



**Response to ASIC
Consultation Paper CP343:
Crypto-assets as underlying
assets for ETPs and other
investment products**

Submission on behalf of Brave New Coin Ltd.

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Introduction

Brave New Coin (BNC) creates proprietary and bespoke institutional grade indices that align to the most liquid areas of the cryptocurrency market. BNC has established an independent, unique and trusted reputation that is strongly aligned to global financial standards.

Since its launch in 2014, BNC has been a leading provider of aggregated pricing data for crypto assets. BNC's core indexing methodology has been independently audited against key IOSCO principles.

BNC now connects to over 250 individual exchanges, for the purposes of aggregating and calculating spot prices and reference rates for around 2,000 individual cryptocurrencies and digital assets (and their respective fiat and crypto pairs). In addition, BNC's pricing engine monitors and, to the extent possible, verifies exchange-traded volumes for calculating the aggregated rates, as well as measuring free-float supply and tracking market cap.

Using a combination of these volume-and market-weighted calculations, along with a series of documented and semi-automated data capture and quality processes, BNC has developed a core pricing engine that can generate spot prices and market reference rates at a minimum of 30 second intervals, 24/7.

In the absence of formal standards around digital asset identifiers and classifications, BNC has also developed a Taxonomy (a reference database and classification system for cryptographic assets), which allows market participants to construct asset allocations within their portfolios, and track their holdings including corporate actions such as hard forks.

Responses to ASIC's Questions

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.

BNC's Response: Yes. Regulated products such as ETPs will offer investors diversification while mitigating some of the costs (and reducing some of the friction) of directly holding the underlying assets.

In terms of investor demand, there are a number of factors to consider:

1. Various research suggests that 15%-25% of the Australian populations owns (or has owned) cryptocurrency
2. Globally, 45% of family offices are planning to invest in cryptocurrencies, and more asset managers are reported to be interested in bitcoin ETFs
3. BNC itself tracks more than a dozen exchanges that currently offer BTC-AUD markets - daily traded volumes in these AUD spot markets alone is around USD\$20m. This volume increases

to USD\$30m if all AUD markets are included, and exponentially more if all crypto-crypto pairs and/or exchanges that are available to Australian customers are included.

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 there are sufficient venues able and willing to provide such facilities within Australia.

B1Q3 If you are a clearing participant, would you be willing to clear crypto-asset ETPs? Please provide your reasons.

N/A

B1Q4 If you are a trading participant, would you be willing to trade crypto-asset ETPs? Please provide your reasons.

N/A

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?

Based on the factors listed in B1 (a) to (e), we would agree with this descriptive approach. However, we note that these factors also represent a mix of subjective/objective, quantitative/qualitative and regulatory factors. Overall, it would be important to adopt a broad, principles-based approach, that enables issuers and managers to determine and establish appropriate criteria for their products, and avoid an overly prescriptive model.

B1Q6 Do you have any suggestions for additions or modifications to the factors in proposal B1? Please provide details.

In our view, the absence of a single factor (as listed in B1 (a) to (e)) should not in itself be fatal to an ETP. For example, if in B1 (d) a regulated futures and derivatives market for crypto-assets did not currently exist in Australia (but was available and accessible in other jurisdictions) should that be an impediment to launching ETPs?

We would therefore suggest the following alternative wording of B1 (d):

EITHER

"(d) a regulated market for trading linked to the crypto-asset (such as futures, options, spot or ETPs) in a comparable jurisdiction; and"

OR

"(d) evidence of a trusted market that complies with local regulation, licensing and KYC/AML guidelines to protect against market manipulation; and"

[We also note the following developments in respect to Canada:

- 1. Canada has listed the first crypto-asset ETFs, for bitcoin and ether.*
- 2. Currently, there are no "direct" crypto-asset derivatives for bitcoin or ether on either the Toronto Stock Exchange (TSX) or the Montreal Exchange.*
- 3. However, there are two derivative-type products available in Canada:*
 - a) ETFs that track crypto futures - these ETFs are listed on the TSX*
 - b) options on the Canadian crypto ETFs themselves - these standard put/call options are listed on the Montreal Exchange*
- 4. We expect that this will change, with the anticipated launch of bitcoin, ether and other crypto-asset futures, swaps and options in Canada within the next 6 months]*

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 provide details.

We would like to see consideration given to a market framework that supports and facilitates product passporting and reciprocal licensing arrangements that also recognizes the status of regulated ETPs and licensed participants from other relevant jurisdictions.

B2Q1 Do you agree that a new category of permissible underlying asset ought to be established by market operators for crypto-assets? If not, why not?

We welcome the opportunity to bring regulatory clarity and market certainty to the definition of certain crypto-assets, namely those that may not fall within the current notion of "permissible underlying assets" (securities, derivatives, debentures, bonds, currencies, or commodities). In particular, the lack of an explicit definition of "utility token" has been seen as an obstacle to market development and innovation. This has been the cause of some frustration, since it can raise the presumption that a crypto-asset is a security (and should be regulated as such) unless they it can be proved otherwise. In reality, and from a practical and objective perspective, there are other suitable and non-security definitions that can be applied to crypto-assets that should not render them as unsuitable as "permissible underlying assets". However, will the categorisation of crypto-assets be based on

technical, functional, economic, financial, contractual or regulatory definitions? Will the absence of a new category be fatal to ETPs for crypto-assets? Will the new category be capable of adapting to market innovation?

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?

Yes. As an index provider that has aligned our processes to key IOSCO principles for financial benchmarks, we believe that these are reasonable expectations to set.

B3Q2 Are there any practical problems associated with this approach? If so, please provide details.

No.

B3Q3 Do you think crypto-assets can be priced to a robust and transparent standard? Please explain your views.

Yes. There are sufficient processes and safeguards that can be built into the asset criteria, market eligibility, calculation methodology and business rules associated with data sampling, market monitoring, price discovery, reporting and indexing to achieve acceptable standards of transparency and robustness. Brave New Coin has specialised in aggregated pricing and indexing services for crypto-assets since 2014, and has established objective, automated and auditable processes.

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.

From our experience, an index using trade and/or order book data sourced from multiple exchange platforms with additional controls to protect against adverse market conditions and manipulation is currently the most robust and transparent pricing available to crypto assets. An index using quoted derivatives from a regulated market may present greater governance monitoring assurances, but the limited number of markets and the fact that they currently only engage in weekday trading compromises index robustness, and frequent price disparity to spot markets can compromise accuracy (assuming the underlying is physical bitcoin).

As a general observation, pricing and indexing methods will continue to evolve and mature, as more participants and more products come to market. For example, the combination of liquid spot markets, regulated derivatives and other risk management and hedging tools will only enhance and support price discovery for crypto-assets.

B4Q1 Are there any other good practice expectations in INFO 230 that need to be clarified or modified to accommodate crypto-asset ETPs?

No.

C1Q1 Do you agree with our proposed good practices in relation to the custody of crypto-assets? If not, why not? Please provide any suggestions for good practice in the custody of crypto-assets.

Yes.

C1Q2 Are there any practical problems associated with this approach? If so, please provide details.

The main issue is managing operational security in such a way that it does not compromise orderly and efficient asset transfers and reporting, nor should it introduce an additional layer of execution risk.

C1Q3 Do you consider there should be any modifications to the set of good practices? Please provide details.

Some consideration should be given to defining the respective roles and responsibilities of "master custodians" and "sub-custodians" in relation to crypto-assets.

C1Q4 Do you consider that crypto-assets can be held in custody, safely and securely? Please provide your reasons.

Yes. Adequate systems currently exist, subject to their appropriate design, deployment and management. There are a number of recognised providers (including major custodians and trust banks) already offering custody solutions for crypto-assets.

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.

Consideration should be given to the treatment of "corporate actions" as they relate to crypto-assets. For example, how will custodians process a hard fork, a token burn, a token rename, an air drop or other event that relates to an underlying crypto-asset within an ETP.

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, to the extent that these similar requirements are designed to enable ETP issuers, managers and authorised participants to establish and demonstrate their competence in the area of crypto-assets.

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?

Broadly, yes.

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.

Consideration should also be given to qualitative factors in the choice of trading platform or venue, such as applicable trading fees, account management (deposits and withdrawals), security arrangements, dispute resolution and compliance with relevant industry-based certification or delegated self-regulation.

C2Q3 Are there any practical problems associated with this approach? If so, please provide details.

Consideration should be given to improving data dissemination on entities who have registered with AUSTRAC - either by publishing the full register (rather than the current on-line "look-up" service), or assigning a unique AUSTRAC registration ID and requiring registrants to displaying the status of their registration on their website and other relevant information.

C2Q4 Are there any other matters related to holding crypto-assets that ought to be recognised in the risk management systems of REs and highlighted through ASIC good practice information? Please provide details and any specific proposals.

In the absence of formal identifiers (such as ISIN or CUSIP) for crypto-assets, REs should ensure that their middle and back-office systems (e.g., reference databases and asset registries) can uniquely identify crypto-assets by their commonly used names (long and short form) and market symbols (ticker codes) especially where symbols may change, or duplicate symbols exist, or symbols are the same as other common assets, such as listed equities.

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.

Yes, to the extent that these similar requirements are designed to enable ETP issuers, managers and authorised participants to establish and demonstrate their competence in the area of crypto-assets.

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.

Broadly, yes, although further clarification should be given in regard to environmental risk in relation to proof of work crypto-assets and energy consumption. However, it would be counter-productive to market maturity and innovation if RE's for crypto-asset ETPs are being held to a higher disclosure standard or different "burden of proof" than RE's for non-crypto asset ETPs.

C3Q2 Are there any practical problems associated with this approach? If so, please provide details.

These disclosure obligations would be made more workable if RE's could make reference to work that has already been done by companies such as Brave New Coin in creating a formal classification system for the different types of crypto-assets, according to their technical specifications and other key attributes.

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?

Tax risk, in view of any uncertainty that pertains to the tax treatment for some crypto-asset holdings and related transactions.

C4Q1 Are there any aspects of the DDO regime that need to be clarified for investment products that invest in, or provide exposure to, crypto-assets?

No.

D1Q1 Do you agree that crypto-assets are capable of being appropriate assets for listed investment entities on Australian markets? If not, why not?

Yes.

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.

D1Q3 Are there any practical problems associated with this approach? If so, please provide details.

No.

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?

No.

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?

Yes, subject to clarification on what "significant" means in this context. (For example, is it different from "material"?)

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?

It should depend on the allocation by type of crypto-asset - for example, a fiat- or asset-backed stable coin might warrant a different consideration to other cryptocurrencies or utility tokens.

E1Q1 Do you agree with our proposal to establish a new asset kind that will cover crypto-assets?

As noted above, we would broadly agree with the descriptive approach to defining "appropriate underlying assets" in B1 (a) to (e). However, we note that these factors also represent a mix of subjective/objective, quantitative/qualitative and regulatory factors. Overall, it would be important to adopt a broad, principles-based approach, that enables issuers and managers to determine and establish appropriate criteria for their products, and avoid an overly prescriptive model.

E1Q2 Do you consider that crypto-assets may be captured by the existing asset kinds? If so, please explain.

As noted above in our response to B2, we welcome the opportunity to bring regulatory clarity and market certainty to the definition of certain crypto-assets, namely those that may not fall within the current notion of "permissible underlying assets" (securities, derivatives, debentures, bonds, currencies, or commodities). In particular, the lack of an explicit definition of "utility token" has been seen as an obstacle to market development and innovation. This has been the cause of some frustration, since it can raise the presumption that a crypto-asset is a security (and should be regulated as such) unless they it can be proved otherwise. In reality, and from a practical and objective perspective, there are other suitable and non-security definitions that can be applied to crypto-assets that should not render them as unsuitable as "permissible underlying assets". However, will the categorisation of crypto-assets be based on technical, functional, economic, financial, contractual or regulatory definitions? Will the absence of a new category be fatal to ETPs for crypto-assets? Will the new category be capable of adapting to market innovation?

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)?

No. The basis for singling out bitcoin and ether is not immediately apparent. From a practical perspective, bitcoin is either a store of value (like gold) or a currency (it is recognised as a means of payment), and as such should fall within an existing asset classification. On the other hand, while ether could also be regarded as a currency (a means of payment) it is primarily a utility token (it provides access to a range of services such as network computing, data processing, smart contract execution and identity management). When considering other crypto assets such as ripple, litecoin or cardano, these are primarily utility tokens that support payment and remittance platforms, or similar network connectivity and related functions. The distinction being made for bitcoin and ether in this context is unlikely to stand the test of time from the standpoint of market maturity, user adoption and innovation.

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?

Only in respect to clarifying the status of crypto-assets defined as utility tokens that can equally be considered as relevant, appropriate or qualifying underlying assets for an ETP.