Blockchain Australia - Submission to Treasury

Response to Consultation: Regulating Digital Asset Platforms

1st December 2023

Blockchain Australia

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Subject: https://treasury.gov.au/consultation/c2023-427004

Table of Contents

1. Executive Summary

Blockchain Australia, along with its members, has identified two key observations within our industry that guide our approach in shaping policy to best protect consumers.

Consumer Behaviour Towards Market Accessibility: Our view, informed by input from our members, is that consumers will tend to gravitate towards platforms that readily offer the services they desire, irrespective of location of those businesses, rather than showing a preference to Australian businesses, where they may be better protected. This trend is demonstrated by the widespread adoption of international platforms like Celsius and FTX in Australia, highlighting a clear customer preference for accessibility and service availability over geography of the service provider.

Primary Consumer Risk: The paramount risk facing consumers in our industry is the potential loss of assets and funds held by others. This concern has been underscored by the recent global spate of bankruptcies, resulting in billions in financial losses for consumers globally. Notably, the majority of these failures, with the exception of FTX, which engaged in misappropriation of user assets, stemmed from various forms of lending activities (e.g. Alameda Research, Three Arrows Capital, Celsius, BlockFi, Babel, Voyager, Zipmex). Like most modern businesses, cyberattacks remain a threat, particularly given the digital nature of crypto-assets.

In light of these insights, Blockchain Australia advocates for the following three strategic objectives to enhance consumer protection and industry integrity:

1. Ensuring Operational Safety It is imperative that digital asset platforms operate predictably and meet high standards, minimising the risk of loss for consumers in a failure.

2. Availability of In-Demand Products We urge the Treasury to encourage regulatory frameworks that enable sought-after products to be offered in a safe and regulated manner in Australia, and for that framework to attract products to Australia.

3. Balanced Regulatory Approach We emphasise the importance of retaining talent and attracting innovation to Australia, particularly in areas where the risk of loss is minimal. Without Australian businesses, it will prove difficult to prevent consumers from using unregulated offshore platforms, whereby their exposure to risk would be amplified.

These objectives underpin Blockchain Australia's approach and response in advocating for a balanced and consumer-focused regulatory framework. Further information on reaching these objectives is detailed in *Section 6 - Recommendations*.

Blockchain Australia

2. Blockchain Australia Overview

This submission is made by Blockchain Australia, in collaboration with its members and industry stakeholders.

Blockchain Australia is the peak industry body representing Australian businesses and business professionals participating in the digital economy through blockchain technology. Blockchain Australia encourages the responsible adoption of blockchain technology by the government and industry sectors across Australia as a means to drive innovation and create jobs in Australia.

The Blockchain Australia membership base consists of 130+ leading cryptocurrency and Blockchain centric businesses and 115+ individuals across multiple verticals including:

- Accounting and Taxation
- Artificial Intelligence
- Banking
- Cyber Security
- Development
- Building & Construction
- Digital ID
- Energy and Resources
- Art & Entertainment
- Gaming
- Health and Wellbeing
- Insurance
- Investment
- Legal
- Recruitment
- Real Estate
- Risk and Compliance
- Supply Chain
- Venture Capital
- Custody

Blockchain Australia gives special thanks to the following members for their role in hosting the policy response sessions and contributing to this submission:

- DCE Working Group Chair - Tom Bennett, Head of Operations, Swyftx
- DCE Working Group Co-Chair - Michi Chan, VP Regulatory Compliance, Crypto.com
- DCE Working Group Board Sponsor - Jackson Zeng, CEO, Caleb & Brown
- Digital Assets Working Group Board Sponsor - John Bassilios, Partner, Hall & Willcox

We also thank the Department of Treasury for taking the time to consider our submission and welcome any opportunity for further dialogue.

Please direct any enquiries to:

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3. Methodology

In response to the Consultation Paper, Blockchain Australia has gathered input from our member base.

Blockchain Australia has a membership base of 130+ businesses, 28 of which are classified as Digital Currency Exchange (DCE) members. Almost all of these members would meet the definition of a "Digital Asset Facility" set out in the current proposal in the Consultation Paper.

We extended an invitation to all our DCE members to contribute to a collective response to this consultation. Additionally, we welcomed participation from other members who have interests in the regulatory framework surrounding Digital Assets. We have a DCE Working Group and a Digital Assets Working Group, and we thank the participation across both Working Groups.

Through this inclusive approach, we garnered insights from 70+ organisations over the course of four video conferences and asynchronous written input, which has been incorporated into this response for Treasury's consideration.

4. Recommendations

4.1 Ensuring Operational Safety

It is imperative that digital asset platforms operate with the highest standards of safety, minimising the risk of loss for consumers.

This specifically relates to:

a) Ensuring there is no misappropriation of user funds or assets;
b) Ensuring there is sufficient operational capability for safekeeping of digital assets; and
c) Where lending activity takes place, that is not conducted using an unknowing customer's funds (a), or in a way that introduces risk to the platform's ability to meet its operational capabilities (b).

We have observed that a common issue raised in the Consultation Paper was the different business models between exchanges and brokerages. Some responses will include recommendations for operational differences between Digital Asset Exchanges and Digital Asset Brokerages.

Topic	**Recommendation**	**Question Set for Detailed Response**
Low Value Facility	Remove the individual customer calculation. If the individual customer threshold must be included, make it based on token values, not fiat values, so as to account for market volatility. Or increase the low threshold to $15,000, to account for the current bear market, and market volatility.	2
NTA Requirement	Recommend a scaling approach starting at $1m up to $5m	4

4.2 Availability of In-Demand Products

We urge the Treasury to encourage regulatory frameworks that enable sought-after products to be offered in a safe and regulated manner in Australia.

In Australia, we have observed consumers opt for offshore platforms that offer:

a) A wide listing of a variety of digital assets;
b) Lending and Staking products
c) Both brokerage and exchange models

Topic	**Recommendation**	**Question Set for Detailed Response**
Exchanges	Australian exchanges have to be able to meet market demand. Otherwise customers will use offshore unregulated exchanges, defeating the purpose of this regulation.	9
Brokerages	Clear definition of what is considered a broker, removing any ambiguity as to who digital asset facility issuers are.	3

4.3 Balanced Regulatory Approach

We emphasise the importance of retaining and attracting innovation through balanced regulation, particularly in areas where the risk of asset or fund loss is minimal, to reduce the risk that consumers seek unregulated offshore platforms as they cannot locate the products they seek in Australia.

Blockchain Australia and its participating members have identified this relates to:

a) Decentralised Finance (DeFi); and
b) Gaming, Entertainment, and other Non-Fungible Tokens (NFTs).

Topic	**Recommendation**	**Question Set for Detailed Response**
Gaming / NFTs	Do not create a regulatory burden on Gaming and Entertainment	14
DeFi	All DeFi requires a further consultation	6

4.4 Transitional Considerations

We have included an additional recommendation category for considerations during the transition period as industry adopts the new regime.

Topic	Recommendation	Question Set for Detailed Response
Safe Harbour	Because the line between Financial Products Tokens and Non-Financial Products Tokens remains blurry, we recommend a commitment of no enforcement action related to dealing in tokens where this remains ambiguous.	1
12-Month Transition Period	A transition period should be provided whereby platforms have 12 months to submit their licence application from the point in time that the Bill receives Royal Assent, however given the likely bottleneck of Digital Asset Facilities all simultaneously submitting, applicants should be also given an automatic approval to continue operation until their application is reviewed and either approved or denied by ASIC.	16

5. Detailed Responses

Questions (Set 1)

Prior consultation submissions have suggested the Corporations Act should be amended to include a specific 'safe harbour' from the regulatory remit of the financial services laws for networks and tokens that are used for a non-financial purpose by individuals and businesses.

What are the benefits and risks that would be associated with this? What would be the practical outcome of a safe harbour?

Under the current proposal, financial services laws would be extended to Digital Asset Facilities providing "Financialised Functions" of Tokenised Non-Financial Products. Given that licensed Digital Asset Facilities will have met the new minimum standards for each Financialised Function, we believe that consumer risks will have been fully addressed.

However, with the Consultation Paper not including a clear delineation between Tokenised Financial Products and Tokenised Non-Financial Products, in conjunction with the rapidly developing nature of features within a given Digital Asset, there remains uncertainty where a Digital Asset widely recognised as a Non-Financial Product by the industry may be interpreted as a Financial Product by a regulatory body.

This poses a risk to innovation where Digital Asset Facilities face an ambiguous breach of the requirement for Financialised Functions to be provided exclusively for Tokenised Non-Financial Products.

Given that this Consultation Paper addresses the obligations and risks to consumers associated with Digital Asset Facilities, we recommend the inclusion of a "safe harbour" for scenarios in which a Digital Asset Facility is deemed to have been providing Financialised Functions for a Tokenised Financial Product where they have otherwise met all of their other obligations under the AFSL.

Questions (Set 2)

Does this proposed exemption appropriately balance the potential consumer harms, while allowing for innovation? Are the proposed thresholds appropriate?

How should the threshold be monitored and implemented in the context of digital assets with high volatility or where illiquid markets may make it difficult to price tokens?

We recognise the need to strike an appropriate balance between protecting consumers, by ensuring platforms holding sufficiently significant values of assets are captured by the regulatory regime, while promoting innovation and early-stage companies to enter the market. This is a challenging and delicate balance to strike.

Our members are supportive of a low-value facility exemption with a threshold linked to the *aggregate value of assets held on a platform*, however, a threshold linked to the value of assets *held by an individual customer* will likely hinder new entrants in the market.

By way of example, an early-stage company who is trying to enter the market or test a new product may need to:

- Refuse a customer access to their platform; and / or
- Limit individual users' activity on the platform,

These actions would be taken to ensure the value of their assets remain below the designated individual customer asset value threshold. An early-stage company seeking to enter the market may look to operate under this low-value facility exemption until they have built some baseline operating capital or have developed a sufficient product and customer base to support external investment, in order to meet the Net Tangible Asset requirements outlined under Question Set 4.

Secondly, there may need to be consideration for scenarios where price volatility briefly places a Digital Asset Facility above the low-value facility exemption temporarily, as well as a process for determining how long a business has until they must submit their AFSL application.

There are a number of ways this important issue could be addressed, including:

- Removal of the $1,500 per-user threshold, which would provide flexibility to businesses by limiting the number of customers they take on to manage the volatility risk of exceeding the thresholds and is the option preferred by our members;
- Raising the per-user threshold to $15,000;
- Having the threshold calculated only at a point in time, for example when an asset is provided by a customer, which would provide certainty to businesses when growing and give them the ability to manage compliance practically but create a potential for an unlicensed offering with substantial un-custodied assets; and,
- Having a requirement, once a threshold is surpassed, for a licence application to be *made within a designated period, eg. 12 months,* with a transitional approval to operate until the application is either approved or denied by ASIC.

Notwithstanding the position of our members outlined above with regards to the individual customer asset threshold, if such a threshold were to be introduced, our members are of the strong opinion that $1,500 is far too low given the typical profile of a Digital Asset Facility user. According to BTC Market's Investor Study Report published in April 2022, the average user holds a portfolio of approximately $7,000. Our members propose that $15,000 would be a more reasonable threshold, if such a threshold linked to the value of individual customer assets were to be introduced.

In addition to existing use cases of DCEs, the Digital Asset industry is likely to see innovation in the payments space. A threshold of $1500 is likely to hinder adoption of new technologies if such businesses are limited by thresholds well below a user's monthly payments activity, as this would still limit consumer risk by any single new market Digital Asset Facility.

Our members are supportive of an approach using aggregate asset value as the key threshold to exempting low-value facilities from the proposed regulatory regime. However, in line with the low-value exemption for Purchased Payment Facilities (PPFs) under Australian payment regulation, our members propose that a $10 million threshold be considered. The stored value facility exemption is a closer equivalent and better matches risks where assets are held for customers, and this threshold more appropriately suits the nature of crypto assets with high volatility. Such a threshold also promotes alignment and consistency across regulatory frameworks, and provides scope for new market entrants to manage their customers' risk.

We also propose that a reasonable and appropriate method be used for the calculation of the value of assets held on the platform, that takes into account the volatility of market prices of crypto assets. One such method of calculation would be to utilise a rolling 3 month average of the value of assets held on the platform. This method would assist managing volatility which is not caused by the platform and, coupled with a safe harbour process to apply for a licence, would appropriately manage the risks facing consumers and provide a clear pathway for businesses to obtain licensing as they grow.

Questions (Set 3)

What would be the impact on existing brokers in the market? Does the proposed create additional risk or opportunities for regulatory arbitrage? How could these be mitigated?

We understand that the proposed framework referenced in this question is an application of the dealing authorisation under s766C and the incidental exemption under s763E but applied to digital asset facilities that are dealing in digital assets.

Given a number of our members are considered ‘brokers’ under a common industry definition of that term, we request that clarification is provided on what is considered a ‘broker’ under the regulatory framework. Our members are of the understanding that a ‘broker’ under the proposed regulatory framework will refer to a platform or person who deals in, or arranges for another person to use, a digital asset facility, while members who are brokers in the traditional sense will be deemed issuers of a digital asset facility. This is an important clarification for our members.

Based on our understanding, we are supportive of the proposed requirement to hold a licence under 3.1(d) and the ‘incidental’ exemption proposed under 3.1(e). We believe this incidental exemption will allow merchants to operate using regulated digital asset facilities, promote innovation of new use cases, while ensuring consumers are still protected.

Questions (Set 4)

Are the financial requirements suitable for the purpose of addressing the cost of orderly winding up? Should NTA be tailored based on the activities performed by the platform provider?

Does the distinction between total NTA needed for custodian and non-custodian make sense in the digital asset context?

The paper proposes the primary purpose of the NTA requirement for custodians of assets is to ensure there is sufficient operating capital for the orderly winding up of the platform. However, our members are of the opinion that an NTA requirement for custodians linked to the value of funds held by the platform is not the most appropriate or effective means of ensuring this underlying purpose is met.

Firstly, linking an NTA requirement to the value of, at times, assets with high degrees of volatility poses operational challenges for platforms. Capital raising to meet growing NTA requirements can take significant amounts of time, noting market movements in asset prices occur rapidly, creating a timing issue for platforms.

Secondly, and most importantly, linking an NTA requirement for custodians to the value of assets held does not necessarily mitigate the risk for which the requirement is imposed - namely the risk that there is insufficient operating capital for the orderly winding up of a platform. Linking the NTA requirement with a metric more closely related to the costs of winding up a company would better serve this purpose.

On this basis, we propose that the NTA requirement starts at $1m and scales in line with 6 months' of the platform operating expenditure up to a max NTA requirement of $5 million. If Treasury is inclined to keep the NTA linked to the value of assets held on the platform, we similarly request that the NTA requirement starts at $1m and scales in line with 0.5% of the value of assets held on the platform up to a maximum NTA requirement of $5 million.

With regards to the question of NTA requirements tailored to the activities performed by the platform, we do not believe this is required, particularly if the NTA requirement is linked to the operating expenditure of the platform.

Our members believe the distinction between a custodian and non-custodian makes sense in the digital asset context.

Given the industry in which we operate and the nature of assets commonly held by Digital Asset Platforms, our members request clarification and confirmation of whether digital assets, both stablecoins and non-stablecoins alike, are considered 'cash equivalents' for the purposes of meeting the NTA requirement. Our members propose that the definition of 'cash equivalents' be expanded to include asset backed stablecoins (or 'payment stablecoins' as referenced by Treasury's Payments System Modernisation (Licensing: Defining Payment Functions) Consultation Paper).

Questions (Set 5)

Should a form of the financial advice framework be expanded to digital assets that are not financial products? Is this appropriate? If so, please outline a suggested framework.

Do not extend the application of the financial advice framework to digital assets that are not financial products. Tokenisation of an asset does not change the underlying properties of an asset. It does not make sense to apply the framework to an asset that is not a financial product on the basis that that asset has been tokenised.

However, a customer engaging with a licensed financial adviser will likely expect the adviser to be able to provide advice not only on the digital asset facility to use, but also the digital assets they should invest in. It is unlikely that this customer will be aware of the distinction between digital assets that are financial products and those that are not financial products. We recommend that clarity and guidance is provided to licensees operating under this regime on how to assess whether a digital asset is a financial product. Ensuring advisers are clear and confident on which digital assets they are authorised to provide financial advice on will mitigate the risks of customers falling prey to unlicensed advice.

We further recommend approaching the regulation of financial advisers carefully to avoid unnecessarily increasing the cost of advice, thereby impacting the affordability and accessibility of advice to consumers who need it most.

Questions (Set 6)

Automated systems are common in token marketplaces. Does this approach to pre-agreed and disclosed rules make it possible for the rules to be encoded in software so automated systems can be compliant?

Should there be an ability for discretionary facilities dealing in digital assets to be licensed (using the managed investment scheme framework or similar)?

For facilities in which digital assets are traded in a discretionary facility, akin to passively managed or actively managed funds, further consultation should be done in understanding their risks and characteristics. At a high level, such products share many similarities with managed investment schemes.

Questions (Set 7)

Do you agree with the proposal to adopt the 'minimum standards for asset holders' for digital asset facilities? Do you agree with the proposal to tailor the minimum standards to permit 'bailment' arrangements and require currency to be held in limited types of cash equivalents? What parts (if any) of the minimum standards require further tailoring?

The 'minimum standards for asset holders' would require tokens to be held on trust. Does this break any important security mechanisms or businesses' models for existing token holders? What would be held on trust (e.g. the facility, the platform entitlements, the accounts, a physical record of 'private keys', or something else)?

Our members are supportive of adopting the minimum standard for asset holders for digital asset facilities, including the requirement that digital assets be held on trust. The trust arrangement should ensure protection for consumers in the event of an insolvency of the digital asset custodian.

The answer to the question regarding whether tokens being held on trust break important security mechanisms or business models is dependent on the detailed requirements of the trust arrangement. For example, platforms, both brokers and exchanges, often hold digital assets in an omnibus arrangement.

Additionally, we note that there is consensus among DCE members that the industry at large would benefit from the ability to hold on trust and segregate client assets in fiat currency. However, the current banking environment forces most DCE members into either offshore banks, non-ADI payment providers, or one or two small banks. This creates potential systemic risk in

Australia, similar to what took place in the US in March 2023 as a result of a bank having a heavy concentration of highly correlated customers (DCEs in this case), or Australian consumers at risk of loss due to the failure of an offshore bank holding a domestic DCE's funds. We highly recommend Treasury address the issue of debanking of the digital asset industry and enforce the provision of trust accounts for regulated Digital Asset Facilities under the new framework.

Questions (Set 8)

Do you agree with proposed additional standards for token holders? What should be included or removed?

Our members are, in principle, supportive of the additional requirements for token holders and are appreciative of the Treasury proposing tailored requirements that are appropriate to our industry and the underlying technology, while also providing sound protections for customers.

However, we request that further clarification is provided with regards to the practical application of the proposed requirements. The further clarification that is requested is outlined below:

- Section 4.1(b)(i) requires tokens be held through arrangements that ensure tokens are safeguarded in ways that "reasonably balances security and the timely processing of requests to exercise platform entitlements." We are supportive of this principle, but request that further details and examples of how this should practically be implemented by our members be provided; and,
- Section 4.1(b)(ii) requires tokens to be only held "using custody software that is continuously monitored and routinely audited." Again, we are supportive of this requirement and given the importance of the integrity of software used to hold tokens, are of the opinion that this will help ensure customer assets are appropriately safeguarded. We request that "continuously monitored" be defined further, outlining the practical requirements of how such software should be appropriately monitored on a continuous basis. Similarly, we request that "routinely audited" be defined further. We submit that a guide such as a requirement that the provider of custody software be ISO27001 audited and certified and undergo annual Penetration tests by an appropriately experienced third party Penetration Testing provider would provide a suitable standard.

Questions (Set 9)

This proposal places the burden on all platform providers (rather than just those facilitating trading) to be the primary enforcement mechanism against market misconduct.

Do you agree with this approach? Should failing to make reasonable efforts to identify, prevent, and disrupt market misconduct be an offence?

Should market misconduct in respect of digital assets that are not financial products be an offence?

Our members agree with the Treasury's proposed minimum standards for intermediating platform entitlements and transactional functions. The requirement to make reasonable efforts to identify, prevent and disrupt market misconduct on platforms should focus on methods used to identify market abuse based on:

(a) a thorough risk assessment by the platform; and

(b) the nature, scale and complexity of the platform's business.

The nature of a global and highly mobile crypto-asset industry means digital asset platforms face a different set of risks of market misconduct. Specifically, these businesses do not operate in an environment similar to traditional tier 1 and tier 2 financial product exchanges, and should be required to have reasonable procedures and controls in place for their own platform to deter and disrupt market misconduct. Trading is the principal nexus where market misconduct will likely occur and we submit any offence should be limited to trading on digital asset platforms.

However, we suggest that the requirements to identify, prevent and disrupt market misconduct be broken down into 'minimum requirements' and 'additional requirements', with the minimum requirements applying to all platform providers and the additional requirements applying specifically to those platform providers who are operating the underlying order books and pairing buyers and sellers within a transaction. These two sets of requirements are to reflect the fact that not all platform providers in the ecosystem (for example 'Brokers') have the ability and access to identify, prevent and disrupt market misconduct to the extent that those in the ecosystem who are operating the underlying order books (for example 'Exchanges').

We understand the policy desire to have digital asset platforms work together to attain a 'complete picture of transactions occurring in the token ecosystem'. It is important that platforms, regulators and other relevant organisations collaborate to achieve this objective in the longer term. We believe it would be appropriate for 'failing to make reasonable efforts to identify, prevent, and disrupt market misconduct' to be an offence only if this complete picture were in place.

Market surveillance requirements applicable to traditional tier 1 exchanges would be less relevant or applicable for the digital asset platforms due to the differences in how price discovery works.

With respect to token disclosure requirements for non-financial products proposed, our members agree with the approach outlined under section 4.3(f). Our members, however, are strongly opposed to the application of Design and Distribution Obligations (DDO) to non-financial products. Our members believe Target Market Determinations (TMD) should be required for financial products at the facility level only rather than at the token level regardless of whether the tokens are grouped as a 'series' or individual (unless the token is a financial product). Ongoing changes in price, utility, market sentiment for tokens occur frequently, and continual disclosure would be needed to meet requirements. Holding non-financial products to the DDO and TMD standard is unnecessary and uneconomical.

Questions (Set 10)

The requirements for a token trading system could include rules that currently apply to 'crossing systems' in Australia and rules that apply to non-discretionary trading venues in other jurisdictions.

Do you agree with the suggested requirements outlined above? What additional requirements should also be considered?

Are there any requirements listed above or that you are aware of that would need different settings due to the unique structure of token marketplaces?

Digital asset platforms have limited control over some matters such as the impact of forking events and customers sending tokens to platforms via unsupported networks. Each platform's business operating model will have its own way of responding to and managing each type of scenario. Each platform's response will differ depending on what makes strategic and commercial sense for them. As such, while the industry is generally supportive of the overall approach for token trading, we caution Treasury against any overly prescriptive regulation in this area which may reduce the degree of autonomy needed for platform businesses to operate uniquely and competitively.

For example, we support the proposal requiring that digital asset platforms with token trading functions to have policies and procedures that implement measures for recovering tokens sent by account holders to the platform provider's correct address on the wrong network, where technically possible. However we would not support a requirement to provide such a service free of charge.

In relation to token listing, to meet the requirement for assessing networks against the objective criteria outlined, there must be sufficient public information for all tokens. This is not the case. For some tokens, the required information simply cannot be obtained. We do not support the prescriptive approach to requirements for assessing token networks under 5.1(d)(i). We believe a more suitable approach would be to require that these criteria are assessed against what information is publicly available at the time of the listing and reasonable steps being required to update the information when it becomes available, and should not be held liable for misstatements made by token issuers which the platform relies upon in listing a token.

Questions (Set 11)

What are the risks of the proposed approach? Do you agree with the suggested requirements outlined above? What additional requirements should also be considered?

Does the proposed approach for token staking systems achieve the intended regulatory outcomes? How can the requirements ensure Australian businesses are contributing positively to these public networks?

Our members agree the approach for token staking systems should achieve the intended regulatory outcomes and are generally supportive of the requirement for digital asset platforms to assess node validators and to provide disclosures.

However, in relation to objective criteria to be applied for assessment, there needs to be sufficient public information for all tokens in order to meet this requirement. As mentioned above, the required information cannot be obtained for some tokens. Therefore we do not support the prescriptive approach to requirements for assessing token networks under 5.2(e)(i). We believe a more suitable approach would be to require that these criteria be required to be assessed where the relevant information is available at the time of product launch and updated.

In providing account holders with a direct entitlement to 'unstake' any staked assets, platform providers will need to ensure entitlements to unstake are reasonable and take into account the applicable unbonding or lockup periods associated with particular assets and proof of stake networks. This means certain staked assets not necessarily being available to the user 'at call'. Our members request that the regulatory framework take this into account and allow platform providers to operate within the parameters of the respective proof of stake networks, with appropriate disclaimers provided to customers.

Questions (Set 12)

How can the proposed approach be improved?

Do you agree with the stated policy goals and do you think this approach will satisfy them?

Where platform providers offer the tokenisation function as a service, we agree the proposed approach is appropriate. However, questions arise as to whether entities that tokenise assets direct to members of the public will be unregulated, whether these entities will be required to use a regulated platform provider as an intermediary, and whether asset-tokenising entities will have the option of obtaining their own digital asset facility licence as an alternative to using an intermediary.

Further to the above, we request that the term 'programmed' under section 5.3(h) be further defined in order to determine whether the requirements under this section are practical or possible.

Questions (Set 13)

Is requiring digital asset facilities to be the intermediary for non-financial fundraising appropriate? If so, does the proposed approach strike the right balance between the rigorous processes for financial crowdsource funding and the status quo of having no formal regime?

What requirements would you suggest be added or removed from the proposed approach? Can you provide an alternate set of requirements that would be more appropriate?

Our members believe that the proposed approach for funding tokenisation will *not* satisfy the policy goal of supporting Australian entrepreneurs, creative producers, researchers, not-for-profits, and software developers or implementing controls to mitigate risks. The proposed requirements are disproportionately onerous on intermediaries and those who seek to use the technology of tokens for a non-financial purpose. The principle of technology neutrality is violated if a non-financial product or fundraising (such as the sale of a token which is not a financial product) and licensing is required as a result of the choice of technology. It is likely that issuers of tokens (whether NFTs or other tokens) will continue choose to launch elsewhere and Australian consumers will be deprived the protections of the Australian legal system and potentially be denied the ability to access, and simply partake from other platforms by finding participating through offshore vendors.

We submit that issues around non-financial fundraising are worthy of further consultation, and detailed consideration of their own bespoke process, and should be deferred until that has occurred and any regulation is properly technologically neutral and contains clear delineation of financial product tokens and non-financial product tokens, if that is not to be introduced within this framework.

Questions (Set 14)

Do you agree with this proposed approach? Are there alternate approaches that should be considered which would enable a non-financial business to continue operating while using a regulated custodian?

Custodians by their nature, within the proposed approach, will require licensing. Non-financial businesses interacting with a custodian who is licensed, should not also bear the responsibility of licensing, if Australia is regulating who holds an asset, provided that asset is a financial product.

That would be double dipping who requires a licence, and bears final responsibility for those assets.

An AFSL should not be required for non-financial business, forcing them to use “custodial only arrangement” platforms. This requirement will limit startups in Australia in the ways they can innovate, due to the restrictive format of receiving the custody-only arrangement of regulated custodians.

Questions (Set 15)

Should these activities or other activities be added to the four financialised functions that apply to transactions involving digital assets that are not financial products? Why? What are the added risks and benefits?

As debentures and margin lending products are inherently higher risk products, our members are pleased to see the provision of some clarity over these activities and arrangements sooner rather than later. These activities align with ASIC’s recent enforcement actions and we believe their addition as financialised functions for regulation is appropriate, but that further consultation should be undertaken to set the regulatory burden appropriately.

Questions (Set 16)

Is this transitory period appropriate? What should be considered in determining an appropriate transitionary period?

The currently experienced processing times for ASIC to consider an Australian Financial Services Licence raise concerns with our members about the 12 month transition period, as a great burden will be placed on the regulator to process what is likely to be a large number of licence applications in that period (estimated to be in excess of 100 simultaneous applicants).

ASIC already advises that innovative or complicated licence applications are likely to take longer to assess, and our members report that crypto related or crypto-adjacent licence applications appear to fall well outside the current ASIC Service Charter timelines, no doubt due in part to ASIC taking care to carefully consider the novel issues which may arise and the ongoing regulatory gaps. It may well be that the licensing framework provides sufficient certainty to assist ASIC in reducing the processing times experienced and that ASIC has additional funding to ensure all licence applications are made within the transitionary period, and the importance of an orderly transitionary period .

Additional time will be required for platform providers seeking to use a sub-custodian which have been excluded by the $5m NTA requirement, so that an ASIC-licensed sub-custodian service can be found. Currently no such service provider exists in the market.

Negotiating onboarding with a custodian can be a major exercise and often takes many months.

Where a facility is no longer subject to the low-value facility exemption, additional time will be required for the platform provider to apply for a new licence or authorisation and continue operations until the application is approved or rejected by ASIC.

We submit that a transitionary period which is linked to a licence application being submitted, with safe harbour applying until determination of that licence application, would resolve concerns around a 12 or 24 month period of transition. This would mean that applicants need to submit their licence application by the deadline rather than have their application approved by the deadline. This would also provide ASIC with the time they may need to process such licence applications. Additional safe harbour should be provided to DCEs and brokers, where their chosen custodian's application is denied by ASIC, such that they have a practical timeframe to find an alternative.