**PROPERTY EXCHANGE AUSTRALIA LTD**

# RESPONSE TO IPART DRAFT REPORT

## Review of the Pricing Framework for Electronic Conveyancing Services in NSW

**Terms used in this response**

| | |
|---|---|
| ABA | Australian Banking Association |
| API | Application Programming Interface |
| ACCC | Australian Competition and Consumer Commission |
| APRA | Australian Prudential Regulatory Authority |
| ARNECC | Australian Registrars' National Electronic Conveyancing Council |
| ASIC | Australian Securities and Investment Commission |
| ASX | Australian Securities Exchange |
| ATO | Australian Taxation Office |
| CFR | Council of Financial Regulators |
| COAG | Council of Australian Governments |
| DMC | Dench McClean Carlson |
| ECNL | Electronic Conveyancing National Law |
| eConveyancing | Electronic settlement and lodgement |
| ELN | Electronic Lodgement Network |
| ELNO | Electronic Lodgement Network Operator |
| Financial institution | Whether as transaction participant or settlement facilitator |
| IGA | InterGovernmental Agreement for an Electronic Conveyancing National Law |
| IPART | Independent Pricing and Regulatory Tribunal of New South Wales |
| Land Titles Register | Land title registry in each State and territory that creates and maintains land title records |
| MORs | Model Operating Requirements (and proposed here as National Operating Requirements: NOR) |
| MPR | Model Participation Rules (and proposed here as National Participation Rules (NPR) |
| NECDS | National Electronic Conveyancing Data Standard |
| NSW ORG | New South Wales Office of the Registrar General |
| NSW LRS | New South Wales Land Registry |
| Participation Agreement | Overarching agreement between PEXA and each Subscriber |
| PEXA | Property Exchange Australia Ltd (formerly National E-Conveyancing Development Limited) |
| Practitioner | Conveyancer or Lawyer |
| RBA | Reserve Bank of Australia |
| Representative Subscriber | A legal practice or conveyancing practice that has entered a Participation Agreement with PEXA |
| Responsible Subscriber | Defined in the MPR and typically the incoming mortgagee. This Subscriber is ultimately responsible for the lodgement case, lodgement instructions, fees and any requisitions |
| Registrars of Title | Registrars in each State and territory of Australia responsible for ensuring the integrity of land title systems |
| Sponsor | Infotrack, GlobalX, Veda, SAI |
| Subscriber | A party that has entered a Participation Agreement and met the eligibility criteria prescribed in the MPR. In PEXA, Subscribers are either Representative Subscribers, financial institutions or other principals |
| Unsigning | Where a document or settlement schedule has been digitally-signed, but due to a change in data, is treated as not having been digitally-signed |
| VOI | Verification of Identity |

## 1. EXECUTIVE SUMMARY

1.1 This paper sets out PEXA's response to the draft findings and recommendations in the draft report (**IPART Draft Report**) published on 20 August 2019 by the NSW Independent Pricing and Regulatory Tribunal (**IPART**) in respect of its "*Review of the pricing framework for electronic conveyancing services in NSW*" (**Pricing Review**).

1.2 Importantly, PEXA notes IPART's finding that PEXA's prices are reasonable when compared to all modelled estimates of a benchmark efficient ELNO. This was a core task within the terms of reference issued to IPART by the NSW Premier (**Terms of Reference**) and firmly within IPART's expertise. In making this finding, IPART appropriately acknowledged that:

(a) the first mover was likely to incur substantial costs from R&D;

(b) PEXA created the eConveyancing market, educated stakeholders and developed processes and standards; and

(c) PEXA's prices were reasonable in comparison to all scenarios modelled by IPART.

1.3 However, while PEXA supports some of IPART's other findings and draft recommendations in principle, many of them require further analysis as to the associated costs and benefits before an appropriate market structure is finalised.

1.4 Prior to commenting on the specific draft findings and recommendations of the IPART Draft Report, PEXA wishes to make an overarching submission in relation to this Pricing Review. In PEXA's view, it is crucial that any recommendations IPART may be considering are grounded in a factually sound understanding of the history, economics and technical details of eConveyancing so that a safe and effective regulatory framework that promotes efficiency, national consistency and security, with minimum conditions for safe and effective competition, may be developed. Moreover, it is incumbent on all involved in this discourse to keep Australian homeowners front of mind, to ensure that any eConveyancing regulatory solution provides the most safe, secure and cost-effective way to give effect to the purchase and sale of homes. PEXA's ELN is essential national infrastructure that underpins a large portion of Australia's economy. Given the critical nature of this infrastructure caution and care must be taken when considering any proposed regulatory intervention that has not been fully considered or assessed, particularly with regard to the potential cost and risk implications for Australian banks, financial regulators (such as APRA and ASIC), State land registries and revenue offices. Accordingly, there is no room for error or teething problems when dealing with the most important asset that most Australians will own in their lifetimes – the family home.

1.5 PEXA believes there is a real and substantial risk that IPART's findings and recommendations would introduce inconsistency between States that could result in detriment to consumers. ELNOs and most financial institutions are national bodies that operate on a national level, with nationally consistent pricing. There are many efficiencies to be gained from regulations and business processes being nationally consistent. PEXA is supportive of the need to focus efforts on developing safe and effective competition in eConveyancing through national consultation. However, in PEXA's view, there is a real and substantial risk that IPART's findings and recommendations could result in detriment to consumers because they lack sound understanding of the technical, legal and financial underpinnings of eConveyancing and suggest State based solutions are workable when they will result in inefficient regulatory fragmentation. For example, the suggestion in Draft Recommendation 4 that the NSW ORG could implement interoperability through ELNO licence conditions would be infeasible and high risk, particularly given the complexities involved in financial settlement and the fact that the NSW ORG does not have the expertise to advise on financial settlement components of eConveyancing. PEXA

strongly supports a process that will deliver insights and data to enable fact based decisions. Accordingly, what is required is careful consideration of any proposed regulation pursuant to a national level consultation that cannot be rushed. Without an appropriate in-depth understanding of the key issues, regulators run a risk of compromising critical digital infrastructure that supports the $6-$7 trillion Australian property market.

1.6 PEXA is concerned that a number of assertions made in the IPART Draft Report, particularly in relation to market structure and interoperability, are based on assumptions that were not supported by consultation or appropriate prior fact finding. In part, PEXA considers this can be attributed to the limited scope of IPART's Terms of Reference, and the fact that the IPART Issues Paper[1] asked only for feedback on issues relating to price, not on feedback on whether interoperability was feasible or which model would be viable. Consequently, in PEXA's view, IPART did not consult extensively on the technical details, or other obstacles and complexities, that will be involved in designing and implementing any of the forms of interoperability proposed. As a result, certain findings and recommendations in the IPART Draft Report are based on inaccurate assumptions that undermine their veracity by failing to understand the true costs and risks involved in interoperability, as well as the technical intricacies and nuances of eConveyancing. In these circumstances the risk of regulatory error is substantial and this is likely to harm Australian consumers.

1.7 For instance, IPART's proposed hybrid model of interoperability, which involves both bilateral connections and an access regime, substantially understates the complexity, cost and risk of establishing such a system. There appear to be no examples of this type of interoperability being introduced in any similar system anywhere in the world. Some key instances of the understated costs and challenges associated with interoperability in the IPART Draft Report are as follows:

(a) IPART has not considered how the liability, risk and insurance issues relating to interoperability would be resolved with all the stakeholders in the Australian property industry. It took PEXA several years to negotiate these frameworks, and culminated in PEXA entering into Participation Agreements with representatives of lawyers and conveyancers (and their insurance companies) in every State in Australia, as well as over 50 Participation Agreements with banks. The legal, liability and insurance framework associated with an interoperable system would be substantially more complicated, and as noted both by DMC in the IGA Draft Final Report[2] and Dr Rob Nicholls in the NSW Interoperability Report[3], it is not clear how this could be resolved. In particular, in order to introduce bilateral interoperability, it will be necessary to determine a legal and liability framework that is satisfactory to all of these parties, and to renegotiate all of these agreements. This will be very challenging, as has been noted by DMC, who PEXA understands is the only party to have interviewed these other stakeholders to ascertain their views on the topic.

(b) The real and substantial risk of technical error associated with data synchronisation technology, which would be required under any bilateral connections model of interoperability, has not been considered in the IPART Draft Report, nor have the potential ramifications of such an error for everyday Australians involved in buying or selling property in real time.

(c) IPART has not acknowledged the significant expenditure that would be incurred by financial institutions, land registries and State revenue offices in order to support interoperability, both in terms of implementation and ongoing maintenance.

[1] *Review of the pricing framework for electronic conveyancing services in NSW: Issues Paper*, IPART (12 March 2019).
[2] *Review of the Intergovernmental Agreement for an Electronic Conveyancing National Law: Draft Final Report*, DMC (26 July 2019).
[3] *Interoperability between ELNOs: Final Report*, Independent Chair of the Interoperability Working Groups (25 July 2019).

(d) For PEXA, the costs of interoperability are not limited to the development of APIs, but would necessarily include costs to redesign and rebuild PEXA's platform to allow synchronisation with another platform.

1.8 It is unsurprising given the complex issues that this form of interoperability raises there are no examples of it being introduced in any comparable system anywhere in the world.

1.9 In PEXA's view, it is crucial that IPART considers the full range of costs included in interoperability. Several key stakeholders have identified, on a number of occasions, the costs associated with establishing integration infrastructure in the event that interoperability is introduced, for example:

(a) Financial institutions have indicated in numerous forums and submissions, including in the IGA Draft Final Report, that it will cost between $6-$10 million to establish further payment integration infrastructure with each infrastructure ELNO. There would also be ongoing maintenance costs of around $234,000 per year.[4] These costs will ultimately be passed through to Australian consumers, eroding the cost savings achieved through the efficiencies eConveyancing has created to date in a traditionally paper-based industry.

(b) State Governments estimate they will incur between $500,000 and $2 million to establish new integration connections with each additional ELN (plus the ongoing maintenance costs). We note that as each State has a land registry office and a revenue office, it will need to establish two connections for each additional ELNO that enters the market. These costs will ultimately be borne by Australian consumers.

(c) The ATO will incur upfront and then ongoing maintenance costs to integrate with each infrastructure ELNO. Again, these costs will ultimately be borne by Australian consumers.

(d) PEXA advises that there will be significant costs, estimated at between $25-$30 million (not including costs of renegotiating the legal and contractual framework) to redesign its entire system to accommodate any form of direct connection interoperability, if this is even feasible.

1.10 We believe that the estimated cost across the industry to introduce the bilateral method of interoperability between PEXA and another ELNO is between $96-$160 million. There would be further costs to introduce additional ELNOs into the bilateral interoperability model. If that additional ELNO is not ultimately viable, this investment by the industry would be wasted. We note that the viability of the additional ELNOs in the market is far from assured as:

(a) None of them have generated any revenue;

(b) None of them have processed any financial settlement transactions;

(c) The experience and cost base of PEXA suggests that it will be very difficult for two ELNOs to reach viable scale in this market; and

(d) While PEXA required approximately $400 million of investment to reach viability, the highest level of investment that any other ELNO has attracted appears to be significantly less.

1.11 Table 1 below indicates the substantial estimated build costs that each relevant stakeholder will incur in establishing infrastructure connections and reconfiguring existing infrastructure and systems.

[4] IGA Draft Final Report, p 70, para 5.49.

*Table 1:Estimated build cost for each relevant stakeholder to establish connections and reconfigure existing infrastructure and systems*

| Participant | Quantity | Estimated Build Cost Range Per Participant Per Connection | Total Estimated Build Cost Range |
|---|---|---|---|
| Integrated Settlement Banks | 11 | $6M - $10M | $66M - $110M |
| Land Registries | 5 | $500K - $2M | $2.5M - $10M* |
| Revenue Offices | 5 | $500K - $2M | $2.5M - $10M* |
| PEXA | 1 | $25M - $30M | $25M - $30M** |
| Total | | | $96M - $160M |

Note: Dependent on the model of interoperability, Integrated Settlement Banks, Land Registries and Revenue Offices may incur these costs each time a new ELNO is on-boarded.
* As any further jurisdictions are activated for eConveyancing, Land Registries and Revenue Offices in those jurisdictions will face these costs for each ELNO seeking to integrate with their systems.
** This is an initial, high level estimate by PEXA. Full analysis of the intricacies of any eventual model of interoperability would have to be conducted to determine the final cost.

1.12 These investments, plus the risk to consumers of increased errors occurring in transactions due to increased complexity (discussed further below), must be balanced against the relatively small size of the notional benefit that can be obtained through interoperability. In PEXA's view, IPART has failed to appreciate the complexities, costs and risk involved in designing and implementing its recommended interoperability models.

1.13 In establishing and advancing eConveyancing, everyday Australian consumers and the economy have benefited significantly through the efficiencies PEXA has delivered as a result of significant investment in digitally transforming a traditionally paper heavy industry. IPART appropriately acknowledges that consumers now save approximately $66 per transaction through utilising eConveyancing services in comparison to the prices they would pay under traditional paper settlement agent services. These consumer benefits have been achieved in a relatively short timeframe and largely independent of regulatory intervention.

1.14 However, IPART has failed to weigh the risks and costs associated with any such interoperability model against the significant benefits and cost savings as a result of broader efficiency gains Australian consumers are already experiencing because of eConveyancing. Importantly, PEXA notes that while upwards of an estimated $250 billion of property is transferred each year in Australia,[5] the total addressable market for ELNOs is only in the range of $200-$240 million (less than 0.1% of the volume transacted).[6] Accordingly, the costs, risks and benefits of any proposed regulatory framework need to be identified (and where applicable addressed) in order to avoid any regulatory error that may erode or remove benefits Australian consumers have been delivered to date, and ensure that the best answer for Australian consumers is reached. However, this is only achievable through an appropriate national consultation process that incorporates expertise from a range of appropriately placed regulators, bodies and stakeholders.

1.15 Given the systemic importance of the sector, any introduction of interoperability must be carefully structured to not introduce further risks of fraud and cyber security into the system. PEXA has a proven track record in strengthening the security settings of the entire conveyancing market. There are constant attacks on all parts of the eConveyancing ecosystem, with a particular focus on the links with the lowest levels of cyber security defence.

[5] *Property market chart pack – September 2019*, Core Logic.
[6] IGA Draft Final Report, p 74, para 5.72.

1.16 Each failure or fraud in property settlement typically results in substantial hardship for individuals and families. PEXA spends more than $10 million annually on cyber defence, and is constantly introducing new initiatives to improve its security and where possible that of Subscribers. The broader Australian financial industry spends hundreds of millions of dollars each year on cyber security.[7] Any introduction of interoperability (particularly the bilateral approach proposed) will inevitably introduce new points of complexity and vulnerability into the system which will become targets for attack.

1.17 Separately, PEXA similarly queries the factual basis for many of the findings and recommendations in Dr Rob Nicholls NSW Interoperability Report, which has suggested solutions that introduce unacceptable levels of risk to everyday Australian consumers. This is because the proposals rely on data synchronisation between ELNOs in order for each respective ELNO system to communicate and transfer common data sets across infrastructure. Notwithstanding this however, the NSW Interoperability Report does correctly identify there are a number of complex issues that must be resolved before any interoperability model could be agreed, including:

(a) how a liability regime would work under an interoperable eConveyancing system;

(b) whether the structure would be insurable (if it is in fact technically or commercially workable);

(c) feedback from industry that suggested the costs and inconvenience of learning and using two different ELNO systems was a real issue; and

(d) that stakeholders would only support interoperability provided it didn't increase cost, risk, complexity or liability.

1.18 What is clear is that many of the issues identified have yet to be consulted on, or reviewed, let alone resolved. For example, the NSW Interoperability Report's own insurance report indicates there is an outstanding question as to whether such interoperability arrangements could even be insurable.

1.19 Moreover, what is most obviously missing from the findings and recommendations arising out of the various reviews conducted so far is a sound understanding of the technical underpinnings, and financial and legal implications of any interoperability or regulatory solution for eConveyancing.

1.20 PEXA believes careful consideration of any proposed regulation of competition in the eConveyancing services market is necessary and strongly believes that the development of such regulation cannot be achieved in a piecemeal way that cuts corners on the facts and consultation. Accordingly, PEXA strongly supports a process that will deliver detailed insights and data to enable fact based decisions. PEXA also believes that industry and government must continue working together to develop a nationally consistent approach that will minimise the jurisdictional variations that drive complexity, cost and inefficiency.

1.21 While the ACCC is well placed to comment and advise in relation to the competition issues involved in eConveyancing, the ACCC itself has previously said that it "*does not have the relevant expertise to comment on the specific technical details of the interoperability mechanisms for the ELNO market*."[8] It is this technical detail that needs to be resolved and understood in order to determine whether the interoperability solutions put forward in NSW are fit for purpose and meet industry requirements regarding risk, cost, liability and complexity. Accordingly, PEXA believes that further cross disciplinary analysis is needed at the national level involving a number of appropriate regulators and bodies, including the ACCC, CFR and ARNECC.

[7] James Eyers, *Banks must share cyber threat intel: Byres*, AFR (16 May 2019), https://www.afr.com/companies/financial-services/banks-must-share-cyber-threat-intel-byres-20190516-p51o1z

[8] *Response to Issues paper – review of the InterGovernmental Agreement for an Electronic Conveyancing National Law,* ACCC (26 March 2019), p 3.

1.22 It is PEXA's history in delivering electronic lodgement and settlement services to the industry that underpins its responses to the draft findings and recommendations of the IPART Draft Report. PEXA looks forward to the opportunity for further consultation and continued engagement with all interested parties on all these matters.

## 2. FLAWS IN THE IPART PROCESS

2.1 Interoperability, including the challenges it presents, was not canvassed in detail in IPART's consultation. Accordingly, IPART did not consult extensively on the technical details, complexities or risks involved in designing and implementing any of the proposed interoperability models. Consequently, certain findings in the IPART Draft Report are based on inaccurate facts and assumptions that undermine the workability of the recommendations made, and increase the risk of regulatory error, to the detriment of Australian consumers.

2.2 PEXA is concerned with a number of assertions made in the NSW-commissioned reports produced by: (1) Dr Rob Nicholls – the NSW Interoperability Report; and (2) IPART – the IPART Draft Report, which inaccurately describe certain aspects of eConveyancing, particularly in relation to financial settlement arrangements. Further reviews must be conducted with an appropriate factual foundation. In particular:

(a) **IPART has misunderstood the process of payment integration.** Payment integration for transaction banking is a critical component of financial settlement (and is distinct from infrastructure integration via RBA-RITS). PEXA believes that IPART has misunderstood this process, and has based its assumptions on factual inaccuracies, fundamentally undermining the credibility and viability of some of IPART's recommended interoperability solutions. A key example is IPART's suggestion that 72% of property reservation batches involved only major banks, which means that it would be possible to execute settlement using only the RBA-RITS integration.[9] IPART's assertion does not take into account the situation where a major bank has a paying position in settlement, as a result of funds having first been advanced from a trust account at that bank. In order to facilitate a transaction that requires money to be contributed from a practitioner trust account, integration is necessary between the paying bank and an ELNO to allow funds to be drawn from that practitioner trust account and be contributed to the settlement. In PEXA's experience, 50% of transactions require funds to be contributed from a practitioner's trust account. In order for an interconnected ELNO to execute trust instructions provided by a PEXA practitioner, it will be necessary for that ELNO to maintain the same connections that PEXA has with payment-integrated retail banks. Where ELNOs do not have the same payment integration capability, such settlement would not be possible using RBA-RITS settlement alone.

(b) **IPART has incorrectly asserted that there are currently two ELNOs already integrated and enabled for financial settlements.**[10] PEXA understands it is currently the only eConveyancing platform with full capability that has completed lodgement and settlement transactions and has developed its own proprietary settlement model. Although Sympli, via the ASX, may be enabled for RBA-RITS integration, this alone would not be sufficient to execute PEXA-collected settlement instructions, as Sympli has not integrated with retail banks for trust account support. Notably, settlements solely using RBA-RITS integration account for less than 40% of the total number of settlements. Accordingly, fully functional settlement enablement for other ELNOs will not exist until the issue of payment integration between ELNOs, the RBA and all 11 financial institutions is resolved. This necessarily raises the question of whether duplication of payment integration connections is most efficient for industry.

[9] IPART Draft Report, p 33, para 4.4.2.
[10] IPART Draft Report, p 30, para 4.3.3; p 31, para 4.3.4.

(c) **It is unclear what information IPART considered when assessing the costs of the interoperability solutions recommended.** The costs involved in developing and maintaining interoperability are not limited to establishing the connections between platforms, but also extend to developing the software and logic to accept, process and collaborate data. These are all entirely new costs that have not been contemplated by IPART. For example, there will be significant costs associated with the significant redesign that PEXA will be required to undertake and whose platform was developed with no contemplation of interoperability. Further, PEXA notes that IPART has not accounted for the costs of the banks that will be required to integrate a second ELNO platform to enable bilateral interoperability.

2.3 Another issue that is not recognised in the IPART analysis is that bilateral connections between ELNOs will require replication of PEXA's connections, including to retail banks. It is those bespoke connections (i.e. payment integrations) which have been cited by the ABA as being prohibitively expensive for financial institutions. For example, the ABA has previously indicated that it cost one major bank more than $10 million to build their current connection with PEXA, and flagged that it would potentially incur similar costs in order to establish equivalent connection with each new ELNO as it enters the market.[11] PEXA notes that this estimated cost relates to a bank as a payment facilitator, not a Subscriber. PEXA also notes it is possible for a bank to act as either a payment facilitator or a Subscriber. The costs of payment integration must not be equated to the cost of using a second ELN. In these circumstances, the costs incurred by financial institutions under any mandated interoperability solution would almost certainly be passed through to Australian consumers eroding the cost savings that have been achieved for consumers so far.

2.4 PEXA also strongly disagrees that the additional costs of interoperability are small for PEXA, industry or consumers. PEXA has been clear that the costs of interoperability are not limited to the costs of developing APIs, but will include the costs of rebuilding the PEXA platform in order to enable synchronisation with another platform. Equally, IPART has not acknowledged the significant costs to integrated service providers to support an interoperable model. In PEXA's view, IPART (and AECOM) do not possess the relevant information or understanding of PEXA's existing software and application to be able to make this assessment.

2.5 The more detailed review into interoperability conducted in NSW recently by Dr Rob Nicholls, that led to the publication of the NSW Interoperability Report, revealed that there are many questions and issues still to be resolved in the consideration of interoperability. For completeness, PEXA notes it does not agree with many of the findings of the NSW Interoperability Report. However, PEXA does agree that there are many issues yet to be worked through, particularly in respect of interoperability.

2.6 Additionally, the proposal that (1) bilateral connections be developed between competing infrastructures, and (2) new entrants be given the opportunity to access PEXA's existing infrastructure means that PEXA would need to manage the complexity of two interoperability approaches – bilateral connections and an access regime, which will significantly increase complexity, risks and costs.

2.7 Moreover, PEXA cautions against IPART's assumption that interoperability will lead to innovation. PEXA submits that if interoperability were mandated and ELNOs were required to establish all the necessary integrations to facilitate interoperability links, it is questionable whether innovation would necessarily manifest as an outcome. This is because lodgement and settlement execution under such a model would require uniformity and the mirroring of data across ELNO workspaces in order to communicate data. This requirement would stymie innovation, as each ELNO at the infrastructure level would be required to mirror the capability of the other. For example, were an ELNO to accept payment by credit card, unless the counterparty ELNO to a transaction were also able to do so, it would not be possible (despite it being possible if the entire transaction were conducted on a single ELNO).

[11] *Review of the Intergovernmental Agreement for an Electronic Conveyancing National Law – Issues Paper*, Submission from ABA (10 April 2019), p 3.

2.8 It is these types of issues that must be subject to appropriate industry consultation at the national level to enable fact-based decision making. Accordingly, PEXA strongly believes that a rigorous cost-benefit analysis of interoperability is required.

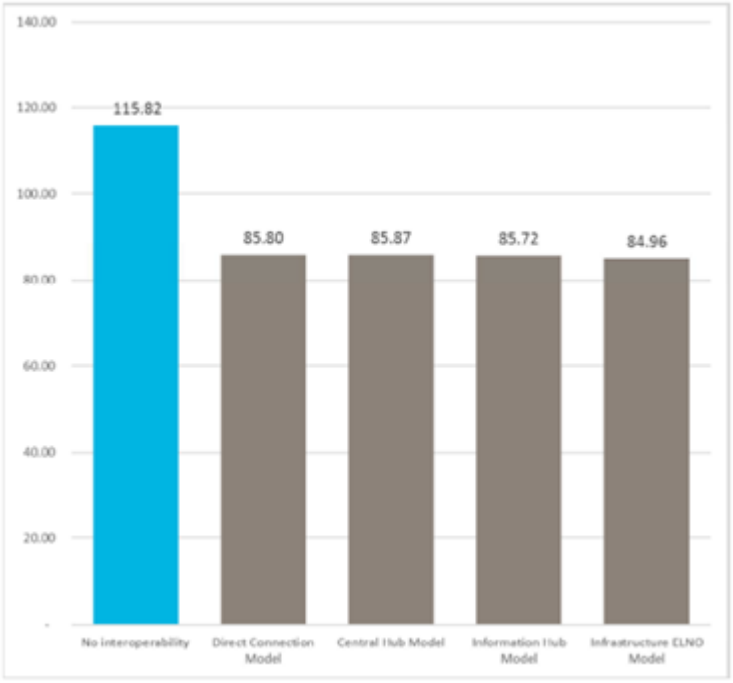
***Network Effects and Interoperability***

2.9 IPART and a number of stakeholders are concerned about the potential for high costs related to network effects to influence the development of competition in the market.[12] These network costs include the costs to users of having to learn more than one ELNO's system, the costs to practitioners of obtaining separate digital signing certificates for each ELN and the costs to financial institutions of building network connections with each ELNO. IPART proposes interoperability as a means to address these network effects.[13]

2.10 However, IPART has not established that costs related to network effects are sufficiently high to constitute a material barrier to entry, or that costs will remain high in the absence of interoperability. Indeed, IPART has not attempted to quantify the costs associated with network effects for users and practitioners and it is unclear whether these costs would be higher than the potential benefits associated with subscribing to a new ELNO. IPART's consultants' analysis of the costs associated with alternative interoperability options concludes there is no material difference between any of the options that enable interoperability, as can be seen from Figure 1 below.

[12] IPART Draft Report, p 10, para 3.4.
[13] IPART Draft Report, p 21, para 4.

*Figure 1: Industry 5 year levelised transaction cost for each interoperability model*




*Source: AECOM's draft report, Figure 16.*[14]

2.11 In PEXA's view, IPART has not appropriately considered the potential costs and benefits before recommending a particular interoperability framework is suitable. Mandating a particular model of interoperability may impose costs or risks on market participants, including scope for regulatory error that would negate potential benefit. Given the success and innovations that have already been achieved in eConveyancing to date with limited regulatory intervention, and the fact competitors are emerging and have demonstrated they will compete on price and innovation, there is a real case that the competition that has already emerged amongst ELNOs will further promote competition on price, service offerings and innovation.

2.12 IPART recommends a hybrid interoperability regime,[15] where:

(a) Direct connections are mandated between the two existing ELNOs; and

(b) New ELNOs are given the opportunity to either establish direct connections with existing ELNOs or seek access to the infrastructure of the existing ELNOs.

2.13 IPART introduces two pricing concepts to support the interoperability regime,[16] although the presentation of these two pricing concepts in the IPART Draft Report is conflated:

(a) If direct connections are established, IPART recommends that ELNOs calculate a cost-reflective transfer price for interoperable transactions to share costs fairly between ELNOs, using a schedule of costs set by NSW ORG and ARNECC.

(b) If access is sought to the infrastructure, IPART recommends that new entrant ELNOs negotiate commercial agreements to access such infrastructure, including an access price. IPART does not suggest that access prices should be regulated, but rather that any disputes should be arbitrated. For example, Sympli has sought access to the financial settlement infrastructure to

[14] *Estimating costs of electronic conveyancing services in NSW: Draft Report,* AECOM (19 August 2019), figure 16, p 41.
[15] IPART Draft Report, p 31-32, para 4.3.4.
[16] IPART Draft Report, p 32, para 4.4.1.

an ASX subsidiary. IPART goes on to suggest an access framework could be modelled on the cash equities settlement market, as we discuss in the next section.

2.14 IPART does not set out its proposed transfer pricing methodology, but uses information estimated by AECOM to illustrate how a transfer price for direct connections can be estimated. IPART's illustrative estimate is approximately $13 per transaction, paid by the non-lodging ELNO (**Non-lodging ELNO**) to the ELNO that is responsible for lodgement (**Lodging ELNO**).[17] The calculation includes an estimate of capital costs for title lodgement and financial settlement, however this is a very small amount compared to the full breadth of other fees, costs and expenses. In practice, the transfer price may be higher or lower than IPART's illustrative estimate, reflecting the activities undertaken by the Lodging ELNO and Non-lodging ELNO, the pricing methodology and the assumptions, including the treatment of capital costs and the number of transactions. IPART's illustrative transfer price is not an estimate of the price to access the existing ELNO's financial and settlement infrastructure.

2.15 However, there is likely to be a material difference between the transfer price associated with direct connection and the access price associated with access to infrastructure. PEXA expects the price to access the existing ELNO's infrastructure would likely be closer to the price for a benchmark efficient ELNO estimated by IPART. Indeed, given that IPART found that PEXA's prices were reasonable in comparison to all scenarios modelled by IPART (implying that PEXA's price are below cost reflective levels in some or all scenarios),[18] it may be that the efficient price for accessing an existing ELNO's infrastructure is, in fact, higher than the price for a benchmark efficient ELNO estimated by IPART.

***Regulatory Framework***

2.16 With respect to regulatory uncertainty, we agree with IPART that uncertainty is likely to increase the risk of the eConveyancing market and deter entry.[19] However, while there are costs associated with regulatory uncertainties, in PEXA's view, IPART has not appropriately considered the costs associated with regulatory errors. Regulatory error may result in inefficient prices, increased regulatory burden and deterred entry. These errors are more likely to arise if not enough time and consultation between regulators, industry, and relevant stakeholders is allowed to develop an appropriate regulatory framework whereby issues can be appropriately addressed. Accordingly, IPART has not provided sufficient evidence that the cost of a two-year moratorium outweighs its benefits.

2.17 In PEXA's view, if IPART proposes to retain findings on market structure in its final report, IPART must ask the appropriate questions of those stakeholders able to provide information to support those findings. PEXA understands that various key stakeholders have raised concerns in other recent reviews regarding the costs, risks, security and liability of the model of interoperability proposed to date.

2.18 In PEXA's view, the appropriate course would be for IPART to refrain from including those findings in its final report in order for an appropriate national review to proceed with industry wide consultation.

2.19 PEXA is concerned that the NSW Interoperability Report and IPART Draft Report have inaccurately understood or described certain aspects of eConveyancing financial settlement arrangements and strongly believes that any further reviews should be conducted with a robust factual foundation. PEXA believes it is critical that any further national review must be informed by the relevant facts. PEXA considers that further reviews should follow a similar fact-finding and consultative process as that followed by DMC in the Review of the InterGovernmental Agreement for an Electronic Conveyancing National Law.

2.20 By way of example, the review by the CFR into both clearing and settlement in the cash equities market in Australia was commenced in 2012 with an initial review, followed by a further review in 2015. As

[17] IPART Draft Report, p 35, para 4.4.5.
[18] IPART Draft Report, p 36, para 5.1.
[19] IPART Draft Report, p 10, para 3.4.

a result of the 2015 review, the CFR issued policy statements in 2016 and 2017. When citing the CFR review process as a comparable regulatory reform model, PEXA notes that DMC appropriately referred generally to the review of the Australian cash equities market and cited the '*Minimum Conditions for Safe and Effective Competition in Cash Equity* ***Clearing*** *in Australia*' (emphasis added). In contrast, IPART focussed more narrowly on only the outcome of the CFR's '*Minimum Conditions for Safe and Effective Competition in Cash Equity* ***Settlement*** *in Australia*'(emphasis added), suggesting that these solutions could simply be transplanted to the eConveyancing context, which ignores the substantial differences between the two industries.

2.21 While DMC recommends that a review of competition in eConveyancing be conducted by the CFR, building on their earlier work in respect of developing safe and effective competition in the Australian cash equities market, IPART simply recommends that a Registrar General could take CFR's findings from those reviews and apply them to eConveyancing. In PEXA's view, a further review, building on earlier work must be conducted before outcomes are determined. Further, PEXA notes that Registrars of Title are not the appropriate body to evaluate and set rules for financial settlement. Rather, given the complexities and technical detail involved in eConveyancing, particularly in relation to addressing issues such as liability, insurance, security and risk, what is required is a national consultation led by CFR, in collaboration with the ACCC and ARNECC, that incorporates cross disciplinary expertise from a range of relevant stakeholders and experts, to ensure a safe and effective regulatory solution is produced for eConveyancing that benefits consumers.

## 3. STATE OF THE ECONVEYANCING MARKET

**Draft Recommendation 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.

**Draft Finding 1**

The eConveyancing market in NSW is currently highly concentrated and is likely to remain concentrated in at least the short term.

3.1 PEXA strongly believes any monitoring or regulation of the eConveyancing market should be conducted by a national regulator, rather than on a state-by-state basis, in order to preserve national consistency, which is vital to ensuring industry efficiency.

3.2 PEXA is willing and able to be involved in any future national review process stemming from Draft Recommendation 1 and is prepared to offer its expertise derived from the experience it has obtained as the initial ELNO since commencing operations in 2013.

3.3 PEXA does not believe that State bodies alone are appropriate regulators for the national eConveyancing market. PEXA endorses the approach outlined in IPART's Terms of Reference, which states that "*The NSW government recognises that electronic conveyancing is a national reform and strongly supports a nationally consistent regulatory regime*".[20] Further, the IPART Draft Report acknowledges that:

> "*ELNOs and many financial institutions are national organisations, and thus, gain efficiencies from regulations and business processes being as consistent as possible across jurisdictions.*

[20] Gladys Berejiklian MP, *Review of Electronic Conveyancing Services in NSW – Final Terms of Reference*, NSW Government (29 January 2019), https://www.ipart.nsw.gov.au/files/sharedassets/website/shared-files/investigation-section-12-publications-pricing-regulation-of-electronic-conveyancing-network-operations-in-nsw/terms-of-reference-review-of-pricing-regulation-of-electronic-conveyancing-network-operators-in-nsw-january-2019.pdf.

*We support the conclusions reached by the IGA review draft report that national consistency of regulation is beneficial…"*[21]

In PEXA's view, allowing State bodies to lead regulatory processes and inform governance of the eConveyancing market is fundamentally incompatible with the commitment of governments under the IGA to the development of a nationally consistent regulatory regime. PEXA's view is that IPART's recommendations should seek to avoid pursuing outcomes in the eConveyancing market in advance of national regulation any more than is required to meet IPART's Terms of Reference. However, PEXA is concerned that this is not true for some of IPART's draft recommendations, particularly the draft recommendation that a direct connection between the two current ELNOs be implemented as soon as possible. PEXA's view is that this recommendation risks irreversibly changing the eConveyancing market, without appropriate consultation and an understanding of the facts, that will effectively tie the hands of all future national regulators.

3.4 Any assessment of the state of competition in eConveyancing moving forward must be carefully conducted by appropriate technical experts, as well as national regulators and bodies, including the:

(a) ACCC – which has expertise in relation to competition issues;

(b) CFR – which could offer advice in relation to the financial settlement aspects of eConveyancing leveraging, where relevant, on its review work on the Australian cash equities market (which is outlined in further detail below at paragraphs 3.18 to 3.28);

(c) ARNECC – which has responsibility for ensuring an appropriate governance framework is established; and

(d) State based Registrar Generals – which have expertise in relation to land title information and maintaining the Torrens title register.

3.5 The ACCC would be well placed to oversee the regulatory process and advise on competition issues. Moreover, it has already indicated its intention to be involved, while consulting closely with ASIC, the RBA and other interested stakeholders.

3.6 In addition to the ACCC's role, the CFR could offer assistance in conducting an assessment of the effectiveness of competition and inform governance decisions. Importantly, the CFR is a respected, overarching body of national financial regulators that is able to bring a national focus to this next stage of development of the national eConveyancing system, and has prior experience conducting investigations and industry reviews in relation to the Australian cash equities market.

3.7 In PEXA's view, ARNECC and the Land Titles Registries would necessarily be involved in this process to ensure there is expert subject matter input on land titling legislation and registry practices and requirements. ARNECC's participation in the proposed process is crucial, as ARNECC can facilitate the identification of any differences between property conveyancing and securities trading.

3.8 In any case, given the high level of complexity involved in eConveyancing, particularly in understanding the technical details of Australia's world first eConveyancing technology, input from a range of regulators and stakeholders will be required. Accordingly, PEXA considers it critical that the proposed consultation process also includes input from a range of technical experts that will each be able to contribute to reaching a safe and effective solution.

[21] IPART Draft Report, p 15, para 3.7.

3.9 PEXA is willing and able to be involved in any future national review process stemming from Recommendation 1 and is prepared to offer its expertise derived from the experience it has obtained as the initial ELNO since commencing operations in 2013.

**Draft Recommendation 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.

**Draft Finding 2**

Interoperability would improve competition in the eConveyancing market and would reduce barriers to entry.

**Draft Finding 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.

3.10 PEXA believes that the cash equities market is fundamentally different to the Australian eConveyancing market. There are numerous reasons for this which we set out below. In particular, we note that every equities settlement transaction is between two highly credit worthy and sophisticated parties, and is supported by collateral. Thus, the failure of a settlement in the cash equities market is highly unlikely to lead to financial loss for any party. In contrast, in the Australian eConveyancing system, there are usually four parties (rather than two), there is no collateral or other financial protection, and most of the parties are Australian consumers who are carrying out the largest transaction of their lives. Any settlement failure is likely to lead to severe financial hardship for individuals or families. Accordingly, careful in-depth consideration is required with regard to any proposed regulatory framework that may increase risk to everyday Australian consumers, and the integrity and reputation of eConveyancing as safe and secure, particularly given it is now a critical and complicated piece of digital infrastructure that supports a fundamental pillar of the Australian economy – the property market.

3.11 Further, notwithstanding PEXA's view that cash equities settlement is substantially simpler and less risky than eConveyancing, and extensive work has been carried out by numerous regulators over many years, there has been no interoperability introduced in Australian cash equities settlement. This is in part because these reviews have found that a single provider of services in the cash equities settlement market is not only efficient and cost-effective, but importantly, the safest model for market functionality and financial stability, notwithstanding the provider of those services in the case of the Australian cash equities settlement market is a private operator – the ASX.

3.12 PEXA supports the development of a nationally consistent, safe and effective regulatory framework for eConveyancing and appreciates the comparison of eConveyancing to the cash equities clearing and settlement market in Australia. Given the CFR's and ACCC's extensive work in reviewing competition issues for the Australian cash equities markets, PEXA supports the development by the CFR, in collaboration with the ACCC, of minimum conditions for safe and effective competition in the national eConveyancing market. The CFR and ACCC have ample experience overseeing such national consultation processes and are uniquely placed to leverage (where relevant) off the framework

developed in their review of competition in cash equities clearing and settlement in Australia, including the development of minimum conditions for safe and effective competition in eConveyancing.

3.13 However, PEXA has two primary concerns with IPART's Recommendation 2:

(a) As noted above, PEXA opposes the involvement of State bodies in leading the development of a national regulatory regime and strongly believes that the establishment of any regulatory framework must be conducted by an appropriate national regulator that incorporates stakeholder feedback pursuant to a a rigorous national consultation process that will enable fact based decision making.

(b) The development and implementation of any regulatory framework, including minimum conditions, must not be rushed, but rather be the subject of in-depth analysis by a range of relevant stakeholders, national bodies and regulators in order to fully understand the nuanced technical, regulatory, legal and economic details of eConveyancing and arrive at an appropriate regulatory model. PEXA reinforces IPART's acknowledgment that whilst there are overarching similarities between the cash equities and eConveyancing markets, there are also key differences, and it is these differences that must be accounted for in developing a safe and effective regulatory framework for eConveyancing.[22] Without adequate regard to these differences, the regulatory framework for eConveyancing will be wholly inadequate to address the needs of industry and consumers. When developing an appropriate framework priority must be given to:

(i) maintaining a safe and secure system for Australian consumers;

(ii) preserving the integrity of the Land Titles Register; and

(iii) addressing the concerns raised by industry to ensure an interoperable system does not increase costs, risks, liability and complexity.

3.14 While transactions in the Australian cash equities market are less complex than an eConveyancing transaction, useful guidance can be taken from the extent of the consultation and preparation that was undertaken by the CFR, ACCC, RBA and ASIC with regard to the development of an appropriate framework to facilitate safe and effective competition in settlement and clearing services in the cash equities market. During this process, regulatory requirements and mechanisms were subject to careful consideration and public consultation processes at each stage of development. This has ensured the development of a safe and effective regulatory framework for the benefit of consumers, and not created a regulatory environment that either put consumers at greater risk, or eroded the benefits that consumers in the Australian cash equities market have come to enjoy pursuant to the efficiencies that technology has provided.

3.15 Similarly, in respect of eConveyancing, PEXA agrees with IPART and believes it is critical that any proposed regulatory arrangements are subject to a full assessment of risks pursuant to a fact-finding national consultation process that provides detailed technical, economic, data and competition insights to enable fact-based decisions that are focused on ensuring any regulatory solution delivers safety, security, affordability, national consistency, industry efficiency, and demonstrates sensitivity to risk and liability, as well as the technical nuances of interoperability.

3.16 In PEXA's view, the IGA Draft Final Report correctly acknowledges that:

- *"the ECNL opened the way for competition but did not provide any regulatory guidance on the arrangements for competition. This is in contrast to the regulatory guidance provided for*

[22] IPART Draft Report, p 13, para 3.5.3.

*competition in clearing Australian cash equities in relation to the Australian share market."* [23]

- *"The three national financial regulators (RBA, ASIC and APRA) and the ACCC carefully considered all of the issues associated with competition and developed the Minimum Conditions for Safe and Effective Competition. The regulations for competition in the eConveyancing environment similarly need to be agreed by the national regulators before any models of competition including interoperability are determined."* [24]

3.17 PEXA has identified those minimum conditions for competition in cash equities that require further exploration in an eConveyancing context include:

(1) adopting appropriate safeguards in the settlement process in order to preserve efficiencies and afford equivalent priority to those accessing the settlement platform (ultimately consumed); and

(2) access to securities settlement 'infrastructure' on a non-discriminatory basis.

***Timeline of reviews by the CFR and ACCC on the Australian cash equities market***

3.18 To date, the CFR, in collaboration with the ACCC and other relevant regulators and agencies, has undertaken a number of investigations into the Australian cash equities market, which have been based on rigorous analysis considering all the costs, risks and issues and involving all interested and relevant stakeholders pursuant to appropriate consultative processes. The outcome of these processes has enabled fact based decision making that has been instrumental in ensuring that the appropriate market structure has been in place for the benefit of consumers.

3.19 In order to demonstrate the extent of the consultation and preparation required in respect of the cash equities market, which is less complex than eConveyancing because it involves transactions between sophisticated and high credit worthy counterparties who are supported by significant collateral, below is a timeline of the reviews undertaken to date by the CFR and ACCC on the Australian cash equities market:

- On 21 October 2011, the CFR released a consultation paper on proposals to enhance the supervision of Australia's financial market infrastructure.[25] In that paper, the CFR noted that it would be working with the ACCC to develop further analysis of competition issues.

- On 15 June 2012, the CFR and ACCC released a discussion paper on competition in clearing and settlement of Australian cash equities.[26] The focus of the work was clearing of ASX listed equities, reflecting emerging interest from several potential alternative providers offering competing counterparty (**CCP**) services. Work was carried out by ASIC, the RBA, the Australian Treasury, and the ACCC, who sought views from stakeholders in relation to potential implications of competition on the stability of, and access to, the market.

- In December 2012, based on its analysis and 16 submissions, the CFR released a 'Conclusions Report', which made recommendations to government on how to approach competition in the clearing and settlement of cash equities.[27] The CFR found that:

[23] IGA Draft Final Report, p 35, para 4.19.
[24] IGA Draft Final Report, p 35, para 4.20.
[25] *Review of Financial Market Infrastructure Regulation – Consultation Paper*, Council of Financial Regulators (October 2011), http://archive.treasury.gov.au/documents/2201/PDF/CFR_review_of_FMI_regulation_issues.pdf.
[26] *Competition in the clearing and settlement of the Australian cash equity market – Discussion Paper*, Council of Financial Regulators (June 2012), https://treasury.gov.au/sites/default/files/2019-03/Australian_cash_equity_market_Discussion_Paper.pdf.
[27] *Competition in Clearing Australian Cash Equities: Conclusions*, Council of Financial Regulations (December 2012), https://treasury.gov.au/sites/default/files/2019-03/Competition-in-clearing-and-settlement-of-the-Australian-cash-equity-market.pdf.

(1) making changes to support competition would involve significant costs; and

(2) that the benefits of competition were not readily quantifiable.

- Nevertheless, the CFR concluded that these concerns did not rule out the prospect of competition developing entirely, but acknowledged that it was not the appropriate time for changes that would have further cost implications for industry, especially given market conditions and pressures on participants to cut costs. Accordingly, the CFR recommended that:

  (1) any decision on a licensing application from a CCP be deferred for two years;

  (2) the agencies work with the ASX and industry to develop a code of practice for clearing and settlement of cash equities in Australia, based on principles developed by the agencies that would establish a formal and transparent commitment to industry; and

  (3) at the end of the two years, the CFR, RBA, ASIC and ACCC carry out a public review of the Code's implementation and effectiveness, and ASX's adherence to it.

- On 11 February 2013, the Australian Government announced that it had accepted the CFR's recommendation to defer consideration of competition for two years.[28] Also in February 2013, the Australian Government endorsed the CFR's recommendation to develop a set of 'minimum conditions' for safe and effective competition.[29]

- In August 2013, the ASX published the Code of Practice for the Clearing and Settlement of Cash Equities in Australia.[30]

- On 11 February 2015, at the conclusion of the two-year moratorium on clearing licences, the Australian Government announced that the CFR and the ACCC would commence a review of the policy position on competition in the clearing cash equities market to determine whether circumstances had changed for the development of competition.[31]

- In June 2015, following consultation, the CFR published a conclusions report on the findings of their 2015 review.[32] The CFR made three key conclusions:

  (1) that the policy approach should be one of openness to competition;

  (2) that competition, even if permitted, may not emerge for some time, if at all; and

  (3) that the relevant regulators should have powers to deal with an ongoing monopoly.

- Based on these conclusions, the CFR recommended that Minimum Conditions be formulated and regulatory expectations for the ASX in clearing and settlement be publicly set out. The CFR also recommended that legislative changes be implemented to allow the relevant regulators to impose requirements on the ASX consistent with the regulatory expectations.

---

[28] *Introduction of the ASX Code of Practice for Clearing and Settlement of Cash Equities in Australia*, Council of Financial Regulators (18 July 2013), https://www.cfr.gov.au/news/2013/mr-13-04.html.

[29] *Review of Competition in Clearing Australian Cash Equities: Conclusions*, Council of Financial Regulators (June 2015), at 1, https://treasury.gov.au/sites/default/files/2019-03/C2015-007_CFR-ConclusionsPaper.pdf.

[30] *ASX Cash Equities Clearing and Settlement Code of Practice*, ASX (August 2013), https://www.asx.com.au/cs/documents/asx-code-of-practice.pdf.

[31] The Hon Josh Frydenberg MP, *Review of Competition in clearing Australian cash equities*, http://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/media-releases/review-competition-clearing-australian-cash-equities. *See, Review of Competition in Clearing Australian Cash Equities – Consultation Paper*, Council of Financial Regulators (February 2015), https://www.cfr.gov.au/publications/consultations/2015/review-of-competition-in-clearing-australian-cash-equities/pdf/review-of-competition-in-clearing-australian-cash-equities.pdf.

[32] *Review of Competition in Clearing Australian Cash Equities: Conclusions*, Council of Financial Regulators (June 2015), https://treasury.gov.au/sites/default/files/2019-03/C2015-007_CFR-ConclusionsPaper.pdf.

- On 30 March 2016, the Australian Government endorsed the recommendations made in the CFR and the ACCC's June 2015 report.

- In October 2016, the CFR and ACCC released two policy statements in response to the CFR's Conclusions: (1) '*Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia*' (**Regulatory Expectations**); and (2) *'Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia'* (**Minimum Conditions (Clearing)**).

- In March 2017, the CFR and ACCC released a consultation paper (**March 2017 Consultation Paper**),[33] which sought views on whether the prospect of competition in the settlement of cash equities in Australia may have increased, and invited feedback on the development of policy guidance for such competition.

- In September 2017, CFR released a policy paper in response to the March 2017 Consultation Paper **(Safe and Effective Competition Policy Paper)**,[34] which summarised key feedback from stakeholders and the views of the CFR and ACCC with regard to how that feedback should be addressed within the policy framework.

- In parallel with the publication of the Safe and Effective Competition Policy Paper, the CFR and ACCC published the *'Minimum Conditions for Safe and effective Competition in Cash Equity Settlement in Australia'* (**Minimum Conditions (Settlement)**),[35] which provided a set of controls for competition in the settlement of cash equities in Australia aimed at addressing barriers and risks that had been identified by stakeholders responding to the March 2017 Consultation.

- In September 2017, in light of the work involved in the Minimum Conditions (Settlement), the CFR made amendments to the:

    - Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia (originally published in September 2016);[36] and

    - Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia (originally published in 2016).[37]

- In July 2018, the CFR and ACCC commenced work with the government to develop legislative changes that would provide ASIC and the ACCC with the powers necessary to enforce the CFR's Regulatory Expectations and Minimum Conditions (Clearing).

---

[33] *Safe and Effective Competition in Cash Equity Settlement in Australia – A Consultation Paper by the CFR*, Council of Financial Regulators (March 2017), https://www.cfr.gov.au/publications/consultations/2017/safe-and-effective-competition-in-cash-equity-settlement-in-australia/pdf/consultation-paper.pdf.

[34] *Safe and Effective Competition in Cash Equities Settlement in Australia: Response to Consultation*, Council of Financial Regulators (September 2017), https://www.cfr.gov.au/publications/consultations/2017/safe-effective-competition-response/pdf/response-to-consultation.pdf.

[35] *Minimum Conditions for Safe and Effective Competition in Cash Equity Settlement in Australia – A Policy Statement by the CFR*, Council of Financial Regulators (September 2017), https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2017/minimum-conditions-safe-effective-competition/pdf/policy-statement.pdf.

[36] *Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia – A Policy Statement by the CFR*, Council of Financial Regulators (September 2017), https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2016/minimum-conditions-safe-effective-cash-equity/pdf/policy-statement.pdf.

[37] *Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia*, Council of Financial Regulators (September 2017), https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2016/regulatory-expectations-policy-statement/pdf/policy-statement.pdf.

***A sound understanding of the technical features of eConveyancing and the differences between eConveyancing and the cash equities market is crucial***

3.20 Given the CFR's and ACCC's extensive work in reviewing competition issues for the Australian cash equities market, PEXA supports the development by the CFR, in collaboration with the ACCC, of minimum conditions for safe and effective competition in the national eConveyancing market. However, in PEXA's view, the development of any minimum conditions for competition in eConveyancing must have:

(a) a paramount focus on delivering safe, secure and affordable property transactions for Australian consumers dealing with their primary or only asset;

(b) a sound understanding of eConveyancing, including an in-depth understanding of the technical details and costs associated with the software, cybersecurity and IT intricacies that underpin the current services offered, particularly in relation to financial settlement and lodgement; and

(c) a nuanced appreciation of the differences that exist between the markets of cash equity settlement and eConveyancing. These differences have significant implications for the development of an appropriate regulatory framework for eConveyancing and must inform any regulatory response (these differences are explained in more detail below).

3.21 As IPART notes,[38] the cash equities market in Australia comprises:

(a) trading platforms, which match buyers and sellers of securities;

(b) clearing services, currently provided by a central counterparty that manages the pre settlement risks between counterparties to a trade; and

(c) securities settlement services, which involves the transfer of title to the security and transfer of cash.

3.22 As at the date of this submission, there is some competition in securities trading in Australia. However, clearing and settlement facilities are only provided by the ASX (although the *Corporations Act (2001)*(Cth) does not prohibit competition). In 2017, the CFR and ACCC concluded that the prospect of competition emerging had increased and, as a result, updated their competition policy framework.

3.23 In PEXA's view, the similarities between the two markets include the following:

- electronic platform providing settlement services for of buyers and sellers;
- high value of transactions managed by platforms (market capitalisations of $2 trillion in respect of the Australian cash equities market and $6-$7 trillion in respect of the Australian property market);[39]
- relatively low level of contestable fees ($105 million for the cash equities market and $200 - $240 million for the eConveyancing market);[40]
- requirement for significant and expensive backend infrastructure, including network connections with a large number of financial institutions and the RBA;
- requirement to handle highly sensitive and valuable data;

[38] IPART Draft Report, p 14, box 3.1.
[39] IGA Draft Final Report, p 74, para 5.72.
[40] IGA Draft Final Report, p 74, para 5.72.

- exposure to significant risk during financial payment and settlement; and
- exposure to risk of title fraud.

3.24 There are key differences between the two markets, some of which have been summarised in the table 2 below.

| *Table 2: Key Differences between the Cash Equities Market and eConveyancing Market* | | | |
|---|---|---|---|
| | **Difference** | **Cash Equities Market** | **EConveyancing Market** |
| 1 | Number of participants per transaction | Two parties in every share trade transaction – buyer and seller, sometimes represented by agents (also potential clearing/settlement agents). | More complex as there are often four or more parties (represented by Subscribers) in any given transaction, representing vendor, purchaser, incoming and outgoing mortgagee. Each Subscriber assembles information over the course of a transaction (i.e. information is accumulated as the participants add information to the transaction over the course of the transaction). Each Subscriber interacts and communicates with the other Subscribers, which results in a multitude of permutations and complexity. A greater number of Subscribers results in greater complexity of connection. |
| 2 | Economic importance to consumers | The IGA Draft Final Report asserts that the eConveyancing platform and the cash equities market are of similar economic importance to the wellbeing of Australians.[41] However, the cash equities market generally involves a relatively small portion of a consumer's asset portfolio. Financial risks to investors, while still important, are not of the same magnitude and severity as those faced by consumers in the eConveyancing space. | The eConveyancing market routinely deals with the average Australian consumer's sole or primary asset. Any exposure to financial risk during payment or settlement has an enormous impact on homeowners. As such, any regulation, particularly relating to interoperability models, must be carefully considered to minimise risks to consumers.[42] |
| 3 | Characteristics of a typical consumer | A mixture of sophisticated and retail consumers who are generally of high credit worthiness and possess significant collateral. | Primarily everyday Australians, and some property investors. |
| 4 | Protection against default | Multiple layers of protection for failed trades e.g. through a default fund held by clearing house. Creditworthiness of counterparties is assessed and dealt with via guarantees and indemnities (with the participants liable themselves). Australian regulatory standards require ASX's CCPs and ASX Clear to establish recovery tools under their operating rules to address any credit losses or liquidity shortfalls they may face as a result of clearing participant default. | Very limited protection for Australian consumers in conveyancing transactions. Dealing directly with consumer's funds and title in as close to real time as currently possible.<br><br>Subscribers handle the funds of end users (Australian property buyers and sellers). Ultimately, it is the Australian end user that wears the consequences of a failed conveyancing transaction.<br><br>Liability regime still needs to be determined for a multi ELNO environment. |

[41] IGA Draft Final Report, p 75, para 5.74.
[42] IGA Draft Final Report, p 64, para 5.8.

| | | | |
|---|---|---|---|
| 5 | Competition | In the cash equities market, whilst the Corporations Act does not prohibit competition, the ASX is the monopoly supplier of clearing and settlement services. Regulatory change was required to give the regulators the power to implement and enforce minimum conditions. | Currently in the eConveyancing market, only PEXA has established an operational financial settlement and lodgement infrastructure. Sympli has not completed any financial settlement transactions to date, and currently only has capability to lodge one document in Queensland and Victoria, respectively.<br><br>Competition is emerging. In addition to Sympli, LEXTECH (Purcell Partners), a third market participant, has obtained the first stage of approval to operate an ELNO. However, like Sympli, LEXTECH will need to invest significantly to become operational, let alone reach the same level of capability of PEXA.<br><br>State based Registrar Generals have power to influence the market, including by imposing conditions on ELNOs in the market. |
| 6 | Cost and complexity of connections | The ASX settlement requires connections with RBA, financial institutions and share registries (e.g. Computershare Limited, Link Market Services Limited). | Settlement in eConveyancing requires connections with the RBA, at least 11 financial institutions and with the relevant land registry offices, applicable revenue offices and the ATO.<br><br>An estimate of cost to each financial institution of $6-$10 million to establish each connection and at least $234,000 per year in support costs.[43]<br>Connection to land registry and revenue bodies also involves significant costs, both in development and ongoing maintenance. The estimates from titles and revenue offices to connect to a new ELN range from a few hundred thousand dollars to $5 million. |
| 7 | Role of State regulatory bodies | The ASX is not subject to any state-specific regulation. The development of minimum conditions for safe and effective competition was conducted by national regulators (i.e. CFR and ACCC). | As land registry and revenue offices vary according to each jurisdiction, the imposition of approval conditions by Registrar Generals as a method of regulation is likely to introduce complexity, inefficiency and fragmentation in the market. IPART's recommendation that the NSW ORG adopt regulation (including provision of minimum conditions) for eConveyancing by leveraging the CFR's work is ill-conceived and a national model is necessary. |

[43] *Review of the Intergovernmental Agreement for an Electronic Conveyancing National Law – Issues Paper*, Submission from Australian Banking Association (10 April 2019), p 3.

| | | | |
|---|---|---|---|
| 8 | Settlement period | The ASX has a T+2 settlement period, meaning that trades are settled two business days after the trade date. | PEXA conducts settlement of trades in real-time, transaction by transaction. Risk of error is significantly increased if data is required to be mirrored and synchronised across ELNO platforms. |
| 9 | Frequency of transaction | Cash equities are traded on a relatively frequent basis by investors. Consequently, consumers encounter fees in this market several times a year. | On average, Australian homeowners enter into property transactions once every 10.5 years.[44] The existing PEXA fee of $112 translates to $224 (assuming a transaction involves both buying and selling) per 10.5 years or $21 per annum. |
| 10 | Cost of fees relative to value of asset being transferred | The value of any cash equities trade is dependent on the value of the security and the volume to be traded. However, settlement and clearing fees are higher than the fees for eConveyancing services relative to the asset value. | The cost of fees in eConveyancing is a smaller percentage of the total value of the property when compared to cost of fees for clearing and settlement services in cash equities relative to the asset (i.e. securities). |

3.25 Given the clear functional differences between the Australian cash equities and eConveyancing markets, a simple 'transplant' of regulatory models will not be adequate to ensure that the efficiency or security of Australia's eConveyancing system is preserved. In comparison to the cash equities market, eConveyancing is demonstrably more complex, involves a larger number of parties to a transaction, and is of greater importance to everyday Australian consumers, as it often involves their sole or primary asset. Accordingly, what is needed is a pragmatic national consultation process with input from relevant stakeholders and regulators who have appropriate expertise to fully understand the nuanced technical, regulatory and economic details of eConveyancing, in order to arrive at a regulatory framework that is suitable and benefits Australian consumers.

3.26 Moreover, globally, the sole market where interoperability has been implemented is in the European market for cash equities clearing. In Europe, regulators created a single market across national borders through a complex model of interoperability between clearing houses, driven by a desire to expand the scale of clearing services by piecing each of the European national markets together. These unique circumstances do not exist in the context of the Australian cash equities market, or the eConveyancing market for that matter. Unlike the cross-border linkages in the European clearing market, interoperability in the Australian eConveyancing market would involve fragmentation of the market through multiple ELNOs, and then subsequent integration of those ELNOs through interoperability at high cost, while adding significant risk to the ELNO landscape. In the absence of the scale benefits and unique European market context that spurred interoperability reform in the common market of Europe, arguments in favour of implementing interoperability in Australia have generally been found uncompelling.

3.27 In PEXA's view, settlement in eConveyancing clearly benefits from scale, and it is this economy of scale that allows PEXA to deliver the best service for Subscribers. The Australian eConveyancing market is a relatively small domestic market, involving $200-$240 million fees per annum. This represents 0.1% of the $250 billion of property transferred each year in Australia.[45] For a domestic

[44] IGA Draft Final Report, p 77, para 5.99.
[45] *Property market chart pack – September 2019*, Core Logic.

market the size of eConveyancing, it is likely that a single infrastructure ELNO provides the most efficient and lowest risk solution.

3.28 Proper in-depth consideration of the risks and complexities unique to the eConveyancing market must be undertaken by appropriate national regulators through a national consultation process in order to develop a safe and effective regulatory framework, including minimum conditions for competition.

**Draft Recommendation 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 Finding 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.

3.29 PEXA agrees with IPART's conclusion that vertical integration can provide greater efficiency because it reduces errors, saves Subscriber's time and allows for transparency when consumers are comparing the prices of complementary products.[46] As IPART recognises, the MORs currently require an ELNO to structurally or functionally separate related upstream and downstream services.[47] Noting that the current version of the MORs were published 21 December 2018 and became operative from the effective date of 25 February 2019,[48] following a lengthy review by ARNECC, PEXA supports IPART's draft recommendation for the further review of the MORs to monitor the impacts of vertical integration.

3.30 However, PEXA notes that the IGA Draft Final Report recommends that the MORs be reviewed by a qualified economic regulator, citing the ACCC as an appropriate regulator.[49] PEXA suggests that ARNECC conduct a review with the ACCC, to ensure that the review processes are not inefficiently duplicative.

## 4. MARKET STRUCTURE AND INTEROPERABILITY

**Draft Recommendation 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.

**Draft Recommendation 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.

[46] IPART Draft Report, p 17, para 3.8.1.
[47] IPART Draft Report, p 19, para 3.8.1.
[48] *See, Model Operating Requirements – Version 5,* ARNECC (December 2018).
[49] IGA Draft Final Report, p 100; *See, also* IPART Draft Report, p 19, para 3.8.1.

**Draft Recommendation 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).

**Draft Finding 4**

The direct connection or an information hub models provide the greatest prospects for competition, differentiation and innovation between ELNOs.

**Draft Finding 6**

The incremental capital cost of a direct connection between the two current ELNOs is relatively low.

***Introduction***

4.1 PEXA does not support Draft Recommendations 4 and 5. Given the economic importance of real property, and by extension, any platform that facilitates property trades, it is vital that any regulatory framework for eConveyancing be designed in such a way that risks and costs to Australians that wish to sell or buy property are not increased.

4.2 Interoperability is far more complex than has been suggested in the IPART Draft Report. In the IGA Draft Final Report, DMC indicate that:

> "*Interoperability has proven to be a complex challenge and we are not recommending any immediate solution. We have provided our view that the shallowest interoperability approach provides the best chance of developing an acceptable model with reasonable costs and risks*."[50]

4.3 DMC also note that:

> "*The stakeholder feedback clearly identifies that a national view is required; [stakeholders] do not want different competition and interoperability solutions in different jurisdiction*."[51]

4.4 PEXA agrees with DMC's views in the IGA Draft Final Report that:

- The minimum conditions for safe and effective competition in eConveyancing should be established and, if interoperability is preferred, a cost benefit analysis be conducted.[52]
- The current regulatory framework does not prohibit the inefficient duplication of infrastructure. Competition at the user interface and Subscriber management level will allow Subscribers to choose the platform they wish to transact from and solve for multi-homing concerns. [53]
- It is logical to consider PEXA as a potential infrastructure provider (hub) for connections with land registries, revenue offices, the ATO and financial institutions, given PEXA was created under the IGA for this purpose.[54]

[50] IGA Draft Final Report, p 91, para 5.165.
[51] IGA Draft Final Report, p 91, para 5.169.
[52] IGA Draft Final Report, p 6, para 1.8.
[53] IGA Draft Final Report, p 66, para 5.27.
[54] IGA Draft Final Report, p 98, para 5.230.

- The approval of a second ELNO has increased costs and consumption of key resources due to the complexities of connectivity. These cost impacts will continue to be felt by industry if new ELNOs duplicate backend infrastructure and connections.[55]

- Financial institutions are unlikely to derive benefit from competition, given establishing connections to facilitate payment and settlement will foreseeably cost tens of millions of dollars.[56]

- Competition does not provide any benefit to regulatory bodies and there will be significant costs associated with additional ELNOs connecting to land registries and revenue offices. [57] Ultimately, however, any increased cost borne by such regulatory bodies will be passed through to Australian consumers that will bear these additional costs in the form of increased prices.

- Access to PEXA's settlement platform by way of an access arrangement must be given serious consideration as a potential market structure which will address concerns about multi-homing, network effects and the cost of duplicating infrastructure to ELNOs, financial institutions, land registries and revenue offices.[58]

4.5 Moreover, the NSW Interoperability Report correctly identifies several complex issues that are yet to be resolved before any model could be agreed, including:

- how a liability regime would work under an interoperable eConveyancing system;[59]

- whether the structure would be insurable (if it is in fact technically or commercially workable);[60] and

- that stakeholders would only support interoperability provided it didn't increase cost, risk, complexity or liability.[61]

4.6 Many of the issues and challenges with interoperability that have been identified have yet to be consulted on or reviewed, let alone resolved. The NSW Interoperability Report's own insurance report found that "*the insurance market will struggle to provide a sustainable solution for the proposed interoperability model."*[62] In the event there is an issue with a property transaction conducted through an interoperable framework, as the liability regime is yet to be determined, it will be very difficult to determine fault. The risk to Australian consumers if they are forced to wait for such liability to be determined cannot be understated and must be taken into account as a consideration in relation to any proposed interoperable framework or model.

4.7 IPART's proposed hybrid model is likely to introduce considerable uncertainty and complexity, translating into significantly increased costs. PEXA submits that IPART has failed to consider the full extent of the costs involved in implementing its proposed model of interoperability. Further, PEXA's view is that interoperability should not be implemented in NSW through ELNO licence conditions as this piecemeal approach to regulation that will result in a regulatory fragmentation and regime rife with inconsistency that will consequently lead to increased costs for consumers.

[55] IGA Draft Final Report, p 69, para 5.42.
[56] IGA Draft Final Report, p 70, para 5.51.
[57] IGA Draft Final Report, p 70-71, para 5.54-5.57.
[58] IGA Draft Final Report, p 97, para 5.220.
[59] NSW Interoperability Report, p 107, para 11.1.
[60] NSW Interoperability Report, p 110, para 11.4.
[61] NSW Interoperability Report, p 112.
[62] *Insurance Review – eConveyancing Interoperability Regime,* Willis Towers Watson (5 February 2019), p 10.

4.8 In the IPART Draft Report, IPART recommended that building direct connections between the two existing ELNOs is the preferred approach to achieve the benefits of competition in a "cost-efficient" way. Further, IPART recommended that interoperability could be implemented on a national basis by ARNECC through the MORs, but otherwise in NSW potentially through ELNO licence conditions.

4.9 IPART's draft recommendation appears to be based on the following reasoning:

- interoperability would improve competition in the eConveyancing market by opening up network effects;
- there are two ELNOs already operating in NSW;
- a bilateral connection model between the two existing ELNOs is likely to be the most cost-efficient way to achieve interoperability in the short term, while maximising the potential for competition and innovation; and
- the incremental capital cost of a direct connection between the two current ELNOs is relatively low.

4.10 PEXA does not support IPART's draft recommendations 4 and 5. PEXA believes that the technical, financial and legal complexities and risks involved with interoperability have been significantly understated in the IPART Draft Report. The lack of understanding about fundamental technical aspects of eConveyancing, coupled with insufficient regard to industry feedback, has led to findings and recommendations that rely on inaccurate facts and assumptions. The consequences of such regulatory error could undermine the safety and security of the current eConveyancing system to the detriment of industry, and the welfare of Australian consumers.

***Interoperability is highly complex and requires further consideration and analysis***

4.11 In PEXA's view, IPART's conclusions about the preferred model of interoperability are premature, given the complexity involved in establishing interoperability links between ELNOs. IPART's proposed 'hybrid model',[63] which involves initial bilateral connection, followed by either further direct connection or the establishment of an infrastructure access regime, fails to consider the full complexity and cost of direct connection. In contrast, DMC cautioned against implementing interoperability links in the short term acknowledging in the IGA Draft Final Report:

> "*Interoperability has proven to be a complex challenge and we are not recommending any immediate solution. We have provided our view that the shallowest interoperability approach provides the best chance of developing an acceptable model with reasonable costs and risks.*"[64]

4.12 PEXA agrees with this conclusion and believes the technical, financial and legal complexity and risks involved with interoperability have been significantly understated in the NSW reports, being the NSW Interoperability Report and the IPART Draft Report.

4.13 The IPART Draft Report states:

> "*In our analysis of the preferred model of interoperability, we considered that it is important to assess costs and benefits based on the current structure of the market: that is, there are two ELNOs already operating, and a third has obtained the first stage of approval to commence operating."*[65]

[63] IPART Draft Report, p 31-32, para 4.3.4.
[64] IGA Draft Final Report, p 91, para 5.165.
[65] IPART Draft Report, p 21, para 4.1.

4.14 However, IPART's characterisation and analysis of the existing market structure is flawed. As the IGA Draft Final Report accurately notes:

(a) only PEXA is fully enabled for financial settlement;

(b) duplication of infrastructure is inefficient and costly and must be a key consideration in any assessment of the viability of any proposed interoperability model; and

(c) competition can exist at the user interface level.

4.15 DMC has conducted the only review that attempts to explore the benefits, costs and risks of interoperability, appropriately finding that a thorough analysis by appropriately qualified regulators must be undertaken in order to understand the full impact of each model proposed to date. DMC explored in detail the alternative solutions that were advanced in the NSW Interoperability Report, such as a common user interface and Subscriber portability. However, these alternatives were given very little consideration or support in the NSW Interoperability Report.

4.16 PEXA agrees with DMC that a shallow approach to interoperability, which minimises the duplication of connections and settlement and lodgement infrastructure, is likely to be the least complex, and therefore the solution that involves the lowest cost and risk. However, it is crucial that the technical, financial and legal complexities (particularly in relation to the liability regime and insurability of eConveyancing), that are involved in any proposed interoperability or regulatory solution are fully understood and addressed. In PEXA's experience such issues can only be resolved through collaboration with all relevant stakeholders pursuant to an appropriate national consultation with reasonable timeframes.

***There must be a pragmatic national solution***

4.17 The intention of the IPART Pricing Review was always to create a single national system and IPART appropriately acknowledged that "*We support the conclusions reached by the IGA review draft report that national consistency of regulation is beneficial".*[66]

4.18 PEXA maintains that an interoperability solution preferred by one State alone will not be workable for either PEXA's national platform or for national industry members as it will increase costs and complexity to the detriment of Australian consumers. A solution that will drive up complexity and therefore costs for industry, other relevant stakeholders (such as Subscribers, financial institutions, land registries, revenue offices, the RBA and the ATO) is not acceptable, as ultimately these costs will be passed through to everyday Australian consumers, diluting or removing the cost efficiencies that eConveyancing has thus far achieved and delivered.

4.19 The total addressable market for ELNOs is in the $200-$240 million range. However, the Australian property market that eConveyancing critically supports is valued at around $6-7 trillion.[67] A solution which either creates uncertainty or adds additional risk for consumers would therefore be equally unacceptable. As there is no room for error or "teething problems" when dealing with everyday Australian's homes and money, it is critical that the costs, risks and benefits associated with any regulatory solution are identified and addressed in order to ensure that a pragmatic national solution that benefits everyday Australian consumers is reached, and not a solution that puts such consumers at increased risk or expense.

4.20 Accordingly, any further national review must be informed by the appropriate facts in order to enable fact based decisions. PEXA considers that any further reviews must follow a fact-finding and consultative process as that followed by DMC and be conducted on the national level.

[66] IPART Draft Report, p 15, para 3.7.
[67] IGA Draft Final Report, p 6, para 1.8.

***Assessment of interoperability must be based on prudent principles***

4.21 PEXA outlined in its response to the NSW Directions Paper[68] and the IGA Issues Paper[69], the principles PEXA believes are critical to consider in any assessment of the viability of any interoperability model, those principles are:

(1) interoperability cannot increase the risk of fraud or error in conveyancing transactions, relative to the risk for transactions conducted in a stand-alone ELN. The integrity of the register, the prevention of fraudulent activity and the recording of system-produced errors are paramount;

(2) financial settlement interoperability cannot be the subject of a mandate by any State or Registrar General given the broad impact on financial services. Financial settlement interoperability must be workable and be based on sound technical understanding;

(3) interoperability must promote competition and innovation by allowing ELNOs to compete on features including, but not limited to price. In a sensitive technology-driven market like eConveyancing, competition on quality and innovation is likely to be significant to Subscribers;

(4) interoperability must not increase costs to consumers;

(5) interoperability must not negatively impact the user experience, including through additional risk and/or complexity;

(6) interoperability must preserve the existing benefits of choice in relation to practice management software (or integrated software provider), without duplicating the functions that integration already provides; and

(7) development and regulation of any model of interoperability must be consistent with national principles of good regulation.

4.22 These principles should be used to test and assess the suitability of any proposed interoperability model.

***A cost/benefit analysis must be undertaken***

4.23 PEXA agrees with DMC's reiteration of the critical importance of ensuring that the benefits, costs, complexity, risks and liability of any proposed interoperability model are carefully considered and resolved before any interoperability model is adopted.[70] As DMC suggests, interoperability must deliver simple, consistent and cost-effective outcomes, which is developed within national principles of good regulation and do not introduce any additional risk for homeowners.[71]

4.24 A rigorous qualitative and quantitative cost-benefit analysis of interoperability, involving a national consultation process, is required to understand the real costs, risks and benefits associated with each proposed interoperability model, particularly with regard to addressing issues associated with any liability regime. In PEXA's view, the principles outlined above must be used to assess the viability of each proposed interoperability model.

4.25 PEXA has previously advocated for the consideration of interoperability to be led nationally by ARNECC. However, PEXA acknowledges the importance, complexity and risk associated with

[68] *Directions Paper on proposed eConveyancing interoperability regime,* NSW ORG (6 February 2019).
[69] *Review of the InterGovernmental Agreement for an Electronic Conveyancing National Law – Issues Paper,* DMC (13 February 2019).
[70] IGA Draft Final Report, p 82, para 5.131.
[71] IGA Draft Final Report, p 47, para 4.103.

ensuring the settlement aspects in any interoperability solution are appropriately addressed. Accordingly, PEXA considers the CFR, in collaboration with the ACCC, should conduct this cost-benefit analysis process, with expert input from technical experts, ARNECC and other relevant industry stakeholders. The original objectives of COAG in establishing the IGA were to extend the seamless national economy initiative into the conveyancing sector to drive efficiencies in existing practice for the ultimate benefit of Australian consumers. These objectives must remain central to the national eConveyancing framework.

4.26 PEXA submits that implementing interoperability will involve not just the cost of developing APIs, but the cost to PEXA and others to update their systems to support new interactions and build out business rules, as shown on page one of this submission. There will also be significant costs incurred in developing and maintaining interoperability. Any potential benefits of interoperability must therefore be identified and found to exceed the costs (including the significant risks and liability implications) of interoperability before any particular model is pursued.

4.27 DMC appropriately acknowledge that:

> "*[t]he complexities of eConveyancing increased with the introduction of a second ELNO. The connection costs increase the resource requirement for entry and operations for both ELNOs and the connected parties. This requires management of complex change control issues given the number of connections*."[72]

Figures 10, 11 and 12 of the IGA Draft Final Report provide a good visual representation of the increased complexity, risk and cost that will ensue if new entrant ELNOs are required to duplicate PEXA's existing settlement and lodgement connections infrastructure (extracted below for ease of reference). Accordingly, PEXA believes it is imperative that further analysis is conducted to appropriately address the technical, financial and legal risks (including issues concerning liability and insurability), as well as the costs of any proposed regulatory solution, in order to determine whether the benefits of introducing such a regulatory framework do in fact outweigh the costs and risks.

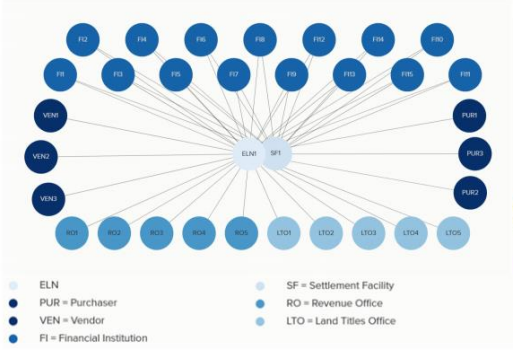



Figure 10 - Connection complexity with one ELN

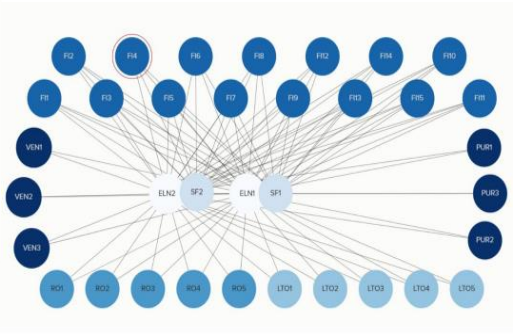


Figure 11 - Connection complexity with two ELNs

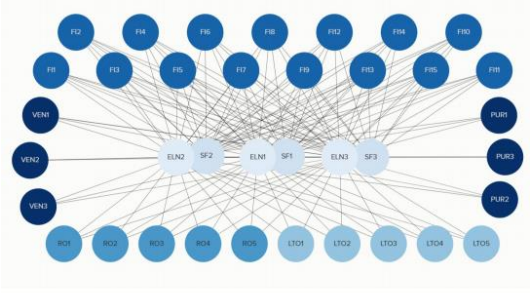


Figure 12 - Connection complexity with three ELNs

4.28 In PEXA's view, an ELNO that did not seek to replicate PEXA's ettlement model could:

[72] IGA Draft Final Report, p 71, para 5.60.

(a) provide for source funds from an ELNO Source Account only (similar to the PEXA Source Account and without providing an option for practitioner trust accounts);

(b) require provision of all funds directly from an RBA Exchange Settlement Account (such as where all incoming funds are provided from a major bank with no partial contribution from trust accounts); or

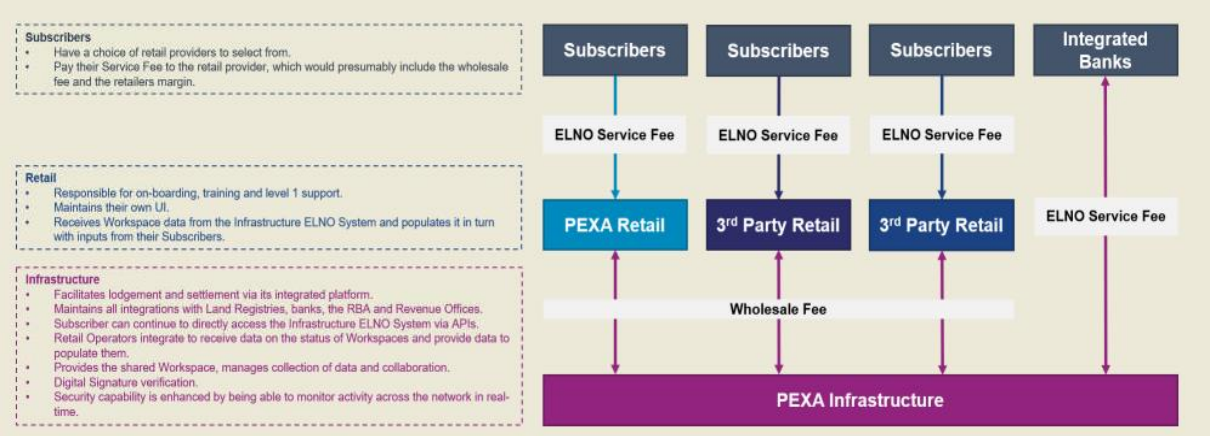
(c) arrive at some other method for funding settlements.

4.29 These options could avoid the duplication of the payment connections that PEXA has established.

***PEXA makes the following comments on the interoperability models under consideration***

In this section, PEXA provides observations in relation to the key interoperability models currently being explored.

## *A. Infrastructure ELNO Model*




***Description of Model***

4.30 Under the 'infrastructure' or 'sponsor' interoperability model, PEXA would utilise its existing lodgement and financial settlement infrastructure to provide settlement and lodgement services to retail/resellers for a wholesale fee. At the retail level, reseller or retail ELNOs would own and maintain their own user interface. The role of retail/resellers under this model would include onboarding Subscribers, verifying and auditing Subscribers, providing training and customer support, as well as processing the data provided to them from Subscribers.

4.31 Under this model, Subscribers would be able to continue to directly access ELNOs via APIs. The only integration required for resellers would be with PEXA's infrastructure hub, through which Retail ELNOs would be able to provide data.

4.32 The infrastructure ELNO would be the Lodging ELNO for all transactions utilising its established and currently operational integrations with financial institutions, land registries, revenue offices and RBA. The infrastructure ELNO would provide the shared workspace, as well as manage the collation of data and collaboration. Digital signature verification would also be provided at this layer.

4.33 Given PEXA already has established secure and proven integrations with land registries, revenue offices, financial institutions and the RBA, PEXA is well positioned to offer lodgement and financial settlement services to the market at the wholesale level. However, PEXA notes it would have no objection with new entrant ELNOs separately establishing their own lodgement and financial settlement infrastructure.

***Benefits***

4.34 There are a number of benefits associated with this model, including:

(1) ***Preservation of security and risk minimisation:*** The current security measures and framework will be preserved under this model, ensuring Australian consumers will continue to have certainty and trust in respect of the handling of their personal data and the execution of financial settlement aspects of their transactions.

(2) ***Timing and operational certainty:*** As this model of interoperability is closest in form to the current state of affairs in eConveyancing, there is certainty that this model would be workable with current functionality, subject to the regulatory framework being implemented. PEXA's financial settlement and lodgement technology is a world first. There is no guarantee that it can be replicated by other ELNOs. Additional lodgement capability could be added incrementally over time at minimal risk and complexity.

(3) ***No duplication of infrastructure:*** Duplication of financial settlement and lodgement infrastructure would be avoided under this model. DMC correctly acknowledges that it is not commercially viable for financial institutions to establish and maintain connections with more than one ELNO.[73] PEXA's existing integrations with financial institutions, revenue offices, land registries, the RBA and other ELNOs would be made available pursuant to an appropriate regulatory regime.

(4) ***Low complexity:*** This model likely involves the lowest amount of complexity in implementation as: (1) the infrastructure ELNO will always be the Lodging ELNO and the single source of truth; (2) the current liability and insurance regime would be maintained; (3) settlement regulation would remain unaffected reducing risk, as there would only be one set of integrations (which already exist) with financial institutions, land registries, revenue offices, the ATO and the RBA; and (4) the signing process would be maintained as authorisation and current digital certificates would not need to be replaced.

(5) ***Innovation and competition supported at the desktop/retail layer:*** Interoperability would be available at the desktop/user interface level facilitating competition with respect to end user experience. If this model is adopted, there is potential for a number of reseller/retail ELNOs to enter and successfully compete at the retail level.

(6) ***Liability and insurance:*** The current liability regime would be maintained as PEXA would remain responsible for lodgement and financial settlement. This would reduce regulatory uncertainty and maintain the high security and service standards that have already been established.

(7) ***Choice of ELNO for Subscribers (data entry):*** In respect of data entry (as opposed to settlement), Subscribers would likely have increased choice at the desktop layer, as retail ELNOs will compete on price and usability to gain market share.

***Consequences***

4.35 A number of consequences must be considered with this model, including:

(1) ***Competition focussed at retail/reseller layer:*** Given core data fields must be mirrored in each ELNOs respective Workspace at the infrastructure level and be identical for lodgement and settlement to occur, competition would be focussed at the retail layer. In PEXA's view, this would be the case under any proposed interoperable solution due to the technical and security requirements of lodgement and financial settlement.

(2) ***Regulatory regime:*** It would be necessary to develop an appropriate regulatory regime whereby reseller ELNOs would pay a fee to the infrastructure ELNO in order to access and utilise existing settlement and lodgement infrastructure of the infrastructure ELNO.

(3) ***Prices regulated:*** Prices would need to remain capped at the infrastructure/wholesale layer. However, PEXA notes IPART found that PEXA's prices are reasonable in respect of all

[73] IGA Draft Final Report, p 70, para 5.50 - 5.51.

modelled scenarios. Moreover, these prices were the outcome of extensive negotiations with industry when PEXA had no market share and had to compete against traditional paper conveyancing. Given this solution is already in place, and the complexity involved in renegotiating such arrangements, PEXA believes this model would involve significantly reduced complexity of price and other regulation. PEXA also anticipates any issues could be resolved quickly.

(4) ***Changes to regulatory framework:*** Some changes to the ECNL and MORs would be required to establish separate regulatory provisions in respect of wholesale ELNOs and resellers, including the introduction of a new category of regulated entity which could be responsible for Subscriber onboarding and other functions.

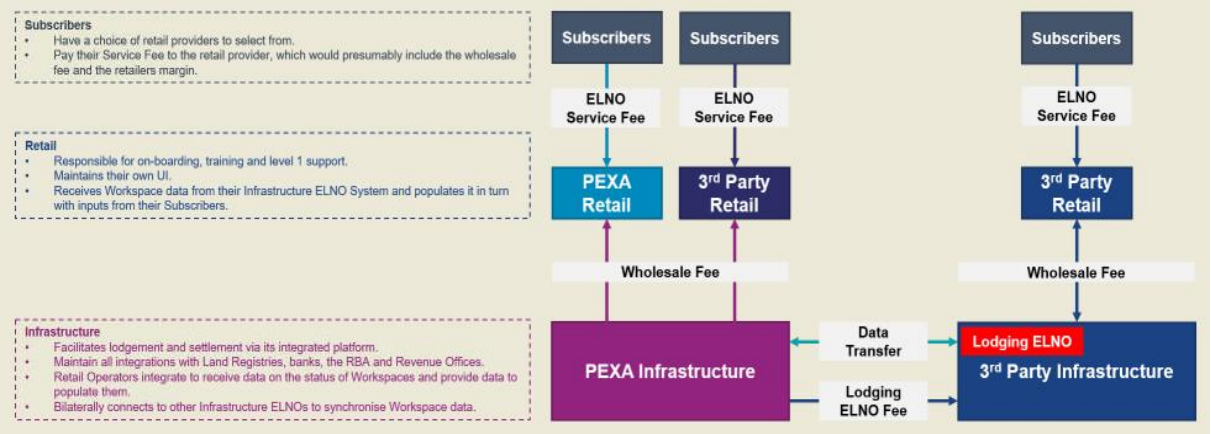
(i) **Regulators for wholesale layer:** Appropriate national regulators would be required to regulate the wholesale level of eConveyancing. RBA, ASIC, ACCC and ARNECC would be well placed to assist with this.

(ii) **Regulator for retail layer:** The appropriate regulator for the retail layer would be ARNECC.

***Market structure and likely number of ELNOs***

4.36 Under the Infrastructure/Wholesale Model, there would be only one wholesale infrastructure ELNO whose established settlement and lodgement infrastructure would be utilised by all. Pursuant to an appropriate regulatory regime and regulated wholesale price, duplication of infrastructure in the eConveyancing market could be avoided, while competition at the retail level could be developed. It is foreseeable that a number of retail/reseller ELNOs could successfully enter and compete under this market structure.

### *B. IPART's proposed 'hybrid' model: Bilateral Connections and Infrastructure model of interoperability*




***Description of Model***

4.37 Under the hybrid bilateral and infrastructure model of interoperability proposed by IPART, there would be two infrastructure ELNOs: (1) PEXA; and (2) a third party infrastructure ELNO (likely Sympli) that would be required to build and maintain its own settlement and lodgement infrastructure by establishing integrations with land registries, revenue offices, financial institutions, the ATO and the RBA. Each of these infrastructure ELNOs would be required to connect to each other in order to create a data transfer pathway.

4.38 Similar to the infrastructure ELNO model discussed above at paragraphs 4.30 to 4.36, each reseller or retail ELNO would be responsible for maintaining their own user interface, providing Subscribers with training, onboarding and customer support as well as collecting data from Subscribers.

4.39 In addition, and similar to the bilateral connections model discussed below at paragraphs 4.48 to 4.53, each infrastructure ELNO would be responsible for lodging data, but only one ELNO, the Lodging ELNO, would facilitate lodgement and settlement. IPART has proposed that a transfer fee would be payable by the Non-lodging ELNO to the Lodging ELNO to compensate the Lodging ELNO for use of their lodgement and settlement infrastructure. Each ELNO would collect data, which would be transferred to a counterparty ELNO.

4.40 PEXA questions the $13 cost reflective fee proposed by IPART to be paid to the Lodging ELNO by all other integrated ELNOs to a transaction. PEXA notes that IPART does not set out its proposed transfer pricing methodology in the IPART Draft Report, but uses information estimated by AECOM to illustrate how a transfer price for direct connections can be estimated. IPART's illustrative estimate is $13 per transaction, paid by the Non-lodging ELNO to the ELNO that is responsible for lodgement. The calculation includes an estimate of capital costs for title lodgement and financial settlement, but this is very small compared to other fees. PEXA notes that in practice the transfer price may be higher or lower than IPART's illustrative estimate reflecting the activities undertaken by the Lodging and Non-lodging ELNOs, the pricing methodology and the assumptions including the treatment of capital costs and the number of transactions. In PEXA's view, the consultation process should cover not only identification of a schedule of costs, but also determination of an appropriate pricing methodology.

4.41 PEXA notes that, as indicated by IPART in the IPART Draft Report, this illustrative transfer price is not an estimate of the price to access the existing ELNO's financial and settlement infrastructure. There is likely to be a material difference between the transfer price associated with direct connection and the access price associated with access to infrastructure. PEXA would expect the price to access existing ELNO's infrastructure would likely be closer to the price for a benchmark efficient ELNO

estimated by IPART, and a potential retailer would therefore charge a price closer to this benchmark efficient ELNO than $13. Care must be taken to not engineer perverse incentives into the choice by each ELNO of whether to invest in developing particular capabilities.

4.42 Practitioners and financial institutions would be free to choose to use any platform they wish for data entry purposes. However, it should be noted there will not be a choice of which ELNO executes the transaction as this will be determined by business rules in order to preserve the necessary levels of certainty and security that are required for the execution of settlement and lodgement. The ELNO which executes the transaction could be determined in different ways, including: (1) whether the ELNO is capable of completing a transaction; or (2) on the basis of which ELNO is the Responsible Subscriber (which as the visual depiction of the model above depicts would be the Lodging ELNO).

4.43 Data synchronisation and cross ELNO recognition would also be required to enable each respective ELNO to transfer data between ELNO workspaces in order to enable lodgement and settlement to occur in synchronisation in real time. To compensate the Lodging ELNO, the Non-lodging ELNO would pay a transfer fee to the Lodging ELNO to compensate it for the cost incurred in establishing, maintaining and using its infrastructure.

4.44 The significant departure from the status quo that this model presents would require the existing contractual framework, which was the outcome of extensive negotiations over several years, to be completely re-negotiated (including the risk and liability arrangements). It would also require PEXA to contemplate and resolve issues with regard to circumstances where there is no contractual relationship between an ELNO and an end user.

***Benefits***

4.45 The following benefits are associated with this model:

(1) ***Commitment of investment from all ELNOs***: Similar to the bilateral connections model, each infrastructure ELNO would be committed to investment in the eConveyancing industry as it would be necessary for each of these ELNOs to establish financial settlement and lodgement infrastructure and a compelling user interface in order become functional and compete. Competition would also be encouraged at the retail level in respect of user interfaces. However, there will be significant duplication of costly infrastructure.

***Consequences***

4.46 A number of consequences must be considered with this model, including:

(1) ***The most complex of all the models*****:** Implementation of the hybrid bilateral connections model will result in significantly increased complexity from a technical, legal, financial and regulatory perspective as it will involve a significant departure from the current market structure. There will be increased complexity in relation to, amongst other things: (1) the complex regulatory, technical and commercial orchestration that will be required to accommodate the new entrant ELNOs establishing their own connections with other ELNOs, all 11 financial institutions, the land registries and revenue offices. Technical, regulatory and legal solutions would need to be reworked for both lodgement and financial settlement; (2) data synchronisation, which has not been tested and will require workspaces to operate in synchronisation. This is a technically complex feature of this model which will increase risk of systematic error as there will no longer be a single source of truth; (3) trust account authorisations and arrangements will also need to be reworked and resolved; (4) the signing process, including development of new signing certificates; (5) liability regime will need to be addressed and solutions provided for; (6) insurance issues will need to be resolved.

(2) ***Significant costs due to complexity and extensive duplication:*** Increased complexity associated with implementing what is in essence two interoperability models will require a significantly more nuanced interoperability design that will require significant investment and time to design, negotiate and implement. Moreover, this model will result in extensive duplication of infrastructure as the third party infrastructure ELNO will need to establish their own connections with other ELNOs, all 11 financial institutions, the land registries and revenue offices (which is equal to 10 statutory bodies), RBA and ATO. As DMC acknowledges in the IGA Draft Final Report, these stakeholders will incur significant costs in establishing connections with additional ELNOs. In respect of financial institutions, the significant cost to connect with additional ELNOs is likely to result in such connections being deemed commercially not viable. However, if they were required to establish these connections pursuant to a mandate the costs would ultimately be passed through to consumers. In respect of the land registries, revenue offices, and the ATO, Australian consumers will ultimately have to pay for the cost of establishing additional connections in private entities.

(3) ***Security and privacy issues:*** Under the bilateral connections model, data transfer pathways increase with the number of connections that exist as between ELNOs and other industry stakeholders. As the number of connections increases, so too does the risk of a data breach, as systematic risk is added to the eConveyancing ecosystem with each additional connection, and security of the system can be compromised by its weakest link. Given highly sensitive personal data is handled in eConveyancing transactions, significant investment in cyber security will be required by industry to ensure consumers are not harmed and the integrity of the Land Titles Register, and ultimately the industry, is not jeopardised.

(4) ***Liability regime will need to be redeveloped:*** The bilateral connections model will require a complete restructure of the existing liability regime.

(5) ***Insurance uncertainty:*** It is unclear at this stage whether this new liability regime (which is yet to be considered) would be insurable on any terms.

(6) ***Increased pricing:*** Given the considerable costs and risks that will be incurred by industry as a result of the significant duplication of infrastructure and the requirement to develop new technical, security, liability and regulatory solutions to accommodate this structure, it is very likely that prices paid by Australian consumers for eConveyancing services will increase as stakeholders will be required to increase prices to recover costs.

(7) ***Significant additional risk due to substantial complexity and uncertainty:*** The requirement to interoperate two models at the same time will involve significant complexity which translates to risk for Australian consumers in conducting their property transactions. It is likely that many of the technical, security, commercial, liability, insurance and regulatory issues outlined in respect of the bilateral connections model and the infrastructure model above would be amplified under this model.

(8) ***Technical uncertainty and synchronisation costs:*** Data synchronisation across ELNO workspaces involves an innate risk of synchronisation errors that significantly increases systematic risk in the eConveyancing system. Costs associated with such errors are not limited to monetary loss, but also would extend to consumers potentially losing trust in the integrity of eConveyancing generally, which could have broader implications for the Australian economy; particularly given eConveyancing is mandated in certain States.

(9) ***Investment in innovation in settlement and lodgement infrastructure will be stymied:*** The requirement for workspaces to be synchronised in real time under the bilateral connections model necessarily requires functional consistency between ELNOs with regard to financial settlement and lodgement infrastructure. However, a consequence of this is innovation in

settlement and lodgement infrastructure will be stymied as the incentive to invest in developing more efficient technologies will be almost entirely removed, as any technological developments in settlement or lodgement would need to be shared with market participants to ensure data synchronisation is maintained. This would remove any competitive advantage that could be gained through investment in innovation in settlement and lodgement innovations. Logically ELNOs would cease all efforts at material innovation – it would simply be a cost that would be appropriated (at a lower cost) by other ELNOs prior to implementation.

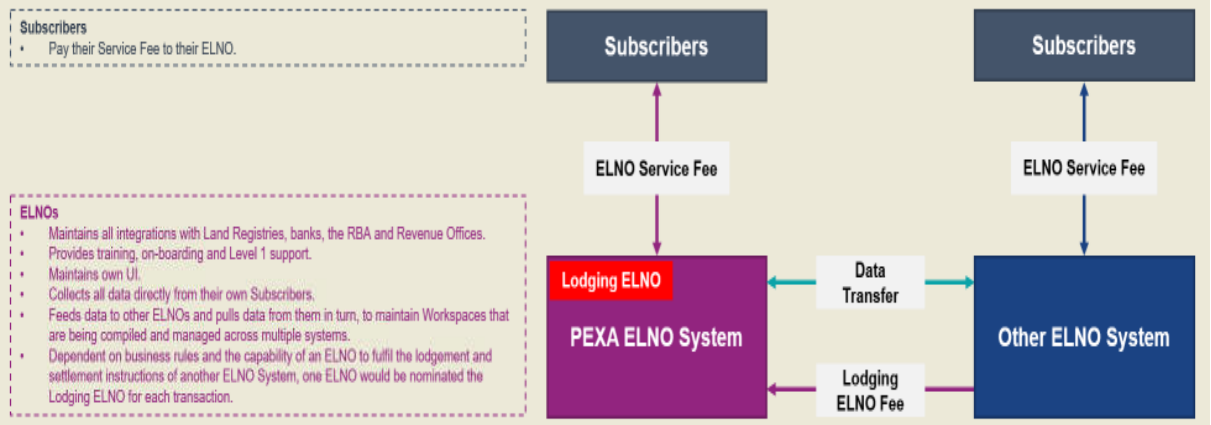
(10) ***Supporting financial settlement transactions:*** PEXA currently provides a sophisticated support centre that assists its Subscribers to collaborate and complete financial settlement transactions via the PEXA platform; in reviewing and assessing interoperability models, careful consideration will need to be given as to how to provide support and enable multi-party transactions where the ELNO has no contractual relationship with some of the participants.

(11) ***Timing – implementation could take over two years:*** Given the extent of the technical, commercial and regulatory issues outlined above that will need to be worked through; it could take more than two years for a bilateral model to be implemented. Given the increased complexity associated with this model, design and implementation could result in an even longer timetable than the bilateral connections model.

***Market structure and likely number of ELNOs***

4.47 Under this model of interoperability, two ELNOs could potentially be fully integrated with connections to all financial institutions, land registries, revenue offices and other ELNOs. Other ELNOs would focus on offering low cost front-end reselling. Potentially, two wholesale ELNOs may emerge with a number of retail/reseller ELNOs. However, this model is the most complex of the three considered as it would require vertical and horizontal interoperability between reseller ELNOs and interoperability at the wholesale infrastructure level. Accordingly, it would likely introduce unacceptable levels of risk into the system, be difficult and expensive for industry to implement, and likely carry no clear benefit to consumers as the cost savings eConveyancing has brought would likely be eroded through inevitable price increases due to the need for all relevant stakeholders to recover such cost.

### *C. Bilateral/Direct Connections Model*




***Description of Model***

4.48 Under a 'direct connections' or 'bilateral connections' model of interoperability, each ELNO would be required to build and maintain its own settlement and lodgement infrastructure by establishing integrations with the land registries, revenue offices, financial institutions, the ATO and the RBA. Each ELNO would also be required to maintain and develop its own user interface, provide training, onboarding and customer support.

4.49 Each ELNO to a transaction would be responsible for lodging data, but only one ELNO, the Lodging ELNO, would facilitate lodgement and settlement. IPART has proposed that a cost reflective transfer fee would be payable by the Non-lodging ELNO to the Lodging ELNO to compensate the Lodging ELNO for execution of the transaction and use of its infrastructure.

4.50 The bilateral connections model would involve the same issues discussed at paragraphs 4.40 to 4.44 above in relation to the bilateral connections component of the 'hybrid interoperability model'.

***Benefits***

4.51 The following benefits are associated with this model:

(1) ***Commitment of investment from all ELNOs:*** Under a bilateral connections model, each ELNO would be committed to investing in the eConveyancing industry as it would be necessary for each ELNO to establish financial settlement and lodgement infrastructure and a compelling user interface in order to become functional and compete.

(2) ***Infrastructure ELNOs would avoid need for pricing regulation:*** Competition between infrastructure ELNOs would drive competitive pricing by these ELNOs and avoid the need for price regulation.

(3) ***Consistent ELNO standards:*** As ELNOs would have the opportunity to compete on their desktop user interfaces and infrastructure (financial settlement and lodgement) offerings, industry standards could be consistently developed for all ELNOs.

***Consequences***

4.52 A number of consequences must be considered with this model, including:

(1) ***Technical uncertainty and synchronisation costs:*** Data synchronisation across ELNO workspaces involves an innate risk of synchronisation errors that significantly increases

systematic risk in the eConveyancing system. Costs associated with such errors are not limited to monetary loss, but also would extend to consumers potentially losing trust in the integrity of eConveyancing generally, which could have broader implications for the Australian economy, particularly given eConveyancing is mandated in certain States.

(2) ***Duplication of infrastructure and cost to industry and consumers:*** All new entrant ELNOs would be required to establish their own connections with other ELNOs, all 11 financial institutions, the land registries and revenue offices (which is equal to 10 statutory bodies), the ATO and RBA. As DMC acknowledges, financial institutions, land registries and revenue offices will incur significant costs in establishing and maintaining connections with additional ELNOs. In respect of financial institutions, the significant cost to connect with additional ELNOs is likely to result in such connections being deemed commercially not viable to pursue. However, if they were required to establish these connections the costs would ultimately be passed through to consumers. In respect of the land registries, revenue offices, and the ATO, Australian consumers will ultimately have to pay for the cost of establishing additional connections in private entities.

(3) ***Security and privacy issues:*** Under the bilateral connections model, data transfer pathways increase with the number of connections that exist as between ELNOs and other industry stakeholders. As the number of connections increases, so too does the risk of a data breach, as systematic risk is added to the eConveyancing ecosystem with each additional connection, and security of the system can be compromised by its weakest link. Given highly sensitive personal data is handled in eConveyancing transactions, significant investment in cyber security will be required by industry to ensure consumers are not harmed and the integrity of the Land Titles Register, and ultimately the industry, is not jeopardised.

(4) ***Liability and insurance:*** The bilateral connections model will require a complete restructure of the existing liability regime. It is unclear at this stage whether this new liability regime (which is yet to be considered) would be insurable on any terms.

(5) ***Increased pricing:*** Given the considerable costs and risks that will be incurred by industry as a result of the significant duplication of infrastructure and the requirement to develop new technical, security, liability and regulatory solutions to accommodate this structure, it is very likely that prices paid by Australian consumers for eConveyancing services will increase as stakeholders will be required to increase prices to recover costs.

(6) ***Increased complexity:*** Implementation of the bilateral connections model will result in increased complexity from a technical and regulatory perspective as it will involve a significant departure from the current market structure. There will be increased complexity in relation to, amongst other things: (1) the complex regulatory, technical and commercial orchestration that will be required to accommodate the new entrant ELNOs establishing their own connections with other ELNOs, all 11 financial institutions, the land registries and revenue offices. Technical and regulatory solutions would need to be reworked for both lodgement and financial settlement; (2) data synchronisation, which has not been tested and will require workspaces to operate in synchronisation. This is a technically complex feature of this model which will increase risk of systematic error as there will no longer be a single source of truth; (3) trust account authorisations and arrangements will also need to be reworked and resolved; and (4) the signing process, including development of new signing certificates; (5) liability regime will need to be addressed and solutions provided for; (6) insurance issues will need to be resolved.

(7) ***Investment in innovation in settlement and lodgement infrastructure will be stymied:*** The requirement for workspaces to be synchronised in real time under the bilateral connections model necessarily requires functional consistency between ELNOs with regard to financial

settlement and lodgement infrastructure. However, a consequence of this is innovation in settlement and lodgement infrastructure will be stymied as the incentive to invest in developing more efficient technologies will be almost entirely removed, as any technological developments in settlement or lodgement would need to be shared with market participants to ensure data synchronisation is maintained. This would remove any competitive advantage that could be gained through investment in innovation in settlement and lodgement innovations. Logically ELNOs would cease all efforts at material innovation in this model – it would simply be a cost that would be appropriated (at a lower cost) by other ELNOs prior to implementation.

(8) ***Benefits of competition would be limited:*** Competition under the bilateral connections model is conceptually possible at the wholesale layer; however, as core functionality and data fields in each ELNO to a transaction will need to be in sync for lodgement and settlement, competition will be extremely limited and significantly disincentivised for the reasons outlined above.

(9) ***Timing – implementation could take over two years:*** Considering the extent of the technical, commercial and regulatory issues outlined above that will need to be worked through, it could take more than two years for a bilateral model to be implemented.

***Market structure and likely number of ELNOs***

4.53 Under the bilateral connections model, there is potential for multiple ELNOs to become fully integrated with all relevant stakeholders. However, the commercial reality of high investment costs associated with each ELNO establishing connections will likely result in few ELNOs emerging, with the emergence of a duopoly (at best) becoming the likely market structure. Moreover, due to the security and technical requirements involved with lodgement and settlement, innovation and competition would only be possible at the desktop or user interface layer, with higher prices to users and consumers the likely outcome.

**Draft Recommendation 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.

4.54 As stated throughout this submission, PEXA does not support any form of a bilateral connections model of interoperability. However, in the event that such a model is nevertheless mandated, PEXA would support a consultation process to set a schedule of costs that can be used by ELNOs to calculate a cost-reflective transfer price for interoperable transactions.

4.55 In PEXA's view, this consultation process should be at the national level rather than at the state level. A national level process would avoid fragmentation in the market and the introduction of complexity, inefficiency, and potential inconsistencies. For these reasons, PEXA considers the CFR, in collaboration with the ACCC, should conduct this consultation process, with expert input from technical experts, ARNECC, State based Registrar Generals (including NSW ORG) and other relevant industry stakeholders.

4.56 PEXA also notes that IPART does not set out its proposed transfer pricing methodology in the IPART Draft Report, but uses information estimated by AECOM to illustrate how a transfer price for direct connections can be estimated. As PEXA notes at paragraph 2.13 above, in practice the transfer price may be higher than IPART's illustrative estimate depending on what activities Lodging and Non-lodging ELNOs are reflected, including pricing methodology, and what assumptions are made with regard to the treatment of capital costs or number of transactions. In PEXA's view, the consultation process must cover more than merely identification of a schedule of costs, but also determine an appropriate pricing methodology.

4.57 Finally, PEXA notes that, as indicated by in the IPART Draft Report,[74] this illustrative transfer price is not an estimate of the price to access the existing ELNO's financial and settlement infrastructure. There is likely to be a material difference between the transfer price associated with direct connection and the access price associated with access to infrastructure. PEXA would expect the price to access existing ELNO's infrastructure would likely be closer to the price for a benchmark efficient ELNO estimated by IPART. Indeed, given that IPART found that PEXA's prices were reasonable in comparison to all scenarios modelled by IPART (implying that PEXA's prices are below cost reflective levels in some or all scenarios) it may be that the efficient price for accessing an existing ELNO's infrastructure is, in fact, higher than the price for a benchmark efficient ELNO estimated by IPART.

4.58 Care should also be taken to ensure that there are no perverse outcomes or incentives for ELNOs to not invest in developing capability with regard to certain document types due to the high cost of introducing and maintaining those documents or connections. Any transfer price for interoperable transactions will need to adequately reflect the investment required for one ELNO to support the transactions that another is unable to facilitate. PEXA suggests that ARNECC and the NSW ORG will need to ensure that the MORs require all ELNOs to offer all documents in all jurisdictions.

[74] IPART Draft Report, p 34, para 4.4.5.

## 5. ELNO COSTS AND PRICES

**Draft Recommendation 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).

**Drafting Finding 8**

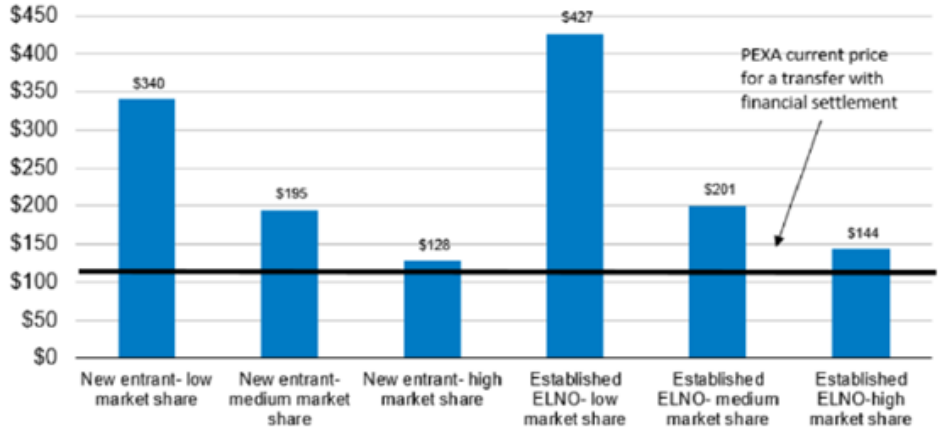
Maintaining the current pricing framework for eConveyancing will ensure consumers pay no more for eConveyancing than they did for paper conveyancing.

5.1 PEXA notes IPART's finding that PEXA's prices are reasonable when compared to all modelled estimates of a benchmark efficient ELNO. In reaching this finding, IPART has appropriately:

- acknowledged that the first mover is likely to incur substantial costs from R&D;
- acknowledged that PEXA educated the market and developed processes and standards; and
- found that PEXA's prices are reasonable compared to all modelled scenarios.

5.2 However, given the price ceiling recommended by IPART is below the estimated efficient price of both established ELNOs and new entrant ELNOs under all market share scenarios considered by IPART (as can be seen in Figure 2 below), PEXA queries the basis for IPART's draft recommendation that PEXA's current retail prices should be used as a price ceiling for all retail prices for eConveyancing services, and submits that the ceiling for maximum prices (if any) should be the price of an efficient benchmark ELNO.

*Figure 2: Prices for a benchmark efficient ELNO (transfer with financial settlement)*




**Note:** These building block modelled prices assume that all recommended price increases occur in the first year of the regulatory period.

*Source: IPART's Draft Report, Figure 5.1; AECOM modelled efficient costs.*

5.3 In the IPART Issues Paper, IPART indicated it would recommend prices based on the costs of a benchmark efficient ELNO.[75] IPART also acknowledged in the IPART Draft Report that its recommended pricing framework should be flexible and account for new entrant ELNOs that may have different cost structures from PEXA, in order to encourage innovative pricing models, including subscription or membership fees.[76]

5.4 While PEXA understands this pricing approach, caution and further consideration of this approach is necessary to ensure that no significant competition issues or unintended consequences arise. PEXA's pricing was developed after extensive negotiation with all stakeholders in the industry (including the ACCC) to ensure value was shared appropriately across the industry and that high-volume participants did not receive a significant competitive advantage due to discounting.

5.5 By recommending a maximum price below efficient prices, IPART acknowledges that new entrant ELNOs may not be able to recover operational costs incurred in the initial five to ten years of operation and refers to 'various technology firms' that typically do not make a profit in their initial operational years.[77] However, IPART does not provide information about the firms surveyed, or whether these firms are comparable to ELNOs, or if the industries that these firms operate in are in fact comparable to eConveyancing. Moreover, IPART does not provide evidence that firms in the eConveyancing market will be able to compete and make a profit in the long term, nor does IPART recognise that PEXA has already been in business for six years. In this regard, PEXA notes it is still yet to make a profit and has operated at a loss since it commenced operations. Most importantly, IPART does not explain how these initial losses would ever be recovered if IPART's draft recommendation that maximum prices remain constant in real terms is maintained; since IPART's own analysis suggests that these maximum prices are lower than efficient costs it is unclear how an efficient ELNO could ever hope to recover its costs by charging these prices.

5.6 Setting maximum prices below efficient prices is likely to distort the market by raising barriers to entry, resulting in a deterioration of services offered to Subscribers, and deterring innovation and investment. Accordingly, in PEXA's view, the evidence provided in the IPART Draft Report for setting a maximum price for eConveyancing services lower than the prices of a benchmark efficient ELNO is not compelling, given the potential detriment to competition, services and innovation. Moreover, given the existing contractual and regulatory price cap on PEXA's current prices, PEXA maintains there is a strong case for IPART to engage in price monitoring, rather than imposing a maximum price on ELNOs, which is well within IPART's Terms of Reference. However, if IPART were to push forward with recommending a maximum price for ELNO services, the maximum price should correspond with the maximum prices of a benchmark efficient ELNO in order to not risk distorting the market and potentially deterring innovation and future investment in eConveyancing services.

5.7 In addition to the submission above, PEXA seeks to clarify several points and ensure the following inaccuracies are amended in IPART's final report:

(a) At page 4 of the IPART Draft Report, IPART has incorrectly stated that PEXA charges a fee for digital certificates required to securely access PEXA's system.[78] This statement should be amended, as digital certificates are not required to access the system, but only to sign documents. It is the case that Subscribers can have many users who can access the system without digital certificates. Digital certificates must be obtained for parties who are required to sign documentation (i.e. "Signers"), which are typically a sub-set of users. This is also a requirement under the MORs.

[75] IPART Issues Paper, p 34, para 5.3.
[76] IPART Draft Report, p 44.
[77] IPART Draft Report, p 40, para 5.2.
[78] IPART Draft Report, p 4, para 2.3.1.

(b) At page 43, PEXA seeks a correction of the statement that PEXA supports a building block approach to pricing if price regulation does eventuate.[79] PEXA has consistently submitted that a building block approach is not appropriate. This statement should be corrected before the finalisation of IPART's report.

(c) At page 49, IPART states that certain settlement agents only monitor a workspace on the day of settlement.[80] PEXA seeks clarification in relation to this statement, as PEXA is not aware of this practice and queries how it could occur in compliance with the regulatory framework and PEXA's Participation Agreement.

**Draft Recommendation 8**

If an ELNO unbundles its prices for the financial settlement and lodgement components of a service, then the sum of the separate prices for financial settlement and lodgement components must not exceed the regulated maximum for the bundled price.

5.8 PEXA does not support IPART's draft recommendation that the sum of the unbundled prices for financial settlement and lodgement components of a service must not exceed the regulated maximum for the bundled price.

5.9 PEXA notes that the regulated maximum price for the bundled price includes significant cost synergies which realise when financial settlement and lodgement services are undertaken jointly. Hence, when these services are undertaken separately, these cost synergies and corresponding savings do not eventuate. As there are no cost synergies, the sum of the cost of undertaking financial settlement and the efficient cost of undertaking lodgement will be higher than the cost of undertaking the two services jointly. As a consequence, the sum of the separate prices for the two services will be higher than the regulated maximum for the bundled price.

5.10 PEXA also notes that financial settlement is not regulated by the MORs, and in PEXA's strong view, the State Registrar Generals are not able to regulate or set pricing in relation to financial settlement activities.

**Draft Recommendation 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.

5.11 PEXA notes that any such provision can only apply to services provided by, or as part of, the ELN and that there is an existing regulatory and contractual price cap on PEXA's ELN services, which includes a requirement for publication of a pricing table on the ELNO's website (see MORs 5.4).

5.12 IPART recommends that an ELNO should set prices for any new eConveyancing service to reflect costs, based on a building block methodology. However, it is PEXA's view that IPART has not demonstrated that regulating new eConveyancing services is necessary. This is because it may be that there will be competition in the provision of these new eConveyancing services. Separately, IPART has not established that the benefits of regulating prices for any new eConveyancing services would outweigh the costs. Furthermore, PEXA is concerned that the broad scope of this recommendation, and the imposition of a specific form of price regulation on any new service, might deter ELNOs from

[79] IPART Draft Report, p 43, para 5.3.
[80] IPART Draft Report, p 49, para 5.6.

modifying their service offer and pricing policies, going against IPART's intent of incentivising product and service innovation.

5.13 Moreover, even if it is established that some new eConveyancing services require regulation, PEXA's view is that IPART has not provided evidence that a building block approach would be the best approach to determine regulated prices. In addition to our general concerns with the use of building block regulation for eConveyancing, PEXA is also concerned about the significant practical difficulties in applying a building block model to new services in the context of opex and capex costs that are shared across services.

**Draft Recommendation 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.

5.14 IPART recommended that the maximum price of any residual dealings, which can currently only be completed on paper in NSW, be set by determining the relevant category of service of each dealing, and setting the price equal to the prices for that category that PEXA is currently charging.[81] IPART's Draft Recommendation 10 seems to be based on its assessment of PEXA's current prices as being reasonable and appropriate as a maximum price for providing eConveyancing services. This assessment of PEXA's current prices formed the basis of IPART's Draft Recommendation 7.

5.15 While PEXA agrees with IPART's assessment that PEXA's current prices are reasonable, PEXA believes it would not be appropriate to extend the same assessment to prices for dealings that are not currently offered. PEXA's approach to pricing 'other land registry documents' is based on PEXA's estimation of the costs that are likely to incur in undertaking these dealings. However, whether these prices are a reasonable estimate of other categories of residual dealings will only be known when PEXA can start offering those residual dealings. In PEXA's opinion, setting maximum prices for a service before the true costs of providing the service have been determined can distort the market. For example, if the true costs are higher than initially envisaged, PEXA would not be able to recover the costs of providing those services as the maximum price would be lower than the efficient price. In PEXA's view, the need to regulate the prices of residual dealings, and the appropriateness of PEXA's current pricing as applied to these residual dealings, should be assessed once the residual dealings are mandated to be completed electronically and the true costs of providing those services will be revealed.

5.16 PEXA also notes that IPART's Draft Recommendation 10 does not seem to allow for a similar indexation mechanism as included in Draft Recommendation 7. IPART did not explain why maximum prices for residual dealings should not be indexed in a similar way to how prices for current services are. PEXA is concerned that without an indexation mechanism, the maximum prices that the ELNOs would be allowed to charge for these services would, *ceteris paribus*, become lower than the efficient prices for delivering these services. If maximum prices are lower than efficient prices, the ELNOs would not be able to recover their costs and this would distort the market. In PEXA's view, an appropriate indexation mechanism should be included when determining maximum prices for services.

**Draft Recommendation 12**

ELNOs not be required to offer nationally consistent pricing, but they may choose to do so on a commercial basis.

**Draft Finding 7**

[81] *Other Land Registry Documents*, PEXA (accessed on 27 September 2019), https://www.pexa.com.au/other-land-registry-documents-pricing; *See also*, IPART's Draft Decision, Table 5.3.

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.

**Draft Finding 9**

Other jurisdictions could adopt a similar framework for recommending ELNO prices.

5.17 IPART recognised that stakeholders expressed a strong preference for nationally consistent pricing but nevertheless recommended that ELNOs not be required to offer nationally consistent pricing. IPART's Draft Recommendation 12 appears to be based on the observation that there may be differences in costs across jurisdictions, and so ELNOs should be able to vary prices by jurisdiction.

5.18 While there would undoubtedly be efficiency benefits in having any differences in costs across jurisdictions being reflected in different prices across jurisdictions, these efficiency benefits need to be balanced against the increase in costs that would arise if pricing were not nationally consistent. The ABA has stated that differences in pricing between jurisdictions adds around 10-15% to member banks' costs. The Law Society has also stated that nationally consistent pricing results in lower administrative costs. IPART itself supports the conclusion reached by the IGA Draft Final Report that national consistency of regulation is beneficial, as ELNOs and many financial institutions are national organisations, and thus, gain efficiencies from regulation and business process being as consistent as possible across jurisdictions.[82] PEXA's submission is that these increases in costs outweigh the efficiency benefits that would be achieved through prices that vary by jurisdiction.

5.19 IPART states that ELNOs may choose to offer nationally consistent prices on a commercial basis, but PEXA's submission is that this commercial decision may not be open to ELNOs. If pricing is regulated, and regulated prices are set independently by IPART and other jurisdictional regulators, it may not be open to ELNOs to offer nationally consistent prices; there may be no single price that complies with regulatory decisions in each jurisdiction. For this reason, it is PEXA's submission that regulated pricing should be on a nationally consistent basis, and regulatory decisions should not be based on the assumption that ELNO's commercial decisions can deliver nationally consistent prices in the absence of nationally consistent regulation.

[82] IPART Draft Report, p 15, para 3.7.

## 6. PRICING FOR NSW LAND REGISTRY SERVICES

**Draft Finding 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.

6.1 PEXA understands that NSW LRS has developed a new multi-ELNO platform and has announced a proposal to introduce additional fees for ELNOs. As IPART notes, NSW LRS already charges lodgement support services (**LSS**) fees and registration fees to ELNOs and consumers, respectively.

6.2 PEXA agrees with IPART's draft finding that NSW LRS should be able to absorb the cost of expenditure on technology upgrades. NSW LRS should not be permitted to recover the incremental cost of a technology upgrade from PEXA, or PEXA's members, via an additional fee as the new platform does not provide any additional benefit to PEXA. PEXA agrees with IPART's conclusion that "*the expenditure was best categorised as an expenditure on technology to provide an existing service, rather than a new service."*[83] Further, PEXA notes IPART's recognition that PEXA has been able to deliver cost savings to LRS through increased eConveyancing volumes.[84]

6.3 PEXA agrees that NSW LRS should be entitled to recover the cost of that investment from second and future ELNOs.

## 7. PRICES FOR REVENUE NSW SERVICES TO ELNO

**Draft Recommendation 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.

**Drafting Finding 11**

Including Revenue NSW in the governance framework would reduce total costs to the industry, and deliver greater efficiencies.

7.1 Under IPART's Draft Recommendation 13, Revenue NSW could charge ELNOs a maximum price of $15.20 (indexed by CPI annually) per support inquiry received to recover costs relating to ELNO subscriber support.[85]

7.2 IPART's Draft Recommendation 13 was based on the following reasoning:

(a) Revenue NSW undertakes additional functions, and incurs additional costs, as a result of eConveyancing. The parties who can influence these additional costs are in the best position to bear these costs. PEXA accepts the conclusion that eConveyancing imposes additional costs

[83] IPART Draft Report, p 53, para 6.3.
[84] IPART Draft Report, p 54, para 6.4.
[85] IPART Draft Report, p 63, para 7.5.1.

on Revenue NSW and agrees with the proposition that the parties that are able to influence these additional costs are in the best position to bear these costs.

(b) Prices that recover Revenue NSW's costs should apply to all ELNOs, to ensure competitive neutrality.[86] PEXA supports this conclusion and considers that consistent treatment of ELNOs will ensure competitive neutrality and also promote efficient decisions by ELNOs.

(c) The appropriate form of price regulation is maximum prices that are directly connected to ELNO's actions, as this will encourage efficient use of Revenue NSW's services.[87] PEXA supports the use of maximum prices, although considers that the lack of competition for Revenue NSW means that there is no incentive for Revenue NSW to charge any less than the maximum price. PEXA also supports regulated prices that are directly connected to ELNO's actions and agrees that this will promote efficient decisions by ELNOs.

7.3 While PEXA supports the methodological framework that IPART has proposed for regulating prices for Revenue NSW, PEXA has significant concerns about the recommended maximum prices. In particular, PEXA is concerned about IPART's Draft Recommendation 13 that the maximum price charged by Revenue NSW for each support inquiry should be $15.20 (indexed by CPI annually). PEXA understands that this draft recommendation is largely based on information provided by Revenue NSW, which has not been subject to review by stakeholders, and has not been benchmarked against other estimates of efficient costs. However, in PEXA's view it is even more important that cost information from Revenue NSW is subject to careful regulatory scrutiny than it is that information on the cost of ELNOs be subject to careful regulatory scrutiny. The reasons are that there is emerging competition between ELNOs that will limit the prices that ELNOs can charge and there is a price benchmark for eConveyancing that was established when eConveyancing was competing with paper conveyancing to attract customers.

7.4 For example, PEXA understands that one of the key drivers articulated by Revenue NSW for support inquiries from ELNOs was the eligibility of property titles to be electronically tradable. This is not a matter controlled or initiated by an ELNO, but rather the NSW LRS / NSW ORG. In light of this example, PEXA seeks full disclosure of all of the elements taken into account in calculating the support inquiries figure in order to respond appropriately to this recommendation.

7.5 PEXA has concerns that the maximum price of $15.20 per support inquiry (indexed by CPI annually) overstates the efficient cost of support inquiries. For these reasons, and because of the absence of competitive constraint for Revenue NSW, PEXA submits that IPART should carefully scrutinise information on costs provided by Revenue NSW.

[86] IPART Draft Report, p 55, para 7.1.
[87] IPART Draft Report, p 55, para 7.1.

## APPENDIX A – AECOM'S ANALYSIS

### 1. THIS APPENDIX PROVIDES A REVIEW OF THE APPROACH ADOPTED BY AECOM TO:

(a) estimate efficient transaction costs for a benchmark efficient ELNO; and

(b) estimate transaction cost for the industry for each of the four proposed models of interoperability.

1.2 AECOM determined the following:

(a) The capital cost for a benchmark efficient ELNO is $5.5 million;

(b) The benchmark efficient transaction cost range between $42-$77 for an established ELNO and between $55-$122 for a new entrant ELNO, depending on the market share. These transaction costs assume that any capital investments made by the established ELNO have been already fully depreciated.

(c) There is no material difference in transaction costs between any of the interoperability models over the first five years for the scenario modelled.[88]

1.3 AECOM's estimates of costs are based on a series of assumptions, including assumptions about efficient capital and operating expenditures, resources and marketing activities, the status and development of the market, and the structure of the interoperability models. We note the following:

(a) AECOM makes specific assumptions on market shares, number of subscribers, number of transactions by jurisdictions, organisation size, and the time of entry in the market of ELNOs. It is unclear whether these assumptions are supported by evidence.

(b) AECOM does not take into account tax liability or the costs associated with multiple title transactions

1.4 AECOM undertakes a sensitivity analysis to test how sensitive its estimates are to a subset of the assumptions made. AECOM found the following:

(a) its estimates of efficient transaction costs for a benchmark efficient ELNO can vary by +/- 6%;

(b) its estimates of transaction costs for the industry for each of the four interoperability models can vary by +/- 12%.

1.5 AECOM's sensitivity analysis considers only a subset of the assumptions made to estimate the costs and that the change in costs is based on modifying one assumption at the time. It is unclear what the impact on the estimated transaction costs would be if the remaining assumptions made by AECOM are tested and/or multiple assumptions are changed at the same time.

[88] *Estimating costs of electronic conveyancing services in NSW: Draft Report,* AECOM (19 August 2019), p 44.