

# **REVIEW OF** THE PRICING FRAMEWORK FOR ELECTRONIC CONVEYANCING SERVICES IN NSW

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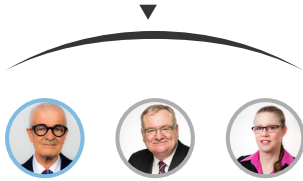
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## Tribunal Members



### The Tribunal members for this review are:

Dr Paul Paterson, Chair

Mr Ed Willett

Ms Deborah Cope

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## Invitation for submissions

IPART invites written comment on this document and encourages all interested parties to provide submissions addressing the matters discussed.

Submissions are due by 17 September 2019

We would prefer to receive them electronically via our online submission form\_ [www.ipart.nsw.gov.au/Home/Consumer\\_Information/Lodge\\_a\\_submission](http://www.ipart.nsw.gov.au/Home/Consumer_Information/Lodge_a_submission).



### You can also send comments by mail to:

#### **eConveyancing Review**

Independent Pricing and Regulatory Tribunal  
PO Box K35  
Haymarket Post Shop, Sydney NSW 1240

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# 1. Executive Summary



The development and implementation of eConveyancing has been a **success story of digitisation**. A paper-based system of real property title lodgment and financial settlement has been transformed to one that operates electronically, saving time and reducing the potential for errors and fraud, and continuing to protect the integrity of land registries and financial transactions.

New entities – electronic lodgment network operators (ELNOs) – have been created, and the roles of solicitors, conveyancers and settlement agents have changed.



## The Australian eConveyancing market is well advanced

This market has evolved to the point where **three states including NSW have mandated** most property transactions to be completed electronically.

However, there are elements of the market's current structure that require further examination, particularly with respect to governance, the scope for competition, the regulation of the financial settlement component of transactions and the pricing regulatory framework. For example:

- The market is highly concentrated, with two ELNOs licensed to operate in NSW
- One of the existing ELNOs, PEXA, effectively has 100% of the market as the other, Sympli, has yet to transact in NSW.
- Competition is hampered by ELNOs' inability to interoperate with each other in transactions involving multiple parties

The Independent Pricing and Regulatory Tribunal of NSW (IPART) is conducting one of several independent reviews<sup>1</sup> of these elements. The NSW Government has directed us to assess the state of the market, and then recommend an appropriate pricing regulatory framework that includes:



A **maximum price or pricing methodology** for the provision of services by an ELNO



**Maximum prices or pricing methodologies** for services provided to ELNOs by NSW Land Registry Services (NSW LRS) and by Revenue NSW.

In doing so, we must consider the need to protect customers from excessive prices while allowing ELNOs to recover their efficient costs, and the need to promote competition in the market. Effective competition can drive both lower prices and innovation in service delivery.

This report sets out our draft findings and recommendations, discusses the supporting analysis, and seeks comment from all interested stakeholders.

<sup>1</sup> An independent reviewer (Dench McClean Carlson) is reviewing the Inter-governmental Agreement for an Electronic Conveyancing National Law, focusing on governance and regulatory matters, including competition. The NSW Government has also established working groups with an independent chair to develop proposals for interoperability solutions that could be applied at a national level.

## Maximum prices for all ELNOs should be set at PEXA's current prices and indexed by CPI

The eConveyancing market will remain highly concentrated in at least the short term. Although competition is emerging, the lack of interoperability between ELNOs' systems is constraining its development.

We found that PEXA's current prices are reasonable, and that there is no compelling evidence to move away from the existing pricing regulatory framework set by the Registrar General. We recommend that maximum prices for any ELNO be set as PEXA's current prices with an annual CPI cap from 1 July 2020 for two years.

Interoperability between ELNOs has **significant potential to promote competition**, as it allows each party in the settlement process to use the ELNO of their choice. We consider that building direct connections between the two existing ELNOs is the preferred approach to achieve the benefits of competition in a cost-efficient way. We recommend regulators require the two existing ELNOs to build direct connections.

Regulators should allow subsequent new entrant ELNOs to choose between:

- Connecting to existing lodgment and financial settlement infrastructure
- Developing their own infrastructure and connecting to the other ELNOs in the market.

We found that NSW Land Registry Services (NSW LRS) has made savings from the increased uptake of eConveyancing so can absorb the cost of investing in a new platform to connect multiple ELNOs without introducing a new fee.

Revenue NSW's prices should be set to recover some of the costs it incurs in providing duties verification services, as these services are outside its core tax collection activities. We recommend maximum prices be set to recover the costs that ELNOs directly impact and could avoid or minimise.

## eConveyancing market will remain highly concentrated in at least the short term

Submissions agreed that the industry is undergoing **considerable change**, in terms of competition and the regulatory environment. Uncertainty about interoperability and other aspects of the future state of the market could constrain competition.

While competition from a new entrant, Sympli, is emerging, this ELNO has not yet started operations in NSW,<sup>1</sup> and has undertaken only a few transactions in Victoria and Queensland. Our modelling suggests that under current cost structures, the market is likely to remain concentrated.

To develop competition in the eConveyancing market, the regulatory framework could be modelled on the competition framework for Cash Equity Settlement providers in Australia.



<sup>1</sup>Sympli is licensed to operate in NSW and has announced plans to transact in NSW.

This would involve regulators providing guidance to new entrant ELNOs and setting licence conditions based on ELNO business plans, instead of a two-year moratorium on new entry.

## PEXA's current prices are reasonable as maximum prices for all ELNOs

We asked our consultant, AECOM, to **estimate the costs that a benchmark efficient ELNO would incur** in providing eConveyancing services from 2020-21 to 2023-24. We applied our standard building block method to model prices that would allow a benchmark efficient ELNO to recover those costs. We found that PEXA's existing prices were reasonable compared to all modelled scenarios.

We also investigated prices being charged by settlement agents, both for paper settlements prior to the eConveyancing mandate, and for 'e-settlement' services, where the agents take on some of the administrative tasks of running a PEXA workspace. We found that PEXA's prices are no higher than the prices paid for paper settlement.

Based on our findings on the state of the market and a benchmark efficient ELNO's costs, we consider that PEXA's current prices are reasonable, and appropriate as a maximum price for any ELNO in the short term.



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## Existing price regulatory framework should remain in place while competition develops

We found no compelling evidence to support moving away from the existing regulatory framework. Under this framework, movements in an ELNO's maximum prices are controlled through an **annual CPI minus X cap** (with X currently set to zero). We consider this framework should remain in place while competition in the eConveyancing market develops. This would mean that maximum prices for all ELNOs are set at PEXA's current (real) prices from 1 July 2020, and would be indexed annually by CPI for two years.

## Interoperability between ELNOs would promote competition

Without interoperability subscribers must use the same ELNO to complete a property transaction. We found that implementing interoperability has substantial potential to promote competition. It would allow users to **choose their preferred ELNO and open up the network effects** in the eConveyancing market, permitting ELNOs with a smaller subscriber base to compete. Effective competition would drive innovation and lower costs.

We analysed **four interoperability solutions** and compared their **potential to promote competition and their costs**. We found that **building direct connections** between these ELNOs:

- has more potential to promote competition than a full central hub or access regime model.
- is more cost efficient than an information hub model until there are three or more ELNOs in the market.



The additional **costs of interoperability to the ELNO market as a whole are small** and are outweighed by the benefits.

We consider regulators should require that a direct connection is built between the existing ELNOs in the short term. To enable the development of efficient and effective competition, regulators should also implement a framework that **allows new entrant ELNOs to choose between: using existing infrastructure; or building their own infrastructure** and establishing direct connections with other ELNOs.

Under this model, each ELNO in an interoperable transaction would bear some of the costs of the transaction. However, the ELNO that is responsible for lodgment (or third party fees) would bear more costs. Therefore, if this model were adopted, **a cost-reflective transfer price should be set** to ensure the costs are shared between the lodging and non-lodging ELNO. Assuming that the lodging ELNO incurred all capital costs and other fees, the non-lodging ELNO would pay a transfer price of around \$13 to the lodging ELNO (and share the costs of interoperability insurance). Note that this transfer does not represent an additional charge to subscribers.



### NSW LRS has made savings from eConveyancing and so can absorb the costs of upgrading its system to accommodate multiple ELNOs

NSW LRS has invested funds in building a new platform that allows multiple ELNOs to obtain land title information and lodge changes to titles and seeks to recover those costs through an additional charge on ELNOs. NSW LRS sought to recover these costs from the ELNOs that connect to the new platform. We found that NSW LRS should be able to absorb the cost of any incremental investment in technology to permit connection by multiple ELNOs.

We consider that the **LSS fees being charged already cover the costs of technology required to deliver services to ELNOs**, whether that be one or several ELNOs. NSW LRS has also been able to reduce its costs significantly as a result of the transition from a wholly paper-based conveyancing process to a majority eConveyancing environment.

## Revenue NSW's prices should be set to recover some of the costs of its duties verification services

In our Issues Paper we asked the threshold question whether a taxing agency should be permitted to charge for performing its core function of collecting taxes. We consider that eConveyancing has resulted in Revenue NSW undertaking additional functions (duties verification services) and incurring additional costs outside its core tax collection function.

Because ELNOs are not able to influence all of the costs associated with Revenue NSW's duties verification service, we consider that these **prices should recover only the cost items that ELNOs impact and could avoid or minimise**.

These include the variable costs related to providing ELNO subscriber support, testing for ELNO system upgrades that exceeds base level frequency, and providing bespoke services to ELNOs.

We recommend that Revenue NSW prices to ELNOs are also CPI indexed annually.



**Table 1.1 Revenue NSW maximum prices to ELNOs (real \$2018-19)**

ELNO cost	IPART maximum price to ELNOs
<b>Costs relating to ELNO subscriber support</b>	\$15.20 per support inquiry to Revenue NSW (based on reported Revenue NSW costs)
<b>Testing for ELNO product releases that exceed base level frequency. (Base level is two major and two minor releases per year, per ELNO)</b>	\$125,000 per ELNO for each product release that exceeds base level
<b>Bespoke service changes</b>	Costs are likely to vary, and so Revenue NSW and ELNOs should negotiate a price for these activities through contractual arrangements (with any disputes being resolved by the eConveyancing national regulator) <sup>a</sup>

<sup>a</sup> The IGA review has proposed several options for a new eConveyancing regulator  
Source: IPART, information provided by Revenue NSW.





HAVE  
YOUR SAY

## Have your say on our draft recommendations

For this review, we are conducting public consultation as well as detailed analysis. To date, we have:

- ▼ Released an **Issues Paper** in **March 2019** outlining our proposed approach to the review and invited comment, and
- ▼ Considered all submissions to our Issues Paper and undertaken analysis to develop our **Draft Report**.

We are now inviting submissions on the findings and recommendations in this Draft Report. Submissions are due by **17 September 2019**. Information on how to make a submission is provided on page iii at the front of this report.

We will hold a public forum in **Sydney on 3 September**. This will provide the opportunity to comment on our draft recommendations. We invite any interested person to register to attend these forums on the IPART website:

[www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au).



We will consider comments at public forums and submissions to our Draft Report in preparing our Final Report and recommendations for the Minister for Customer Service by **November 2019**.

## 1.4 List of draft findings and recommendations



### Our draft findings are:

- 1 The eConveyancing market in NSW is currently highly concentrated and is likely to remain concentrated in at least the short term.
- 2 Interoperability would improve competition in the eConveyancing market and would reduce barriers to entry.
- 3 While vertical integration may lead to efficiencies in the eConveyancing process, which will ultimately benefit consumers, vertical integration also has the capacity to stifle competition in upstream and downstream markets.
- 4 The direct connection or an information hub models provide the greatest prospects for competition, differentiation and innovation between ELNOs.
- 5 The incremental capital cost of a direct connection between the two current ELNOs is relatively low.
- 6 An access framework could be based on the cash equities market where existing ELNOs or service providers are compelled to facilitate access to services on a transparent and non-discriminatory basis, and the ACCC is given the power to arbitrate disputes where access negotiations between an incumbent and new entrant fail.
- 7 The MORs address the appropriate treatment of pass through costs, such as ELNO insurance premiums, fees imposed by external agencies and changes in the law.
- 8 Maintaining the current pricing framework for eConveyancing will ensure consumers pay no more for eConveyancing than they did for paper conveyancing.
- 9 Other jurisdictions could adopt a similar framework for recommending ELNO prices.
- 10 NSW LRS has made savings from eConveyancing and so can absorb the cost of modifying its technology platform to permit connection by multiple ELNOs.
- 11 Including Revenue NSW in the governance framework would reduce total costs to the industry, and deliver greater efficiencies.



### Our draft recommendations are:

- 1 The eConveyancing market be monitored at least every 2 years, ideally by a national regulator such as the ACCC (or on a state-by-state basis by regulators including IPART), to assess the effectiveness of competition and inform governance and pricing policy decisions.
- 2 NSW ORG work with ARNECC to model the competition framework for eConveyancing on the framework developed by the Council of Financial Regulators and the ACCC in their review of competition in cash equities clearing and settlement in Australia.
- 3 Due to the continuing development of the eConveyancing market, the national eConveyancing regulator review the adequacy of the MORs to address the impacts of vertical integration.



### Draft recommendations (continued):

- 4 A direct connection between the two current ELNOs be implemented as soon as possible to promote competition. Preferably, interoperability between the two current ELNOs would be implemented on a national basis by ARNECC through the MORs, but otherwise, should be implemented in NSW potentially through ELNO licence conditions.
- 5 New entrant ELNOs to negotiate commercial agreements to access existing infrastructure, or build their own infrastructure and establish direct connections with other ELNOs. Any disputes over price and or non-price terms and conditions would be subject to arbitration provided by a party mutually agreed by the participants or by a regulator.
- 6 NSW ORG work with ARNECC to set a schedule of costs that can be used by ELNOs to calculate a cost-reflective transfer price for interoperable transactions to ensure that costs are shared fairly across ELNOs.
- 7 Maximum prices for all ELNOs be set at PEXA's current (real) prices from 1 July 2020 and CPI indexed annually (as defined by the MORs) for two years, before being reviewed again, ideally by a national regulator such as the ACCC (or on a state-by-state basis by regulators including IPART).
- 8 If an ELNO unbundles its prices for the financial settlement and lodgment components of a service, then the sum of the separate prices for financial settlement and lodgment components must not exceed the regulated maximum for the bundled price.
- 9 ELNOs be permitted to set prices for any new eConveyancing service to reflect costs (based on the building block methodology). ELNOs must notify prices for new eConveyancing services to the regulator at least two weeks before they are effective. Prices must also be published on the ELNO's website.
- 10 Maximum prices for each category of residual dealing made available for eConveyancing be set as shown in Table 5.3. ELNOs and NSW LRS work together to determine the appropriate category for each residual dealing.
- 11 ELNOs be able to pass through as an additional charge the efficient costs of implementing interoperability (but these costs should be reviewed in two years by the eConveyancing regulator, or sooner if an interoperability model is implemented).
- 12 ELNOs not be required to offer nationally consistent pricing, but they may choose to do so on a commercial basis.
- 13 Revenue NSW charge ELNOs the following maximum prices (indexed by CPI annually):
  - \$15.20 (in real \$2018-19) per support inquiry received, to recover costs relating to ELNO subscriber support
  - For any tests that exceed base level frequency (ie two major and two minor tests per year per ELNO to be provided at no charge), \$125,000 per test (in real \$2018-19), per ELNO
  - Prices for bespoke service changes to be determined by contractual negotiations between ELNOs and Revenue NSW.





## Structure of this report

The remainder of this report discusses our analysis, draft findings and draft recommendations in detail. It is structured as follows:

- ▼ **Chapter 2** discusses the context for our review, including the approach we used to reach our draft recommendations
- ▼ **Chapter 3** discusses our draft findings and recommendations on the state of the eConveyancing market
- ▼ **Chapter 4** discusses our draft findings and recommendations on interoperability
- ▼ **Chapter 5** discusses our draft findings and recommendations on ELNO costs and prices
- ▼ **Chapters 6 and 7** set out our draft findings and recommendations on Land Registry Services and Revenue NSW's costs and prices
- ▼ **Appendices A-F set out:**
  - Our terms of reference
  - A list of submissions received on our Issues Paper
  - Additional information about the weighted average cost of capital (WACC) calculation used in the price modelling for ELNOs
  - Steps in eConveyancing process compared to paper conveyancing process
  - Diagrams of the contestability of activities and infrastructure under different interoperability models
  - The legal and regulatory framework for eConveyancing.