

ASIC CONSULTATION PAPER 343

Crypto-assets as underlying assets for ETPs and other investment products

To whom it may concern,

Please see our joint submission on behalf of the following institutions regarding ASIC's request for comment upon, and response to, Consultation Paper 343.

 **MHC Digital Finance**

MHC Digital Finance
[REDACTED]



TCM Global Asset Management
[REDACTED]



Blockchain Assets Pty Ltd
[REDACTED]



Apollo Capital
[REDACTED]

ASIC CP 343 Joint Submission
27 July, 2021

	Question	Response
	B1Q1: Do you consider that crypto-asset ETPs should be available to retail investors through licensed Australian markets? Please provide details, including data on investor demand where available	<p>We welcome ASIC's initiative to make crypto-asset EFTPs available to retail investors through licenced Australian markets and believe there is retail investor demand for such products.</p> <p>However, by restricting retail access to BTC and ETH, retail investors are denied the diversification benefits and net gains they could potentially make from other crypto-assets. By limiting the ETPs offerings to BTC and ETH, we are disadvantaging retail investors. They want exposure to other coins, so they will be driven to exchanges which are offshore and often unregulated.</p> <p>Research suggests that 47% of Australians earning over AUD\$100,000 p.a. have some exposure to crypto-assets, and 4 million Australians are likely to purchase crypto-assets in the next 12 months*. Many of these individuals will not qualify as wholesale investors.</p> <p>If consumers are prohibited from accessing regulated financial products, they are likely to seek exposure to crypto assets elsewhere. A likely alternative is crypto asset exchanges, many of which have questionable reputations and insecure cyber protections.</p> <p>* https://www.afr.com/companies/financial-services/four-million-aussies-set-to-buy-into-crypto-20210608-p57z2g</p>
	B1Q2: Do you consider that crypto-asset ETPs should be cleared and settled through licensed Australian clearing and settlement facilities? Please provide details.	Yes, we believe ETPs should be cleared and settled through licensed parties, broadly in the same manner as other commodity based ETPs.
	B1Q3: If you are a clearing participant, would you be willing to clear crypto-asset ETPs? Please provide your reasons	Not relevant to us.
	B1Q4: If you are a trading participant, would you be willing to trade crypto-asset ETPs	Yes.

	B1Q5: Do you agree with our approach to determining whether certain crypto-assets are appropriate underlying assets for ETPs on Australian markets? If not, why not?	<p>We agree with a framework for selection; however we believe it is key that this framework is flexible as the market is constantly changing, therefore ASIC needs to ensure regular industry consultations. ASIC needs to be supportive of innovation around crypto-asset backed ETPs.</p> <p>We believe futures trading (requirement B1(d)) is not required and can be substituted by a requirement that the crypto-asset be included in an index or price assessment published by S&P, Nasdaq, CBOE or other reputable providers. This will align the requirements with the requirements for commodities as ETP underlyings.</p>
	B1Q6: Do you have any suggestions for additions or modifications to the factors in proposal B1?	Please see above.
	B1Q7 Do you have any suggestions for alternative mechanisms or principles that could achieve a similar outcome to the approach set out in proposal B1	Please see above.
	B2Q1: Do you agree that a new category of permissible underlying asset ought to be established by market operators for cryptoassets? If not, why not?	<p>Crypto-assets should be treated in the same way as commodities for the purposes of Info Sheet 230 in respect of listed products.</p> <p>Crypto-assets are widely-owned bearer assets that are traded globally by as many as 140 million people¹.</p> <p>Existing ETP structures used for gold and other physical commodities are still relevant in the context of crypto-asset ETPs, specifically structured products and exchange traded funds.</p>
	B3Q1: Do you agree with the good practices in proposal B3 with respect to the pricing mechanisms of underlying crypto-assets? If not, why not?	<p>We agree with this in relation to ETPs; however, we re-iterate that this could be applied to assets outside of BTC and ETH, as set out in B1Q1.</p> <p>We agree there need to be minimum standards; however, we believe futures trading is not required and can be substituted</p>

¹ According to Michael Novogratz, quoted in Goldman Sachs Research Report [ISSUE 98](#), May 21, 2021.

		by a requirement that the crypto-asset be included in an index or price assessment published by S&P, Nasdaq, CBOE or other reputable index providers.
	B3Q2: Are there any practical problems associated with this approach? If so, please provide details.	Refer to B3Q1.
	B3Q3: Do you think crypto-assets can be priced to a robust and transparent standard? Please explain your views.	They can, irrespective of them being ETPs. An index standard is as robust and transparent as possible. It is used widely across all asset classes. Some BTC index examples are the CME Group BTC Reference Rate (BRR) and Bitcoin Real-Time Index (BRTI), Bloomberg BTC Index, S&P BTC Index, and NYSE BTC Index. Note also that the nature of open and public blockchain ledgers permit unparalleled flows between exchanges in ways previously unseen in other commodities or financial products, making crypto-assets more robust and transparent.
	B3Q4: Do you consider that a more robust and transparent pricing standard is achievable in relation to crypto-assets? For example, by using quoted derivatives on a regulated market. Please explain and provide examples where possible.	As above. Futures market is useful but not necessary when a reliable index or price assessment is available.
	C1Q1: Do you agree with our proposed good practices in relation to the custody of cryptoassets? If not, why not? Please provide any suggestions for good practice in the custody of crypto-assets.	Yes, segregated client assets, cold storage of crypto-assets, multi-sig wallets and physical security across password and wallet systems are all essential best practices for crypto-asset custody. However, we suggest that ASIC works with insurers to assure that they are able to provide custodians with robust insurance policies.
	C1Q2: Are there any practical problems associated with this approach? If so, please provide details.	See below.
	C1Q3: Do you consider there should be any modifications to the set of good practices? Please provide details.	We believe there would be a number of benefits in mandating Australian custody for RE held crypto-assets so as to enhance investor protection and minimise the risks of overseas jurisdictional risks for investors.

	C1Q4: Do you consider that crypto-assets can be held in custody, safely and securely? Please provide your reasons.	<p>Yes, issues of safety and security are dealt with regularly by ETPs holding commodities, as commodities need to be custodied and often have special storage requirements.</p> <p>The nature of private/public key pairs utilised in crypto-asset wallets means that the security of custody is dependent upon strong physical and IT security. The ownership of assets held under crypto-asset custody arrangements is also verifiable at any time on the public blockchain relating to the asset held. As such, an ETP for crypto-commodities would be inherently more transparent than a similar structure for physical commodities.</p>
	C1Q5: Do you have any suggestions for alternative mechanisms or principles that could replace some or all of the good practices set out in proposal C1? Please provide details.	Due to the further need for education, a set of sound practices issued by ASIC could be more beneficial than a more general principles based approach.
	C1Q6: Should similar requirements to proposal C1 also be imposed through a market operator's regulatory framework for ETPs? If so, please provide reasons and how it could work in practice.	Yes. Currently the tools exist for cold wallet multi-signature solutions with certain number of signatures to interact or transfer eg 2/5 signatures to send. It is a very easy process to set up and operate such a custody set up on any blockchain.
	C2Q1: Do you agree with our proposed good practices in relation to risk management systems for REs that hold crypto assets? If not, why not?	Yes, custody of crypto-assets is key to investor protection.
	C2Q2: Are there any other regulations (other than KYC and AML/CTF) that should form part of an appropriate baseline level of regulation for crypto-asset trading platforms used by REs and connected service providers? Please provide details.	<p>No, KYC/AML regulations applicable to digital currency exchanges are a suitable base and the principles proposed by ASIC give REs flexibility to adopt best practice solutions as they emerge.</p> <p>Minimum capital requirements should also apply to regulated custody providers.</p>
	C2Q3: Are there any practical problems associated with this approach? If so, please provide details.	We do not have a comment on this question.
	C2Q4: Are there any other matters related to holding crypto-assets that ought to be recognised in the risk management systems of REs	Suitable crypto-asset custody is the key risk management issue which REs need to meet, and ensuring a suitable level of internal

	and highlighted through ASIC good practice information? Please provide details and any specific proposals.	expertise in crypto-assets should be demonstrated by REs wishing to issue ETPs.
	C2Q5: Should similar requirements to proposal C2 also be imposed through a market operator's regulatory framework for ETPs? If so, please provide reasons and outline how it could work in practice.	We have no comment on this question.
	C3Q1: Do you agree with our proposed expectations regarding disclosure obligations for registered managed investment schemes that hold crypto-assets? If not, please explain why not.	Yes.
	C3Q2: Are there any practical problems associated with this approach? If so, please provide details.	We have no comment on this question.
	C3Q3: Are there any additional categories of risks that ought to be specified by ASIC as good practice for disclosure in relation to registered managed investment schemes that hold crypto-assets?	We have no comment on this question.
	C4Q1: Are there any aspects of the DDO regime that need to be clarified for investment products that invest in, or provide exposure to, cryptoassets?	We have no comment on this question, other than to say that it will depend on what the Senate Committee resolves, and Parliament enacts. We believe, for example, that legislating for a DAO entity will facilitate disclosure.
	D1Q1: Do you agree that crypto-assets are capable of being appropriate assets for listed investment entities on Australian markets? If not, why not?	We are not a market operator, but we agree with the D1 proposals.
	D1Q2: Do you agree with our proposed expectations for LICs and LITs that invest in crypto-assets to ensure equivalent standards are applied by market operators? If not, why not?	Yes, they are almost all commodities and should be considered appropriate on that basis.
	D1Q3: Are there any practical problems associated with this	The approach to determine and classify appropriate crypto-assets for investment

	approach? If so, please provide details.	entities should be the same as for ETPs including robust and transparent pricing mechanisms for the crypto-asset. For unlisted registered MIS, pricing mechanisms do not need to be as liquid throughout the trading day, if liquidity is weekly or monthly. Having said that, the crypto-assets that meet the minimum requirements that we support (refer above) typically will be liquid enough to meet daily liquidity requirements.
	D1Q4: Are there additional standards which ought to apply via market operators to LICs or LITs that invest in crypto-assets? If so, what are these expectations and why should they apply?	We have no comment on this question.
	D1Q5: Should LICs and LITs only be able to invest significant funds in crypto-assets if this is either set out in their investment mandate or with member approval? If not, why not?	No, as where a LIC or LIT has a mandate to invest in commodities then crypto-assets should be seen as falling within that scope, and therefore should not be the subject to further approval.
	D1Q6: For the purposes of this proposal, we consider a material investment is where an entity invests or plans to invest more than 5% of its funds in crypto-assets. Should another materiality threshold apply?	No, keep it at 5%.
	E1Q1: Do you agree with our proposal to establish a new asset kind that will cover crypto-assets?	We do not believe a new asset kind should be established.
	E1Q2 Do you consider that crypto-assets may be captured by the existing asset kinds? If so, please explain.	Yes, crypto-assets are akin to commodities, as laid out above.
	E2Q1 Do you agree with our approach to restrict the crypto-assets a registered managed investment scheme is authorised to hold (e.g. to bitcoin or ether)?	<p>No, as most crypto-assets are best dealt with as equivalent to commodities which may be traded digitally, we submit ASIC would be making policy decisions as to the kinds of investments which Australian investors should access if it adopts this approach.</p> <p>We respectfully submit that while there may be very sensible reasons for ASIC to seek to restrict registered managed investment schemes to holding Bitcoin and Ether, ASIC should consider the diversification benefits of other crypto assets and should not unduly</p>

		restrict investment opportunities, as long as minimum standards are being met.
	E2Q2 Do you consider there are any other aspects of the AFS licensing regime that need to be clarified or modified to accommodate investment products that invest in, or provide exposure to, crypto-assets?	<p>There has not been a single registered managed investment scheme to date which provides material exposure to crypto assets to investors. We submit this may be as registered schemes must have assets separately custodied and there are no licensed custody providers offering crypto-custody at this time.</p> <p>ASIC should, as part of this consultation, consider what other features of the MIS licensing regime should be amended to encourage and facilitate registered MISs which can offer crypto-asset exposure to Australian retail investors.</p> <p>The absence of a single registered managed investment scheme holding crypto-assets being permitted to date in Australia also contrasts sharply with comments made during digital currency events by ASIC representatives encouraging innovation and implying that licensing should be sought by those involved in crypto-asset businesses where crypto-assets are a financial product. Arguably there has not been adequate guidance issued by ASIC as to how crypto-assets which are financial products can be the subject of licensing within a business model.</p> <p>Clarification of the regulatory perimeter for the AFS licensing regime around crypto-assets would greatly benefit both investment products and the crypto-currency and blockchain industry more broadly.</p>
	Fa. Likely compliance costs	The certainty provided by the new asset category will benefit the industry in the medium term. In the short term, we note the significant compliance costs and potential delay that will be required to accommodate a new category of crypto-asset including the need for a Regulation Impact Statement and further delay in the amendment of laws, instruments or regulations, as well as the engagement of professional services for

		licence variation applications to accommodate the new asset category.
	Fb. Likely effect on competition	<p>We submit that a new category of crypto-asset should be implemented in such a way that offshore providers of investment products backed by crypto-assets are placed on a level playing field with Australian asset managers, and are restricted from unfairly competing with unregulated products.</p> <p>The present time for processing of AFSL applications or variations is not insignificant, and there will be a flood of applications or variations to existing licences if a new category of crypto-asset is created. ASIC should consider the internal cost and time-cost in processing these applications, which will delay and increase costs for new products being made available to Australian retail investors.</p>
	Fc. Other impacts, costs or benefits	<p>The suggestion to restrict suitable crypto-assets to Bitcoin and Ether at this time, and a collaborative process with market operators to set a prescriptive formula to even consider crypto-assets has an immediate cost to businesses wishing to offer crypto-assets.</p> <p>We believe it is not justified from a regulatory policy point of view.</p> <p>Retail investors will continue to invest in crypto-assets beyond BTC and ETH. We believe retail investors are best protected if they can trade on regulated markets in Australia, where they have the best recourse to legal remedies.</p>