



27 May 2022

Director – Crypto Policy Unit
Financial System Division
The Treasury
Via email: Crypto@treasury.gov.au

Dear Sir/Madam,

Crypto asset secondary service providers: Licensing and custody requirements

Chartered Accountants Australia and New Zealand (CA ANZ) welcomes the opportunity to provide feedback on the *Crypto asset secondary service providers: Licensing and custody requirements* consultation paper (consultation paper). We have focused our feedback on those areas where we consider we can add the most value.

Appendix A provides further information about CA ANZ.

General comments

There is currently limited regulation of the crypto asset ecosystem (digital currencies, blockchain etc) in Australia and overseas. Unlike the consumer data right regime, the identification of individuals or businesses engaging in crypto asset transactions does not form part of the typical transaction lifecycle. Missing elements, such as this, could be inadvertently undermining investor confidence and market integrity in the crypto asset ecosystem.

Currently, the rapidly evolving crypto asset ecosystem (crypto) does not clearly fit into Australia's traditional regulatory frameworks. Robust regulation and guidelines, which could be considered in stages, are needed to protect consumers today and build long term trust in crypto.

The introduction of a robust licensing and custody requirements of crypto-asset secondary service providers (CASSPs) may assist in dispelling misconceptions about the US \$2.6 trillion (global) industry, increase credibility and promote investment in crypto assets. However, obligations under proposed licensing and custody should be fit for purpose and be accompanied by appropriate frameworks to support ongoing monitoring and enforce compliance.

It will be key for Government, in partnership with industry, to develop regulations and address existing regulatory gaps to meet the needs of the economy, promote confidence as well as encourage innovation and future growth in the industry.

A challenge for Government will be keeping pace with developments in the crypto asset space such as decentralised finance (DeFi) and protecting Australian consumers when they invest in crypto assets offered by foreign providers. Working with other overseas jurisdictions will be important to determine a collaborative approach and to limit the risk of regulatory arbitrage.

Consultation questions

1. Do you agree with the use of the term Crypto Asset Secondary Service Provider (CASSPr) instead of 'digital currency exchange'?

Yes. We agree that the term is more precise. However, consumers may not understand which organisations or services are captured under the 'secondary service provider' terminology. It may be suitable to also have some separate terms which capture each secondary service for the purpose of consumer education and communication; for example, crypto asset custody and storage, crypto asset exchange, brokerage and dealing services and crypto asset peer-to-peer market.

2. Are there alternative terms which would better capture the functions and entities outlined above?

The crypto asset ecosystem and structure is complex and uses terms which may be misunderstood or not easily understood by all users. It may be useful if the terms used were in plain language, easy to understand and captured specific elements.

Understanding the risks of investing in the crypto asset ecosystem is the responsibility of both providers and investors. We encourage providers to translate their offerings for a wider consumer reach as well as investors to make knowledgeable investment decisions, particularly when engaging with crypto asset ecosystem.

4. Do you agree with the proposal that one definition for crypto assets be developed to apply across all Australian regulatory frameworks?

We consider consistency of a crypto asset definition across all Australian regulatory frameworks is vital to reduce complexity. While we support one definition for crypto assets it must be developed with consideration of the existing definitions for financial products, in particular, existing derived products. A single definition could also incorporate sub-parts to assist in categorisation of crypto 'products' that already fall under the derivatives definition of a current AFSL.

5. Should CASSPrs who provide services for all types of crypto assets be included in the licensing regime, or should specific types of crypto assets be carved out (e.g. NFTs)?

We consider CASSPrs who provide services for all types of crypto assets should be included in the proposed licensing regime. A two-step process, with sufficient implementation time, should be considered to allow existing CASSPrs to transition to a licensing regime.

A potential unintended consequence of carving out specific types of crypto assets from the regime could be CASSPrs disproportionately offering those products to avoid licencing and compliance obligations.

6. Do you see these policy objectives as appropriate?

The policy objectives proposed appear appropriate, however we raise concern in relation to the wording of the second objective which relates to the AML/CFT regime. We consider integration (as opposed to support) with the AML/CFT regime would provide greater certainty on how the proposed licensing regime would support and strengthen the AML/CFT regime.

This reflects our position for consistency across all Australian regulatory frameworks. Regulation of CASSPrs should define them as financial service providers and any service related to a crypto asset should be defined as a designated service.

10. How do we best minimise regulatory duplication and ensure that as far as possible CASSPrs are not simultaneously subject to other regulatory regimes (e.g. in financial services)?

The overall purpose of regulatory requirements should be considered collaboratively across Government departments. A review of current regulation and any existing regulatory gaps should be performed to limit potential duplication. Regulatory requirements should not be limited to the Australian jurisdiction, but also include international requirements which could be translated to apply locally.

We note in March 2022 ASIC has released INFO 269 – Discussing financial products and services online for social media influencers and Australian Financial Services Licensees (AFSLs) using influencers. ASIC also conducted one-on-one interviews with a sample of influencers and AFSLs and gained an understanding of some of the industry's issues, including the fact that the current playing field is not level – advisers are far more strictly controlled than product providers offering crypto assets. We welcome all industry stakeholders working collaboratively to 'fix' the potential for many investors, that invest in crypto assets unaware that they are unregulated, ending up losing money and having no consumer protection to rely on.

The impact (and resources required) for CASSPrs to meet regulatory requirements should be further considered through direct feedback from industry and relevant stakeholders.

11. Are the proposed obligations appropriate? Are there any others that ought to apply?

As noted above, the proposed licensing regime and its interaction with AML/CFT is a clear policy objective. Consideration of the know your client (KYC) requirement under AML/CFT will be one of the key provisions, which in our opinion, could strengthen market integrity in crypto.

Obligation 12 (page 17 of the consultation paper) under the proposed licensing regime is unclear if due diligence procedures will be carried out on individuals who establish and operate CASSPrs or the consumers investing in crypto-assets. We consider it important that identity verification of those both operating and transacting within the crypto asset ecosystem is carried out and this should be made clear within licence obligations.

Further clarity and detail related to proposed obligation (11) '*be regularly audited by independent auditors*' will be essential to ensure this part of the regime is proportionate and effective. Key aspects include:

- Assurance standards, and consistency with the standards issued by the Australian Auditing and Assurance Standards Board (recommend referral to AUASB Staff Guide for Prescribing Assurance and Related Services)
- Qualification and experience requirements for assurance practitioners
- Regulatory framework and oversight
- Potential need for differential assurance requirements for different industries and entity size

We recommend that the Treasury design and establish assurance requirements that are workable, and consistent with existing practice, regulatory frameworks and standards, consultation with the Australian Auditing and Assurance Standards Board and auditing profession will be critical – CA ANZ would be pleased to assist in facilitating this engagement.

We suggest expanding obligation 6 (comply with client money obligations) and 13 (maintain adequate custody arrangements) to extend to include maintaining adequate security controls for management of client private keys.

13. Should there be a ban on not providing advice which takes into account a person's personal circumstances in respect of crypto assets available on a licensee's platform or service? That is, should the CASSPrs be prohibited from influencing a person in a manner which would constitute the provision of personal advice if it were in respect of a financial product (instead of a crypto asset)?

We believe that CASSPrs should be prohibited from seeking to influence a person to acquire, hold or dispose of any crypto holdings under current regulations. However, if they are brought in line with the requirements of existing product providers who require an AFSL, then there should be no need for separate prohibitions.

15. Do you support bringing all crypto assets into the financial product regulatory regime? What benefits or drawbacks would this option present compared to other options in this paper?

If Treasury decides to bring all crypto assets into the financial product regulatory regime (under the *Corporations Act 2001* (Cth)), we suggest that a tailored approach is adopted, with a specific licence category for crypto.

The characteristics of crypto assets, some of which are inherently different to financial assets and incompatible with existing regulatory frameworks, are evolving and as such a Government regulator would need appropriate powers to amend the requirements based on risks that emerge at any point in time.

INFO 269 should assist influencers in their understanding of existing laws within both the *Corporations Act 2001* (Cth) and the *Australian Securities and Investments Commission Act 2001* (Cth) pertaining to them. Given the amount of crypto advertising currently taking place through social media platforms, it would seem wise for regulation within this sector to be implemented sooner rather than later.

The findings of the Australian Law Reform Commission Review into the Financial Services Legislation and the Quality of Advice Review may influence the financial product and advice landscapes. Any changes made in this area need to be flexible and streamlined so that significant changes are not imposed in piece-meal tranches over a prolonged period, as this leads to inefficiencies and uncertainty for all stakeholders – product providers, advisers and consumers.

17. Do you support this approach instead of the proposed licensing regime? If you do support a voluntary code of conduct, should they be enforceable by an external dispute resolution body? Are the principles outlined in the codes above appropriate for adoption in Australia?

Given the international nature of the crypto asset ecosystem, we support co-regulation whereby the industry develops and administers codes backed by a government regulator who can enforce compliance.

We support the Australian Securities Investment Commission (ASIC) as the regulator of the CASSPr licensing regime. We suggest that there is consideration of how the Financial Services and Credit Panel (FSCP) could apply in either the proposed licensing regime or self-regulation.

21. There are no specific domestic location requirements for custodians. Do you think this is something that needs to be mandated? If so, what would this requirement consist of?

With the nature of the crypto ecosystem, a domestic location requirement for custodians in Australia may inadvertently shift custodians offshore to unregulated locations. We suggest that the government considers if foreign custodians could become members of Australia's financial complaints Authority (AFCA) to show their commitment to consumers.

31. Are there other examples of crypto asset that are financial products?

Based on feedback from some of our members, we understand that Crypto asset holders have experienced high volatility in recent times and as such has impacted the value of their portfolio. Consequently, a market has emerged whereby services/offers provide liquidity to crypto asset holders by letting them use their holdings as collateral in exchange for cash without having to sell their crypto. Although in its infancy in some parts of the world, an increasing trend could see investor appetite/trading of this collateral in the foreseeable future, which would imply a derivatives market that is more of a financial product in nature.

Should you have any questions about the matters discussed above or wish to discuss them further, please contact Karen McWilliams via email at karen.mcwilliams@charteredaccountantsanz.com or phone (612) 8078 5451.

Yours sincerely



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Group Executive
Advocacy & Professional Standing



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Appendix A

About Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand (CA ANZ) represents 131,673 financial professionals, supporting them to make a difference to the businesses, organisations and communities in which they work and live. Chartered Accountants are known as Difference Makers. The depth and breadth of their expertise helps them to see the big picture and chart the best course of action

CA ANZ promotes the Chartered Accountant (CA) designation and high ethical standards, delivers world-class services and life-long education to members and advocates for the public good. We protect the reputation of the designation by ensuring members continue to comply with a code of ethics, backed by a robust discipline process. We also monitor Chartered Accountants who offer services directly to the public.

Our flagship CA Program, the pathway to becoming a Chartered Accountant, combines rigorous education with mentored practical experience. Ongoing professional development helps members shape business decisions and remain relevant in a changing world.

We actively engage with governments, regulators and standard setters on behalf of members and the profession to advocate boldly in the public good. Our thought leadership promotes prosperity in Australia and New Zealand.

Our support of the profession extends to affiliations with international accounting organisations.

We are a member of the International Federation of Accountants and are connected globally through Chartered Accountants Worldwide and the Global Accounting Alliance. Chartered Accountants Worldwide brings together members of 15 chartered accounting institutes to create a community of more than 1.8 million Chartered Accountants and students in more than 190 countries. CA ANZ is a founding member of the Global Accounting Alliance which is made up of 10 leading accounting bodies that together promote quality services, share information and collaborate on important international issues.

We have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents more than 870,000 current and next generation accounting professionals across 179 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications.

We employ more than 500 talented people across Australia, New Zealand, Singapore, Malaysia, Hong Kong and the United Kingdom.