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26 March 2019

Ms Anne Larkins
Dench McClean Carlson P/L
Level 5, 99 Queen Street
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By email: alarkins@dmcca.com.au

Dear Ms Larkins

Issues paper – review of the InterGovernmental Agreement for an Electronic Conveyancing National Law

We refer to the issues paper prepared by Dench McClean Carlson dated 13 February 2019 on the review of the eConveyancing Intergovernmental Agreement (IGA).

The ACCC welcomes the opportunity to provide its views in response to the issues paper. This letter draws on previous comments that the ACCC has publicly made in relation to competition in the electronic conveyancing market and on interoperability. The ACCC made comments in its submission to ARNECC on the draft Model Operating Requirements version 5.1, and its letter to the New South Wales Registrar General dated 13 February 2019.

The ACCC has not commented on all issues raised in the issues paper, instead concentrating on those most relevant to its general regulatory functions.

Competition

The ACCC understands from the issues paper that most stakeholders support competition in electronic conveyancing, provided there are no additional costs and no additional risks or liabilities.¹ The ACCC notes that the e-conveyancing market is no longer a single ELNO market since a second ELNO entered the market in November 2018. The paper raises concerns that competition should not come at the expense of quality and suggests that a cost benefit analysis of competition should take place.

In the ACCC's experience, competitive pressure in a market generally promotes lower prices, increased efficiencies and innovation, and better quality services. The ACCC still

¹ Dench McClean Carlson, Issues Paper, Review of the InterGovernmental Agreement for an Electronic Conveyancing National Law, p 16.

considers that tailored ex ante regulation is essential to address issues that are specific to the industry, rather than relying on subsequent regulation or general competition law.

We would caution against an assumption that the cost advantage to consumers must necessarily be small from competition, as appears to be implied by paragraph 5.78 of the issues paper on the basis of current charges. The benefits of competition need to be assessed on the basis of a forward-looking assessment and consider the potential future changes in prices and benefits to innovation from competition.

The issues paper raises the potential that the existing and new ELNOs may choose to operate only in certain jurisdictions in order to generate a profit for the costs involved in set up.² The MORs require ELNOs to provide a minimum set of services to all jurisdictions but we note the concern that the level of service provided might differ between jurisdictions. The effect on competition of ELNOs providing services in all jurisdictions, or select jurisdictions, may require further consideration. This concern about the compliance of ELNOs with minimum service level requirements also relates to the enforcement options available to the jurisdictions, which is discussed below in this letter.

Separation and non-discrimination

At paragraph 5.28 to 5.29 and 6.24 to 6.27, the issues paper notes there is industry concern that ELNOs could enter the conveyancing industry or other related services reducing competition in the industry in the longer term. Third party providers are concerned about ELNOs competing unfairly against them by making favourable commercial arrangements with some parties and not others.³

The ACCC agrees that vertical integration by ELNOs into related parts of the supply chain has the potential to raise concerns in this industry. We agree with the need identified at paragraph 6.27 for rules that are clear and ensure that there are no abuses of market power.

The ACCC's preferred regulatory structure is complete vertical separation between an ELNO and downstream providers, as it removes the incentive to discriminate on both price and non-price terms. However, if an ELNO is permitted to vertically integrate to offer downstream services such as conveyancing services, then it is necessary to have in place robust functional separation requirements or ring fencing. Ring fencing or functional separation arrangements do not remove an operator's incentive to discriminate, but may constrain the operator's ability to do so. Such functional separation requirements may include separation of resources, employees, systems, contractor arrangements and support functions.

The ACCC's view is that it is necessary for ELNOs to have obligations to interact with all participants on equal terms and to provide non-discriminatory access to all users including downstream users such as conveyancers. Non-discriminatory access should include equal treatment for all users of the system on both price and non-price terms such as the same quality, reliability and timeliness of service, and equal dissemination of information to all participants.

Enforcement powers

The ACCC emphasises that compliance provisions must contain a credible threat of enforcement. The existing ability to suspend or terminate an ELNO does not appear to be a credible threat, particularly given the current market structure. We agree it is not a practical tool and could lead to significant disruption, as noted in the issues paper.⁴ The issues paper

² *Ibid*, p61.

³ *Ibid*, p61, 70.

⁴ *Ibid*, p55-6.

notes at paragraph 5.35 that there needs to be powers to direct ELNOs and to apply fines or other penalties. The ACCC agrees these powers are important to promoting compliance. Examples of effective compliance tools applied in other industries include pecuniary penalties and infringement notices for non-compliance, and civil court orders to compel compliance.

In addition to effective compliance tools, the ACCC considers that effective monitoring is necessary, for example information gathering, audits and penalties for non-compliance with audits. The ACCC has previously considered compliance and monitoring requirements in other industries and its view is that an independent entity is often best placed to monitor and enforce compliance.

Pricing

We refer to the reference in the issues paper that, even with two ELNOs in the market, price caps may be necessary until an efficient market develops.⁵ The ACCC's view is that to the extent that the ELNO market is not fully competitive, a price control can ensure that customers benefit from efficiency gains as they would in a competitive market.

The ACCC's general view on pricing constraints is that any proposed pricing regime needs to be considered over the long-term and have a reasonable cost reflective basis for any starting price. It is also important to consider whether both the initial prices and prices over time reflect efficient costs and productivity improvements. Over time, increasing volumes and efficiencies could mean that average costs could decrease while an ELNO's revenue increases. These efficiencies may apply to both the present ELNOs and to new ELNOs. However ELNOs that entered the market first will have a head start on building these efficiencies and volumes. When robust competition is in place with the entry of new ELNOs into the market, then price controls could be potentially removed. The ACCC accordingly recommends periodic price reviews to ensure cost-reflective pricing outcomes.

Dispute resolution

The ACCC emphasises it is important that all users and customers, including conveyancers subscribing to ELNOs and other ELNOs participating in the market, have access to independent dispute resolution and arbitration mechanisms to resolve disputes that may arise. The ACCC also recommends consideration of an independent arbitrator and relevant rules to resolve disputes.

Interoperability

The ACCC notes that the terms of the IGA review proposed that interoperability mechanisms would be considered as part of the review. As the competition regulator, the ACCC has expertise with competition issues including the exercise of market power, problems caused by market structures, and in developing regulatory solutions. In this letter, in providing the ACCC's views on the principles of interoperability and the regulatory framework the ACCC's perspective therefore focuses on competition issues. The ACCC does not have the relevant expertise to comment on the specific technical details of the interoperability mechanisms for the ELNO market.

We note that the issues paper states that the benefits from interoperability are not certain, the costs are significant and an in-depth analysis is required.⁶ The ACCC understands that consideration of the best approach to interoperability may require review to identify the costs of interoperability to all parties. However the ACCC also considers there is potential for such

⁵ *Ibid*, p73.

⁶ *Ibid*, p73.

review to result in significant further delays in introducing interoperability, and it may also be difficult to quantify the exact costs to all parties.

The ACCC does not have a view on the level of costs that would constitute a cost effective model or how these costs should be borne. ELNOs ultimately will need to justify the benefits of competition through lower charges, despite costs incurred in setting up interoperability. It is likely that registries and revenue offices may charge to recover costs incurred in setting up for interoperability.

The benefits of interoperability to competition

The ACCC's overall position is that interoperability is a potentially effective mechanism for ensuring that the benefits of competition are realised while mitigating some of the adverse implications such as market fragmentation and increased operational costs for participants.⁷ Interoperability can thereby promote competition in markets where end users need to connect across networks in order to perform a transaction or function, and where there is the potential for an incumbent service provider to leverage the market power of its network.

The ACCC has considered interoperability in other markets, such as the clearing and settlement market, and the related concept of any-to-any connectivity in the telecommunications market in relation to mobile terminating access services. We consider interoperability to be a mechanism that can reduce network effects and facilitate competition.

In the absence of interoperability in the clearing and settlement of Australian cash equities, both participants to a trade would have to be members of the same cash equity central counterparty (CCP). However, interoperability between two clearing facilities would allow a participant of one CCP to execute centrally-cleared trades with a participant of the other CCP. Without interoperability, network externalities arise since a larger CCP can offer its participants wider access to other traders and hence a deeper market. Participants are more likely to join a large CCP than multiple smaller CCPs due to the costs associated with maintaining multiple clearing memberships. By allowing a CCP to access another CCP's participant network, interoperability minimises the network advantages and market power that accrue to large CCPs, fostering competition between clearing services.⁸ The issues faced in the clearing and settlement market are similar to the issues that may be faced in the ELNO market. Currently, both parties to a conveyancing transaction (and each party's conveyancer and bank) must use the same ELN to conduct the transaction.

In the telecommunications access regime, the ACCC has highlighted the importance of any-to-any connectivity to reduce network effects and facilitate competition. Any-to-any connectivity is a similar concept to interoperability as it enables end-users to communicate with each other regardless of the network to which they are connected.⁹ The ACCC deemed the mobile terminating access services (MTAS) to be a declared service under the relevant access regime,¹⁰ to enable access seekers to obtain access on reasonable terms. The MTAS allows one mobile operator to finish a call on another mobile network, and providing all operators with access to the MTAS achieves any-to-any connectivity. The ACCC considers that any-to-any connectivity can reduce network effects, which arise when there are lower costs or greater benefit to the customer being part of a large customer base. If a customer's network cannot connect to another customer's network then customers will prefer

⁷ Council of Financial Regulators, *Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia* (revised September 2017); *Review of Competition in Clearing Australian Cash Equities: Conclusions*, June 2015.

⁸ Council of Financial Regulators, *Review of Competition in Clearing Australian Cash Equities: Conclusions*, June 2015.

⁹ ACCC, A guideline to the declaration provisions for telecommunications services under Part XIC of the *Competition and Consumer Act 2010*, August 2016

¹⁰ *Competition and Consumer Act 2010*, Part XIC

to subscribe to networks with a larger customer base.¹¹ This is detrimental to competition as it gives the incumbent an unfair advantage over newer or smaller entrants. Accordingly, where a new operator enters the market, the incentives for the established operators to interconnect with the new operator may be insufficient to ensure any-to-any connectivity. The incumbent may have the ability and incentive to use its existing market power either to deny interconnection or to impose charges above economic cost for these interconnection services.¹²

In the context of electronic conveyancing, the ACCC considers interoperability to be an important pro-competitive feature. Interoperability is essential to facilitating the entrance of new ELNOs into the market and can prevent an incumbent from becoming further entrenched as the dominant service provider in the market due to network effects.

The issues paper sets out several models for the ELNO market:

- single ELN (base case) – which operated until November 2018 when a second ELNO Sympli was approved to operate
- multiple independent ELNs
- multiple interoperable ELNs (direct connection) and
- multiple interoperable ELNs (intermediated)
- multiple interoperable ELNs (using an 'infrastructure ELN').

The 'base case' in the issues paper does not appear to be applicable now given the entry of a second ELNO into the market. Consistent with the ACCC's general views on interoperability, the ACCC does not consider the model of multiple independent ELNs to be a desirable model from the perspective of competition. In the absence of interoperability requirements, a new ELNO entering the market will face significant barriers to entering the electronic conveyancing market. Customers may be reluctant to switch over due to real or perceived costs of switching. Even if the new ELNO can offer a better price or a better service, the incumbent ELNO will already have the network advantage of a greater number of users and will be able to leverage this advantage, as each party to a transaction must use the same ELNO. Without interoperability, a new ELNO will be unable to offer subscribers the ability to complete a transaction with parties who are subscribed to a different ELNO. In order to maximise their opportunity to transact with other participants in the market, customers would need to subscribe to every ELNO in the market and are likely to prioritise ELNOs with large customer bases, further entrenching existing market power. Interoperability will allow market participants (such as conveyancers and lawyers) to choose their preferred ELNO while continuing to participate in transactions with participants who are using a different ELNO.

Accordingly, the ACCC considers that the models involving multiple interoperable ELNs, whether by direct connection or intermediated model, are the preferred models for promoting competition in the market. The 'infrastructure ELN' approach might also be able to provide a useful market structure, although it appears to require some significant changes to the role of ELNOs as currently contemplated.

The ACCC also considers that in order to facilitate competition between providers, it is important that it is easy for customers to switch between providers. Interoperability will help enable switching to be as 'frictionless' as possible which will drive efficiencies in the market

¹¹ ACCC, Public inquiry into the declaration of the Domestic Mobile Terminating Access Service - Discussion Paper, August 2018

¹² ACCC, A guideline to the declaration provisions for telecommunications services under Part XIC of the *Competition and Consumer Act 2010*, August 2016

as end users are able to identify and move to the best service. This is likely to create greater incentives for ELNOs to continue to improve their service quality, efficiency and prices to attract customers. The ACCC understands that in relation to customer switching there may be other barriers not resolved by interoperability. However the ACCC considers that interoperability would be a significant step to resolving the likely barriers.

The ACCC emphasises the need for mechanisms to ensure there is competition in the ELNO market. As the key purpose of interoperability is to remove barriers to entry caused by network effects, interoperability is therefore an essential component. While the ACCC does not have views on the specific model of interoperability that should be adopted (whether direct connection or intermediated), the ACCC considers that for any model to be effective it needs to address the specific barriers to entry that are present in the industry.

Regulatory framework for interoperability

The ACCC does not seek to provide comments on the technical aspects of a proposed interoperability model. However, the ACCC provides its views on the important aspects of a regulatory framework to facilitate interoperability.

The ACCC considers that an incumbent ELNO has little incentive to voluntarily develop interoperability arrangements. In an emerging market such as the e-conveyancing market, established ELNOs will have an incentive to refuse to provide interconnection to new entrants, or provide it on unreasonable terms and conditions or at a high price.

For interoperability to overcome these incentives and effectively address the network effects problem, regulatory measures should be in place to facilitate the establishment of effective interoperability on reasonable terms between the incumbent and any ELNO seeking to enter the market. These measures should ideally be in place prior to new ELNOs entering the market, to ensure they are able to compete effectively at the outset. Given the market is still evolving, regulatory measures should also incorporate flexibility and review measures to resolve issues that may arise in the future. As it has turned out, the first new entrant has already commenced operations prior to regulatory measures being resolved.

The ACCC considers there should be a level of industry-specific up front regulation rather than sole reliance on commercial arrangements to facilitate interoperability. In markets with large entrenched operators from which a new entrant requires access or connecting services, it is the ACCC's experience that the relative bargaining power of the parties is unequal, which is not conducive to fair and reasonable commercial negotiations. Regulatory models to solve this problem generally take two overarching forms: upfront requirements, and negotiation with a regulatory backstop of arbitration. Upfront requirements are preferable where measures should be implemented consistently across an industry. However negotiation, with recourse to arbitration, provides more flexibility to market participants and may better accommodate new and emerging markets and new products.

The ACCC considers that in the context of the ELNO market, an appropriate regulatory framework would likely combine both approaches. The upfront regulation applying to all ELNOs (whether existing or new entrants into the market) should require each ELNO to have in place baseline interoperability functionality. The baseline requirements will depend on the model of interoperability adopted. However the requirements should implement practical measures to ensure that an incumbent has the necessary facilities and capabilities in place to connect with new entrants or to the central hub (depending on the model of interoperability adopted), and therefore prevent it exerting its market power by unreasonably delaying facilitating interoperability. The upfront requirements should also include an obligation to engage with other ELNOs in good faith and on reasonable terms, and to act on a non-discriminatory basis.

An arbitration mechanism could be utilised when parties are not able to reach an agreement in negotiations relating to terms not covered by the upfront requirements (the baseline interoperability functionality). The extent to which an arbitration mechanism is needed will depend on how comprehensive the upfront requirements are. The mechanism can provide for arbitration to be conducted by an independent arbitrator rather than by the regulator, and in a commercial manner to facilitate swift and targeted resolution of disputes.

Both upfront requirements and the process for referring disputes to arbitration should be transparent to ensure new entrants are sufficiently informed about the process for setting up interoperability and their options where negotiations with incumbent operators are unsuccessful. The ACCC emphasises the importance of transparency in the regulatory framework, including information provision obligations to level the negotiation playing field. Transparency increases the effectiveness of dispute resolution arrangements and also boosts the accountability of ELNOs.

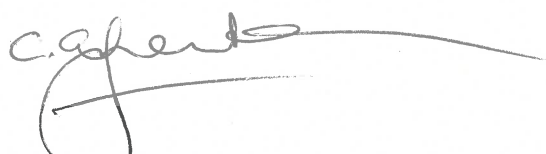
It is important that any model of interoperability that is adopted does not entrench any existing market power or contain any anti-competitive aspects. Fair and non-discriminatory access is more likely to occur where a government or independent body owns and sets the data and/or service standards for interoperability to function. If a private entity owns or sets the standards, or has ownership of the hub in the intermediated model, then there must be sufficient regulatory controls in place to constrain the exercise of its market power. It would undermine the competition benefits of interoperability in the ELNO market if the interoperability mechanism itself provided market power to a private owner or operator without sufficient regulatory constraints.

Further engagement

The ACCC looks forward to continued engagement with you on the development of the IGA and the regulatory regime for the electronic conveyancing sector.

If you have any questions, please contact Michael Eady on 03 9290 1945 or michael.eady@accc.gov.au. We are happy to meet to discuss issues raised in this submission or other areas that you may be investigating.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'C. Cifuentes', with a long horizontal line extending to the right.

Cristina Cifuentes
Commissioner

