



ASIC

Australian Securities &
Investments Commission

REPORT 705

Response to submissions on CP 343 Crypto-assets as underlying assets for ETPs and other investment products

October 2021

About this report

This report highlights the key issues that arose out of the submissions received on [Consultation Paper 343](#) *Crypto-assets as underlying assets for ETPs and other investment products* (CP 343) and details our responses to those issues.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

This report does not contain ASIC policy. For information on ASIC's approach to exchange traded products (ETPs) and other investment products that reference crypto-assets, please see [Information Sheet 225 Crypto-assets](#) (INFO 225) and [Information Sheet 230 Exchange traded products: Admission guidelines](#) (INFO 230).

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A Overview

- 1 In [Consultation Paper 343](#) *Crypto-assets as underlying assets for ETPs and other investment products* (CP 343), we consulted on proposed good practices for exchange traded products (ETPs), listed investment companies (LICs), listed investment trusts (LITs) and unlisted investment funds that hold crypto-assets, to help them meet existing regulatory expectations and operate in a manner that maintains Australia's fair, orderly and transparent markets.
- 2 This report highlights the key issues that arose out of the submissions received on CP 343 and our responses to those issues.
- 3 This report is not meant to be a comprehensive summary of all responses received on every question from CP 343. We have limited this report to the key issues.

Consultation

- 4 The consultation on CP 343 was initially open for a period of four weeks, from 30 June 2021 to 27 July 2021. A substantial proportion of respondents requested extensions to the submission due date for various reasons. We have considered all responses that were received by 16 August 2021.
- 5 We received 10 confidential and 32 non-confidential responses to CP 343 from a broad range of stakeholder groups, including market operators, product issuers, service providers, advisers and industry associations that represented a large member base. We are grateful to respondents for taking the time to send us their comments.
- 6 For a list of the non-confidential respondents to CP 343, see the appendix. Copies of these submissions are currently on the [CP 343 page](#) on the ASIC website.

Feedback received

- 7 There was near unanimous support for ETPs and other investment products that provide exposure to crypto-assets being facilitated within the regulatory framework administered by ASIC. Furthermore, respondents were largely supportive of our proposals.

- 8 The main issues raised by respondents related to:
- (a) the criteria used to determine which crypto-assets are capable of being suitable underlying assets for ETPs;
 - (b) how crypto-assets ought to be classified for the purposes of market operator rule frameworks;
 - (c) the custody of crypto-assets; and
 - (d) ASIC's approach to licensing product issuers that wish to operate managed investment schemes (MIS) that hold crypto-assets.

Our response

- 9 We recognise the interest in, and demand for, ETPs and other investment products that hold crypto-assets in Australia. However, we are also aware of the real risk of harm to consumers and markets if these products are not developed and operated properly.
- 10 ASIC has the function of monitoring and promoting market integrity and consumer protection in relation to the Australian financial system: s12A of the *Australian Securities and Investments Commission Act 2001* (ASIC Act). We consider that ETPs and other investment products that provide exposure to crypto-assets have unique and novel features and risks that must be considered and addressed in light of these functions.
- 11 On that basis, we have implemented our proposals to help facilitate ETPs and other investment products that reference crypto-assets, by:
- (a) operationalising our licensing proposals with modifications in light of feedback received; and
 - (b) publishing good practices for market operators and product issuers in [Information Sheet 225](#) *Crypto-assets* (INFO 225) and [Information Sheet 230](#) *Exchange traded products: Admission guidelines* (INFO 230) largely as proposed in [CP 343](#) with certain clarifications as requested in the feedback received.
- 12 The good practices in INFO 225 and INFO 230 should help market operators and product issuers to meet their respective legislative obligations for the admission, supervision, establishment and operation of these products.
- 13 The subsequent sections of this report explain how our final positions relate to what was proposed in CP 343 and why we have or have not adjusted our proposals in response to feedback.

B Feedback on meeting INFO 230 expectations

Key points

In Section B of CP 343, we proposed good practices for product issuers and Australian market licensees about how crypto-asset ETPs can meet the expectations for ETPs that are set out in INFO 230.

The proposals dealt with the suitability of crypto-assets and identifying features, as well as robust and transparent pricing mechanisms.

While there was strong support for these proposals from some respondents, there was also criticism from others, particularly in relation to:

- the criteria proposed by ASIC to assess whether a particular crypto-asset may be an appropriate underlying asset for an ETP;
- ASIC's position that a new category of permissible underlying assets is warranted for crypto-assets.

We have implemented the proposals largely as they were set out in CP 343 for the reasons outlined below.

Suitability of crypto-assets and identifying features

- 14 In [CP 343](#), we proposed to establish good practices to identify particular crypto-assets that may be appropriate underlying assets for an ETP.
- 15 In particular, we proposed that a market operator should only determine that a crypto-asset may be a permissible underlying asset for ETPs admitted to its market if it is satisfied that:
- (a) there is a high level of institutional support and acceptance of the crypto-asset being used for investment purposes;
 - (b) service providers (including custodians, fund administrators, market makers and index providers) are available and willing to support ETPs that invest in, or provide exposure to, the crypto-asset;
 - (c) there is a mature spot market for the crypto-asset;
 - (d) there is a regulated futures market for trading derivatives linked to the crypto-asset; and
 - (e) robust and transparent pricing mechanisms for the crypto-asset are available, both throughout the trading day and to strike a daily net asset valuation (NAV) price.

16 These factors were intended to help support the maintenance of fair, orderly and transparent markets by ensuring that only crypto-assets which are sufficiently well regarded, capable of being supported within the ETP structure, and less susceptible to price manipulation could become permissible underlying assets.

17 We also stated that, in our view, the only crypto-assets that are likely to satisfy these factors at this point in time are bitcoin (BTC) and ether (ETH).

Note: The crypto-asset, bitcoin, and the network it trades on are both referred to by the same term. For clarity we use the term 'bitcoin' with a lower case 'b' to refer to the crypto-asset.

Stakeholder feedback

18 Many respondents were supportive of our principles-based approach towards identifying which crypto-assets may be permissible underlying assets for an ETP, but some respondents raised concerns, qualifications or made additional comments. These included:

- (a) concerns that needing a regulated futures market for trading derivatives linked to the crypto-asset was too restrictive;
- (b) requests for clarity on whether these factors apply to crypto-assets that are also financial products;
- (c) requests for clarity on how a high level of institutional support and acceptance ought to be determined; and
- (d) suggestions for additional factors or modifications to the wording of the proposed factors.

19 Some respondents did not support our proposed approach. They considered that crypto-assets are capable of being permissible underlying assets without further assessment by market operators on the basis that they should be considered commodities.

ASIC's response

Derivatives requirement

We have maintained the requirement for there to be a regulated futures market for trading derivatives linked to the crypto-asset. We consider this requirement helps support the maintenance of fair, orderly and transparent markets as it helps ensure that only crypto-assets which are less susceptible to price manipulation may be permissible underlying assets.

This factor has the effect of ensuring that at least some part of the trading activity that can help inform the price of the underlying crypto-assets of an ETP will take place on regulated markets that are required by law to have rules and practices to detect, prevent and respond to fraud or manipulation, and are subject to oversight by a body empowered by law to supervise them. We note that, in

some jurisdictions, this may require the market to monitor activity on the underlying crypto-asset spot market(s).

Note: See, for example, [CFTC Staff Advisory No. 18-14](#) (PDF 111 KB) US Commodity Futures Trading Commission, 21 May 2018.

Our review of academic research has uncovered mixed findings on whether spot or futures markets usually lead the price formation process for crypto-assets. However, the contribution of trading on regulated futures markets to some of the price formation process would help reduce some of our concerns about price manipulation risk.

We believe a crypto-asset should only be a permissible underlying asset if at least some part of the trading activity that can help inform the price of an ETP referencing that crypto-asset is:

- subject to a legal requirement to reduce price manipulation risk; and
- subject to oversight by a financial markets regulator.

We also consider that the existence of a regulated futures market helps support the factors of *a high level of institutional support and acceptance* and *a mature spot market*.

This factor is set out in [INFO 230](#).

Financial versus non-financial products

We have clarified in INFO 230 that market operators only need to consider these factors when assessing the appropriateness of crypto-assets that are not financial products. Crypto-assets that are also financial products are subject to the requirements of the *Corporations Act 2001* (Corporations Act) relevant to that class of financial product, and market operators may determine that a particular financial product crypto-asset is a permissible underlying asset on the basis that the relevant class of financial product is a permissible underlying asset. The market operator must still be satisfied that permitting the crypto-asset as an underlying asset is consistent with maintaining a fair, orderly and transparent market.

Note: For the avoidance of doubt, where the crypto-assets are also financial products, the good practices for pricing, custody, disclosure and risk management set out in [INFO 230](#) and [INFO 225](#) remain relevant.

Institutional support and acceptance

We have set out in INFO 230 considerations that may be relevant to market operators in assessing whether there is a high level of institutional support and acceptance of a crypto-asset being used for investment purposes. As these are suggested considerations only, it is a matter for market operators to determine if, and to what extent, they adopt any of these considerations in their product admission assessment process.

Suggestions for modifications from respondents

We have modified the factor dealing with the availability and willingness of service providers to support ETPs that invest in, or provide exposure to, the crypto-asset as suggested by some submissions. In [INFO 230](#), this now refers to the availability and willingness of *reputable and experienced* service providers to support ETPs that invest in, or provide exposure to, the crypto-asset. We accept submissions that the standing of the service providers willing to support the crypto-asset is a relevant factor in assessing whether a crypto-asset is appropriate to be a permissible underlying asset, and consider that *reputable and experienced* is an appropriate level to expect, taking into account the importance of service providers to the proper functioning of an ETP.

We have not included in INFO 230 additional factors that were suggested by respondents. Some examples of additional factors suggested included an audit of a crypto-asset's protocol to assess its viability as an underlying asset for an ETP and principles relating to the role of smart contracts. At this point in time, we consider that the addition of the suggested factors would result in an approach that is more restrictive than is necessary to achieve our regulatory objective, which is to support the fair, orderly and transparent operation of Australia's financial markets. Some factors suggested were also outside ASIC's regulatory remit and expertise. However, we will closely monitor this market as it develops, and will revisit these suggestions if the circumstances justify it.

Commodities

For the reasons set out in the section titled 'Categorisation' below, we do not consider that collectively classifying crypto-assets as commodities is the most appropriate way to facilitate ETPs that provide exposure to crypto-assets.

Crypto-assets are not a homogenous asset class, and the rights, features and risks of crypto-assets can vary greatly. In these circumstances, market operators should have processes to satisfy themselves, on a case-by-case basis, that making a particular crypto-asset a permissible underlying asset is consistent with maintaining a fair, orderly and transparent market.

Categorisation

20 In [CP 343](#), we suggested that market operators should establish a new category of permissible underlying assets for crypto-assets, given their unique characteristics. We proposed to work with Australian market licensees to establish this new category in their rule frameworks.

Stakeholder feedback

- 21 Many respondents were supportive of a new underlying asset class being established for crypto-assets in market operator rule frameworks, considering that this approach:
- (a) reflects the unique nature and characteristics of crypto-assets;
 - (b) helps address uncertainty regarding the classification and permissibility of crypto-assets under market operator rules; and
 - (c) provides a basis for market operators to establish further rules and procedures in relation to crypto-asset products, if they are required, as this area develops and matures.
- 22 However, some respondents were equally critical of this approach, considering that:
- (a) crypto-assets can be supported within existing market operator rule frameworks (generally on the basis that either all crypto-assets can be characterised as commodities or that all crypto-assets that are not financial products can be characterised as commodities); or
 - (b) rather than a new category, ASIC and market operators should adopt the approach of the UK Financial Conduct Authority (FCA) for the categorisation of crypto-assets.
- Note: For information on this approach, see FCA, [Cryptoassets: our work](#), last updated 16 December 2020.
- 23 Some respondents requested clarity on how this categorisation would apply to crypto-assets that were also financial products. Similarly, some respondents expressed concerns that crypto-assets that were also financial products would be ‘double regulated’ if they were caught by both this new category and the category applicable to the relevant class of financial product.

ASIC's response

Commodity-based approaches

Commodity is not a term defined in the Corporations Act and we do not regulate commodities. Respondents suggesting a commodity-based approach generally did not provide their analysis as to how all crypto-assets, or alternatively all crypto-assets that are not financial products, can be considered commodities.

We consider that referring to crypto-assets, collectively, as commodities could obscure a thorough consideration of the features and risks involved with individual crypto-assets.

Unlike more traditional asset classes, the protocols of some crypto-assets can also change over time.

Therefore, we consider a more prudent approach is for market operators to establish a separate underlying asset category for all crypto-assets that are not financial products, so there is certainty as to the permissibility of these assets.

As a result, we have not adopted these suggestions, and have maintained our position that market operators ought to establish a new underlying asset category for crypto-assets in [INFO 230](#).

UK FCA approach

We consider that respondents' comments that we should adopt the FCA approach for the categorisation of crypto-assets in Australia is a matter for the Government.

We also note respondents suggesting this approach generally did not explain how it would operate in the Australian legal and regulatory context. There were also no explanations given as to why it would be a superior approach when categorising crypto-assets for the purposes of permissible underlying asset rules administered by an Australian licensed financial market.

As a result, we have not adopted this suggestion, and have maintained our position that market operators ought to establish a new underlying asset category in [INFO 230](#).

Financial versus non-financial products

We have clarified in [INFO 230](#) that this new category should apply to crypto-assets that are not financial products. Crypto-assets that are also financial products are subject to the requirements of the Corporations Act relevant to that class of financial product. We consider that market operators should assess applications for products referencing these assets on the basis that the relevant class of financial product is a permissible underlying asset. This approach helps reduce the risk of 'double regulation' or the inappropriate treatment of financial products as non-financial products.

C Feedback on responsible entity obligations

Key points

In Section C of CP 343, we proposed good practices for responsible entities (REs) of managed investment schemes that hold crypto-assets.

The proposals dealt with the custody of crypto-assets, the risk management systems of REs and disclosure obligations.

There was very strong support for the intent of these proposals, and feedback from respondents generally related to requests for clarification or suggestions for improvement. However, some respondents considered there should be a stronger legal underpinning to proposals.

We have now implemented our proposals, having adopted suggestions or made clarifications where it was appropriate.

Custody

- 24 In [CP 343](#), we proposed good practices for REs in relation to the custody of crypto-assets, including appropriate safeguards for security of private keys, transaction signing, governance, organisational controls and compensation systems.
- 25 These good practices recognise the unique characteristics of crypto-assets and the specialised infrastructure and expertise that is required to ensure crypto-assets are held in safe and secure custody.
- 26 Robust custody practices are critical. Appropriate safeguards by an asset holder, which can be the RE or a separate custodian, are necessary to protect the assets of the scheme against potential threats, including, but not limited to, cyber-attacks, loss, theft and other fraudulent activity.

Stakeholder feedback

- 27 Many respondents were supportive of our proposals for good practices in relation to the custody of crypto-assets. However, some respondents were concerned that these were only good practices and did not have a stronger legal underpinning. These respondents generally considered that ASIC should implement clear legal requirements in relation to crypto-asset custody.

28

Other respondents raised suggestions, requests or made additional comments. These included:

- (a) suggestions that ASIC should mandate domestic custody of crypto-assets held by Australian schemes;
- (b) requests to clarify whether an entity holding crypto-assets on behalf of the RE of a registered scheme is required to hold an Australian financial services (AFS) licence in respect of this activity;
- (c) requests to clarify the proposed good practices in respect of compensation systems;
- (d) suggestions to improve the good practices proposed by ASIC or to expand the good practices to cover matters we have not mentioned, particularly in relation to requiring particular information security standards such as [NIST CSF](#) or ISO 27001/2; and

Note: See National Institute of Standards and Technology, *Cybersecurity Framework* (NIST CSF) and International Organization for Standardization, ISO/IEC 27001:2013 *Information technology—Security techniques—Information security management systems—Requirements* (ISO 27001) and ISO/IEC 27002:2013 *Information technology—Security techniques—Code of practice for information security controls* (ISO 27002).

- (e) comments that ASIC’s good practices should be principles-based and technology neutral considering the rapidly evolving technological landscape.

ASIC’s response

Legal requirements versus good practices

In [INFO 225](#), we have set out good practices for the custody of crypto-assets.

Good practices are not legal requirements. The legal requirements that apply to the custody of crypto-assets held by a scheme are set out in the Corporations Act, including as modified by relevant class orders, such as [Class Order \[CO 13/1409\]](#) *Holding assets: Standards for responsible entities*.

We do not consider that the good practices we have proposed should be embedded as legal requirements—for example, by amending [CO 13/1409] or otherwise. This is because:

- we do not consider that any changes to the current legal framework are necessary to ensure REs have an obligation to provide safe and secure custody of crypto-assets held by a registered scheme. The good practices are an indication of how we consider this obligation can be met, rather than as requirements themselves;
- what is good practice will change over time, particularly in an area as rapidly changing as crypto-assets. As such, we consider it preferable to maintain the flexibility to readily

adjust these practices as needed, rather than embed them as legal requirements where they could become outdated; and

- we will continue to monitor and enforce the obligations that apply to REs and, where appropriate, will refer to the good practices when doing so.

Mandating domestic custody of crypto-assets

We have not imposed a requirement on REs of registered schemes that hold crypto-assets to engage an Australian domiciled custodian.

While we acknowledge concerns raised by respondents about overseas-based custody of crypto-assets—such as the potential for difficulties in recovering assets across jurisdictions—we consider it would be inappropriate to mandate a domestic custodian requirement because:

- we do not impose Australian domicile requirements for custodians in respect of other asset classes, and we do not consider that the risks associated with crypto-assets are so great as to justify a change to this approach;
- it would reduce choice for REs, who are best placed to determine what is best for their product and investors; and
- it may unfairly restrict competition.

The choice of custodian is a matter for the RE. An RE, having regard to the nature of its product and its legal obligations, may consider that domestic custody of the crypto-assets of the scheme is suitable and appropriate. Equally, they may consider that overseas-based custody is suitable and appropriate.

In making this decision, we expect REs to properly weigh the risks and benefits of different options, including any risks specific to the offshore custody of crypto-assets.

If an overseas-based custodian is used, REs should ensure that their systems and operations properly account for this. For example, REs may need to consider whether the use of offshore custody impacts risk management arrangements—including business continuity plans, operational risks heightened by time zone differences and internal and external audit functions—and that this is reflected in their risk management and compliance plans for each relevant registered scheme.

AFS licensing requirements

In [INFO 225](#), we have clarified that a custodian holding crypto-assets on behalf of the RE of a registered scheme is not required to hold an AFS licence for this activity. This is the case regardless of whether the crypto-assets are financial products.

As set out in [Regulatory Guide 133](#) *Funds management and custodial services: Holding assets* (RG 133), the RE of a registered scheme must hold scheme property on trust for members and can appoint an agent, or otherwise engage a

person, to do anything that the RE is authorised to do in relation to the scheme, including holding scheme property.

An RE or another person engaged by it to hold assets of a registered scheme does not need to hold an AFS licence authorising it to provide a custodial service for this purpose. This is because holding those assets is not a custodial service under s766E(3)(b) of the Corporations Act. Holding assets is part of the operation of the registered scheme by the RE.

Note: In this context, our position on indirect investments through a controlled sub-trust structure (which is explained in [RG 133](#)) applies equally to indirect crypto-asset investments. We do not consider that a controlled sub-trust is a separate scheme. This is because the members (e.g. the responsible entity as trustee) have day-to-day control over the sub-trust. We consider that any property held through a controlled sub-trust is scheme property of the registered scheme that controls the sub-trust. As such, we will regard the sub-trustee of a controlled sub-trust as a custodian who must comply with the relevant legal requirements and, in the context of crypto-assets, should take into account the good practices for custody set out in [INFO 225](#).

Appropriate compensation systems

In INFO 225, we have clarified our views on compensation systems in relation to the custody of crypto-assets.

As set out in RG 133, REs have a significant interest in promoting compliance by the asset holder and, in the event of non-compliance, receiving compensation for loss by the asset holder.

We consider this is particularly the case for crypto-assets, where there have been numerous instances of asset loss around the world. Given the heightened risk environment in relation to crypto-assets, we consider it good practice that REs have access to an arrangement which compensates members of the scheme if the scheme's crypto-assets are lost. The precise nature of the arrangement, including what is covered, how much is covered, and its form—for example, insurance, an asset protection plan or compensation fund—are all matters for the RE to determine, taking into account the nature of its product and its duty to act in the best interest of the members of the scheme.

Note: In this context, REs should also consider the regulatory guidance on liability provisions in custody agreements set out in RG 133.

Mandating cyber security and controls standards

We have not mandated particular standards in relation to the cyber security practices and controls environments of custodians.

As set out in RG 133, all asset holders must have an adequate organisational structure, capacity and resources to perform core administrative activities.

In relation to crypto-assets, a substantial part of the custodian's structure, capacity and resources will reflect the unique environment in which it operates and holds assets. In these

circumstances, having appropriate cyber security practices and controls environments will be key matters for custodians.

However, we have not mandated specific standards, certifications or attestations that must be achieved by custodians of crypto-assets in this regard—for example, SOC 1/2, GS 007, ISO 27001/2, NIST CSF or *Strategies to mitigate cyber security incidents*—as we consider this a matter better left to industry to establish good practice.

Note 1: See System and organisation controls (SOC) reports 1 and 2 (SOC 1/2), Auditing and Assurance Standards Board, Guidance Statement GS 007 *Audit implications of the use of service organisations for investment management services* (GS 007), ISO 27001, ISO 27002, [NIST CSF](#), and the Australian Signals Directorate and Australian Cyber Security Centre, [Strategies to mitigate cyber security incidents](#) (PDF 976 KB).

Note 2: In this context, REs and custodians may also wish to consider the information we have published on [cyber resilience](#).

Instead, we have stated it is good practice that the cybersecurity practices and the control environment of the custodian are independently verified to an appropriate standard.

It is a matter for the RE whether they are satisfied with the standards, certifications or attestations that the custodian has achieved.

Principles-based good practices

We agree with comments from respondents that ASIC's good practices should be principles-based and technology neutral.

To that end, in [INFO 225](#), we have adjusted the good practice relating to signing approaches so it refers to the aim that is being sought (minimising single point of failure risk), rather than specific technologies related to this aim (e.g. 'multi-sig' or sharding).

Other suggestions

We agree with suggestions from respondents that custodians should maintain effective systems and processes for key backup and recovery and that geographically distributed backup sites should be preferred. We have added this as a good practice in [INFO 225](#).

Risk management

- 29 In [CP 343](#), we proposed good practices in relation to the risk management systems of REs that hold crypto-assets. The good practices focused on the appropriate minimum expectations for crypto-asset trading platforms used by REs and service providers in connection with registered schemes that hold crypto-assets. We proposed that any crypto-asset trading carried out by an RE or its service providers should take place on platforms that are subject

to know your customer (KYC) and anti-money laundering and counter-terrorism financing (AML/CTF) obligations.

- 30 We proposed this because we consider that these obligations play a key role in being able to identify traders of crypto-assets and aim to reduce the risk of crypto-assets being used to support criminal activity.

Stakeholder feedback

- 31 Most respondents were generally supportive of our proposed good practices in relation to the risk management systems of REs that hold crypto-assets. However, some respondents raised concerns, qualifications or made additional comments. These included:
- (a) requests to clarify what is meant by KYC and AML/CTF obligations. Related to this, some respondents observed that AML/CTF regulation is at different stages and levels around the world;
 - (b) requests to clarify the extent of the RE's role in verifying the crypto-asset trading platform's compliance with the KYC and AML/CTF obligations. On this issue, one respondent submitted that the RE's role should be limited to forming a reasonable view as to whether a platform is regulated for AML/CTF purposes;
 - (c) concerns that REs and service providers cannot use certain trading platforms—for example, decentralised exchanges—if they comply with this practice; and
 - (d) suggestions for other matters that should form part of the minimum expectations for crypto-asset trading platforms used by REs and service providers.

ASIC's response

KYC and AML/CTF obligations

We have taken into account the observations and suggestions set out above, and have clarified in [INFO 225](#) what is meant by KYC and AML obligations and the extent of the RE's role in verifying the crypto-asset trading platform's compliance with these obligations.

INFO 225 sets out that the RE should be satisfied, based on reasonable due diligence, that:

- any crypto-asset trading platform it relies on is a digital currency exchange provider registered with the Australian Transaction Reports and Analysis Centre (AUSTRAC), or is regulated by one or more laws of a foreign country giving effect to the Financial Action Task Force recommendations relating to customer due diligence and record-keeping; and
- the crypto-asset trading platform's implementation of risk-based AML/CTF systems and controls is supervised or

monitored by a body empowered by law to supervise and enforce the customer due diligence and record-keeping obligations.

It also sets out that the RE should ensure that authorised participants, market makers and other service providers that trade crypto-assets in connection with the product do so on crypto-asset trading platforms that meet the same standard as above.

Decentralised exchanges

We acknowledge that REs and service providers will not be able to use certain trading platforms—for example, decentralised exchanges—if they comply with these good practices. We consider that it is not good practice for REs and service providers to use such platforms until such time as there is a framework for these trading platforms to comply with KYC and AML/CTF requirements.

Other suggestions

We have not added any further minimum expectations for crypto-asset trading platforms used by REs and service providers. In our view, KYC and AML/CTF obligations set an appropriate ‘minimum bar’, and REs are free to exercise their discretion in what crypto-asset platforms they use beyond this.

Disclosure

32 In [CP 343](#), we proposed good practices regarding the RE’s disclosure obligations in relation to a product disclosure statement (PDS) for a registered managed investment scheme that holds crypto-assets. Specifically, we identified matters relating to the characteristics and risks of crypto-assets for REs to consider in the context of their disclosure obligations.

Note 1: See Pt 7.9 of the Corporations Act for obligations that apply to an RE as an issuer of a PDS and Section C of [Regulatory Guide 168](#) *Disclosure: Product Disclosure Statements (and other disclosure obligations)* (RG 168) for guidance on meeting these obligations.

Note 2: Section 1013D of the Corporations Act also requires that a PDS must include information about any significant risks associated with holding a product that a retail client would reasonably require to decide whether to buy the product.

Note 3: In the context of investment products that invest in, or provide exposure to, certain crypto-assets, we consider there must be sufficient information about the characteristics and risks of those crypto-assets in the PDS. There must also be sufficient information about how the product involving crypto-assets is intended to operate and how it is expected to generate a return for investors.

Stakeholder feedback

- 33 Respondents were largely supportive of our approach of identifying matters for REs to consider in the context of their disclosure obligations. Some respondents suggested additional matters that ASIC should specify.
- 34 However, some respondents were concerned that ASIC was attempting to mandate certain disclosures in relation to crypto-assets. Other respondents expressed concerns about matters that had been listed in [CP 343](#), most notably, environmental risk.

ASIC's response

Mandating disclosures

We stated in CP 343 that we were not proposing to mandate matters for disclosure. We have restated this in [INFO 225](#). For the avoidance of doubt, the matters we have identified should only be regarded as illustrations of the types of matters that may be relevant to REs when complying with their disclosure obligations for registered schemes that hold crypto-assets. They do not represent mandatory matters for disclosure.

Disclosure is a matter for REs, and they must determine what is appropriate disclosure in the context of the characteristics, operations and risks of their product.

Suggestions for additional disclosure matters

We have refined the list of matters in INFO 225, incorporating suggestions from respondents as appropriate. However, we were also mindful not to provide an excessively long list of matters, considering that this would neither be useful nor appropriate given that disclosure is a matter for REs and it is not ASIC's role to suggest or provide examples of 'correct' disclosure with respect to crypto-assets.

Environmental risk

In INFO 225, we have clarified that the environmental impact associated with some crypto-assets is only a relevant matter for disclosure to the extent it could affect the value of crypto-assets held by the scheme—for example, if it could negatively impact market sentiment.

D Listed investment entities

Key points

In Section D of CP 343, we proposed that listed investment entities that invest a material proportion of investors' funds in crypto-assets should be subject to the same minimum standards as crypto-asset ETPs.

There was near unanimous support for the proposition that there should be a level playing field between ETPs and listed investment entities. However, some respondents raised questions about the details of the approach.

We consider that market operators are best placed to address these questions, and we are supportive of them developing answers in the context of their broader rule frameworks, subject to the expectation that a level playing field is maintained.

Settings for investment entities

- 35 In [CP 343](#), we proposed to work with market operators to ensure that listed investment companies (LICs) and listed investment trusts (LITs) that invest a material proportion of investors' funds in crypto-assets are subject to the same minimum requirements as ETPs. This would mean that:
- (a) LICs and LITs only invest a material amount of investors' funds in crypto-assets which meet the factors set out in proposal B1 of CP 343; and
- Note: These factors have been reproduced at paragraph 15 of this paper.
- (b) in order to have a structure and operations appropriate for a listed entity, a LIC or LIT that invests a material amount in crypto-assets would be subject to the same minimum standards as to pricing, risk management and custody as ETPs that invest in crypto-assets.
- 36 We proposed this in order to prevent regulatory arbitrage and ensure there is competitive neutrality between different types of products that offer retail investors exposure to crypto-assets. As with ETPs, these requirements are intended to help maintain the integrity of our markets and promote investor protection and confidence.

Stakeholder feedback

- 37 There was near unanimous support for the proposition that listed investment entities that invest a material proportion of investors' funds in crypto-assets

should be subject to the same minimum standards as crypto-asset ETPs. However:

- (a) market operators, as well as other respondents, observed that implementation of minimum standards for LICs and LITs will need to be determined in the context of each market's rule framework; and
- (b) some stakeholders argued that the 'over 5%' materiality threshold proposed in [CP 343](#) was too low.

38 The responses also suggest that there is not a large level of interest among issuers in establishing crypto-asset LICs or LITs, and it may be that product issuers prefer ETP structures for crypto-asset products.

ASIC's response

We agree that market operators are best placed to determine how their rule frameworks should apply to LICs and LITs that invest a material proportion of funds in crypto-assets.

We will work with market operators to establish rule frameworks that achieve a level playing field between ETPs and listed investment entities that invest in crypto-assets. This will include determining an appropriate materiality threshold. We are supportive of market operators conducting their own consultations on these matters, should they wish to do so.

We consider that if rule frameworks for listed investment entities that invest a material amount in crypto-assets are unable to achieve a level playing field with ETPs, then these products should not be admitted.

E AFS licensing

Key points

In Section E of CP 343, we proposed changes to our licensing systems and practices to enable applicants to obtain AFS licences to operate registered managed investment schemes that directly hold certain crypto-assets.

The proposals would establish a new asset kind called ‘crypto-assets’ that would be used in the licensing process as well as impose restrictions on AFS licensees to limit the crypto-assets that could be held by a registered scheme.

While there was support for these proposals from some respondents, there was also criticism from others, particularly in relation to the proposal to impose restrictions on AFS licences.

As a result of this feedback, we have made changes to our approach. Most notably, we will not seek to restrict the crypto-assets a properly authorised registered managed investment scheme can hold.

New asset kind

39 In [CP 343](#), we proposed to establish a new asset kind called ‘crypto-assets’ that can be selected when applying for a new AFS licence, or a variation to an existing AFS licence, to operate a registered managed investment scheme.

40 We proposed this because we considered that crypto-assets that are not financial products did not fall within any existing asset kind that could be selected by an applicant.

Stakeholder feedback

41 Many respondents were supportive of a new asset class being established for the purpose of the licensing regime, considering that it would help facilitate new products. However, some respondents were critical of this approach, considering that:

- (a) all crypto-assets, or alternatively all crypto-assets that are not financial products, should be treated by ASIC’s licensing framework as commodities; or
- (b) ASIC’s licensing framework should adopt the UK FCA approach for the categorisation of crypto-assets.

42 Respondents also requested clarity on how this categorisation would apply to crypto-assets that were also financial products.

*ASIC's response***Commodity-based approaches**

In Section B of this paper, we set out why we disagreed with suggestions that:

- all crypto-assets can be classified as commodities;
- all crypto-assets that are not financial products can be classified as commodities; and
- ASIC should adopt the UK FCA taxonomy of crypto-assets.

While that discussion was in the context of market operator rules for permissible underlying assets, we consider the same reasons as to why we prefer a standalone crypto-asset category can be applied to ASIC's licensing asset kinds.

We also note that commodities themselves do not currently fall within any existing asset kind in the licensing framework. This means that classifying crypto-assets as commodities, by itself, would not resolve the problem that they cannot currently be selected when applying for a new AFS licence, or a variation to an existing AFS licence. We do not propose to add a new commodity asset kind and define it to include crypto-assets.

As a result, we have not adopted these suggestions and have implemented the new asset kind for crypto-assets as proposed, subject to the clarification below.

Financial versus non-financial products

We have clarified in [INFO 225](#) that this asset kind applies only to crypto-assets that are not financial products. Crypto-assets that are also financial products are already supported by the existing asset kinds that refer to the relevant class of financial product—for example, 'financial assets' or 'derivatives'—and we expect licensees to rely on these authorisations to hold crypto-assets that are also financial products.

As a result, our expectation is that, when seeking authorisation to operate registered managed investment schemes that will hold crypto-assets, the applicant should select:

- for crypto-assets that are not financial products, the 'crypto-asset' asset kind; or
- for crypto-assets that are also financial products, the asset kind which corresponds to the crypto-asset's class of financial product.

To establish the 'crypto-asset' asset kind to administer ASIC's licensing functions, we will define crypto-asset as:

'a digital representation of value or rights (including rights to property), the ownership of which is evidenced cryptographically and that is held and transferred electronically by:

- (a) *a type of distributed ledger technology; or*
- (b) *another distributed cryptographically verifiable data structure.'*

Note 1: This definition is deliberately broad to capture the range of assets that could be held by a managed investment scheme. Without limitation, it is intended to encapsulate the full range of 'coins,' 'stablecoins' and 'tokens', as those terms are used by the crypto-asset industry.

Note 2: This definition assists ASIC in administering the AFS licensing regime for managed investment schemes and should not be taken as a definition of crypto-assets for other purposes.

Licence restrictions

43 In [CP 343](#), we proposed that when granting an AFS licensee authorisation to operate a registered managed investment scheme which holds crypto-assets, we would restrict the crypto-assets the registered managed investment scheme can hold by reference to the factors set out in proposal B1 of CP 343.

Note: These factors have been reproduced at paragraph 15 of this paper.

44 We also stated that, given these criteria, the only crypto-assets we would issue authorisations for, at this point in time, are bitcoin and ether.

45 We proposed this because we recognise that crypto-assets vary greatly in their features, characteristics, risks and how they operate, and we consider that only some may be appropriate to be held by a registered managed investment scheme. In these circumstances, we considered that a prudent and cautious approach would be to align ASIC's licensing regime with the criteria proposed for ETPs.

Stakeholder feedback

46 Respondents were generally opposed to this proposal. While some considered there was merit in the intent of ASIC's proposal, they raised concerns that:

- (a) the criteria used to identify appropriate crypto-assets is too restrictive;
- (b) it would result in entities continuously needing to update their licence authorisations as permitted assets evolve; and
- (c) ASIC would not be able to keep pace with the rapidly evolving crypto-asset landscape.

47 Other responses were opposed to both the intent and practicalities of the proposal, considering that:

- (a) the approach amounts to ASIC whitelisting assets that can be held by a registered scheme, which is contrary to a principles-based approach and the intent of the licensing regime;

- (b) ASIC should not be making decisions about what kinds of assets investors may access; and
- (c) other asset classes are not restricted in this way.

ASIC's response

We have not implemented this proposal and have revised our approach.

Under our new approach, which we have set out in [INFO 225](#), AFS licensees, provided they have the appropriate authorisations, will be able to operate schemes that hold any crypto-asset.

In this respect:

- we expect that applicants proposing to operate registered schemes that hold crypto-assets will initially apply for 'named scheme' authorisation (whether the scheme holds one or more crypto-assets). This authorises the licensee to operate only the specific crypto-asset registered scheme(s) named on the licence;
- consistent with [Regulatory Guide 105 AFS licensing: Organisational competence](#) (RG 105), we expect applicants to operate two named crypto-asset registered schemes for at least two years before we will consider granting them broader 'kind scheme' authorisation for crypto-assets. The 'kind scheme' authorisation allows the licensee to operate multiple crypto-asset schemes without needing to vary the licence with each new scheme;
- we will take a strict, case-by-case approach to granting licences, focusing particularly on the matters we have outlined in INFO 225;
- as per our clarification above, the authorisations needed by the applicant will vary depending on whether the crypto-assets proposed to be held by the scheme are financial products;
- registered schemes seeking admission as ETPs or LITs will still need to limit themselves to the relevant market's permissible underlying crypto-assets, meaning that this approach mainly affects unlisted registered schemes; and
- there may still be certain circumstances where we impose restrictions on what crypto-assets can be held—for example, if the applicant requests this.

Appendix: List of non-confidential respondents

- Australian Financial Markets Association
- Blockchain Assets
- Brave New Coin
- CF Benchmarks
- Chi-X Australia Pty Ltd
- CMCC Global
- Cosmos Asset Management
- CPA Australia
- Distributed Storage Solutions
- Ernst & Young Australia
- ETFS Management (AUS) Limited, 21Shares AG and Baker & McKenzie (joint submission)
- Financial Services Council
- Fintech Australia
- Holon Global Investments
- Independent Reserve
- Jarnevic, Elvis
- Lane, Aaron and Berg, Chris (joint submission)
- Lawry, John
- Marshall Investments
- MHC Digital Finance, TCM Global Asset Management, Blockchain Assets and Apollo Capital (joint submission)
- Mills Oakley
- Monochrome Asset Management
- Mycelium
- Neo Legal
- NSX
- Stockbrokers and Financial Advisers Association
- Sydney Stock Exchange
- TCM Capital
- Thomas Murray Digital
- Tilley, Michael
- VanEck Investments Limited
- ZeroCap