



Crypto asset secondary service providers: Licensing and custody requirements

ACCC submission in response to the
Treasury consultation paper

May 2022

Introduction

The Australian Competition and Consumer Commission (**ACCC**) welcomes the opportunity to provide a submission to the Treasury's consultation on the licensing and custody requirements for crypto asset secondary service providers (**CASSPrs**).¹

The ACCC is an independent Commonwealth statutory agency that promotes competition, fair trading, and product safety for the benefit of consumers, businesses, and the Australian community. The primary responsibilities of the ACCC are to enforce compliance with the competition, consumer protection, fair trading, and product safety provisions of the *Competition and Consumer Act 2010 (Cth)* (**CCA**), regulate national infrastructure, and undertake market studies.

The ACCC also runs Scamwatch which provides information to consumers and small businesses about how to recognise, avoid and report scams, including those scams involving crypto assets; and we use a range of measures to disrupt scam activity that targets Australian consumers and small business.

The ACCC considers it is a pivotal time to consult on a regulatory framework for CASSPrs given:

- the significant growth of the crypto asset ecosystem in recent years;²
- the rising numbers of Australians transacting in digital assets;³
- the need for regulatory clarity and certainty for CASSPrs, and confidence for consumers who transact with them, to encourage innovation and competition in this sector; and
- the increasing number of Australians falling victim to scams and the escalating financial loss involving crypto assets in Australia.⁴

This submission focuses on issues most relevant to the work of the ACCC. In particular, the consultation paper questions that consider the:

- policy objectives of a CASSPr regulatory framework (question **6**)
- proposed licensing obligations for CASSPrs, including an obligation that relates to scams (question **11**), and
- whether industry-self regulation is an appropriate way to achieve Treasury's policy objectives (question **17**).

¹ The Treasury consultation paper defines CASSPrs as digital currency exchanges in Australia and other crypto asset service providers including brokers, dealers, exchanges, and crypto asset markets.

² At the start of 2020, the total market capitalisation of crypto assets was around USD 200 billion (AUD 285 billion). As at the start of 2022, this had increased to close to USD 2.2 trillion (AUD 3 trillion).
Coin Dance, [Cryptocurrencies by Market Cap \(historical\) Summary](#), accessed 9 May 2022.

³ As noted in the consultation paper, analysis by the Australian Taxation Office estimated that more than 800,000 Australian taxpayers have transacted in digital assets in the last three years. This represented a 63% increase in 2021, compared to 2020.

Further, a nationally representative consumer survey undertaken by Roy Morgan in December 2021 to February 2022, found that over 1 million Australians aged 18+ (or around 5% of the adult population) hold an investment in a cryptocurrency, with an average value of just over \$20,000.

Sources:

Treasury, [Consultation Paper: Crypto asset secondary service providers: Licensing and custody requirements](#), 21 March 2022, accessed 9 May 2022

Roy Morgan, [Over 1 million Australians now own Cryptocurrencies such as Bitcoin, Ethereum, Ripple, Cardano, Dogecoin and Shiba Inu](#), 12 April 2022, accessed 9 May 2022.

⁴ Crypto-asset scam losses reported to Scamwatch more than tripled from around \$40 million in 2020, rising to around \$129 million in 2021. This exponential growth has continued in 2022, with more than \$103 million in losses to crypto-asset scams from 1 January 2022 to 30 March 2022.

ACCC, Internal ScamWatch Data.

This submission does not respond to other questions from the consultation paper.

The existing regulatory framework for crypto assets and CASSPrs is complex and provides incomplete protection

Under the existing framework, different regulatory regimes apply for financial product crypto assets and for crypto assets that are not financial products.

If a crypto asset is a financial product, it is regulated by the Australian Securities and Investments Commission (**ASIC**) under the *Corporations Act 2001* (**Corporations Act**) and the *Australian Securities and Investment Commission Act 2001* (**ASIC Act**).⁵ In this case, obligations that aim to protect investors apply including prohibitions against misleading or deceptive conduct and “hawking” or pressure selling, disclosure requirements, and, for financial products traded on financial markets, prohibitions on market manipulation.

If a crypto asset is not a financial product, then the Australian Consumer Law (**ACL**) applies. The ACL provides a number of consumer protections, including consumer guarantees and prohibitions against misleading or deceptive conduct.

As crypto assets can be programmed to provide a variety of rights and features, which may vest only in certain circumstances and which may not be clearly disclosed outside of the programmed code, in some cases it can be difficult for regulators, industry and consumers, to determine which regulatory framework applies (the financial product regime or the ACL). Further, as businesses (including CASSPrs), may engage with crypto assets that are financial products and non-financial products, the ACCC delegated regulatory powers in relation to digital currencies and digital tokens (including crypto assets)⁶ under the ACL to ASIC in 2018, to enable ASIC is able to consider consumer protection issues regardless of whether crypto assets are financial products or non-financial products.⁷

CASSPrs provide access to crypto assets in a variety of ways, including the operation of exchanges where crypto assets are bought and sold, and/or providing brokerage services. CASSPrs that exchange fiat currency to crypto assets and have a geographical link to Australia are subject to regulation as digital currency exchanges, which includes a requirement to register with AUSTRAC and meet AML/CTF compliance and reporting obligations. Further, depending on which crypto assets the CASSPr provides access to (financial product and/or non-financial product crypto assets), prohibitions against misleading or deceptive conduct along with other consumer protections apply under either the ASIC Act or the ACL.

Due to the rapidly evolving and complex nature of the crypto ecosystem and differing regulatory frameworks highlighted above, industry faces challenges in determining its

⁵ Whether a crypto asset is considered a financial product depends on its use, as primarily defined in section 763A of the Corporations Act. As noted in the consultation paper, industry has reported difficulty in determining whether the financial products and services regime or the consumer law apply to certain crypto assets.

⁶ **Digital currency** means:

- (a) a digital representation of value that
 - I. functions as a medium of exchange, a store of economic value, or a unit of account; and
 - II. is not issued by or under the authority of a government body; and
 - III. is interchangeable with money (including through the crediting of an account) and may be used as consideration for the supply of goods or services; and
 - IV. is generally available to members of the public without any restriction on its use as consideration; or
- (b) a means of exchange or digital process or crediting declared to be digital currency by the AML/CTF Rules.

Digital token means any digital representations of interests:

- (a) which are transferable; and
- (b) the transfer or distribution of which is recorded and effected through a Distributed Ledger.

⁷ This delegation does not impact on the ACCC’s ability to enforce the consumer law in relation to non-financial products.

regulatory obligations and requirements. Further, consumers also face challenges in understanding their rights and protections under the law in relation to crypto assets, and as noted in the consultation paper, industry has called for a regulatory framework for CASSPrs to provide confidence to consumers about the services they offer and to improve the reputation and credibility of the sector.

Given the significant growth of crypto assets and rising adoption and usage by Australian businesses and consumers highlighted above, we consider it is important that a licensing regime is established for CASSPrs, with appropriate consumer protections to prevent detrimental conduct and to minimise the likelihood of consumer harm. This will also assist in providing regulatory certainty for CASSPrs and confidence to consumers who transact with CASSPrs, which can encourage innovation and competition.⁸

In the section below, we provide responses to questions in the consultation paper that are most relevant to the work of the ACCC.

ACCC responses to consultation questions

Question 6. Do you see these policy objectives as appropriate?

The ACCC agrees with the proposed policy objectives that underpin the proposed licensing regime for CASSPrs. These are:

- minimise the risks to consumers through mandating minimum standards of conduct and business operations for CASSPrs,
- support the AML/CTF regime, and
- providing regulatory certainty about the treatment of crypto assets and CASSPrs.

We support Treasury's approach to develop a licensing regime for CASSPrs that is administered by ASIC with licence obligations that address the specific business operation and conduct risks posed by CASSPrs. We do not consider the alternative option proposed in the consultation paper of industry self-regulation will effectively achieve the desired policy objectives.

However, we do note that licensing regimes, by design, act as barriers to entry and if the licensing requirements are set unnecessarily high, this can restrict entry, innovation and competitive dynamics in a market.⁹ Given this, it is important that Treasury considers the upfront and ongoing costs the licensing regime will impose upon the range of entities that will seek a licence and ways in which the licensing regime can be designed to minimise barriers to entry while still maintaining appropriate operational requirements and conduct obligations. The ACCC also recommends that a review of the licensing framework occur after an initial period of operation to ensure it is fit for purpose.

Question 11. Are the proposed obligations appropriate? Are there any others that ought to apply?

As noted above, the ACCC is supportive of a CASSPr licensing regime and obligations which sets minimum standards for business operations and for conduct in dealing with consumers.

⁸ As noted in the consultation paper, industry has also called for a regulatory framework highlighting that some form of licensing regime for CASSPrs would provide regulatory clarity and help signal to consumers which operators meet certain minimum standards.

⁹ Pearson G, Walpole S, Davies C, [Australia's Licensing Regimes for financial services, credit and superannuation: Three tracks toward the twin peaks](#), Australian Law Reform Commission, Thomson Reuters, accessed 16 May 2022

In particular, the ACCC strongly supports the inclusion of the following license obligations on CASSPrs:

- to respond in a timely manner to ensure scams are not sold through their platform (obligation 9),
- not to hawk specific crypto assets (obligation 10), and
- to maintain appropriate custody arrangements to safeguard private keys (obligation 13).

However, the ACCC is of the view that Treasury should consider whether the proposed licence obligation in relation to scams (obligation 9) could be expanded to include a requirement for CASSPrs to share information and block accounts involved in scam activity and to take appropriate steps to warn consumers about scams involving crypto assets.¹⁰ Further, an additional obligation could be considered requiring CASSPrs to proactively monitor for fraudulent and scam activity.

Losses to scams involving the use of crypto assets have grown significantly in recent years – scams involving the use of crypto assets resulted in losses reported to Scamwatch of around \$40 million in 2020. This tripled to \$129.4 million in 2021 and this growth is continuing in 2022 with more than \$103 million in losses to scams involving crypto assets from 1 January 2022 to 1 May 2022. Based on this growth, we anticipate that Scamwatch will receive reports of close to half a billion dollars in losses to scams involving crypto assets during 2022. Further, the actual value of losses to these scams is likely to be significantly higher, as our research shows that of all scam victims, only 13% make a report to Scamwatch. In 2021 at least 55% of investment scam losses reported to Scamwatch involved crypto assets and 40% of all scam losses involved crypto assets.¹¹

The ACCC's focus in relation to scams is on disruption and prevention which aims to minimise harm to Australians. This approach includes regulating and engaging with legitimate 'intermediary' businesses and platforms used by scammers, such as social media platforms, online marketplaces, financial providers, exchanges and telecommunications companies. We work with these intermediaries, industry and other government agencies to ensure appropriate consumer protections (including those from legislation and Industry Codes) are in place to minimise harm to consumers from scam activity.

The expanded licence obligation and additional obligation we have proposed below, have been developed from our experience in disrupting scam activity and observing what has worked effectively in a range of industries.

We welcome the opportunity to discuss these options further with Treasury.

Expanding obligation 9 to include a requirement for CASSPrs to share information and block accounts involved in scam activity

Where a CASSPr has access to information about accounts, wallets or business names involved in fraudulent activity, there is currently no efficient way to distribute that information in a standardised format with other CASSPrs and regulators, who can then take appropriate actions to block accounts and minimise scam activity in a timely manner.

¹⁰ Expanding obligation 9 could occur in several ways. For example, obligation 9 could be expanded to include two sub-obligations (with requirements around sharing information and blocking accounts involved in scam activity and taking steps to warn consumers) or this could occur through providing regulatory guidance on practices the regulator of the licensing regime would expect entities to undertake to meet this licensing obligation requirement. The Australian Financial Crimes Exchange is an example of how this could work, see <http://www.afcx.com.au>.

¹¹ ACCC, internal Scamwatch data analysis.

The ACCC has observed from the telecommunications and financial sector that the efficient exchange of information on fraudulent accounts between service providers, enables them to quickly block fraudulent accounts, disrupt scam activity and minimise consumer losses. For example, since the introduction of the Reducing Scams Calls Code in late 2020, which set out processes for identifying, tracing, blocking and otherwise disrupting scam calls, there has been 549 million scam calls blocked in Australia and in 2022 Scamwatch has observed an almost 50% reduction in scam calls.¹²

An obligation for licensed CASSPrs to efficiently share information on fraudulent accounts and wallets and to block these accounts and/or flag to consumers an account they are transacting with may be involved in scam activity, significantly reduces scammer's ability to undertake fraudulent activity, in particular as they typically operate across multiple CASSPrs.

We do note that sharing information within industry requires legal consideration and potential exceptions regarding privacy and competition, and welcome further discussions on this.

Expanding obligation 9 to include a requirement for CASSPrs to take active steps to warn consumers about scams involving crypto assets

Our experience in disrupting scams shows that service or platform providers are best placed to warn consumers about scams, at the time when the consumer is engaging with the platform.

We consider that obligation 9, could be expanded on to require CASSPrs *to take active steps to warn consumers of scam activity on their platform*, and this would assist in significantly reducing scams involving crypto assets.

For example, this could involve:

- CASSPrs taking steps to, during the onboarding process, discuss or notify vulnerable consumers about scams involving crypto assets. Scams can disproportionately impact vulnerable consumers such as older Australians. In 2021, The over 65 age group lost the most money to scams with \$81.9 million lost. The ACCC is aware of one CASSPr which is already doing this.
- Prompts and popup scam warnings could be included on a CASSPr's platform (app or website) similar to warnings we have seen in other industries such as in the banking industry, online selling websites or digital platforms.

Impose an obligation for CASSPrs to monitor for fraudulent and scam activity

While we support the proposed obligation for CASSPrs *to "respond in a timely manner to ensure scams are not sold through their platform"* there remains an issue where CASSPrs are not required to take proactive steps detect fraudulent and scam activity operating on their platform.

We consider CASSPrs could have a license obligation to put in place effective fraud and scam detection measures to monitor accounts and wallets for suspicious transactions and to investigate complaints about potential scams operating on the platform.¹³ Similar obligations are in place in other industries, such as those used in the UK's Contingent Reimbursement Model Code for Authorised Push Payment Scams.¹⁴

¹² ACMA, [Scam crackdown results: Telcos block half a billion scam calls](#), 3 May 2022, accessed 14 May 2022. Scamwatch data 1 Jan -1 May 2022 shows a 46.6% reduction in phone scams with 23,209 phone scam reports in 2022 compared to 43,422 for the same period in 2021.

¹³ We note this may not need to be a separate obligation.

¹⁴ Lending Standards Board, [Contingent reimbursement Model Code for Authorised Push Payment Scams - April 2021](#), accessed 12 May 2022.

Question 17. Do you support self-regulation instead of the proposed licensing regime?

Due to the nature of the risks involved and associated consumer harm, the ACCC considers that self-regulation would not adequately protect consumers nor provide the necessary confidence in CASSPrs to realise the benefits from innovation associated with crypto assets.

The ACCC has experience in dealing with self-regulated industries through its role in enforcing industry codes.

In our experience, self-regulation is most effective where there is an established industry body that has:

- wide-spread support of industry
- comprised of representatives of key stakeholders including consumers, consumer associations, government, and industry groups
- operates an effective system of complaints handling
- is able and resources to act as an effective self-regulatory body.

Given the complexity of the issues we are looking to address, the fact that crypto assets are an evolving and disparate industry, we consider a licencing regime will be more effective.

When transacting with CASSPrs consumers face several risks including counterparty and conduct risk, and there have been several high-profile CASSPr failures in recent years, with many crypto asset investors losing funds. It is also difficult for consumers to gauge the quality of service provided and ongoing viability of a CASSPr.

Licensing regimes sets minimum standard for participation in an industry, including financial, operational, technical and personal competence. These minimum standards enable the regulator to play a *'gatekeeper'* role and the requirement to hold a license with the prospect of a license being cancelled if misconduct occurs, enables these minimum standards of conduct and operation within an industry to be maintained.¹⁵ Licences also provides a clear signal to consumers that an entity is meeting the minimum standards on an ongoing basis, enabling consumers to have greater confidence when transacting in an industry.

Therefore, due to the type of risks involved in transacting with CASSPrs and Treasury's policy objectives in regulating them, we consider that a licensing regime administered by ASIC is the most effective way to ensure standards of conduct and operation are maintained and to minimise the risk of harm to consumers.

¹⁵ Pearson G, Walpole S, Davies C, [Australia's Licensing Regimes for financial services, credit and superannuation: Three tracks toward the twin peaks](#), Australian Law Reform Commission, Thomson Reuters, accessed 16 May 2022