

June 30, 2021



Department of the Senate
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Canberra ACT 2600

Email: fintech.sen@aph.gov.au

Dear Sir or Madam,

Ripple welcomes the opportunity to comment on the Third Issues Paper (“the Discussion Paper”) published by the Senate Select Committee on Australia as a Technology and Financial Centre (“the Committee”) on May 18, 2021.¹

Ripple would like to thank the Committee members for the in-depth and comprehensive analysis that has been taken on this subject prior to the publication of the Discussion Paper, including the Issues Paper² published in 2019 and Second Issues Paper³ published in 2020. We are also grateful to the Committee for publishing the findings and recommendations from the consultation process in the Interim Report published in 2020⁴ and, most recently, the Second Interim Report published in 2021.⁵

With over approximately 300 customers as of the date of this letter, Ripple’s software products allow financial institutions to send money globally, on a real-time basis, at a

¹ See

https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Financial_Technology_and_Regulatory_Technology/FinancialRegulatoryTech/Third_Issues_Paper, Senate Select Committee on Australia as a Technology and Financial Centre Third Issues Paper.

² See

https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Financial_Technology_and_Regulatory_Technology/FinancialRegulatoryTech/Issues_Paper, Senate Select Committee on Australia as a Technology and Financial Centre Issues Paper.

³ See

https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Financial_Technology_and_Regulatory_Technology/FinancialRegulatoryTech/Second_Issues_Paper, Senate Select Committee on Australia as a Technology and Financial Centre Second Issues Paper.

⁴ See

https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Financial_Technology_and_Regulatory_Technology/FinancialRegulatoryTech/Interim_Report, Senate Select Committee on Australia as a Technology and Financial Centre Interim Report.

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https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Financial_Technology_and_Regulatory_Technology/FinancialRegulatoryTech/Second_Interim_Report, Senate Select Committee on Australia as a Technology and Financial Centre Second Interim Report.

fraction of the cost of traditional services available to market participants. Using blockchain technology, Ripple allows financial institutions to process payments instantly, reliably, cost-effectively, and with end-to-end visibility anywhere in the world.

Ripple's aim is not to replace fiat currencies, but rather to enable a faster, less expensive, and more transparent method of making cross-border payments that is in the public's best interest. Unlike the large majority of companies seeking to leverage digital assets,⁶ Ripple's customers and partners are regulated financial institutions - banks and payment service providers - who operate within the contours of the existing financial system.

Ripple drives the efficient globalization of value through multiple initiatives with financial services and open-source communities. RippleNet, our enterprise software solution which is powered by a standardized application programming interface and built on the market-leading and open standard, Interledger Protocol, enables financial institutions to facilitate faster and less costly cross-border payments, demonstrating that deep interoperability between commercial financial institutions can make payments truly efficient, particularly in eliminating the uncertainty and risk historically involved in moving money across borders using interbank messaging alone.

In addition, Ripple offers these entities an On-Demand Liquidity capability which leverages XRP - the digital asset native to the XRP Ledger, a distributed ledger platform - as a bridge between fiat currencies, further reducing the friction and costs for commercial financial institutions to transact across multiple global markets. Although Ripple utilizes XRP and the XRP Ledger in its product offerings, XRP is independent of Ripple. The XRP Ledger is decentralized, open-source, and based on cryptography. Ripple leverages XRP for use in its product suite because of XRP's suitability for cross-border payments. Key characteristics of XRP include speed, scalability, energy efficiency, and cost – the benefits of which will be passed on to the Australian consumer and will help reduce friction in the market for cross border payments, thereby removing barriers to Australian growth as a technology and finance centre.

⁶ The terms digital asset, virtual currency, cryptocurrency and others are used interchangeably in the marketplace. For purposes of this comment letter, we use the term "digital asset", and discuss the appropriate taxonomy in more detail in the Appendix of this letter.

With this overview, Ripple respectfully submits feedback to the Committee on the regulation of digital assets, with examples of existing regulatory frameworks in comparable jurisdictions in the attached Appendix.

Ripple appreciates the opportunity to provide feedback on some of the topics highlighted in the Discussion Paper as the Committee studies these important issues, and we would encourage and support further dialogue with all stakeholders. Should you wish to discuss any of the points raised in this letter, please do not hesitate to contact Rahul Advani (Policy Director, APAC) at radvani@ripple.com.

Sincerely,

Ripple Labs, Inc.

APPENDIX

1. Taxonomy for digital assets

It is important to note that there is no single or generally recognised definition of digital assets at present. Ripple respectfully submits such assets should not be solely defined relative to a specific technology (e.g., cryptography), but, for the purposes of regulation, should instead fall under a broader heading such as “digital assets”, and subsequently classified depending on the particular economic function and purpose they serve. Such an approach is consistent with that taken by other jurisdictions like the United Kingdom (“UK”) and Singapore, which have issued classifications that do not depend on whether a business model uses distributed ledger technology or not. A comparison of the taxonomies for the UK and Singapore is provided below, along with our recommendations for a proposed digital asset taxonomy for Australia.

a. United Kingdom

The UK constituted a Crypto Asset Task Force (“CATF”) in 2018, to assess the potential impact of digital assets in the UK and to consider appropriate policy responses. Following the publication of the CATF Report⁷ and subsequent consultation, the Financial Conduct Authority (“FCA”) created a framework for digital assets by categorising digital assets based on their intrinsic structure as well as their designed use, which is outlined in the FCA Guidance on Cryptoassets (“FCA Guidance”)⁸ issued in July 2019.

Under the FCA Guidance, exchange tokens, which *“can be used to facilitate regulated payment services”*⁹ and utility tokens, which *“provide[s] consumers with access to a current or prospective product or service and often grant[s] rights similar to pre-payment vouchers”*¹⁰ are both considered to be “unregulated tokens” (i.e., tokens that do not provide rights or obligations akin to specified investments) that fall outside the FCA’s regulatory perimeter.¹¹

This stands in contrast to security tokens, which are described as *“tokens with specific characteristics that mean they provide rights and obligations akin to*

⁷ See <https://www.gov.uk/government/publications/cryptoassets-taskforce>, Cryptoassets Taskforce: final report.

⁸ See <https://www.fca.org.uk/publication/policy/ps19-22.pdf>, Guidance on Cryptoassets: Feedback and Final Guidance to CP 19/3.

⁹ See FCA Guidance, paragraph 2.15, page 11.

¹⁰ See FCA Guidance, paragraph 2.21, page 13.

¹¹ See FCA Guidance, Appendix 1, paragraph 43, page 35 and paragraph 50, page 36.

specified investments” and do fall within the FCA’s regulatory perimeter as well as that of the Prudential Regulatory Authority, as the case may be.¹²

It is important to note that the FCA has recognized that XRP is a hybrid exchange/utility token, leaving it outside of its regulatory perimeter.¹³

Ripple strongly believes these types of designations, which consider each token’s economic purpose and function in determining the appropriate degree of regulation assigned to them, should be accounted for when designing a taxonomy for digital assets. To the extent digital assets move from one category to another, as the FCA recognizes they might, any treatment should necessarily be flexible enough to account for such a shift.

The FCA taxonomy for digital assets is summarised in Table 1 below.

Regulated Tokens
<p>a. Security tokens: These are tokens that amount to a ‘Specified Investment’ under the Regulated Activities Order, excluding e-money. These may provide rights such as ownership, repayment of a specific sum of money, or entitlement to a share in future profits. They may also be transferable securities or other financial instrument under the EU’s Markets in Financial Instruments Directive II. These tokens are likely to be inside the FCA’s regulatory perimeter.</p> <p>b. E-money tokens: These are tokens that meet the definition of e-money under the Electronic Money Regulations. These tokens fall within regulation.</p>
Unregulated Tokens
<p>Any tokens that are not security tokens or e-money tokens are unregulated tokens. This category includes utility tokens which can be redeemed for access to a specific product or service that is typically provided using a blockchain platform.</p> <p>The category also includes tokens such as Bitcoin, Litecoin and equivalents, and often referred to as ‘cryptocurrencies’, ‘cryptocoins’ or ‘payment tokens’. These tokens are usually decentralised and designed to be used primarily as a medium of exchange. We sometimes refer to them as exchange tokens and they do not provide the types of rights or access provided by security or utility tokens, but are used as a means of exchange or for investment.</p>

Table 1: Summary of the FCA taxonomy for digital assets

¹² See FCA Guidance, Paragraph 1.9, page 4.

¹³ See <https://www.fca.org.uk/publication/consultation/cp19-22.pdf>, FCA Consultation Paper CP19/22, paragraph 2.7, page 8.

b. Singapore

In Singapore, digital assets are regulated either as digital payment tokens (“DPT”) by the Monetary Authority of Singapore (“MAS”) under the Payments Services Act (“PS Act”),¹⁴ or as digital tokens which constitute capital markets products and are regulated under the Securities and Futures Act (“SFA”).¹⁵

The PS Act provides for an activity-based licensing framework for retail payment services which facilitates innovation and mitigates risks. The MAS payments licensing regime encompasses a wide range of payment activities, including the purchase and sale of DPTs, as outlined in the MAS Guidelines on Licensing for Payment Service Providers (“MAS Guidelines”).¹⁶ XRP is classified as a DPT under the MAS taxonomy, and XRP is also explicitly referenced as a DPT in the MAS Guidelines.¹⁷

The MAS taxonomy for digital assets is summarized in Table 2 below.

Digital Payment Tokens
Refers to “any digital representation of value that is expressed as a unit; is not denominated in any currency, and is not pegged by its issuer to any currency; is, or is intended to be, a medium of exchange accepted by the public, or a section of the public, as payment for goods or services or for the discharge of a debt; and can be transferred, stored or traded electronically”.
Digital tokens which constitute capital markets products
MAS will examine the structure and characteristics of, including the rights attached to, a digital token in determining if the digital token is a type of capital markets products under the SFA. This includes, but is not limited to a share, a debenture, a unit in a business trust, a securities-based derivatives contract, or a unit in a collective investment scheme, as defined under the SFA.

Table 2: Summary of the MAS taxonomy for digital assets

c. Proposed digital asset taxonomy for Australia

Taking into account the taxonomies of the UK and Singapore discussed above, we request that the Committee consider adopting a digital asset taxonomy consistent with such global practices, thereby providing clarity to the legal character of digital assets in Australia.

¹⁴ See <https://sso.agc.gov.sg/Acts-Supp/2-2019/Published/20190220?DocDate=20190220>, Republic of Singapore Payment Services Act 2019.

¹⁵ See <https://sso.agc.gov.sg/Act/SFA2001>, Republic of Singapore Securities and Futures Act (chapter 289).

¹⁶ See <https://www.mas.gov.sg/-/media/MAS/Sectors/Guidance/Guidelines-on-Licensing-for-Payment-Service-Providers.pdf>, MAS Guidelines on Licensing for Payment Service Providers.

¹⁷ See MAS Guidelines, page 15. XRP is mistakenly referred to as “Ripple” here.

In line with global practices, we recommend that there be a clear distinction between payment tokens, utility tokens, and security tokens, as outlined below:

- Payments or Exchange tokens: to describe non-fiat native digital assets that are used as means of exchange and have no rights that may be enforced against any issuer;
- Utility tokens: to describe those digital assets that create access rights for availing service or a network, usually offered through a blockchain platform; and
- Security tokens: to describe tokens that create rights mirroring those associated with traditional securities like shares, debentures, security-based derivatives, and collective investment schemes.

2. Regulatory framework for digital assets

In addition to a taxonomy for digital assets, the Committee should also consider an appropriate regulatory framework for digital assets in order to provide legal certainty and attract private investment into Australian digital assets. A comparison of the regulatory frameworks of the UK and Singapore is provided below, along with our recommendation for a proposed digital asset regulatory framework for Australia.

a. United Kingdom

As discussed in section 1(a) above, the FCA Guidance classifies digital assets as either regulated or unregulated tokens. The FCA has determined that exchange tokens and utility tokens (as well as hybrid tokens) are presently outside its regulatory perimeter. Additionally, it is important to note that the FCA Guidance also states that market participants which only provide a platform for the trading of exchange tokens are outside the regulatory perimeter.¹⁸

However, digital asset exchanges will be subject to reporting obligations under the relevant anti-money laundering and countering the financing of terrorism (collectively, “AML & CFT”) regulations.¹⁹

On the other hand, security tokens that amount to a ‘Specified Investment’ under the Regulated Activities Order²⁰ (“RAO”) are deemed to be securities, and are

¹⁸ See FCA Guidance, paragraph 2.3, page 9.

¹⁹ See <https://www.legislation.gov.uk/ukxi/2017/692/contents/made>, United Kingdom Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017.

²⁰ See <https://www.legislation.gov.uk/ukxi/2001/544/contents/made>, United Kingdom Financial Services and Markets Act 2000 (Regulated Activities) Order 2001.

regulated the same as traditional financial securities. Likewise, any advisory services offered in connection with security tokens, or in connection with instruments who derive their value from underlying utility/exchange tokens are also subject to licensing and regulation under the RAO.

b. Singapore

As discussed in section 1(b) above, the PS Act adopts a risk-based approach for regulating payments services activities, consistent with the risks posed by a given activity. Consistent with that core principle, the MAS Guidelines subject all DPT service providers to AML/CFT requirements.²¹ Furthermore, according to the MAS FAQs on the PS Act,²² MAS requires any DPT service provider that facilitates the transfer of DPT or offers custodial wallet services for DPT to also apply AML/CFT measures, to mitigate the risks posed by these services.

The MAS guide to digital token offerings²³ highlights that MAS will examine the structure and characteristics of, including the rights attached to, a digital token in determining if the digital token is a type of capital markets products under the SFA. The expression 'Capital Markets Product' is a super-set of 'Securities' under the SFA, which means that MAS will treat such digital assets as securities. This includes, but is not limited to, a share, a debenture, a unit in a business trust, a securities-based derivatives contract, or a unit in a collective investment scheme, as defined under the SFA. Licensing requirements under the SFA will also apply for dealing in securities tokens.

c. Proposed digital asset regulatory framework for Australia

Taking into account the regulatory frameworks of the UK and Singapore discussed above, we request that the Committee consider adopting a digital asset regulatory framework consistent with these global practices in order to provide legal certainty and attract private investment into digital assets in Australia.

We recommend that such a regulatory framework should align with the following principles outlined below:

- The regulatory framework should be technology-agnostic, and should not explicitly or otherwise endorse any particular technology. In practical terms, this means that financial services using digital assets as a solution should

²¹ See MAS Guidelines, paragraph 4.2, page 8.

²² See <https://www.mas.gov.sg/-/media/MAS/Fintech/Payment-Services-Act/Payment-Services-Act-FAQ-31-March-2021.pdf>, MAS FAQs on the PS Act, paragraph 31.4, page 20.

²³ See <https://www.mas.gov.sg/-/media/MAS/Sectors/Guidance/Guide-to-Digital-Token-Offerings-26-May-2020.pdf>, MAS guide to digital token offerings, paragraph 2.3, page 3.

not be treated differently from financial services embedding legacy architectures, and there should be parity in the treatment of all technology;

- Given the dynamic nature of digital assets, prescriptive regulation risks obsolescence. Prescriptive regulation could also have the unintended consequence of hindering innovation. Therefore, we recommend the Committee consider a principles-based regulatory framework, which will guide market participants to regulatory and policy goals, without imposing an overly prescriptive and onerous process in doing so; and
- The regulatory framework should use a risk-based approach to identify digital asset services that pose sufficient risk to warrant regulation, and where such risks are crucial to address. This is in order to build a simple, secure, and accessible digital assets ecosystem that will encourage investment into digital assets in Australia, while mitigating any potential risks.

The recommended regulatory framework, as proposed above, should be forward-looking and flexible while providing regulatory certainty and consumer safeguards, and at the same time meet the Committee's policy goals of encouraging innovation and growth of digital assets in Australia.