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The Treasury  
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Dear Sir/Madam

### **Treasury 'Initial Coin Offerings' Issues Paper - Blockchain Australia Submission**

Blockchain Australian (**BA**) would like to thank Treasury for the opportunity to provide a submission on the 'Initial Coin Offerings' Issue Paper issued by Treasury in January 2019.

BA is Australia's leading community association dedicated to:

- Education;
- Policy Development; and
- Promotion of Blockchain and Digital Currency in Australia.

Our primary aim is to foster a culture of innovation, sharing and collaboration in the blockchain ecosystem to ensure that Australian businesses and individuals can reap the numerous rewards that blockchain technology offers.

We respond to the various questions posed by Treasury in the Paper as set out below.

#### **1.1. What is the clearest way to define ICOs and different categories of tokens?**

Blockchain Australia (**BA**) generally agrees with the way in which Treasury has described ICO in its paper and the various categories of tokens. However, we note the following additional types of tokens:

- (a) Collectibles (E.g. Crypto Kitties);
- (b) Sovereign issued tokens (E.g. Petro); and
- (c) Privacy coins (e.g. Monero).

#### **2.1 What is the effect and importance of secondary trading in the ICO market?**

Secondary trading is integral to the ICO market for the reasons set out in Treasury's paper and the following additional reasons:



- (a) Investors are more likely to acquire tokens that are liquid as compared to illiquid tokens. This attracts capital at the ICO stage because acquirers know they can dispose of the token when they want to.
- (b) Liquidity allows acquirers to acquire tokens in the secondary market if they were unable to participate in the initial offer.
- (c) Liquidity reduces brokerage fees associated with traditional capital raising and allows Australian start up businesses to access capital outside of the traditional IPO.
- (d) Liquidity allows for price discovery for forks of a token.
- (e) It is also likely to bring institutional investors to the table when pre-sales are made to institutional investors at a discount (usually early on in a token offer), as they know that they can sell their tokens when the tokens are ultimately listed on an exchange.
- (f) Liquidity for businesses that raise through an ICO by accepting other crypto currencies that they can dispose of as and when required to fund their projects.
- (g) Liquidity also allows the development of new financial products – eg ETFs and derivatives over crypto currencies.

BA notes that a regulatory framework is required for market manipulation in the crypto currency space (where the tokens are not financial products listed in a financial markets exchange).

## **2.2 What will be the key drivers of the ICO market going forward?**

- (a) A clear regulatory framework for ICOs given that the action taken by various regulators around the world (including ASIC) has caused concern and thwarted a number of projects that were going to be undertaken in Australia. BA understand that this is primarily as a result of the broad definition of a managed investment scheme in Australia that is likely to capture all types of ICOs. See further discussion of this point in section 4.
- (b) Being able to approach ASIC for “Ruling” type guidance. We understand that ASIC (Innovation Hub) has a tendency to tell all persons thinking of undertaking an ICO that they will likely be operating a managed investment scheme and to seek legal advice. We seek clear ASIC guidance (with worked examples) on the ICO models that it views as being subject only to consumer protection laws.
- (c) The time and cost involved in establishing a managed investment scheme and the fact that generally there are no assets being held for investors in an ICO, means that the MIS regime is not an appropriate regulatory regime for



ICOs. The MIS regime was established in relation to the funds management industry (where there is a beneficial interest in an underlying asset) and was not designed for token offerings. Further if an ICO were treated as a MIS, interests in the scheme could not be listed on a crypto exchange and would need to be listed on a financial market exchange. This is prohibitive as it is unlikely that the tokens or projects would meet the requirements of the listing rules of a licensed securities exchange.

- (d) Lack of regulatory friction and legal certainty with a specific regulatory regime for ICOs would likely be a key driver of the growth of the ICO market in Australia.
- (e) Real world use products and cases funded by ICOs are also likely to drive ICO growth in Australia.
- (f) Developing minimum technology and security standards for projects is also likely to be a key driver.
- (g) Clear tax guidance for issuers and consumers to invest in ICOs and maybe even tax incentives for investors (e.g. ESIC).

### **3.1 How can ICOs contribute to innovation that is socially and economically valuable?**

- (a) Less onerous (to the MIS regime) and clear regulatory framework will encourage innovation that is economically viable – i.e. less regulatory uncertainty and friction.
- (b) More access to capital means more start-ups will be funded and start-ups are generally more inclined to innovate.
- (c) There is not a lot of venture capital funding in Australia and having an appropriate regulatory framework for ICO's will mean that more ventures will be funded.
- (d) Examples include Agrichain, Powerledger, Canya, Soar, Horizon State – all of which have put Australian blockchain start-ups on the world stage attracting global attention, talent and capital to Australia that may not have otherwise occurred.
- (e) If Australia does not create an appropriate legal framework it is likely that we will lose business and talent to overseas markets. In that regard having an appropriate regulatory framework is an opportunity and not doing so is a threat to the industry which is likely to move offshore to jurisdictions with a friendlier regulatory framework.

### **3.2 What do ICOs offer that existing funding mechanisms do not?**



- (a) Founders are not necessarily giving away equity and are gaining access to a wider market of investors.
- (b) Giving access to the general public to opportunities to invest in a start-up venture (cf a company) that they would usually not have access to.
- (c) Access to global capital if the token is not a security or financial product.
- (d) Allowing someone to invest without going through an intermediary (e.g. brokers) and doing away with broker and underwriter fees.
- (e) Consumers than acquire tokens can become part of the project by acquiring tokens that will be used for the project.
- (f) The crowdfunding nature of ICOs means that consumers can invest very small amounts as compared to a minimum \$500 for listed shares
- (g) Digitisation of assets - how assets are owned and wealth distributed will change.

**3.3 Are there other opportunities for consumers, industry or the economy that ICOs offer?**

- (a) Access to investments (consumers) and capital (industry) that they otherwise might not have access to.
- (b) Consumers funding projects that they will use which is customer acquisition for projects as well as fundraising.
- (c) Job creation in Australian, with the chance to become a world leader in blockchain technology.
- (d) Fostering innovation in Australia.
- (e) Creating new competitive business models – eg. Powerledger
- (f) The creation of micro communities and economies.
- (g) Speed of fundraising, less complex way of raising, lowers costs of raising money.

**3.4 How important are ICOs to Australia's capability to being a global leader in FinTech?**

- (a) Blockchain businesses have flocked to jurisdictions that have created specific regulatory frameworks. Billions of dollars of investment capital has flocked to jurisdictions that have established a specific regulatory framework for ICOs (e.g. Malta, Gibraltar etc).

- (b) Fintechs generally leads in innovation and ICOs are a form of innovation funding.
- (c) Innovation will attract the talent and capital that is required to be a global leader.

**3.5 Are there other risks associated with ICOs to raise with policymakers and regulators?**

- (a) Fraud.
- (b) Misleading and deceptive conduct.
- (c) Not being able to deliver what is set out in the whitepaper - technologically and/or the right people and/or not having sufficient funding.
- (d) Not having a proper/sustainable tokenomic model.
- (e) Issuer suggesting they are not required to do what is set out in the whitepaper.
- (f) Issuers raising large amounts of money and only a small portion is used to fund the project.
- (g) Access to unsophisticated investors.
- (h) Unsophisticated investors not being properly educated on the maintenance and use of private keys.
- (i) Someone solves the computer science problem of  $p$  versus  $np$ .
- (j) Not having minimum industry standards that are required to be complied with (including disclosure, technology and security).

**4.1 Is there ICO activity that may be outside the current regulatory framework for financial products and services that should be brought inside?**

BA's preference would not be to bring activity into the current regulatory framework but rather the current regulatory regime is too uncertain and/or too unnecessarily onerous for ICOs. See the discussion in section 4.2 for more information.

Although ASIC has stated that there are ICO models that are only subject to consumer laws, it has not provided any clarity on which ICO models would fall into this category.

**4.2 Do current regulatory frameworks enable ICOs and the creation of a legitimate ICO market? If not, why and how could the regulatory framework be changed to support the ICO market?**

- (a) No - Based on feedback from ASIC, members and lawyers, there is a significant risk that all ICOs are managed investments schemes under Australian law.
- (b) The definition of a managed investment scheme is so broad that it is likely to capture all ICOs.
- (c) The managed investment scheme regime (licensing, registration and disclosure) is not appropriate for ICOs unless it involves the securitisation of an asset (e.g. where an issuer wants to tokenise units in a trust that will hold real property or some other asset or an underlying asset is held on trust for ten holders).
- (d) All ICOs should be excluded from the MIS definition and financial product definition but should be subject to registration and disclosure obligations that include minimum standards (governance, KYC, technology, privacy and security). The exemption should not apply where the ICO merely involves the tokenisation of a security or an interest in a managed investment scheme.
- (e) Crypto currencies networks should be excluded from the requirement to hold a non cash payment facility AFSL but should be subject to minimum disclose obligations that include minimum standards (governance, KYC, technology, privacy and security).

**4.3 What, if any, adjustments to the existing regulatory frameworks would better address the risks posed by ICOs?**

- (a) Creating a minimum disclosure and liability regime for people involved in preparing a whitepaper where it is not regulated as a financial product.
- (b) Bespoke governance body that looks in on those teams doing the ICOs E.g. review board.
- (c) Making any specific regulatory regime subject to compliance with minimum standards set through an industry body.

**4.4 What role could a code of conduct play in building confidence in the ICO industry? Should any such code of conduct be subject to regulator approval?**

- (a) We encourage the adoption of a code of conduct that has minimum standards for disclosure, technology and security). We agree that the code should be subject to regulatory approval



- (b) This would take some time to develop and agree with a regulator so there should be provision for self-regulating industry standards as interim measure.
- (c) Having such standards (assuming compliance with them) would deal with a number of the risk identified above and would also bring greater legitimacy to the ICO industry.

**4.5 Are there other measures that could be taken to promote a well-functioning ICO market in Australia?**

- (a) As above
- (b) Adopting best practice from other countries. For example the work done by the Token Economy Association of Singapore.
- (c) ASIC providing clear guidance with example of when an ICO is or isn't a financial product.

**5.1 Does the current tax treatment pose any impediments for issuers in undertaking capital raising activities through ICOs? If so, how?**

We have been provide with a draft of the submission to be made on this question by Hall & Wilcox and we agree with that submission.

**5.2 Is the tax treatment of tokens appropriate for token holders?**

We have been provide with a draft of the submission to be made on this question by Hall & Wilcox and we agree with that submission.

**5.3 Is there a need for changes to be made to the current tax treatment? If yes, what is the justification for these changes?**

We have been provide with a draft of the submission to be made on this question by Hall & Wilcox and we agree with that submission.

We welcome the opportunity to engage further with Treasury on any aspect of our submission. Please don't hesitate to contact myself or any BA board member.

We would like to acknowledge the assistance provided by John Bassilios from Hall & Wilcox in preparing this response.

Yours faithfully

Alex Saunders

Board Member - Blockchain Australia