1) that PEXA has been working to deliver for Australians since its inception in 2010.

Any regulatory intervention into the e-conveyancing network (including interoperability) should work towards improving the achievement of this goal and the five objectives for the e-conveyancing industry.

Exhibit 1. Objectives and benefits of e-conveyancing



Source: PEXA (2021) IPO Prospectus; PEXA (2020) The Net Economic Value of E-Conveyancing in FY20

1.1.2 PEXA's investment to create e-conveyancing

The story of the development of e-conveyancing is synonymous with the story of PEXA. Since 2010, PEXA has invested significantly to digitally transform paper conveyancing in Australia, and the job is not yet finished.

The history of PEXA is relevant to the questions being considered by IPART as part of Issues Paper 1. Most important is the role that PEXA played as the first mover, which transformed paper conveyancing in collaboration with Governments, Financial Institutions, and conveyancing practitioners. PEXA created a

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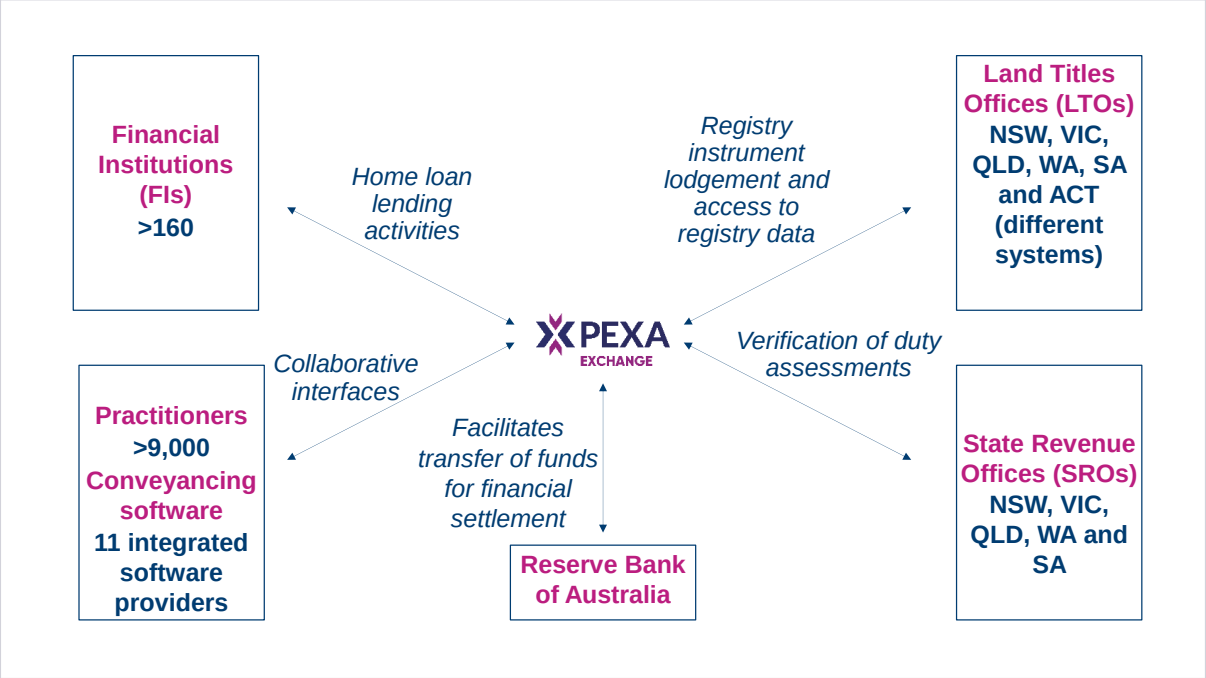
network of relationships and processes (between all these players) for each jurisdiction that currently has e-conveyancing. The one-off connection of these groups into the digital e-conveyancing ecosystem is a process that took years and hundreds of millions of dollars to facilitate, and this network is a significant part of the value of PEXA's business today. Subsequent ELNOs do not need to recreate this network, and without it they would have to make very large investments to set up their own network before they would be able to operate.

Exhibit 2. The e-conveyancing ecosystem today



Source: PEXA internal data

The significant investment, time and effort required to create the present e-conveyancing network is illustrated by PEXA's history. PEXA took years to build the first sets of connections to respective stakeholder groups and then over a lengthy period extended this into other jurisdictions. For instance:

- Land registry and State Revenue Office (SRO) took three years to establish the initial connections with the PEXA Exchange, and then over the next four years established connections with nine Land Registries and SROs;

- Financial institutions took four years to establish the initial connections with the PEXA Exchange and then a further five years to establish connections with most of the remaining financial institutions; and

- Conveyancing practitioners took four years to establish initial connections with the PEXA Exchange and then a further seven years to add about 90% of the others, and it continues to build out the network.

PEXA had to expend considerable effort and resources convincing each of the individual entities within these stakeholder groups to transition to e-conveyancing, which involved installing appropriate IT solutions, converting their business systems and processes, onboarding and training staff and building internal capability to use e-conveyancing. Subsequent ELNOs benefit from this developed network that is now familiar with e-conveyancing and its benefits.

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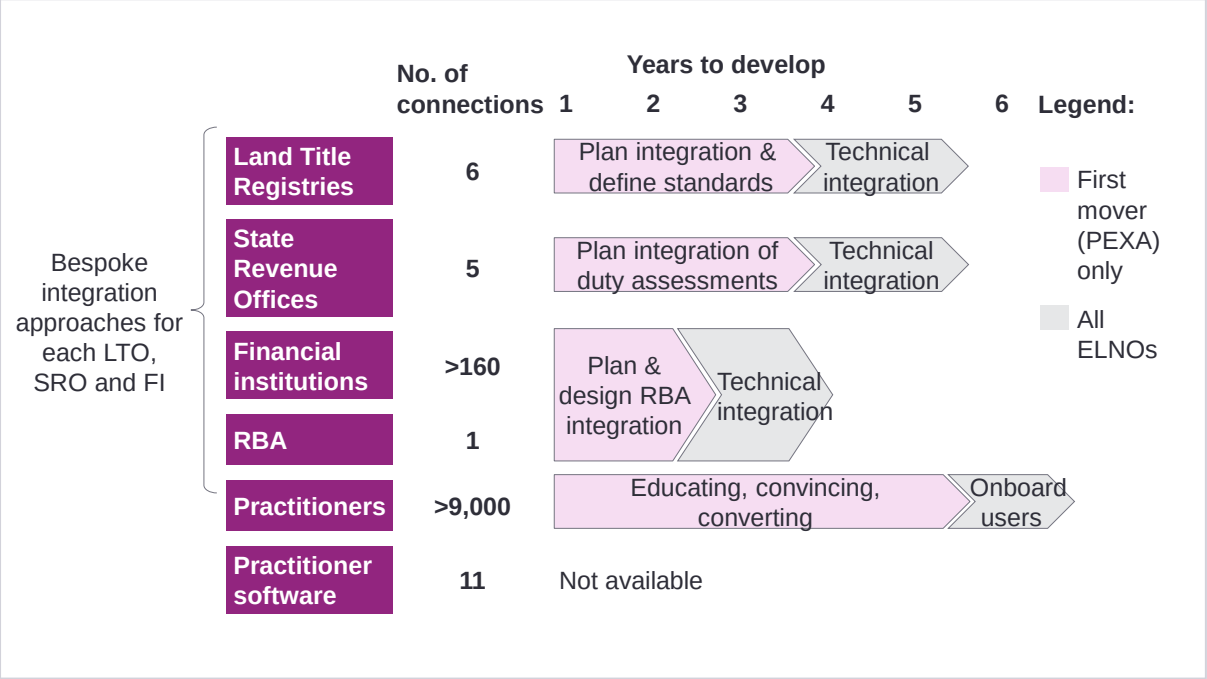
PEXA also expended significant effort and resources over a two to three year period in understanding the conveyancing system, designing data standards, and planning, testing and implementing technical electronic integration. As illustrated in Exhibit 3, subsequent ELNOs benefit from PEXA's work bringing this system into existence, and the time required for them to build a functional system is accordingly much shorter and much less costly.

Exhibit 3. Work required to transform paper conveyancing



Source: PEXA internal data

To build these networks and electronic capabilities over the past 12 years, PEXA's various shareholders took on significant financial risk. PEXA made these investments in circumstances where it had no certainty of success and, at least initially, was not supported by any government mandate. Even with a government mandate, success was not assured – as is illustrated by previous unsuccessful attempts to create electronic conveyancing[1].

PEXA continues to bring the benefits of e-conveyancing to the public and Governments in new jurisdictions, with effort underway to transform conveyancing in Tasmania and NT where it currently does not exist, and in Queensland, Western Australia and the ACT where penetration is limited as adoption is incomplete. Beyond expanding the e-conveyancing network, PEXA also continues to invest a significant and increasing amount in order to sustain and improve current services including in such areas as mitigating cyber risks, renewing technology, and meeting changing regulatory requirements (such as changes in property law, taxation, and the regulation of financial crime).

1.1.3 The outcomes of e-conveyancing

PEXA's efforts were productive. They transformed the inefficient and fraud prone paper-based conveyancing system and delivered a fully integrated digital experience for conveyancing users. The

[1] Early attempts by NSW and Victoria to establish a national e-conveyancing scheme were unsuccessful.

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current e-conveyancing network is a world-first that can facilitate digital lodgement and settlement. It has significantly increased efficiency, reduced errors and risk of fraud, and saved time and costs for lawyers, conveyancers, banks, and the entire Australian property industry. These benefits include:

- A net estimated economic benefit of $240m in FY 2020,[2] providing a material boost to Australian productivity.
- Savings for practitioners of around $66 per transaction compared to paper conveyancing,[3] as well as streamlining conveyancing workflow for both practitioners and financial institutions.
- A material reduction in the risk of fraud, more on-time settlements, and therefore more property purchasers moving promptly into their new homes.
- Real time property industry data that provides important insights supporting efficient property markets and superior public policy and design for the property sector.

Beyond the extensive benefits to participants and users, e-conveyancing is a lighthouse example of a successful private-public partnership and is a national achievement that services the $9 trillion-dollar Australian property market. The e-conveyancing system and associated facilities that PEXA has established provide an essential, safe and reliable service, in circumstances where other countries still have manual systems that proved vulnerable during COVID-19, affecting property markets and the wider economy. However, while the e-conveyancing network that exists today delivers significant benefits to practitioners, banks, and governments, PEXA has yet to fully recover its historic investment.

1.2 Market dynamics of the digital property transaction industry

To design an appropriate approach to pricing for interoperability in e-conveyancing, IPART should have regard to the market dynamics of the broader conveyancing value chain. This is necessary to ensure that its approach to pricing in an interoperable multi-ELNO ecosystem creates appropriate economic incentives for both ELNOs and for other participants in the value chain to promote the core objectives of e-conveyancing (as noted in Exhibit 1 above).

Failure by IPART to have regard to present and emerging market dynamics in setting appropriate inter-ELNO fees carries a substantial risk of regulatory error, which would undermine the core objectives for e-conveyancing outlined in Exhibit 1 above.

1.2.1 The broader digital conveyancing value chain

The digital conveyancing landscape is broader than e-conveyancing. It comprises three key digital tools / markets:

1. Conveyancing and legal practice management software (**PMS**);

[2] PEXA IPO Prospectus (2021); PEXA The Net Economic Value of E-Conveyancing in FY20 (2020).

[3] Independent Pricing and Regulatory Tribunal, 'Review of the Pricing Framework for Electronic Conveyancing Services in NSW' (November 2019), p 60, https://www.ipart.nsw.gov.au/sites/default/files/documents/final-report-review-of-pricing-framework-for-electronic-conveyancing-services-in-nsw-november-2019.pdf

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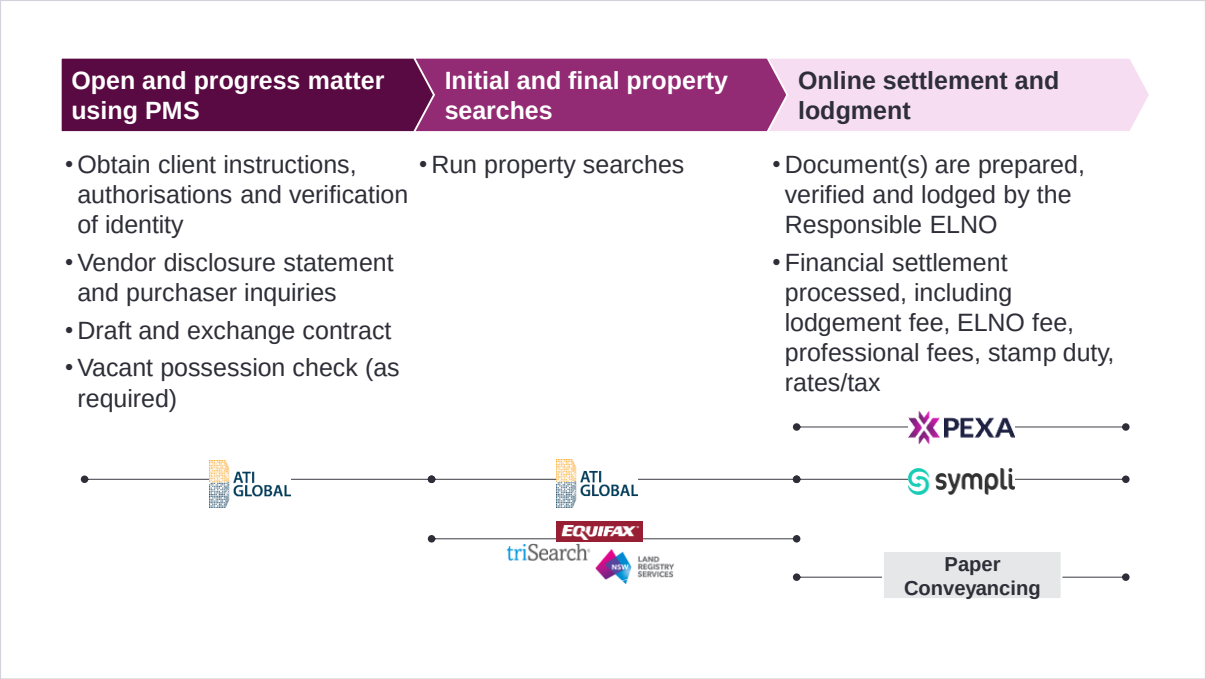
2. Property certificate searches (**Property Search Services**) (which is a segment of the broader information search and brokering services market (**Information Search Services**); and

3. E-conveyancing (comprising lodgment and settlement).

From a conveyancer's perspective (see Exhibit 4), the process of performing a conveyancing transaction first involves the use of a PMS, effectively the command centre for a practitioner's operations and the tool through which a practitioner finds and uses a Property Search Service provider to validate information received. Practitioners also use an ELNO to enable digital execution (lodgment and settlement) of the transaction. Other significant digital tools in the broader digital conveyancing workflow process include digital signatures and Verification of Identity software.

Exhibit 4. Digital conveyancing value chain



Source: PEXA research

1.2.2 PMS is a key centralised technology in the property transaction value chain

PMS is utilised by practitioner firms to enhance productivity and aid in the management of transactions and legal matters. PMS is a centralised technology that is akin to a central command centre for practitioners' operations and through which Information Search Services and e-conveyancing services are selected. Accordingly, PMS is utilised for a broad range of applications:

- For conveyancing practitioners, PMS is used to assist in the preparation of the contract of sale, supporting letters, and other documents required (e.g., mortgage discharge authorities) through to completion, including information searches. PMS can also contain functional integration, which seamlessly connects a practitioner with other downstream tools and services, such as Information Search Services and e-conveyancing services. PMS providers can also offer complementary services such as electronic signature tools and electronic contract products, which allow property contracts to be automatically populated.

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- Beyond the conveyancing process, practitioner firms typically utilise PMS for a much broader set of business needs. For example, practitioners rely on PMS to: (1) manage the entire life cycle of each client file, including property transactions, commercial matters, criminal matters, wills, or other general legal matters; and (2) increase general practice management efficiency via technology, including in relation to document, client, billing and file management features.

1.2.3 Market shares in e-conveyancing services could shift because of vertical integration in digital conveyancing

In recent years, there has been significant regulatory focus on and policy debate surrounding PEXA and the development of an appropriate market structure for e-conveyancing. However, less attention has been paid to the competitive dynamics of other parts of the value chain, which are essential to providing conveyancing and related legal services efficiently.

The ACCC has recently acknowledged that there is an emerging trend toward vertical integration across the broader conveyancing and property transaction value chain, and that these links could lead to anti-competitive outcomes.[4] This is understandable because:

a) there are competitive and pricing advantages to vertical integration due to customer price sensitivity and switching costs are different at various points in the value chain; and

b) the PMS and Information Search Services markets are largely unregulated.

This means the suppliers of PMS and Information Search Services are not subject to the same regulatory restraint as PEXA (which is an ELNO subject to the Model Operating Requirements (**MOR**)). A leading provider of PMS can influence market shares in e-conveyancing by engaging in self-preferencing across their vertically integrated conveyancing workflow technology stack. The market structure facilitates this self preferencing because:

- A practitioner's choice of PMS is often 'sticky' because there are substantial switching costs (such as training, onboarding and data transition costs), contracts are typically subscription-based for a material period, and practitioners rarely if ever multi-home (ie. use more than one PMS provider). By contrast, it is easier to switch Information Search Services and e-conveyancing services, as they are typically utilised on a per transaction basis, and training costs are lower. Consequently PMS can influence choice of an ELNO much more readily than ELNO can influence choice of PMS

- The choice of ELNO is more likely to be driven by convenience to the practitioner (rather than price), because the costs are paid by the end consumers. In contrast, practitioners tend to make sophisticated choices about PMS because it can materially change their productivity, and they pay the costs directly. Consequently, practitioners are far more likely to deliberately select their PMS rather than their preferred ELNO.

- Property owners are likely to be less price sensitive to ELNO charges. Typically, the conveyancing practitioner chooses an ELNO on behalf of the property owner, but the ELNO fee is directly paid from settlement funds. It is not the case that ELNO fees are passed on to end consumers as disbursements, as they are not paid by practitioners in the first instance, but directly from the consumer's funds. Property owners are unlikely to be sensitive to ELNO charges, which are a very

[4] ACCC, Statement of Issues, D&D's proposed acquisition of Link, 16 June 2022.

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small part of the typical overall property transaction (see Exhibit 5). Consequently, a dominant provider of PMS can potentially earn very high margins on ELNO fees charged to property owners.

- As PMS is offered for a subscription fee that practitioner firms typically pay,[5] but ELNO and Information Search Service fees are typically passed through or paid directly by end consumers, a vertically integrated PMS provider with market power can use cross subsidies to retain users. For example, an owner of a vertical stack of technologies may be able to offer discounts on PMS services in order to retain higher margin ELNO business.

Because of these features, it is relatively easier for PMS providers to influence a practitioner's choice of ELNO. A PMS provider with market power will have a stable and significant customer base of conveyancing practitioners and can actively market the e-conveyancing services of one ELNO over another, particularly by integrating its preferred ELNO's services into its PMS offerings so that it becomes the default ELNO for transactions, with information automatically fed through from PMS to ELNO. A dominant provider of PMS is not subject to any specific regulatory restraint and can influence competition in adjacent markets by expanding into e-conveyancing. Unlike e-conveyancing, the PMS market is largely unregulated. By contrast, the MOR are specifically designed to prevent PEXA from expanding upstream or influencing competition in upstream markets, including PMS. PEXA is subject to access, separation and non-discrimination requirements under the MOR. Indeed, PEXA's e-conveyancing services must integrate on an equivalent basis with all PMS providers seeking integration.

[5] By contrast, charges for Information Search Services are passed through to consumers as disbursements, and payments for ELN services are paid directly by consumers (i.e. buyers and sellers of properties).

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Exhibit 5. Example property transaction fee structure

	NSW, Feb 2022	% of total transaction value	% of buyer & seller transaction costs
Median Capital City house prices	$1,420,000	93.5%	
Stamp duty	$62,117	4.1%	63%
Registration lodgment fees	$148	0.01%	0%
PEXA fees (buyer and seller)	**$236**	**0.02%**	**0.2%**
Lawyer/Conveyancer fees (buyer and seller)	$3,600	0.2%	4%
Title and other searches	$339	0.02%	0.3%
Real estate agent commission	$31,950	2.1%	32%
Total transaction costs	$98,390		
Total transaction cost (% of house price)	6.9%		
PEXA fees/transaction costs	0.24%		

Source: Estimates based on PEXA research, February 2022

1.2.4 The most likely entrant to e-conveyancing will be vertically integrated in digital conveyancing

In the broader Australian digital conveyancing value chain, ATI Global – Sympli's 50 per cent owner - is a market-leading provider of PMS and Information Search Services, and is already the most prominent vertically integrated player. Sympli's other 50 per cent owner is Australian Stock Exchange Limited (ASX), another well-resourced and sophisticated backer.

ATI Global directly or indirectly controls a wide range of players across the property transaction value chain (see Exhibit 6 below). In particular, ATI Global is a leading supplier of PMS and Information Search Services in Australia. PEXA research suggests that ATI Global has high share in the PMS market and high share in the Property Search segment of the broader Information Search Services market[6]. ATI Global's PMS offerings often require practitioner firms to enter into relatively long-term contracts.

[6] ATI Global owns and operates market leading InfoTrack, as well as alternative Information Search Service providers - TriSearch and Creditor Watch. Through these entities, ATI Global is able to provide a full suite of Information Search Services (i.e. company, property and personal information searches). Practitioner firms generally favour full-service Information Search Service providers, such as those provided by ATI Global. However, unlike ATI Global, alternative service providers are not fully integrated across the entire conveyancing workflow technology stack.

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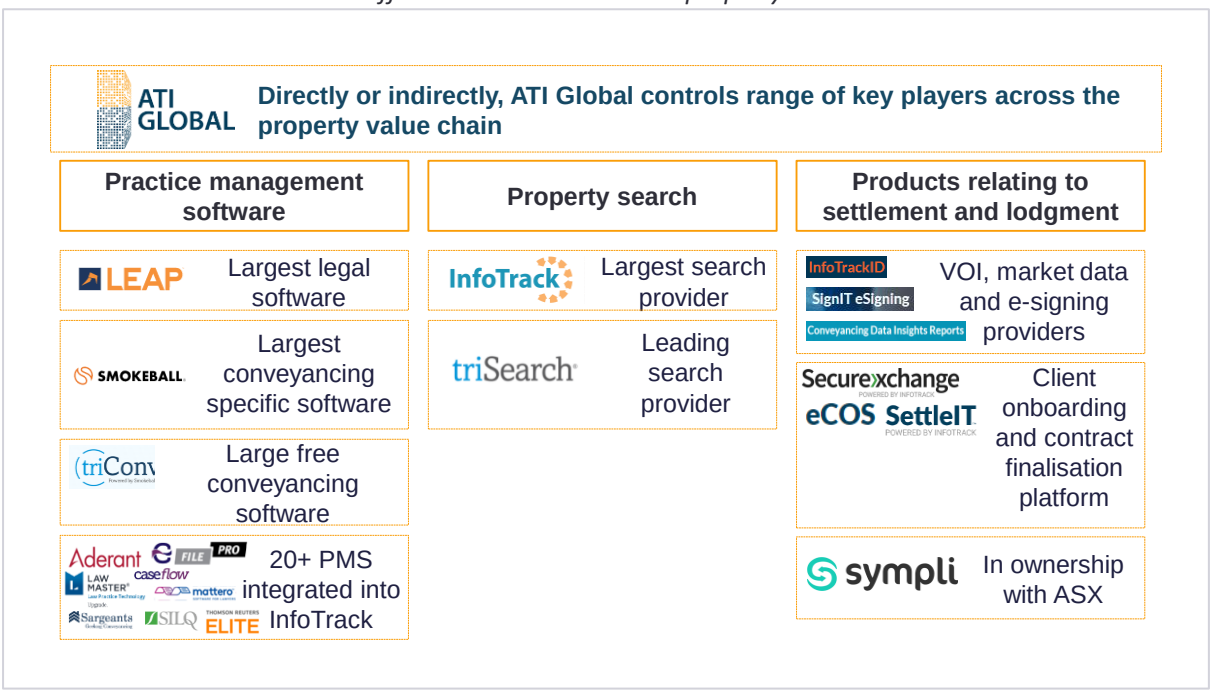
Exhibit 6. ATI Global's owned or affiliated entities across the property transaction value chain



Source: Desktop research

Interoperability will enable Sympli to participate in interoperable e-conveyancing transactions using PEXA's proven infrastructure and network (while Sympli itself is still developing the requisite capabilities). Accordingly, once interoperability is implemented, ATI Global will emerge as the owner/controller of the only fully vertically integrated conveyancing workflow technology stack.

1.2.5 ATI Global will be able to use its vertical integration in digital conveyancing to bolster its market position

Other regulators are concerned about vertical integration in digital conveyancing. The ACCC has expressed concerns about vertical integration arising out of Dye & Durham's proposed acquisition of Link Administration Holdings (**Link**) (**D&D-Link Transaction**),[7] which owns a ~43% stake in PEXA. The ACCC's principal concern, as expressed in its recently published Statement of Issues (**SOI**), is that the D&D-Link Transaction will result in vertical integration in the conveyancing workflow process by aligning, PEXA, a provider of e-conveyancing services, with D&D, a provider of upstream services – specifically PMS and Information Search Services. The ACCC's preliminary view was that the D&D-Link Transaction would allow PEXA / D&D to self-preference each other's services resulting in the foreclosure of competition in one or more markets in the conveyancing workflow.

The ACCC made this finding in circumstances where:

- D&D has very small market positions in PMS and Property Search;
- The MOR contains access, separation, non-discrimination and integration provisions that prevent PEXA from self-preferencing or influencing competition in upstream or downstream markets; and

[7] ACCC, Statement of Issues, D&D's proposed acquisition of Link, 16 June 2022.

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- A practitioner's choice of ELNO is only relevant in relation to one type of matter (property transactions) and only to the final two stages of such matters (lodgment and settlement). As a result, PEXA's integration with PMS providers is a relatively minor feature that does not play a significant role in practitioner's choice of PMS provider.

On 3 August 2022, D&D offered the ACCC a substantial structural remedy whereby it is proposing to divest its entire Australian PMS and Information Search Services business to address the ACCC's concerns outlined in the SOI. The ACCC's consultation process in connection with D&D's proposed remedy is scheduled to close 18 August 2022.

In light of the ACCC's vertical integration concerns in relation to the D&D-Link Transaction, IPART should have regard to how interoperability will facilitate ATI Global and Sympli to become vertically integrated. This vertical integration would be much more significant than the vertical integration between D&D and PEXA because:

- Unlike D&D, ATI Global is a market-leading provider of PMS, with a large and stable customer base given the sticky nature of PMS, and is also a market-leading supplier of Property Search Services. Accordingly, any strategy ATI Global engages in to divert consumers to Sympli once interoperability has been implemented has the potential to result in Sympli gaining market share in e-conveyancing, while entrenching its position in upstream markets.

- As PMS is an inherently 'sticky' upstream product to e-conveyancing, ELNOs cannot influence a practitioner's choice of PMS provider. ATI Global has therefore already likely 'locked in' a significant proportion of customers into its PMS offerings in the lead up to the implementation of interoperability.

- The centrality of PMS to a practitioner's businesses means ATI Global has many marketing / touch points with a significant number of practitioners (due to its dominant position) that provide ATI Global with opportunities for it to:

  - **Cross-promote or exclusively use one ELNO (such as Sympli) to the exclusion of any other (such as PEXA)**. Indeed, because PMS operates at stages in the lead up to lodgment and settlement, these products can readily be utilised to self-preference;

- **Offer discounts that are cross-subsidised across vertically integrated product lines.** As practitioner firms typically pay for PMS services via a subscription,[8] ATI Global could put in place cross subsidies to gain share or support retention across market segments. For example, ATI Global could subsidise Sympli pricing to gain share in e-conveyancing ATI Global (and its owned or controlled entities other than Sympli) is not subject to the MOR, and therefore has no regulatory restraint on its ability to leverage its market leading position in PMS to self-preference Sympli. In addition to the pricing options available to ATI Global/Sympli, ATI Global has no obligation to integrate its PMS with PEXA.

Whilst the purview of IPART's review is specific to e-conveyancing and interoperability price setting, PEXA believes that IPART should have regard to the relationship that will emerge between ATI Global and Sympli with interoperability. Failure to do so, for example by setting inter-ELNO fees too low in the belief that PEXA will be able to adapt, could compromise key e-conveyancing objectives of security, reliability, and access for all.

[8] By contrast, charges for Information Search Services are passed through to consumers as disbursements, and payments for ELN services are paid directly by consumers (i.e. buyers and sellers of properties).

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2 Outlining principles of interoperability fee setting

The Terms of Reference (**TOR**) for this IPART Review direct IPART to consider:

- Supporting and promoting competition through ELNO interoperability pricing (the **Competition Principle**);
- Promoting ongoing investment by ELNOs (the **Investment Incentive Principle**);
- Costs (including operating and relevant capital costs) and risks incurred by different participants in an interoperable transaction and who should bear these costs, (the **Cost Principle**); and
- The current and evolving structure of the interoperable transaction market, with additional ELNOs potentially entering the market over the next 1-5 years (the **Market Structure Principle**).

Relevant considerations that IPART should consider in applying each principle to inter-ELNO pricing in an interoperable e-conveyancing market structure are set out below.

2.1 The Competition Principle

While "supporting and promoting competition" through pricing design is important, competition is a means to a secure, reliable and affordable e-conveyancing system, and not an end in itself. Competition must be assessed in the light of evolving market dynamics both for e-conveyancing and the broader digital conveyancing landscape described in section 1.2.1, to ensure ongoing satisfaction of the core objectives for e-conveyancing.

To date, debate on interoperability has focused on reducing barriers to entry for new entrants on the basis that increased competition would lead to greater efficiencies and innovation in e-conveyancing (that were believed to be larger than the added costs required to establish and maintain interoperability). However, designs for interoperability should not advantage new entrants so as to compromise the ongoing security and reliability of the network – as well as the pursuit of full network coverage. Competition is a means, not an end.

Poorly designed interoperability competition may allow ATI Global (which owns 50% of Sympli) to use its market-leading position in PMS to divert transaction volume to Sympli and cross-subsidise Sympli's ELN services. As PEXA is not vertically integrated and subject to regulatory restraints under the MOR, PEXA will not be able to compete on an equivalent basis with ATI Global / Sympli. If inter-ELNO fees are inadequate, then this market dynamic could have economic consequences for PEXA. It could also stymie any further roll-out of the e-conveyancing network into areas that are not economically attractive given PEXA may not have the resources or incentive to do so.

Consequently, IPART should support and promote competition through fair and equitable pricing principles that will:

- Support the ongoing economic viability of multiple ELNOs; and
- Create incentives to encourage PEXA as the most developed ELNO to invest further in extending network coverage (which remains incomplete) to fulfil a key objective of e-conveyancing - national accessibility for all Australian users.

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2.2 The Investment Incentive Principle

In "promoting ongoing investment by ELNOs", IPART needs to ensure that financial incentives (including Subscriber fees and any inter-ELNO fees) create incentives for ELNOs to continue to invest in the e-conveyancing ecosystem. Although PEXA's coverage is much broader than any other ELNO, it still does not extend to Tasmania and the Northern Territory, and to a variety of more specialised transactions. The coverage of new entrant ELNOs today is much more limited.

Financial incentives to extend coverage are important because of the widening gulf between regulatory assumptions and the reality of network coverage. Although in theory, an ELNO must deliver the capability to lodge all document types in all jurisdictions, there is no obligation to develop the associated settlement capability (either minimal or comprehensive). In any event, the requirement to develop comprehensive lodgment capability appears to be unenforceable in practice:

- Although PEXA has been building functionality and establishing e-conveyancing in jurisdictions on a rolling basis for over a decade, it has only substantially completed e-conveyancing in NSW, South Australia and Victoria. The e-conveyancing network and capability has not been fully built in some jurisdictions (such as Queensland, Western Australia and the ACT), and does not exist in others (such as Tasmania and the NT);
- New entrants will inevitably not be compliant with the requirement to offer comprehensive functionality for many years. Precisely because this requirement is not realistic, it is unlikely that regulators will impose material sanctions. As a result, new entrants will have powerful incentives to delay building comprehensive coverage, and to cherry-pick high volume transactions and jurisdictions for the foreseeable future.

In the absence of appropriate financial incentives, existing ELNOs are likely to delay building novel functionality desired by Titles Offices because the fixed costs to build new functionality are invariably higher for the first mover that has to devise and negotiate a solution with other participants.

Similar issues concerning network coverage arose in the mobile telephony industry and were addressed in the design of its pricing regime. Regulators were concerned that there would be no financial incentive among mobile network operators to build network coverage in low-traffic, regional areas. As a result, the Universal Service Obligation (**USO**) was introduced under which:

- Telstra delivers the universal service obligation to ensure that all Australians have access to payphones and standard telephone services; and
- In order to fund this obligation, a telecommunications industry levy is applied to other mobile network operators, alongside government funding.[9]

The USO is a long-standing and essential consumer protection that ensures everyone has access to basic telephony services regardless of where they live or work. The industry levy provided to Telstra recognised the high public value and economy-wide benefits of providing universal network coverage.

The Commonwealth government implemented the USO to mitigate the negative externalities of a privatised telecommunications industry only providing network coverage in more profitable, densely populated areas of the country. Access to telecommunications services is an essential part of modern life,

[9] Australian Communications and Media Authority, 'Telecommunication funding arrangements' available at https://www.acma.gov.au/telecommunications-funding-arrangements.

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enabling social inclusion, better emergency responses, and access to services. Without the USO, large parts of rural Australia would not have access to standard telephone services. The USO enhances social equity, and the telecommunications levy and government funding ensures that the increased costs of providing this public benefit are shared equitably amongst industry participants.

In a similar vein, a USO could be introduced to e-conveyancing through inter-ELNO fees that provide ELNOs with an incentive to invest the significant costs required to provide services for the high complexity, low volume transactions, and jurisdictions expected to be of a relatively lower volume, such as Tasmania, the ACT, and the Northern Territory.

Further discussion on this topic is included in section 3.3 of this response.

2.3 The Cost Principle

2.3.1 Total cost recovery

In a regulated environment, regulated entities must be recompensed adequately for their capital costs, as well as the marginal cost of providing each service. This is recognised by the pricing principles settled in the Competition Principles Agreement (set out in Annexure A as they apply in various industries), which allow for access providers to recover their fixed costs, as well as their ongoing and historic capital costs.

Within the Competition Principles Agreement, the principle that prices should produce 'revenue sufficient to meet the efficient costs of providing the service' contemplates recovery of access providers' marginal costs as well as recognising:

- a 'return on investment commensurate with the regulatory and commercial risks involved'; and
- 'legitimate business interests' which includes: (i) the costs of an access provider's infrastructure, (ii) its operating costs, and (iii) obtaining a normal return on capital.[10]

Altogether, these principles seek to achieve "revenue sufficiency" for a regulated entity. As the Queensland Competition Authority states, revenue sufficiency is critical because:

> *"… where there are sunk costs, and capacity investment is lumpy, marginal cost lies below average cost. Prices set to recover only marginal cost would prevent a regulated entity from recovering all of its costs. If the firm is not allowed to recover total costs, it will not have appropriate incentives to operate and invest."*[11]

Revenue sufficiency is tied to the Investment Incentive Principle, as well as the ongoing sustainability of the services a regulated entity provides. This is because:

> *"The potential losses from a firm not participating in a market or failing to invest adequately in maintenance and expansion because regulated revenues are*

[10] *Re Telstra* [2006] ACompT 4 [134].

[11] Queensland Competition Authority, Statement of Regulatory Pricing Principles 2013, section 3.4.

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inadequate could be significant and exceed the potential allocative efficiency losses associated with prices that exceed short run marginal cost".[12]

As a result, the principle of revenue sufficiency is a "dominating principle" in economic regulation. Consistent with this principle, in the e-conveyancing context, any fee regime should allow PEXA to meet its "legitimate business needs" which includes recovery of both fixed and marginal costs. This is discussed further in sections 3.1 and 3.2.

In calculating revenue sufficiency, IPART should have regard to likely fluctuations in e-conveyancing revenues, which are closely correlated with property transaction volumes, which tend to be higher if property prices are rising. Consequently, the e-conveyancing industry revenues of the last few years are unlikely to be typical. They were the consequence of a highly buoyant property market in which rapidly rising property prices led to higher turnover, and therefore higher e-conveyancing revenues. Any calculation of revenue sufficiency needs to consider and be robust to a range of property downturn scenarios.

2.3.2 First-mover cost recovery

Revenue sufficiency recognises that a regulated entity that is the 'first mover' should be recompensed for the additional one-time costs it incurs compared to other market participants. In the e-conveyancing context, pricing principles should account for the intangible, existence value that PEXA has created in transforming paper conveyancing, which includes the technical transformation from paper to digitised conveyancing, as well as the effort to build relationships with all relevant e-conveyancing stakeholders, and to on-board and train subscribers.

As PEXA has previously stated, the advent of electronic conveyancing may now seem inevitable, but it is very unlikely that it would have occurred without the dedicated focus and large-scale and risky investment of PEXA, which occurred in circumstances where it had no guarantee of success.[13] In its 2019 review, IPART recognised this existence value, and PEXA's multi-year 'at risk' development effort to bring the ecosystem stating:

- "PEXA as the first mover, incurred costs from… developing the first e-conveyancing platform in Australia (and the first of its kind across international jurisdictions). The first mover is likely to incur substantial costs for research and development; establishing processes and standards that subsequent entrants can follow; [and] building relationships with stakeholders to encourage the uptake of e-conveyancing…; and educating subscribers to use an ELNO platform."[14]

There are a number of precedents for regulators recognising and paying for existence value in regulated markets, consistent with the overarching pricing principle of "revenue sufficiency", including:

- ASX and Chi-X, where the ASX provides clearing and settlement services (analogous to the role of Responsible ELNO) to competitor Chi-X. ASX charges a fee to Chi-X for this service, which is required to be on materially the same terms as the fee charged to ASX affiliated entities (i.e. the

[12] Queensland Competition Authority, Statement of Regulatory Pricing Principles 2013, section 3.4.

[13] See: PEXA's response to ARNECC Responsible Fee Options Paper, p 5.

[14] Independent Pricing and Regulatory Tribunal, 'Review of the Pricing Framework for Electronic Conveyancing Services in NSW' (Final Report, November 2019), p 60, https://www.ipart.nsw.gov.au/sites/default/files/documents/final-report-review-of-pricing-framework-for-electronic-conveyancing-services-in-nsw-november-2019.pdf, 53.

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ASX listing market).[15] This fee takes into account the legitimate business interests of ASX and any parties seeking access to its services;[16]

- Pharmaceutical and creative industries (such as music) whereby higher protection and reward are correlated with high costs for creating or establishing something for the first time, and the cost of imitation is low. In this regard, it is worth noting that the result of PEXA's endeavours is a world-first e-conveyancing ecosystem that is capable of both settlement and lodgment, which has significantly increased efficiency, reduced errors and risk of fraud, and saved time and costs for lawyers, conveyancers, banks, and the entire Australian property industry;

- Prospective greenfield gas pipelines whereby regulatory holidays are available to speculative investors to encourage investment in building out necessary network coverage. The gas access regime allows for pipelines to apply for a 15 year no coverage decision such that there is a commitment that no regulation will apply for that time. The objective of this approach is to address concerns relating to asymmetric truncation of returns and promote investment for infrastructure that serves a public benefit. In this regard, comparisons to e-conveyancing are relevant as inter-ELNO pricing principles must ensure there are appropriate investment incentives to ensure PEXA is able to deliver full national e-conveyancing coverage (including in low population jurisdictions, such as Tasmania, ACT and the NT).

These examples illustrate that where there are high costs for a first mover in establishing an industry, as is the case with e-conveyancing, relevant pricing principles should also reflect through a higher weighted average cost of capital the additional risk taken by a first mover.

2.4 The Market Structure Principle

The structure of the e-conveyancing market is likely to change radically as interoperability is introduced. Pricing of interoperability will play a critical role to creating and reinforcing desired market structures and dynamics. There is a 'Goldilocks problem' with the level of fee payable from Participating ELNOs to the Responsible ELNO:

- If fees are too low (and fail to cover the fixed costs of creating back-end settlement / lodgment capability), then new entrants will be incentivised to simply pursue the role of Participating ELNO. In effect, this would create a wholesale-retail market structure, but the retailers (i.e. Participating ELNOs) would get free access to the wholesale layer and not have to pay for its fixed costs. Such an approach would be out of step with access pricing models commonly utilised in other industries. This would create substantial risks of system under-investment, stalled innovation, and quite possibly a less secure and reliable e-conveyancing ecosystem. These outcomes would not be in the interests of consumers, government or industry and risk undermining the economic sustainability of the e-conveyancing ecosystem;

- Conversely, if fees are too high, this may result in perverse incentives for all ELNOs seeking to be the Responsible ELNO resulting in:

[15] Council of Financial Regulators, 'Regulatory Expectations for Conduct in operating Cash Equity Clearing and Settlement Services in Australia' (Report, September 2017) 6; Australian Securities Exchange, 'ASX Clearing & Settlement: Schedule of Fees' (1 June 2022) available at https://asxonline.com/content/dam/asxonline/public/documents/schedule-of-fees/asx-clearing-and-settlement-schedule-of-fees.pdf.

[16] Council of Financial Regulators, 'Regulatory Expectations for Conduct in operating Cash Equity Clearing and Settlement Services in Australia' (Report, September 2017) 6.

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- ELNOs under-investing in servicing practitioners, and over-investing in establishing and maintaining back-end infrastructure costs; and

- ELNOs under-investing overall when ELNOs compete away the disproportionately high revenue earnt by the Responsible ELNO by seeking to become the 'preferred' provider of financial institutions because the ELNO for the purchaser's bank is entitled to be the Responsible ELNO;

- If inter-ELNO fees are not precise (i.e. some transaction fees are under-priced, and some are over-priced, relative to costs), then new entrant ELNOs are likely to cherry-pick the under-priced transactions, leading to under-investment in the back-end system for some transaction types and in some jurisdictions;

- If inter-ELNO fees are restricted to instances where the Participating ELNO lacks the capability (as proposed at the public hearing), then new entrant ELNOs are likely to cherry-pick high-volume transactions. Further, it would be difficult to test proficiency of the capability.

Setting interoperability fees with due consideration of the following risks will drive all ELNOs established and new entrants to continue to deliver on the core objectives of the e-conveyancing ecosystem.

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3 Defining interoperability costs and their recovery

IPART's first Issues Paper asks which cost categories should be considered in an interoperable fee and how these costs should be recovered between Responsible and Participating ELNOs. IPART should consider four categories of cost:

1. The **marginal cost** of executing the Responsible ELNO role;
2. The cost of **establishing and maintaining interoperability**;
3. The cost of the **universal service obligation** to provide full coverage across Australia; and
4. The cost to **create existing e-conveyancing system** on which interoperability is built.

These costs should be considered in the light of the history of the e-conveyancing market, its market dynamics, and the pricing principles outlined above.

3.1 Marginal costs of executing the Responsible ELNO role

3.1.1 Distinctive costs of the Responsible ELNO role

As IPART recognised in its first Issues Paper, in an interoperable transaction, Participating ELNOs will provide information from their subscribers to the Responsible ELNO which will take on the majority of the effort and risk involved in a transaction. The Responsible ELNO sets up the workspace, liaises with stakeholders, and orchestrates and executes lodgement and financial settlement. It also manages post lodgment and settlement communications. As acknowledged in IPART's first Issues Paper, the Responsible ELNO incurs higher risks and costs than Participating ELNOs, and under current market conditions, PEXA will be the Responsible ELNO for the majority of transactions in many jurisdictions for an extended period of time.

Therefore, as IPART stated as a preliminary view, there should be an inter-ELNO fee from Participating ELNOs to the Responsible ELNO, reflecting its additional costs and risks. The respective roles and responsibilities of the Responsible ELNO vis-a-vis the Participating ELNO are outlined in Exhibit 7.

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Exhibit 7. Role of Responsible and Participating ELNO

Phases	Role of Responsible ELNO	Role of Participating ELNO
Set-up and prepare workspace	**More responsibilities** • Set up and manage workspace by preparing documents for reviewing and signing, liaising with authorities and accounting for duty • Check workspace is ready and resolve errors throughout transaction	**Less responsibilities** • Manage subscribers, respond to requests and sign documents
Lodgment and settlement	• Perform financial settlement and lodge documents with Land Registry	**No responsibilities**
Post lodgment and settlement	• Manage post-settlement communications with ELNOs, banks and land registries • Collect and pay fees associated with financial settlement • Manage lodgment case level errors	

Source: API Portal: 'National e-Conveyancing Interoperability Data Standard'

These marginal costs are significant. As with other technology platform businesses, the marginal cost of any single additional transaction is low (but not zero). However, a step change increase in transaction volume can materially increase costs. Higher transaction volumes increase the load on support functions and technology, including the need to:

- Support queries (e.g. incident management, guidance on how to use residuals etc);
- Manage lodgment case errors or document errors (with Subscribers and/or tech teams and/or external parties);
- Manage post-settlement issues (e.g. mistaken payments); and
- Provide hosting (e.g. server and bandwidth load).

These costs directly relate to performing the function of the Responsible ELNO and Participating ELNOs will not incur many of them. If interoperability were introduced without an adequate inter-ELNO fee to compensate for the higher costs of being the Responsible ELNO, there would be significant incentives for ELNOs to avoid the Responsible ELNO role, further reducing the incentives for new entrants to build the comprehensive functionality that makes them eligible for the Responsible ELNO role more often.

Adding interoperability functionality is likely to increase these marginal costs further, because interoperability creates additional possibilities for issues to arise during a transaction, as detailed below in

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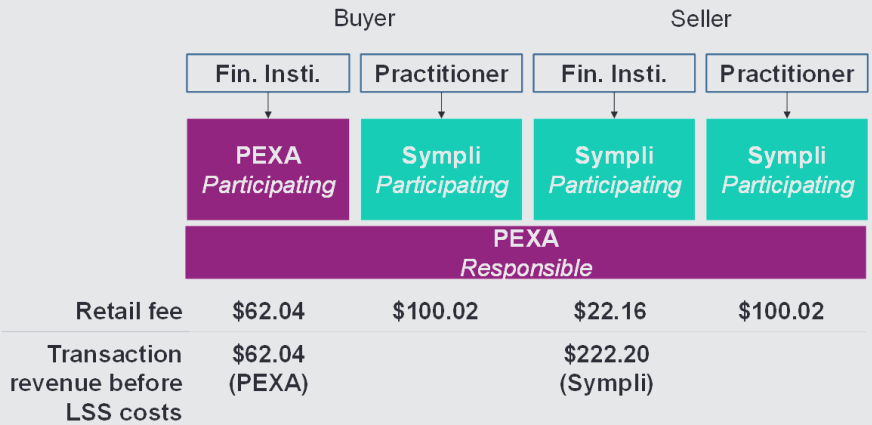
section 3.2. Not only does the Responsible ELNO incur higher marginal costs, under current published pricing, it is likely to have lower revenues. As illustrated in Exhibit 8, under a scenario that would be relatively common, the subscriber revenues of the Responsible ELNO would have been less than 28 per cent of those of the Participating ELNOs, even though the Responsible ELNO would bear the majority of the marginal costs incurred in the transaction. It will be difficult to avoid this outcome by increasing Subscriber charges, which are heavily regulated.

Scenario:
In a 4-party transaction with conveyancers and financial institutions without inter-ELNO fees could result in the following scenario:

Exhibit 8. Example transfer with discharge and mortgage assuming no inter-ELNO fees



**Retails fees include GST*

Source: PEXA and Sympli published pricing as at 4 August 2022

As noted in the Issues Paper, if all ELNOs had equal market share, the costs of performing the Responsible ELNO function would net out. However, as IPART has recognised, PEXA currently has a higher market share (99%) and this is not likely to change immediately even as interoperability is introduced. Sympli is still in the early stages of building its e-conveyancing platform and it is not clear how many jurisdictions and what transaction types it will be able to process. It is also unclear as to when Sympli will be able to provide these services at the volume and level of reliability required. As a result, it is possible that PEXA would remain the Responsible ELNO for a large majority of transactions for many years (notwithstanding that Sympli may be able to be the Participating ELNO for a material number of practitioners for the reasons outlined in section 1.2). As discussed in section 3.4, PEXA has spent more than 10 years building its current level of network coverage. While new entrants may be quicker if they build on PEXA's example, know-how and network, it is likely to be several years before they have equivalent functionality to the PEXA platform.

The absence of inter-ELNO fees, as suggested at the July public hearing, will fail to recognise the added cost of being the Responsible ELNO and will create incentives for new entrants such as Sympli to delay building

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Responsible ELNO functionality for as long as possible. Instead, new entrants will have powerful incentives to cherry pick the most profitable high-volume low-cost roles. In practice, this implies pursuing business from the buyers and sellers of property (or more often, their conveyancing practitioners), primarily for relatively straight-forward transaction types, in jurisdictions with large populations and transaction volumes. Such cherry-picking will be facilitated by the vertical integration of Sympli with its 50% owner ATI Global, which could enable it to capture a substantial part of the conveyancing practitioner market, as discussed above in section 1.2. This cherry-picking could place PEXA in a difficult position even when it is performing the vital Responsible ELNO in most transactions. This outcome will undermine the stability and security of the e-conveyancing system. It is also likely to undermine further investment in expanding the e-conveyancing network to jurisdictions that presently do not have e-conveyancing.

3.1.2 Lodgement Support Service fees

IPART specifically sought input on lodgement support service fees (LSS). Under the current design, the LSS is paid by the ELNO that sends the RIS request, which may not be the Responsible ELNO. The Interoperability Operating Committee (**IOC**) have been devising a solution with three types of scenarios for LSS fees:

- **Non-Usage Event (where the title is not used in the lodgement case) -** The ELNO that requested the LSS for non-usage events will always be fully liable for them and will not be able to apportion them to other ELNOs. For the avoidance of doubt the ELNO that requested the LSS is not necessarily the Responsible ELNO (even though they actually ask the LR for the LSS) as it could be a Participating ELNO whose subscriber adds a title to the workspace;

- **Usage Events (i.e. where the title is referenced in a document within a lodgement case) -** The LSS fee for Usage Events will be apportioned between the Participating (including Responsible) ELNOs according to an agreed formula. This formula will likely include the number of participants that used the LSS in a workspace and the number of documents on which the title was used. The exact formula needs to be worked out and agreed as part of the Business Rules, and the apportioning would be done once lodgement is complete;

- **Registry information re-supply** - The liability for resupply fees (where they are charged) will be borne by the ELNO that requested the resupply (again, the requesting ELNO might not be the Responsible ELNO, but would be the ELNO whose subscriber adds a title to the Workspace).[17]

The formula for apportionment of LSS may form part of future IPART analysis.

IPART has appropriately not sought input on lodgement fees. The IOC has recognised that lodgement fees should be out of scope for apportionment between ELNOs. Lodgement fees will continue to be paid by the parties, not the ELNO, and this arrangement will not be changed by interoperability.

[17] Minutes of IOC Stand-up meeting, Friday 19 March 2021.

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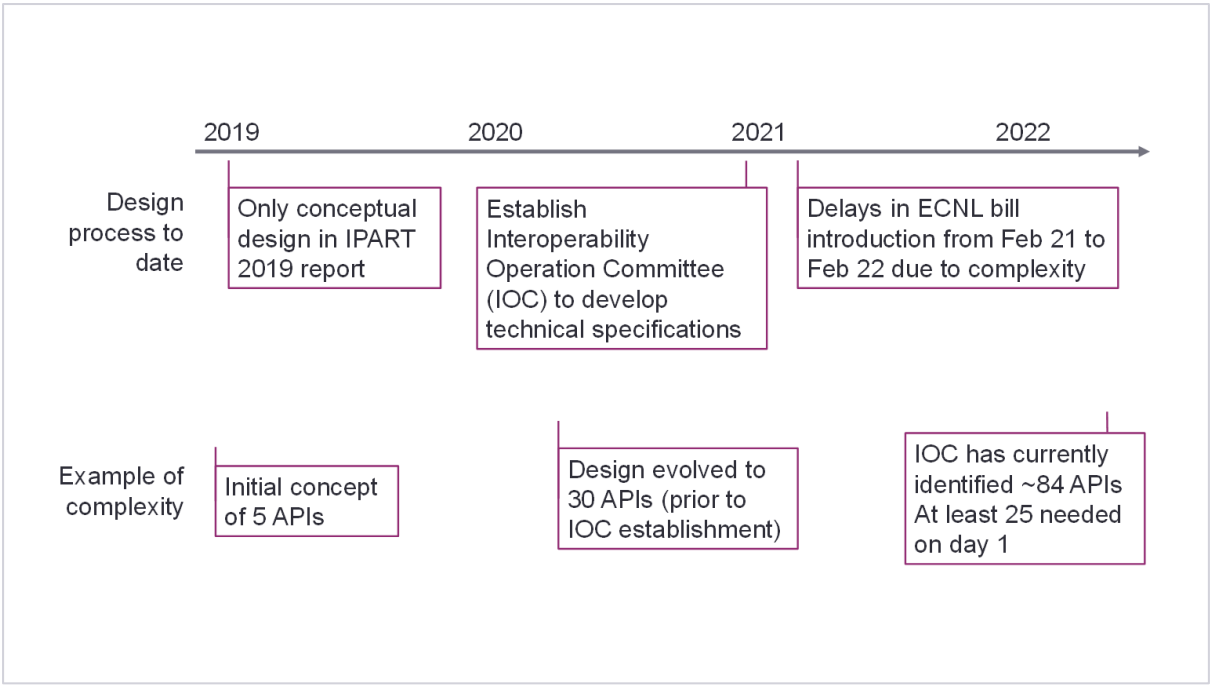
3.2 Costs of establishing and maintaining interoperability

Building the capability for interoperability with other ELNOs is a significant undertaking, as revealed by the last two years of interoperability design. This design process has established that the costs of building interoperability will differ between ELNOs. PEXA will probably incur higher costs because it operates a larger ecosystem, which is more complex, and requires significant increases in expenditure to mitigate new risks associated with ensuring the ongoing security and reliability of the system that meets consumers' expectations.

3.2.1 Costs of establishing and maintaining interoperability remain uncertain

Costs relating to interoperability in 2019 were highly uncertain. First, the models of interoperability that AECOM considered were only conceptual. Secondly, IPART's terms of reference for its 2019 review of e-conveyancing primarily focused on whether ELNO service fees were reasonable under the existing market structure (i.e. without interoperability). Consequently, IPART did not consult widely on the costs relating to interoperability, and where it did, AECOM's findings related to a conceptual model of interoperability that had not been subject to costing or real-world build efforts. More detailed design has shown that interoperability will be significantly more complex, and more costly than was outlined by AECOM, as shown in Exhibit 9.

Exhibit 9. Example of emerging complexity in interoperability design over the last three years



Source: PEXA internal data

It is also possible that the design for interoperability originally adopted by ARNECC will not be fit for purpose because it cannot accommodate additional entrants – if so, the development to date may require significant revision. Indeed, the introduction of interoperability for e-conveyancing has already proven to be more complex than originally anticipated. Estimated costs and timing for the delivery of interoperability have been routinely underestimated.

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The failure to set accurate cost estimates for a technically complex market structure reform, such as interoperability, is consistent with findings and submissions made in connection with the Senate Inquiry regarding Digital Delivery of Government Services. The Senate Inquiry also acknowledged that achieving digital transformation is not limited to investment in technology, it also requires the underlying business processes of the re-engineered technology to be transformed.[18]

Some notable examples of failed or substantially delayed digital transformation projects where costs and delivery timing were significantly underestimated include:

- The NSW Education Learning Management and Business Reform: This reform was aimed at overhauling the NSW Education Department's IT infrastructure. It was originally projected for completion by December 2014 at a budget of $480 million.[19] However, the reform suffered major delays and the NSW Education Department have publicly stated that "essential operational costs, such as implementation and staff training were never budgeted for".[20] By 2016, the cost of the reform had ballooned to a cost of $752 million (almost double the initial estimate). Failures in the reform led to key features of the upgrade being abandoned.

- Australian Stock Exchange – 2020 ASX Trade Outage: In November 2020, the ASX updated its ASX Trade platform to enhance performance. This was a major refresh of the platform to incorporate reforms to the CHESS system. The update was not prepared to be rolled out and resulted in the system crashing and trading being disrupted. An independent reviewer concluded '"*Factors that suggested the ASX Trade system was not ready to go-live, considering ASX's near zero appetite for service disruption. This was the case even though the formal implementation readiness processes were completed and verified by multiple parties without objection to go-live … There were gaps in the rigour applied to the project delivery risk and issue management process expected for a project of this nature, and risk and issue management, project compliance to ASX practices, project requirements and the project test strategy/planning did not meet accepted industry practices.*" [21]

- Failed attempts to introduce interoperability in the cash equities settlement and clearing market. Despite almost 10 years of consultation and public debate on proposals to implement interoperability in this industry, the ACCC and the Council of Financial regulators ultimately determined that interoperability would introduce an unacceptable level of risk to cash equity holders and system operators. Notwithstanding that interoperability was not introduced, effective competition emerged between ASX and Chi-X. As end-users rely on e-conveyancing to safely and securely settle property, there is no tolerance for interoperability increasing risks to consumers. In circumstances where the technical and operational solutions required to facilitate interoperability between ELNOs is still uncertain, PEXA anticipates that additional costs and risks are likely to emerge as the interoperability reform moves forward.

Given the uncertainty and challenges of accurately costing the delivery of significant digital infrastructure or reform, we suggest to IPART that it should recognise that there is an inherent uncertainty as to the costs

[18] Report into Digital Delivery of Government Services, at Chapter 1, para 1.10 available here: https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Finance_and_Public_Administration/digitaldelivery/Report/c01.

[19] James Robertson, 'Learning Management and Business Reform school IT system $270 million over and three years too late', *Sydney Morning Herald* (27 June 2016), https://www.smh.com.au/education/learning-management-and-business-reform-school-it-system-270-million-over-and-three-years-too-late-20160627-gpsyaj.html.

[20] Ibid.

[21] ASIC, 'Update on the Independent Expert Review of November's ASX Trade Outage' available at https://asic.gov.au/about-asic/news-centre/find-a-media-release/2021-releases/21-220mr-update-on-the-independent-expert-review-of-november-s-asx-trade-outage/.

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of establishing and maintaining interoperability. In particular, we suggest that there may be costs to establish and maintain interoperability that are currently unknown, and which will require a further review by IPART as to relevant cost categories in Stage 2 of its review on interoperability pricing. We also suggest future reviews that consider pricing for e-conveyancing services will likely need to consider the scope of costs involved with establishing and maintaining interoperability.

3.2.2 PEXA's current estimates for costs of establishing and maintaining interoperability

At this stage, the anticipated interoperability build costs primarily relate to the technical build required for interoperability. Beyond these costs, significant additional costs will be incurred to accommodate requisite changes to the existing governance, change and release management, contractual, regulatory, legal, risk and liability allocation and insurance framework. There will also be significant training and education costs (both within organisations and external to industry participants). Exhibit 10 provides examples of costs incurred. This list is not exhaustive.

Exhibit 10. Examples of costs of establishing and maintaining interoperability

Type of costs	Examples
Technical costs	• Build infrastructure, including developing 80+ APIs
Management costs	• Develop network level governance and management frameworks • Increased insurance premiums
Risk costs	• Develop and implement new risk and liability allocation regime • Assess and monitor broader network's cybersecurity • Undertake incident management (Business Continuity Plans, Root-Cause Analysis, incident reports with other ELNOs)
Legal costs	• Renegotiate the existing contractual framework • Develop and maintain IOP Agreement between ELNOs
Customer service costs	• Develop and implement a new complaint and dispute resolution framework • Train and support ELNO staff and subscriber staff to use multiple ELNOs • Manage subscribers and ELNOs when transaction issues arise • Handle anticipated increase (due to increased system complexity) in complaints between ELNOs and subscribers
Other…	• To be identified when system working in practice

Source: IPART Issues Paper; PEXA internal data

The implementation of a new risk and liability allocation regime will also be required, and PEXA anticipates there will be a significant increase in consumer complaint handling and support, in addition to increased dispute resolution between ELNOs, which will result in increased ongoing costs.

Interoperability introduces additional complexity and additional digital interfaces. This increases the vulnerability of the system to cyber-attack and failure. As a result, ELNOs will have higher operating costs due to increased expenditure on cyber-security and system maintenance to ensure stability and security that are core objectives of the e-conveyancing system.

As these costs to establish interoperability have been incurred as a result of regulatory directions, ELNOs should be able to recover them as part of the costs of adding interoperability functionality. In addition, the costs of establishing interoperability will also include the Data Standard Levy, imposed when maintenance

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of associated industry standards was transferred from PEXA to NECDS Ltd. These costs should also be recoverable.

3.3 Cost of universal service obligation to provide full coverage in Australia

3.3.1 Implicit cross-jurisdiction/transaction type subsidies are exposed with interoperability

ELNOs are mandated to provide complete coverage of all lodgement instruments in all jurisdictions to ensure that the objective of accessibility to all Australians of a digital conveyancing system is delivered. PEXA as the first mover, is well progressed on this journey but after more than 10 years is still working to expand the e-conveyancing industry to full coverage. While it may not take a new entrant as long to reach the same level of coverage, in part, due to the work PEXA has done to build the industry, there is no mechanism to enforce how and when new ELNOs provide full coverage. As this submission has discussed, depending on how inter-ELNO fees are set, the introduction of interoperability into the e-conveyancing network may create powerful incentives for new entrants to cherry pick to perform the highest revenue and lowest cost roles for the largest volume transactions in the largest jurisdictions. This would result in new entrants delaying the necessary build for full capability (and the associated costs) for as long as possible.

In the likely event that new ELNOs do not reach PEXA's level of coverage for many years, ELNOs will have substantially different fixed costs, and these should be taken into account in setting interoperability prices.

If interoperability price setting fails to adequately recognise and account for the cost of full network coverage, perverse incentives may be created for ELNOs that run counter to the objectives of the e-conveyancing ecosystem.

In the current non-interoperable ecosystem, PEXA and Sympli have flat national pricing for various transaction types. These flat prices imply cross-subsidies that ensure that end retail users in smaller population jurisdictions or those transacting more complex instruments do not pay very high prices. The rationale for this cross-subsidy is that all entities in conveyancing benefit if the number of off-line transactions is minimised, enabling them to all minimise reserve capacity for offline transactions. The cross-subsidy may also reflect the preference of ARNECC, as an intergovernmental body made up of States and Territories, for fiscal equalisation principles that so far as possible deliver an equivalent level of government services to residents of different states.

Expanding into new jurisdictions is a largely fixed cost, irrespective of the size of the jurisdiction. It is also a lengthy and costly exercise, taking years, significant financial investment, and organisational focus. Expanding coverage of transaction types has similar dynamics. 85% of transactions occur through one of five instruments, and 95% of transactions occur through one of seven. The remaining 5% of transactions involve 200-300 instruments. As shown in Exhibit 11, the likely e-conveyancing revenue is likely to be much lower in jurisdictions that have not yet become part of the e-conveyancing network, and consequently building e-conveyancing capability for them is likely to be less economically attractive than in larger jurisdictions.

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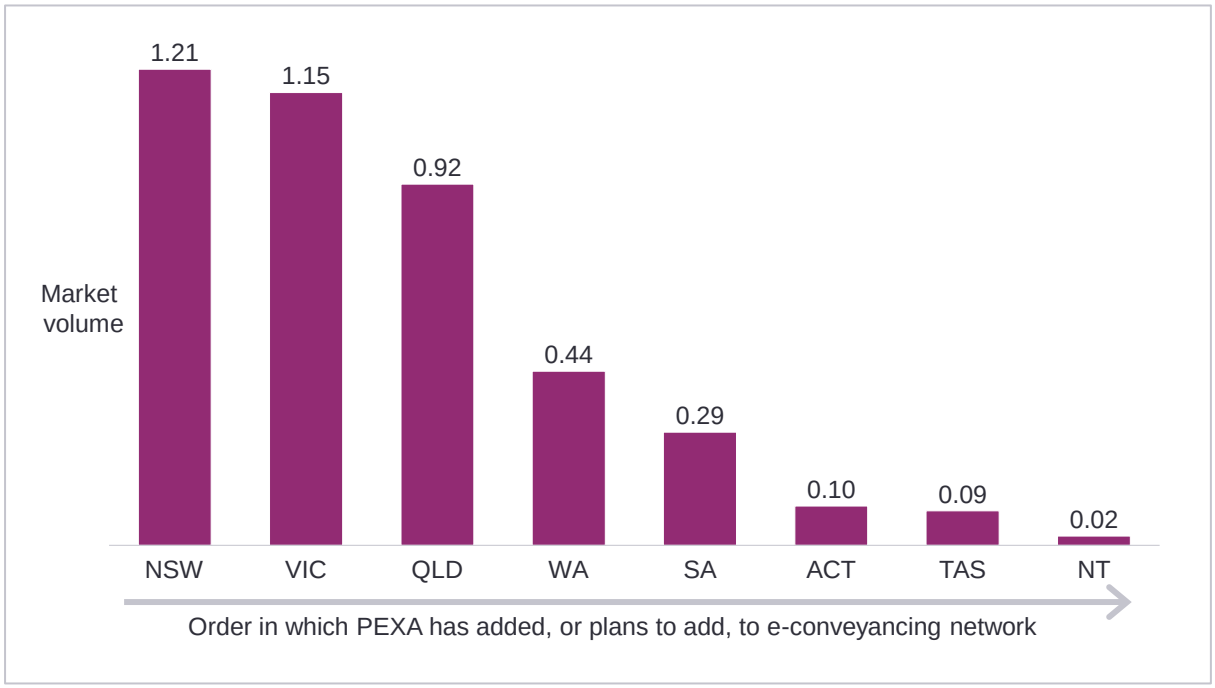
Exhibit 11. Estimated total addressable volume by jurisdiction (FY21, millions)



Source: PEXA IPO Prospectus (2021)

However, the prices charged to subscribers, are typically similar across jurisdictions and transaction types, and do not reflect much higher fixed costs per transaction for lower volume transactions. Without this pricing policy, the fees charged to some end retail users would be very high (for example, if a user lodged an application to register a writ in the ACT).

Repricing smaller volume transactions to be more cost-reflective is not practical. These prices are now largely fixed by regulation (with caps on price increases set by ARNECC), and significant differences between jurisdictions are unlikely to be politically acceptable.

The implicit cross-subsidies are sustainable under the current non-interoperable regime, in which PEXA has a high market share across transactions and jurisdictions. PEXA can economically expand into small jurisdictions and more complex transaction types by recovering the cost of its investment over a long time period, and from higher volume transactions. Even where the revenues did not cover the fixed costs, PEXA has built functionality, recognising the public interest in a universal service that is echoed by the requirement in an interoperable regime for all ELNOs to provide comprehensive coverage.

3.3.2 Implicit cross-jurisdiction/transaction type subsidies are exposed with interoperability

In practice, interoperability exposes these cross-subsidies, potentially leading to a market structure in which no player can afford to build and support e-conveyancing infrastructure for small population jurisdictions or low-volume transaction types. In its current form, and without careful design of inter-ELNO fees, interoperability will allow new entrants to cherry-pick high volume transaction types, potentially offering prices that do not include the fixed costs of building back-end settlement and lodgement functionality for other transactions. Sympli has already proposed different discounts for financial institutions and practitioners. Discounts for larger volume transactors are likely given the experience of pricing in other industries. This would likely to lead to ELNOs investing less in creating and maintaining

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small-volume transaction types, so that the conveyancing industry (and therefore the public) misses out on the potential savings from using an electronic platform for these transactions

As discussed above in section 2.2, while regulations require all ELNOs to build comprehensive lodgement functionality (but not comprehensive transaction / financial settlement functionality), these regulations appear to be unenforceable in practice. Even if a new entrant were strongly motivated to build comprehensive functionality, it would probably take several years to do so given that it has taken PEXA more than 10 years to build services that still fall short of the comprehensive service ideal. Given this reality, it is likely that a new entrant will be able to delay for an extended period any enforcement of the regulatory requirement to build comprehensive capability. In the meantime, the new entrant can cherry-pick high volume transactions or jurisdictions for that extended period.

In the absence of appropriate inter-ELNO pricing, it is also likely that when Titles Offices desire new functionality, both incumbent and new entrant ELNOs are likely to delay. The first mover will almost inevitably incur higher fixed costs, because it has to devise and negotiate a solution with other participants. Subsequent followers are likely to build very similar functionality, but at materially lower costs.

3.3.3 Sound economic incentives will ensure ongoing investment to facilitate national network coverage

Rather than relying on a largely unenforceable regulatory requirements, IPART needs to consider how inter-ELNO fees and other fee arrangements can create incentives for ongoing investment in building and maintaining comprehensive electronic conveyancing capabilities. Possible mechanisms to avoid the problems of cherry-picking include:

- Changing subscriber fees to be more cost-reflective – which potentially implies large increases in prices for small jurisdictions or low volume transactions;
- Specific Universal Service Obligation payments to ELNOs in return for building and maintaining functionality that is not otherwise economic; and
- Inter-ELNO fees from a Participating ELNO to a Responsible ELNO that recover some or all of the fixed costs of building functionality, which reduce the incentives for cherry-picking.

We suggest IPART should also have close regard to the principles and mechanisms utilised under the Universal Service Obligation established to mitigate the negative externalities of a privatised telecommunications industry and ensure all Australians had network coverage (see section 2.2).

3.3.4 An inadequate inter-ELNO fee will have economic consequences for PEXA and compromise national e-conveyancing coverage

Without a substantial inter-ELNO fee that adequately reflects fixed costs, and given current pricing to subscribers, the profitability of both incumbent and new entrant ELNOs will largely depend on their share of the Participating ELNO role. This illustrates how new entrants will have powerful incentives to delay their regulatory obligation to build Responsible ELNO capability for as long as possible. There is also a possibility of either the incumbent or the new entrant being unprofitable, which is likely to destabilise the industry, putting at risk the security, reliability, and affordability which is fundamental to e-conveyancing. Introducing a substantial inter-ELNO fee would materially improve the economics of the-conveyancing market by creating sufficient incentives for ELNOs to take on the Responsible role and continue expansion of the network into new jurisdictions and transaction types.

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We expect that more detailed modelling will need to be carried out on this issue for Stage 2 of IPART's inquiry and would be happy to support this.

It might be argued that inter-ELNO fees that recover fixed costs effectively compel new entrants to "pay twice" – they would both pay to build their own functionality, and they would pay the bulk of inter-ELNO fees while the incumbent retained a market share of more than 50 per cent. There are a number of problems with this argument:

- In reality, new entrants are likely to delay building comprehensive functionality for as long as possible, reflecting their financial incentives – often they will not have "paid once".

- Because new entrants can learn from the functionality built by the first mover, their fixed costs should be materially lower – they will pay materially less to build their own functionality.

- New entrants are also likely to have materially lower fixed costs because they can plug into an existing network, rather than needing to expend effort to ensure that a critical mass of transactors use the platform (this issue is considered further in section 3.4 below).

An alternative argument is that new entrants should only pay a fee reflecting fixed costs where they lack the capability to perform the relevant Responsible ELNO role. There would be significant problems with this proposal in practice. It is likely to lead to ongoing disputes about whether the new entrant has really built equivalent functionality. A new entrant might also economise to build relatively low-quality Responsible ELNO capability, reflecting the incentives to minimise spend on back-end functionality when the bulk of the revenues are earnt by the Participating ELNOs. Those most adversely affected would be financial institutions, which conduct many transactions. They might well choose to remain with an established ELNO. The established ELNO would then be the Responsible ELNO for the vast majority of transactions, but new entrants would not be obliged to pay for any of its fixed cost.

As outlined, PEXA believes this is a significant issue that has the potential to compromise the core objectives of the e-conveyancing ecosystem if not adequately reflected in interoperability price setting. Alternatively, if IPART considers that mechanisms for recovering costs of universal service obligations are beyond the scope of its inquiry, it should state this explicitly lest its work be misinterpreted as concluding that such recovery is inappropriate.

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3.4 Cost to create the existing system on which interoperability is built

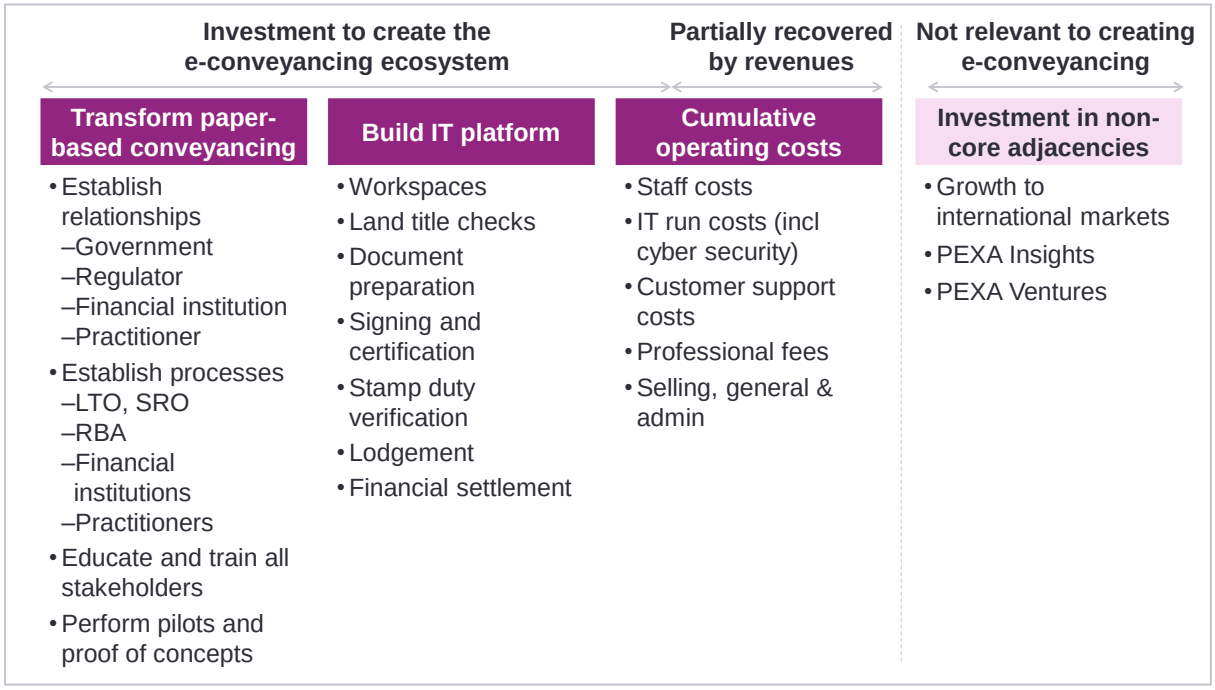
3.4.1 PEXA risked significant investments to transform paper conveyancing into e-conveyancing

As outlined in section 1.1, PEXA in collaboration with Government and other stakeholders (such as financial institutions) collectively transformed the paper conveyancing industry into e-conveyancing. This undertaking carried significant investment risk with no guarantee of success. Previous attempts by NSW and Victorian Governments to do so had not succeeded.

In transforming paper conveyancing, PEXA invested in one-off activities to build the processes and relationships (across institutions and jurisdictions) that today enable e-conveyancing to exist and enable other ELNOs to enter the e-conveyancing market. The activities and investment made by PEXA over this time (detailed in Exhibit 12) include:

- Acquiring know-how about conveyancing and developing how to make it work in an online environment;
- Gaining the cooperation of key stakeholders (such as State and Territory Titles Offices and Revenue Officers and financial institutions);
- Gaining the buy in of thousands of conveyancing practitioners – noting that e-conveyancing would not be viable without their near-universal support and participation; and
- Designing and building, for the first time, the IT system and connections to each key stakeholder in the e-conveyancing network.

Exhibit 12. PEXA contribution to create e-conveyancing



Source: PEXA financial data

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The cumulative cost of these activities since 2010 is large and PEXA's total aggregate revenues to date are less than these historical costs. A specific valuation of PEXA's contribution to the creation of the e-conveyancing industry is more relevant to IPARTs second Issues Paper on this topic. We can provide further details on this at the appropriate time. The point of this submission is to establish that it is appropriate for inter-ELNO fees to recognise the value of PEXA's historic investment to create the e-conveyancing network, without which interoperability would be impossible.

3.4.2 PEXA's ability to earn a recovery on its investment in creating e-conveyancing is put at risk by interoperability

In an e-conveyancing industry without interoperability, PEXA would have more opportunity to recover the invested costs in creating the industry by relying on its first mover advantage and the strength of its network with financial institutions and practitioners. PEXA would still need to compete with new ELNO entrants who could offer a range of services across the market. However, the introduction of interoperability puts the recovery of these invested costs at greater risk by enabling new entrant ELNOs to piggy-back off the network and ecosystem created by PEXA.

IPART's 2019 "Review of the Pricing Framework for E-conveyancing Services in NSW" found that e-conveyancing pricing was reasonable relative to the costs of constructing an efficient ELNO. This pricing factored in an allowance for a return on invested capital (or return on assets – see Exhibit 13 below).

However, IPART's 2019 review does *not* imply that PEXA will earn an appropriate return on capital with current e-conveyancing pricing *if the system is interoperable*. In this regard:

- IPART examined a regime where interoperability was in the early stages of consideration and assumed PEXA would have substantial market share for many years to recover the costs of transforming paper conveyancing. In the current proposed interoperability regime, PEXA's market share is likely to fall more quickly than IPART previously assumed, and PEXA will therefore have less time to recover its up-front costs.

- IPART also examined a regime with very strong transaction volumes. With rising interest rates, property transaction volumes have already declined and are likely to continue to fall, which will substantially reduce the revenue pool of the entire e-conveyancing market and may trigger another pricing review to ensure e-conveyancing prices are still reasonable under slower market conditions.

- IPART also did not have regard to the implications of interoperability resulting in ATI Global/Sympli emerging as the only vertically integrated conveyancing workflow stack, nor the ability it will have to leverage its position in PMS to: (a) direct e-conveyancing transaction volume to Sympli; and (b) cross-subsidise products across its vertically integrated conveyancing workflow process. PEXA as a standalone ELNO will not be able to compete with ATI Global/Sympli on an equivalent basis, which means it will be difficult for PEXA to earn a recovery on its investment in creating e-conveyancing.

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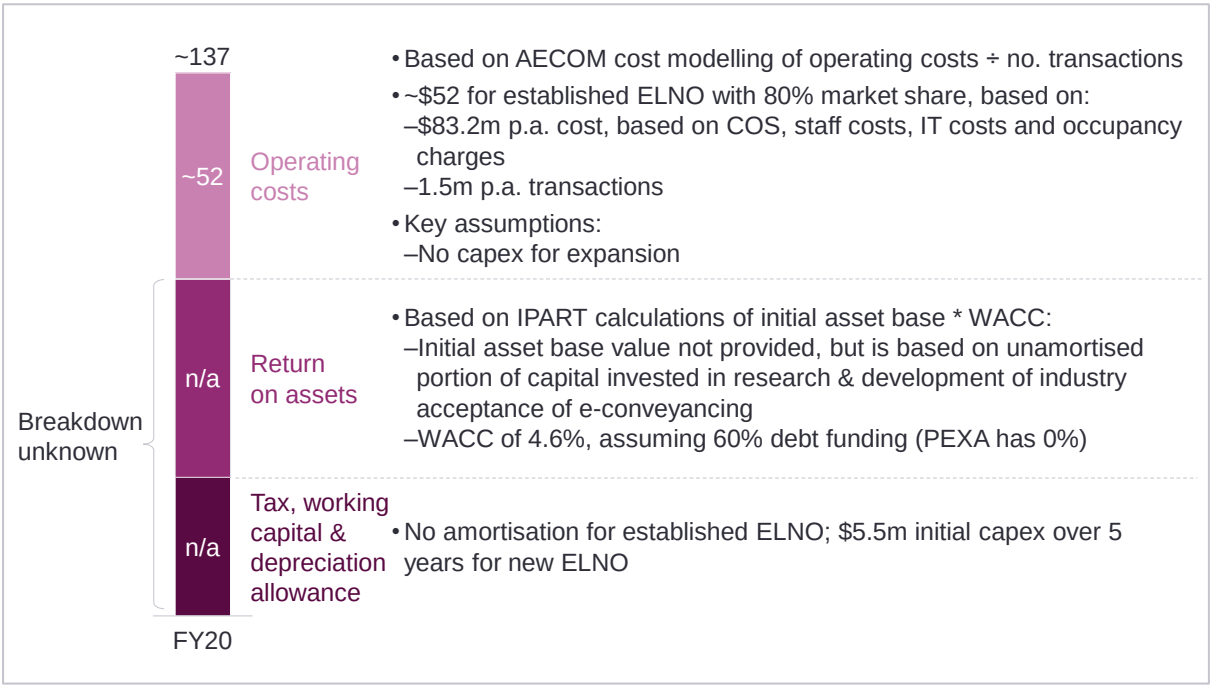
Exhibit 13. Cost per transfer for high market share efficient ELNO, $ per transaction (transfer)



Source: Independent Pricing and Regulatory Tribunal, 'Review of the Pricing Framework for Electronic Conveyancing Services in NSW' (November 2019); AECOM report 'Estimating costs of electronic conveyancing services in NSW' (2019); PEXA data (updated PEXA financial and volume, April 2021)

3.4.3 Compromising the ability to earn a return on investment creates long term market issues in e-conveyancing and beyond

It is a basic economic principle that markets should be designed so that market participants receive a fair and reasonable return on productive assets (see section 2.3). As this basic economic principle is commonly applied in various industries, comparisons with approaches to price setting in these industries can guide interoperability price setting. As identified in IPART's Issues Paper, parallels with e-conveyancing can be drawn to a number of industries with access regimes fee arrangements. Under a plausible set of scenarios, where PEXA remains the Responsible ELNO for the majority of transactions, PEXA's role is akin to that of an access provider.

This is because via interoperability and its role as the Responsible ELNO, PEXA will be providing Sympli with access to its proven, reliable and secure network capabilities to allow it to participate in interoperable transactions.

It follows that pricing principles that are commonly adopted in statutory access regimes or network-based industries are analogous to e-conveyancing and should be considered by IPART. Many of the examples identified by IPART in its Issues Paper pertain to access regimes for infrastructure whereby access seekers pay access providers for access to their infrastructure or network. Key features of these regimes are identified in Annexure A.

Access regimes require prices to be regulated so that access seekers pay an economically efficient price. These principles apply regardless of the mode of regulatory control - whether it is a negotiate-arbitrate approach, or a form of direct price control.

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Arguably, there is not a precise industry analogy with e-conveyancing. The key features of an access-regulated industry typically include that an access provider has a service, which has characteristics that make the provider a monopoly, or close to a monopoly. As a result, access regulation is generally concerned with regulating 'bottleneck power' where access to physical infrastructure is a barrier to entry.

PEXA's network and services are theoretically replicable by another entrant ELNO with sufficient time and investment. However, absent interoperability, the barriers to doing so are substantial. Only PEXA has proven capability and network coverage to perform lodgement and settlement efficiently, securely and at scale across all jurisdictions that have determined to introduce e-conveyancing and all transaction types. In its role as industry reform facilitator and network enabler, PEXA developed the PEXA Exchange that today delivers e-conveyancing services by connecting thousands of property market participants onto one platform. By contrast, Sympli has no proven capability or network, which will mean PEXA will be the Responsible ELNO for the majority of transactions for an extended period of time.

In these circumstances, PEXA's role as the Responsible ELNO is analogous to the role of an access provider so long as PEXA remains the Responsible ELNO for the majority of transactions and jurisdictions. Accordingly, the pricing principles noted in this paper are relevant and should be adopted by IPART in its approach to inter-ELNO pricing (irrespective of the form of regulation that IPART ultimately determines is appropriate).

Supporting this view, we note that following the Hilmer Review[22], State and Commonwealth governments agreed on a set of commonly applicable pricing principles that are enshrined in various legislative and regulatory instruments and typically adopted in access regimes (discussed further in Section 2).[23] These principles have been applied in a range of industry settings (as outlined in Annexure A), and provide that the price an access provider may charge to an access seeker should:

- be set to generate revenue sufficient to meet the efficient costs of providing access to the service;[24]
- include a return on investment commensurate with the regulatory and commercial risks involved;[25]
- be reflective of the legitimate business interests of the access provider, including its cost of infrastructure, operating costs and return on capital;[26]
- incentivise productivity or cost enhancements;[27]
- preserve the public interest of the use of the service;[28] and
- enable the safe and reliable operation of the services.[29]

[22] National Competition Policy Review - conducted by the Independent Committee of Inquiry in 1993.

[23] See for example, section 44ZZCA of the *Competition and Consumer Act 2010 (Cth) (**CCA**);* s 152BCA of the CCA in relation to the regulation of telecommunication service providers; and clause 6 of the Competition Principles Agreement, which was agreed to by NSW and relevantly is incorporated into the *Independent Pricing and Regulatory Tribunal Act 1992 (NSW).*

[24] *Competition and Consumer Act 2010* (Cth) s 44ZZCA(a)(i); Competition Principles Agreement cl 6.4(i)(ii) and (vii).

[25] *Competition and Consumer Act 2010* (Cth) s 44ZZCA(a)(ii); Competition Principles Agreement cl 6.4(i).

[26] *Competition and Consumer Act 2010* (Cth) s 44X(1)(aa)(a); Competition Principles Agreement cl 6.4(i).

[27] *Competition and Consumer Act 2010* (Cth) s 44ZZCA(c); Competition Principles Agreement cl 6.4(vii).

[28] Competition and Consumer Act 2010 (Cth) s 44X(1)

[29] Competition Principles Agreement cl 6.4(vi).

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The argument that a fee should be paid to PEXA for providing connections to its customers is even stronger than when government regulates "bottleneck power". Under the current e-conveyancing market structure, the major constraint is building a network with critical mass – before an operator can attract substantial business it must establish necessary integrations with major stakeholders, such as financial institutions, land titles offices, revenue offices, and the RBA, and establish enough relationships with subscribers that they will have confidence that other subscribers are also part of the network. It must also prove to ARNECC and the Registrars that its systems are sufficient, reliable and resilient.

This network that PEXA has built is a substantial asset. Without interoperability, there is no compelling reason for subscribers to become customers of another ELNO unless they know that many other subscribers will also become customers. Such network effects are a common feature of online platforms, and it is very unusual for government to intervene to require the owner of one network to provide access to all its customers to the owner of another network. The benefits of such a network are typically seen as the reward to the first mover for the considerable effort of convincing people to join the network.

PEXA's network is not simply the consequence of government mandates. Sympli completed its first practitioner on-boarding and its first electronic lodgement in Queensland in December 2018. At this time, PEXA had less than 20% market share in the Queensland sector (with the remainder paper based) and there was no government mandate for e-conveyancing. Sympli has had ample time and opportunity to invest in its systems and build a network of customers, but did not do so.

Consequently, when new entrants make their systems interoperable with PEXA's network, they are not just benefiting from PEXA's work with numerous players to set the relevant IT standards, its example of how to build the IT platform, and its creation of new business processes. They also benefit significantly from the ability to connect with PEXA's customers without needing to wear out shoe leather to individually convince paper-based practitioners to radically change their business systems, learn how to use a new e-conveyancing system, and adopt a new way of working. When they benefit from connection to this network, it is consistent with basic regulatory principles that they pay for PEXA's costs to create it. As such, the fee to PEXA should not be construed as new entrant paying twice for fixed costs (for their own build and PEXA's).

IPART's preliminary view is that it is reasonable for ELNOs to recover the additional costs establishing and maintaining interoperability. The same logic implies that it is reasonable for PEXA to recover the costs of building the underlying platform on which that interoperability is built.

More broadly, if interoperability is introduced without a pricing mechanism that enables PEXA to recover a fair return on the costs it incurred in creating the e-conveyancing ecosystem, then government regulation would in effect undermine the value of PEXA's asset. This outcome would undermine private sector confidence in future investment not just in e-conveyancing, but in other industries. It would send a powerful regulatory signal that would deter future public private partnerships and investments of national significance. The potential to undermine investor confidence is even more salient because governments sold PEXA to private investors as a going concern.

3.4.4 A common user charge is a potential method to enable PEXA to recover its investment in creating e-conveyancing through interoperability fees

Recognising PEXA's investment in creating e-conveyancing and allowing it to earn a return on this could be enabled through an inter-ELNO service fee. This could take the form of a Common User charge that all ELNOs (except PEXA) would pay for each transaction to PEXA as the founding ELNO, whether or not it was the Responsible ELNO. This charge would be deducted from retail fees (after transaction charges e.g. LSS),

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and before fees are distributed between Responsible and Participating ELNOs. Importantly, a common user charge would not result in any increase in fees to subscribers.

The revenue collected through the inter-ELNO common user charge would depend on the market share of ELNOs. If PEXA continues to service most of the market, it would collect little common user charge, and it would earn a return on its investment in creating e-conveyancing directly through subscriber fees. IPART's 2019 report found that these fees would provide PEXA with a reasonable – but not excessive – return on investment. If PEXA rapidly loses market share, then new entrants would pay common user charges to PEXA that would enable PEXA to earn a return on its investment. This would support stability of the e-conveyancing industry and the objectives of IPARTs current review (we outline this further in section 3.4.6 below).

3.4.5 There are parallels between a common user charge in e-conveyancing and other industries

There are comparable industry examples to e-conveyancing where Government has permitted private sector participants to charge for the existence value of the systems and infrastructure they have created (see Annexure A). While the form of these fee structures vary, the common economic principles that underpin each of these case studies is that a first mover should receive a fair and reasonable return on its investments and productive assets to ensure there are appropriate incentives to promote ongoing and sustainable investment in infrastructure, network relationships and innovation.

A key theme that e-conveyancing has in common with these industries is that the first mover has invested heavily to create the network / infrastructure on which relevant stakeholders (including suppliers and consumers) are able to engage in commercial dealings, the sum of which has generated efficiencies and economic productivity.

In the e-conveyancing context, without PEXA's investment of hundreds of millions of dollars over a decade to create the seamless digital network of relevant conveyancing stakeholders, including financial institutions, practitioners, LTOs, SROs and the RBA, Sympli's entry could not have occurred. Sympli will only have access to PEXA's network, infrastructure and customers because of the Responsible ELNO model of interoperability.

A common user charge to recognise the value of access to the network and PEXA's historic investment is analogous to other digital network-based industries, where common user charges enable the first mover to recover costs. For example, various digital platforms charge participants not only for the services they provide, but for access to the intangible value of the ecosystem they have created, and in which they continue to invest (see Exhibit 14 below). Google's Play Store, Apple's App Store and the Microsoft Store, as digital storefronts for mobile apps, charge a 10-30% commission on sales of apps distributed through their respective stores. The charge recognises that these platforms have invested in the creation of a network that allows developers to not only optimise and distribute their apps, but to reach millions of users around the world. The establishment of this user base required sustained investment over a significant period and is now essential for developers building their own businesses. Like PEXA, these digital app stores also provide a range of associated tools and infrastructure, such as assisting with certain compliance requirements, help services, and a consistent, safe and secure payments mechanism – all of which took dedicated time, effort, and investment to create.

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Exhibit 14. Digital network businesses with a proxy common user charge

	Description	Example
Subscription	*Fee to platform owner for services*	• Health Industry Claims and Payment Service (HICAPS) charges a monthly fee of $25 for HIPCAPS and EFTPOS
		• Bloomberg Terminal and Refinitiv Eikon have monthly fees
Commission	*Fee to platform owner to access customers*	• App stores such as (Google, Apple and WeChat) charge a commission on sales of many apps distributed through their respective stores
		• Online trading platforms such as eBay charge a commission on sales and insertion fee in some cases
		• Riding sharing platforms such as Uber, charge a service fee on the ride fare
Royalty	*Fee to IP owner for right of use*	• In the music industry the owners of the intellectual property (i.e. the song) charge royalties to other parties for its use
		• eBooks can be purchased via the Amazon's Kindle book store. Authors are paid a royalty in accordance with their contract

Source: Desktop research

3.4.6 A common user charge could help rather than hinder competition in e-conveyancing

PEXA understands that the purpose of introducing interoperability into e-conveyancing is to lower the barriers for new entrants to enter the industry and therefore increase competition within the industry. Increasing competition is expected to deliver increased efficiency and enhance innovation. PEXA supports IPART in the pursuit of increased competition in the industry and believes a common user charge to recognise the cost of creating e-conveyancing would help, rather than hinder competition in the industry.

As demonstrated in section 1.2.5, it is a plausible scenario that ATI Global/Sympli will use its vertical integration to gain share in e-conveyancing. In this scenario, PEXA would be forced to re-prioritise investment and focus on the same areas as Sympli (to remain competitive). This would most likely mean innovations focused on high value and volume jurisdictions and transaction types, at the expense of network expansion to remaining jurisdictions and transaction types (e.g. Tasmania and NT). In this scenario, the goals and objectives of the e-conveyancing industry would be compromised and interoperability will have failed its core purpose.

A common user charge paid by all other ELNOs to the founding ELNO, PEXA, to recognise its costs to create the network, would reduce the probability of this scenario and support long-term competition in e-conveyancing by maximising the chances that both PEXA and Sympli are able to profitably operate in the industry. This is because PEXA as the founding ELNO has structurally higher fixed costs than a new entrant who benefits from technological improvements and efficiencies that PEXA has created through investment over the last ten years (particularly given PEXAs role as the established ELNO who is still transforming paper conveyancing in new jurisdictions).

A common user charge will result in a new entrant's costs increasing, however, this would be tied to their market share and can be set at a level that ensures their viability. It may also have the added benefit of giving a new entrant incentives to take share of both Responsible and Participating ELNO roles, as larger

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market shares would be required to recover a new entrants fixed costs. This is consistent with the need to create financial incentives for new entrants to build back-end capabilities, rather than just relying on a vague, and largely unenforceable regulatory requirement.

As outlined, PEXA believes this is a significant issue that has the potential to compromise the core objectives of the e-conveyancing ecosystem if not adequately reflected in interoperability price setting. If IPART considers that mechanisms for PEXA to recover its one-off costs of creating the e-conveyancing system are beyond the scope of its inquiry, it should state this explicitly lest its work be misinterpreted as concluding that such recovery is inappropriate.

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4 Deciding on a form of regulation

The second key question on which IPART sought responses is the form of regulation to set the level of interoperability fees between Responsible and Participating ELNOs.

4.1 Form of regulation should be dictated by e-conveyancing objectives

As established in section 1.1.1, the goal of the e-conveyancing industry is to deliver a **more secure, reliable, and affordable method of conducting property transactions for all Australians**. Supporting this goal are the five objectives of e-conveyancing, to create less risk, less complexity, lower costs, accessibility for all Australians (in all jurisdictions) and all transaction types, and to enable continued innovation. The form of regulation should be oriented around consideration of this goal and set of objectives.

The other consideration around choosing a form of regulation is alignment with the regulatory principles outlined above in section 2, particularly the principle that successful private investment should receive a fair and reasonable return on invested capital. Direct or indirect intervention that impinges on this principle would undermine future private sector investment confidence that could have long-term impacts on the e-conveyancing industry and flow-on to industries beyond.

4.2 The key choice is between arbitration and regulated price setting

IPART laid out in its first Issues Paper for consideration two forms of regulation to determine interoperable transaction fees between Responsible and Participating ELNOs:

1. Negotiate-arbitrate model; or
2. Regulated method.

As IPART has indicated in the first Issues Paper, the effectiveness of a negotiation tends to depend on the extent of competition and the degree of market power held by negotiating parties. In the current situation, PEXA's large market share and position in the e-conveyancing market, as well as Sympli's position as a new entrant, make resolution by negotiation on pricing difficult.

In addition, the negotiations may become more complicated and protracted as the number of ELNOs increases.

If negotiation is unlikely to lead to resolution, then the real choice between the two forms of regulation outlined is whether interoperability fees should be set by an arbitrator or by an economic regulator.

4.3 The case for an economic regulator (e.g. IPART) to be the decision maker

The optimal decision-maker depends on the nature of the decision required. In making e-conveyancing interoperability pricing decisions, the principles applicable in other access regimes and network based industries (as discussed in section 3.43.4) are all relevant and should guide decisions (whether they are made by an arbitrator or regulator). As outlined above in section 2, price setting for inter-ELNO fees affects not only the share of profit between ELNOs but may well shape their behaviour and affect the public interest by undermining the security, reliability, and affordability of conveyancing.

Because of these substantial public interest considerations, an economic regulator should be appointed, as either the arbitrator or the regulator that sets the method for determination and actual levels of prices.

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An economic regulator such as IPART is better equipped than a commercial arbitrator for the following reasons:

- An economic regulator such as IPART has significant **expertise specific to e-conveyancing** that an arbitrator may lack. This expertise is likely to develop, both through interoperability price-setting issues, and through other price-setting issues (such as determining appropriate Subscriber prices). Greater expertise is likely to lead to better quality decisions in a complex area that does not have clear precedents and has industry-specific market dynamics;

- An economic regulator such as IPART is **familiar with market regulation**, and how it may affect market structure, conduct and performance, that then affect public interest outcomes. A commercial arbitrator may be less familiar with such issues. The ability to craft new regulation is important in the e-conveyancing market because it has many unique features and is still relatively early in its development life cycle;

- An economic regulator such as IPART is better positioned to **consider the public interest** whereas a commercial arbitrator may tend to be more limited in focusing on how the decision will affect the negotiating parties. A focus on the public interest is important because interventions in payments between ELNOs will ultimately change market structure, affecting consumers;

- An economic regulator can provide **greater continuity**, whereas a different commercial arbitrator may be appointed each time an issue arises. Continuity for e-conveyancing price setting is important because it is likely to be a recurring issue as the existing e-conveyancing ecosystem matures, new jurisdictions are added to the network and market dynamics evolves (e.g. as new ELNOs enter or the impact of vertical integration across the value chain becomes apparent).

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Annexure A: Relevant access regime pricing principles referred to in IPART's Issues Paper

Industry	Access Regime	Pricing principles
Tele-communications	Mobile Terminating Access Service Regime (MTAS) Regulated under Part XIC of the *Competition and Consumer Act 2010* (Cth)	***Pricing principles:*** When setting a price in an access determination the ACCC must take into account (among other things) the following under s 152BCA of the CCA: • **Marginal costs** – marginal costs of providing the service are recoverable in the fee charged to access seekers.[30] • **Ongoing capital expenditure** – efficient capital expenditure that promotes the long-term interests of end-users is recoverable in the fee charged to access seekers under the MTAS regime.[31] • **Existence value** – any price set includes the 'legitimate business interests' of an access provider, which refers to an access provider's interest in recovering the costs of its infrastructure, its operating costs, and obtaining a normal return on its capital.[32] ***Note:*** Telstra provides the universal service obligation pursuant to the Telecommunications (Consumer Protection and Service Standards) Act 1999 (Cth), which is a separate obligation to the MTAS regime. Telstra is required to ensure that all Australians have access to payphones and standard telephone services. In order to fund this obligation, a telecommunications industry levy is applied to other firms, alongside government funding.[33]

[30] *Competition and Consumer Act 2010* (Cth) ss 152BCA(d); (f); and (g).

[31] Competition and Consumer Act 2010 (Cth) s 152(a)–(b).

[32] *Re Telstra* [2006] ACompT 4 [134].

[33] Australian Communications and Media Authority, 'Telecommunication funding arrangements' available at https://www.acma.gov.au/telecommunications-funding-arrangements.

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Industry	Access Regime	Pricing principles
Rail access	Tarcoola-Darwin Rail Network Negotiate Arbitrate Regime Regulated under Part IIIA of the *Competition and Consumer Act 2010* (Cth)	***Pricing principles:*** An access provider is entitled to: • **Marginal costs** – recover costs associated with provision of services at an efficient market rate.[34] • **Ongoing capital expenditure** – a commercial return on costs associated with the provision of railway infrastructure services.[35] • **Existence value** – an appropriate commercial return on the initial capital expenditure on railway infrastructure.[36]
Rail access	NSW Rail Access Regime Regulated under schedule 6AA of the *Transport Administration Act 1988* (NSW) and the *Independent Pricing and Regulatory*	***Pricing principles:*** Under the NSW Rail Access Regime, the Independent Pricing and Regulatory Tribunal takes into account the following principles when setting floor and ceiling prices, as well as resolving disputes: • **Marginal costs** – an access provider is entitled to recover efficient marginal costs of providing the service.[37] • **Ongoing capital expenditure** – ongoing capital expenditure used to improve the rail network is recoverable through the fee set for access seekers. IPART is required to take into account 'the owner's legitimate business interests and investment in the facility'[38] in reviewing any pricing dispute and 'the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake'.[39]

[34] Essential Services Commission of South Australia, 'Tarcoola-Darwin Railway: 10-year review of revenues Final Report', page 13.

[35] Essential Services Commission of South Australia, 'Tarcoola-Darwin Railway: 10-year review of revenues Final Report', page 13.

[36] Essential Services Commission of South Australia, 'Tarcoola-Darwin Railway: 10-year review of revenues Final Report', page 13.

[37] *Independent Pricing and Regulatory Tribunal Act 1992* (NSW) s 24B(3)(a); Competition Principles Agreement cl 6.4(i)(vi)–(vii).

[38] *Independent Pricing and Regulatory Tribunal Act 1992* (NSW) s 24B(3)(a); Competition Principles Agreement cl 6.4(i)(i).

[39] *Independent Pricing and Regulatory Tribunal Act 1992* (NSW) s 24B(3)(a); Competition Principles Agreement cl 6.4(i)(iii).

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Industry	Access Regime	Pricing principles
	Tribunal Act 1992 (NSW)	• **Existence value** – historic capital expenditures must be considered in relation to any access pricing disputes by IPART,[40] Historic capital expenditure is also considered when setting the opening regulatory asset base for the regime.[41]
Rail access	Tariffs Model for coal-related services Regulated under the *Queensland Competition Authority Act 1997* (Qld)	***Pricing principles:*** The Queensland Competition Authority must ensure that a price is set which: • **Marginal costs** – will 'generate expected revenue for the service that is at least enough to meet the efficient costs of providing access to the service…'.[42] This applies to both the reference tariff level, and any arbitration that occurs to resolve a dispute. • **Ongoing capital expenditure** – includes 'a return on investment commensurate with the regulatory and commercial risks involved'.[43] Further, the price must 'provide incentives to reduce costs or otherwise improve productivity'.[44] • **Existence value** – includes 'a return on investment commensurate with the regulatory and commercial risks involved'.[45]
Port access	Port Access Negotiate Arbitrate Regime	***Pricing principles:*** The access regime is administered by the Essential Services Commission of South Australia, and it must take into account the pricing principles under the Competition Principles Agreement when settling any access disputes,[46] which includes that:

[40] *Independent Pricing and Regulatory Tribunal Act 1992* (NSW) s 24B(3)(a); Competition Principles Agreement cl 6.4(i)(i)–(iii).

[41] Independent Pricing and Regulatory Tribunal, 'Review of the NSW Rail Access Undertaking: Issues Paper' (November 2021), 29; NSW Rail Access Undertaking (1999) sch 3, cl 3.2(a).

[42] Queensland Competition Authority Act 1997 (Qld) s 168A(a).

[43] Queensland Competition Authority Act 1997 (Qld) s 168A(a).

[44] Queensland Competition Authority Act 1997 (Qld) s 168A(d).

[45] Queensland Competition Authority Act 1997 (Qld) s 168A(a).

[46] *Maritime Services (Access) Act 2000* (SA) s 32(1)(a)–(h); approved in the National Competition Council's assessment of the access regime, see National Competition Council, 'South Australian Ports Access Regime: Final Recommendation' (29 September 2021) 63.

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Industry	Access Regime	Pricing principles
	Regulated under the *Maritime Services (Access) Act 2000* (SA)	• **Marginal costs** – marginal costs of providing access to the infrastructure are recoverable in the fees set in a negotiation.[47] • **Ongoing capital expenditure** – ongoing capital expenditure is recoverable from access seekers.[48] • **Existence value** – historic capital expenditure is recoverable from access seekers.[49]
Electricity	Electricity Network Access Negotiate Arbitrate Regime Regulated under the *National Electricity Law* and the *National Electricity Rules*	***Pricing principles:*** Fees set for negotiated distribution services under the *National Electricity Rules* should account for: • **Marginal costs** – efficient costs of providing the service. However, shared costs of distributors (i.e. distributors will use many of the same resources to provide direct-priced services and negotiated distribution services) cannot be priced in the same way for negotiated access users.[50] • **Ongoing capital expenditure and existence value** – ongoing and historic capital expenditure are treated the same way in the NER. Distributors can recover capital expenditure through the access fees charged.[51]
Electricity	Direct Price Control Regulation for Energy Distribution	***Pricing principles*** – When the Australian Energy Regulator sets a fee for a standard distribution service, the price must take into account the following principles: • **Marginal costs** – marginal costs are recoverable from the fees paid for a service. Underspending in any given year can be rolled forward and used as an incentive to build efficiency into the system.[52]

[47] Competition Principles Agreement cl 6.4(i)(vi)–(vii).

[48] Competition Principles Agreement cl 6.4(i)(i) and (iii)

[49] Competition Principles Agreement cl 6.4(i)(i)–(iii).

[50] Australian Energy Regulator, 'Distribution Cost Allocation Guideline' available at: https://www.aer.gov.au/system/files/AER%20Final%20decision%20-%20Distribution%20cost%20allocation%20guidelines%20%2826%20June%202008%29.pdf.

[51] National Electricity Rules Ch 6 Pt D.

[52] National Electricity Rules Ch 6 Pt C.

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Industry	Access Regime	Pricing principles
	Regulated under the *National Electricity Law* and the *National Electricity Rules*	• **Ongoing capital expenditure** – ongoing capital expenditure is encouraged by incentive schemes that will increase the revenue cap for that distribution service provision.[53] • **Existence value** – all capital expenditure is recoverable at a set return on investment.[54]

[53] *National Electricity Rules* r 6.5.1; Australian Energy Regulator, 'AER Capital Expenditure Assessment Outline for Electricity Distribution Determinations' (February 2020); National Electricity Objective, as outlined in s 7 of the *National Electricity Law*.

[54] National Electricity Rules r 6.5.1.

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