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## **RE: Submission to Token Mapping Consultation Paper**

### **Introduction**

Distributed Storage Solutions Limited (DSS) welcomes the opportunity to provide comments on the Treasury's *Token Mapping Consultation Paper*. This is an important discussion that needs to be had prior to the introduction of any new regulations or guidance, so that there is a common understanding of what types of crypto-assets should and should not fall within the financial services regulatory perimeter in Australia.

**DSS firmly believes that not all crypto-assets are financial products, and that it would be unwise for the Treasury to regulate all crypto-assets as such under the *Corporations Act 2001*.**

In developing a fit-for-purpose framework, the Treasury must ensure that any regulatory framework strikes a balance between consumer protection and innovation. It is also important that Australia has a competitive regulatory framework on the international stage. In particular the Treasury should benchmark against the European Union, Hong Kong, Dubai and the United Kingdom. These jurisdictions are currently leading Australia in their approach to crypto-assets.

DSS see three broad outcomes:

1. Tokens that are solely used as financial products or services are already likely to fall within the perimeter of the financial regulators. This may include, for example, ETFs, tokenised public equity shares, and ADI-issued tokenised deposits such as Australian dollar-backed stablecoins. This may also capture non-fungible tokens (NFTs) that are issued for the purpose of fractionalising illiquid investment assets.
2. Tokens that are not intended to be investment products first and foremost (even though they may have some of the features of financial products) should not be regulated as such – but noting that consumer protection laws and AML/CTF laws could still apply. This may include a wide range of projects including: technology services, identity management services, charities and cooperative community-based initiatives.
3. In cases where the Treasury has identified gaps in the regulatory framework for tokens which are not financial products and for which no existing laws apply, specific

legislation that seeks to address these issues could be considered. (This is similar to the intention of the EU's Markets in Crypto Assets (**MiCA**) legislation which applies to crypto-assets where there is a gap in existing EU law.)

This submission outlines our responses to Treasury's questions where DSS believe it can make an important contribution, adding context to the above three regulatory scenarios. Given the importance of the FIL token to our business model, DSS focus on Filecoin in our submission.

## **About Filecoin**

The Filecoin network (Filecoin) is a decentralised peer-to-peer network that stores files, with built-in economic incentives to ensure files are stored reliably over time. Think Amazon AWS or Google Cloud – but distributed, and up to 20x cheaper.

Filecoin has been globally market-validated. In excess of 13,500 PB of data storage capacity has been committed to the network. Furthermore, a consortium including Microsoft, SAP, Alibaba, Huawei and others has recently committed US\$1.3bn to building Filecoin infrastructure (according to CoinDesk a news outlet).

Filecoin is hyper-local. With thousands of nodes globally, the data is distributed securely in every corner of the planet. Alternatively, you can choose to have your data only secured in a discrete sovereign location by design. The design of Filecoin also allows you to break your data into shards so that no storage provider holds a complete dataset, adding an additional layer of protection.

Filecoin is secure. There is no centralised data storage solution that offers the immutability of Filecoin. Some of the methods that are used by Filecoin include a "proof of replication" where the protocol scans the entire network for storage health to prove the integrity of the stored data. Transactions including storage and retrieval of data are also recorded on the blockchain, providing an immutable audit trail of the integrity of a customer's data.

Filecoin is efficient. Storing large amounts of data with increased performance and decentralised archiving. Filecoin storage costs begin at or around \$0.19 per TB/month compared to up to \$24 per TB/month for Amazon S3. Because of the decentralised nature of Filecoin, users can choose their preferred tradeoff between cost, redundancy and speed.

Filecoin is programmable. Developers will be able to deploy smart contracts to access functionality within the Filecoin ecosystem. This has a broad range of applications from AI to High Performance Computing in a wide range of fields such as medical research, climate change and finance. This will only accelerate from March 2023 with the launch of the Filecoin Virtual Machine.

Underpinning the Filecoin ecosystem is the FIL token. FIL is a utility token<sup>1</sup> that is used to incentivise storage providers on the Filecoin network. Storage providers earn FIL tokens by committing storage capacity or by providing a reliable storage service. The FIL token is then used in the Filecoin ecosystem by users to pay for storage and retrieval of data as well as perform other transactions on the network such as fees for executing smart contracts.

### **About Distributed Storage Solutions (DSS) and the role of FIL in our operations**

DSS is Australia's largest Filecoin storage provider. We are a digital asset infrastructure business that stores data for some of the world's largest and most respected organisations including the Victor Chang Cardiac Research Institute, NASA, University of Southern California and the National Oceanic and Atmospheric Association.

These organisations work with extremely large and computationally heavy datasets. DSS provides these organisations with secure and decentralised cloud storage and associated computer processing power, and is remunerated with FIL tokens. For users, their computing assets are hosted in Australian data centres at a small fraction of the cost that they would ordinarily pay to traditional data centres such as AWS.

The Victor Chang Cardiac Research Institute, a customer of DSS, will save in approximately \$200,000 p.a. on cloud computing services through its adoption of Filecoin services. This significant saving enables these funds to be redirected back into its core activity of life saving medical research. It is also better for the environment, and members of the Filecoin network are currently seeking to have the entire global network of storage providers procuring 100% renewable energy by 2025.

DSS has been funded by Australia's leading fund managers, family offices and Australian corporate executives who see future innovation for the fast-growing cloud storage sector. DSS is currently an unlisted public company (limited company), with imminent intent to list its securities in either Australia, Canada or the United States.

The range of clients that benefit from DSS' services demonstrates the utility and benefits of the Filecoin system to Australia across a range of industry verticals. However, if users of the Filecoin storage network face friction in acquiring and using FIL, this would negatively impact on DSS and on other Australian businesses, and would subsequently cause users to drive their business offshore, where they would be subject to fewer consumer protections, and where there may be greater AML/CTF risks.

Similarly, users may be driven to less efficient and less green methods of computer storage even if their initial preference was to use DSS' distributed and secure on-shore storage facilities, due to the high frictions associated with using FIL in Australia in such a scenario.

Additional frictions would also have the unintended consequence of increasing the costs to provide storage, and eliminating the savings that this new technology can provide to end

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<sup>1</sup> The term utility token is used loosely to mean a token which provides access to a service or product on the Filecoin network. It is not intended to reference any legal definition of utility token under a specific regulatory framework.

users. For example, in a scenario where the Victor Chang Cardiac Research Institute has to treat FIL as a financial product on its balance sheet, and consequently must obtain Board clearance in order to leverage DSS storage services, that would create excess bureaucracy with no discernible benefit to either party, and puts DSS at an unfair disadvantage relative to other storage providers.

Further, it would be a suboptimal policy outcome if DSS were to be inadvertently characterised as a NCPF provider, or as an exchange, broker-dealer, or custodian, on account of its acceptance of FIL in exchange for its storage services. To illustrate the point – if DSS is compared to a cloud storage provider such as Amazon’s AWS, or Microsoft Azure, it would be an inconsistent and illogical outcome if DSS and/or FIL were to be regulated as a financial product when the provision of traditional cloud services is not. As the consultation paper notes in paragraph 8, the regulatory approach should ensure “that ‘functionally-equivalent’ products should be treated equivalently” to “remove barriers to technological innovations”.

### **Policy and Regulatory Options for Australia**

Overall, the Treasury’s paper sets out a detailed approach to the difficult challenge of mapping the wide range of tokens in the crypto-asset ecosystem. While it may be desirable by the policy community that Australia seeks to develop a framework that fits within its existing regulatory regime, it is also important to ensure that Australia is not out of step with leading jurisdictions.

Specifically with regard to developing a taxonomy of crypto-assets – this may be useful but should be kept at a high level to ensure that the regulatory framework is able to adapt as technology and the ecosystem evolves. Should the Treasury be inclined to develop a model that regulates crypto-assets based upon their characteristics, then it is important to ensure that these are not overly prescriptive, and aligned to the developments of larger jurisdictions such as the European Union’s MiCA framework.

As the paper notes in paragraph 9, Australia differs from other jurisdictions which may be guided by a risk-based or activities-based framework. However, Treasury should consider the merits of an activities-based regulatory approach such as the regime recently implemented by Dubai’s new Virtual Asset Regulatory Authority (**VARA**). This seeks to capture the activities of nearly all virtual asset businesses – regardless of the specific tokens in which they are dealing – and in doing so applies proportional and risk-adjusted rules to service providers and product issuers. This approach has already been used in Australia’s current financial services framework to regulate specific activities. Some examples include: claims handling and settling, funds management and custody, providing financial advice and making a market. An activities-based approach could make it clear what crypto-asset activities are or are not regulated.

Ultimately it is important that tokens such as FIL are not inadvertently considered to be a financial product, when the features and functions of the FIL token make it clear that it is only intended to be used to facilitate operations within the Filecoin ecosystem of participants – the users, and suppliers, of secure cross-border distributed data storage. This is the approach that DSS understands Treasury to have outlined in its token mapping paper.

### **Response to the Treasury’s Consultation Questions**

*Q5. This paper sets out some reasons for why a bespoke 'crypto asset' taxonomy may have minimal regulatory value.*

- a) What are additional supporting reasons or alternative views on the value of a bespoke taxonomy?*
- b) What are your views on the creation of a standalone regulatory framework that relies on a bespoke taxonomy?*
- c) In the absence of a bespoke taxonomy, what are your views on how to provide regulatory certainty to individuals and businesses using crypto networks and crypto assets in a non-financial manner?*

The Treasury's paper notes that crypto-assets are not a homogenous asset class and that there are clear financial and non-financial uses for crypto networks. DSS agrees that it would not be a helpful exercise to create an exhaustive, bespoke taxonomy as this would be impractical to update given the rapid pace at which new technologies and business models emerge.

The Treasury's paper outlines four product types under which a high level taxonomy of crypto-assets could be grouped. Care should be taken to ensure that such a high level taxonomy is not inconsistent with regimes that have been implemented in other jurisdictions. For example, the UK outlines three broad token types: e-money tokens, security tokens, and unregulated tokens which fall outside of the 'regulatory perimeter' (including: utility tokens and exchange tokens). There is a risk that tokens that fall within the regulatory framework overseas are not captured by any proposed Australian framework and vice versa. Such regulatory arbitrage could be detrimental to the development of the ecosystem in Australia if any regulatory regime becomes overly onerous and incentivises founders and developers to relocate overseas to destinations such as Berlin, London and Dubai.

**If FIL were to be considered a financial product under Australia's token mapping regime, it would put Australian users of FIL at a regulatory disadvantage and likely force business to more favourable jurisdictions, where they could access Filecoin's storage solutions with fewer frictions.**

Alternatively, in the absence of a bespoke taxonomy, where protocols or projects must seek to make a determination under which broad category they fall under, an activity-based regulatory approach could be considered by the Treasury. Rather than determine whether or not a token system falls in or outside of the functional perimeter, and whether or not it is considered a financial product under the *Corporations Act*, an activity-based framework is distinct from a product-based approach in that it focuses on the obligations of service providers more than the specific nature of the tokens in which they offer services. This could be a preferred approach, rather than attempting to categorise token systems and make them fit into the existing financial services framework.

VARA is one such regulatory body which has taken on an activity-based regulatory approach, outlining in clear terms the responsibilities of market participants that undertake seven licensed virtual asset activities. These are: advisory services, broker-dealer services, custodial

services, exchange services, lending and borrowing services, payments and remittances, and virtual asset management and investment services. VARA's regime also includes rules for token issuers, including White Paper standards.

*Q7. It can be difficult to identify the arrangements that constitute an intermediated token system.*

- a) Should crypto asset service providers be required to ensure their users are able to access information that allows them to identify arrangements underpinning crypto tokens? How might this be achieved?*
- b) What are some other initiatives that crypto asset service providers could take to promote good consumer outcomes?*

In cases where a token system is not captured by the financial product regulations, and where existing laws are not sufficient to allow the consumer to provide informed consent and benefit from appropriate safeguards, it may be prudent to ensure that consumers can access a minimum standard of transparent and up-to-date information regarding the crypto token they wish to interact with. DSS suggest that the Treasury review VARA's standalone rulebook on token issuance, which has been published online at [www.vara.ae](http://www.vara.ae). We believe that this would resolve the concerns raised in Question 7.

*Q8. In addition to the functional perimeter, the Corporations Act lists specific products that are financial products. The inclusion of specific financial products is intended to both: (i) provide guidance on the functional perimeter; (ii) add products that do not fall within the general financial functions.*

- a) Are there any kinds of intermediated crypto assets that ought to be specifically defined as financial products? Why?*
- b) Are there any kinds of crypto asset services that ought to be specifically defined as financial products? Why?*

Where tokens perform a utility and access function, then these should be carved out from the *Corporations Act*. This may include a wide range of projects including: technology services, identity management services, charities and cooperative community-based initiatives. DSS believes that the Filecoin token would fall in this category.

*Q10. Intermediated crypto assets involve crypto tokens linked to intangible property or other arrangements. Should there be limits, restrictions or frictions on the investment by consumers in relation to any arrangements not covered already by the financial services framework? Why?*

Australia has a well functioning financial services framework and where crypto-assets are a financial product by intent, this framework already provides consumers with a wide range of protections. Where crypto-assets are not a financial product first and foremost, DSS believes that there should not be any additional limitations or restrictions. There are a number of laws that already apply to crypto-asset consumer products, regardless of the product being purchased, such as misleading and deceptive conduct and anti-money laundering laws.



However, as discussed, the Treasury may wish to consider additional arrangements for crypto-asset service providers and/or token issuers to provide the end user with additional information, in order to ensure that they are well informed in their purchasing decisions.

We thank Treasury for the opportunity to contribute to the Token Mapping policy consultation.