

4 March 2019

Division Head
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: ICO@TREASURY.GOV.AU

Dear Sir/Madam

Submission on Treasury Initial Coin Offerings Issues Paper January 2019

Background and introduction

The Corporations Committee of the Business Law Section of the Law Council of Australia (the **Committee**) believes that blockchain technology offers some exciting opportunities for those that are involved in raising equity and creating new businesses. The Committee has considered the policy and practical issues raised in the Treasury Initial Coin Offerings Issues Paper January 2019 (**Issues Paper**) including some preliminary thoughts on an appropriate regulatory model in the context of offering of tokens to the wider public via a token generation event or initial coin offering (**TGE or ICO**).¹

Based on our experience, TGE do not always comply with existing laws set out in the *Corporations Act 2001* (Cth) (**Corporations Act**), particularly with respect to disclosure, structuring and obligations owed to investors.

The Committee strongly advises against creating any specific exemption from the application of Corporations Act or the Competition and Consumer Act to facilitate TGE or ICOs for three key reasons. First, this safe harbour may effectively allow people to continue to disregard consumer and investor protections which are at the heart of the Australian system when conducting TGE or ICOs. Second, as a safe harbour could be relied on by equally anyone engaging in a TGE, those in the traditional markets may abandon the more highly regulated financial products and instead rely on TGE to raise capital, undermining the robustness of Australia's current corporate and financial regulatory regime. Third, if the law is not technologically neutral, even where people are seeking to issue or trade traditional financial products, these may be inadvertently captured where they use a blockchain back end. An unintended consequence of this is that the nature of the product itself may be changed simply by changing the technology. Of course, this would depend on the nature of any safe harbour itself but its potential to undermine the current regime is not insignificant.

¹ We prefer the nomenclature TGE to ICO as there is a risk that using the ICO nomenclature connects the token offering model too closely to the well understood (but vastly different) IPO process.

Nevertheless, non-compliance with the Corporations Act may also be due to difficulties experienced by those conducting TGE or ICOs in ascertaining the limits of the Corporations Act's regulation or understanding how to properly comply with the requirements. To prevent this, the Committee recommends providing further guidance with respect to when a product may be captured and the limits of the Corporations Act more broadly, as well as the requirements under the Australian Consumer Law. This would assist those engaging in TGE, whether as issuers, purchasers (investors) or otherwise, to understand and have the opportunity to comply with their obligations.

The Committee suggests that Treasury ought to consider from first principles the application of the current regime to TGE, identify any gaps that may arise and ascertain how these might be managed.

Outline

This paper sets out:

1. A summary of existing policy (Existing policy);
2. Principles to be considered in any regulatory regime for TGE (Key regulatory principles);
3. Response to Treasury's questions;
4. Other issues on the regulation of token offerings; and
5. Additional recommendations regarding:
 - a. Investor protection for products which are not regulated under chapter 7 of the Corporations Act;
 - b. Regulatory oversight; and
 - c. Maintaining technologically neutral policy.

Existing policy

In considering the future of Australia's policy with respect to TGE, we should consider the regulatory response to date with respect to both digital currencies and ICOs. Unlike elsewhere, bitcoin and other digital currencies are recognised as products that are not money, or financial products, nor are they illegal. From a policy perspective in 2015, the Senate Economics Reference Committee was of the view that digital currencies were covered by the consumer protection provisions of the *Competition and Consumer Act 2010 (CCA)*.^{2, 3} No change should be made to this position.

² See Senate Inquiry, paras 2.20, 5.15 and 5.27.

³ Australian Consumer Law, s2 "goods"

goods includes:

- (a) ships, aircraft and other vehicles; and
- (b) animals, including fish; and
- (c) minerals, trees and crops, whether on, under or attached to land or not; and
- (d) gas and electricity; and
- (e) computer software; and
- (f) second-hand goods; and
- (g) any component part of, or accessory to, goods.

It is likely that 'computer software' or a component part of, or accessory to such a good, is broad enough to include digital currencies however this may need to be considered further.

More recently, in 2018 both the Australian Securities and Investments Commission (**ASIC**) and the Reserve Bank of Australia's Payment Systems Board made statements with respect to ICOs. ASIC's statement in INFO 225 *Initial Coin Offerings and Crypto-Currency* (**INFO 225**) is relevant for two key reasons. First ASIC reiterates its position taken in 2014 that it does not consider Bitcoin to be a financial product and indicates that some products issued by ICO will similarly not be financial products.⁴ This establishes that certain products created by TGEs will not be regulated under chapter 7 of the Corporations Act.

Second, ASIC provides that the principle of not engaging in conduct that is misleading or deceptive or likely to mislead or deceive is of paramount importance when issuing products through TGE. This applies regardless of whether the product is a financial product fall under the Corporations Act or the *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**) or some other form of good or service under the purview of the Australian Consumer Law.

The Reserve Bank of Australia reiterated previous statements that '*cryptocurrencies do not meet the usual attributes of money and ... are not seen as raising significant policy issues for the Bank*'.⁵ However on the subject of ICOs it cautioned that '*There have been reports of many ICOs that have failed or have been fraudulent; various estimates suggest that anywhere between 20 and 80 per cent of ICOs are fraudulent*'.⁶

These comments should be considered in any approach going forward.

Key regulatory principles

The Committee believes that purchasers of tokens issued in TGE or ICOs must be protected from information asymmetries which arise particularly when trying to price unknown future value. It is for this reason that any regulation must be premised on the overriding principle that issuers or offerors should not engage in conduct that is false, misleading or deceptive or likely to have that effect (as those terms have now come to be understood). This principle is apparent in both corporations and consumer law.

This information asymmetry is frequently alleviated with disclosure. Like Treasury, the Committee's experience has been that green and white papers issued by token issuers have not met standards that we have come to know in other capital market transactions. To protect purchasers, guidance might be provided explaining that TGE offering documents are required to (at a minimum) be clear, concise and effective, having regard to the investors and the nature of the proposal.⁷

Overall, a regulatory model for tokens should:

⁴ ASIC Information Sheet INFO 225 – Initial coin offerings and crypto-currencies (September 2017, updated May 2018) (available online at <http://asic.gov.au/regulatory-resources/digital-transformation/initial-coin-offerings-and-crypto-currency/>) (**INFO 225**).

⁵ Reserve Bank of Australia, Payments Systems Board, *Annual Report 2018*, p.52, available online <https://www.rba.gov.au/publications/annual-reports/psb/2018/pdf/2018-psb-annual-report.pdf>.

⁶ Reserve Bank of Australia, Payments Systems Board, *Annual Report 2018*, p.59, available online <https://www.rba.gov.au/publications/annual-reports/psb/2018/pdf/2018-psb-annual-report.pdf>.

- be technology neutral, that is the regulation should not be driven by product design but by legal rights and responsibilities;
- as far as possible retain the current legal and regulatory framework set out in the *Corporations Act 2001* (Cth) (**Corporations Act**);
- promote efficiency in the capital formation process. The regime should be appropriate and no more onerous than it reasonably needs to be;
- provide purchaser protection based on the nature of the risks posed and the persons who are likely to or able to invest;
- promote disclosure of all relevant information and emphasise the obligation to act in a way other than that which is false, misleading or deceptive, or likely to mislead or deceive;
- protect purchasers from unfair dealings with insiders who had access to material non-public, price sensitive information;
- reduce the likelihood of omitting important information when advertising or marketing TGE or tokens; and
- have a reasonable focus on the information needs of investors.⁸

Further detail regarding these requirements is set out below.

Response to Treasury's questions

Below are our comments on the specific questions raised by Treasury. We explore some of these questions in more detail in the sections following this table.

KEY QUESTION	
1.1. What is the clearest way to define ICOs and different categories of tokens?	<p>While lessons could be learned from other 'quality' regulators like the Swiss Financial Market Supervisory Authority a better approach is to consider the Australian context including previous reform in this field (as identified above).</p> <p>Broadly we suggest that the universe of tokens can be broken into one of three types:</p> <p>Financial product tokens: these issue traditional financial products using a blockchain underlying technology. Some of these use smart contracts to issue shares or other interests. These tokens may either inadvertently be financial products or may purposely be designed to fall within a category of financial product. For instance, some start-ups have attempted to conduct equity token sales (sales of shares in cryptographic form). Others have issued tradable assets 'backed' by and redeemable for precious metals (which frequently have features of derivatives) or tokens backed by real estate (which may be considered to be interests in a managed investment</p>

scheme). Note also that unlike elsewhere around the world, tokens which are facilities through which a payment is made in fiat currency other than by cash will be considered to be non-cash payment facilities.

Whilst places such as Delaware have passed laws allowing companies to maintain a list of shareholder names on a blockchain to enable blockchain-based stock trading it is questionable whether such amendments are needed in the Australian environment. Given the tendency towards being technology neutral, a register can already be kept by computer⁹ and may be kept at a place in this jurisdiction where work involved in maintaining the register is done¹⁰ it is arguable that this requirement may be fulfilled with a blockchain or distributed ledger technology in the back end.¹¹

Digital currencies (not regulated as financial products): unlike other countries, Australia has long recognised a narrow category of digital currencies. Digital currencies may be used as a medium of exchange but do not fulfil the characteristics of money. Nor are they considered to be financial products.¹² Instead these digital currencies have been considered to be covered by the consumer protection mechanisms in the CCA.¹³ This is reflected in the definition of ‘digital currency’ in section 6 of the *Anti-Money Laundering Counter-Terrorism Financing Act 2006* (Cth) (**AMLCTF Act**) and in section 195.1 of the *A New Tax System (Goods and Services Tax) Act 1999* (Cth) (**GST Act**).¹⁴

Some tokens which are considered to be ‘payment tokens’ will fall within this definition. Others will not.

Utility tokens: these include in-app coins or app tokens that are not able to be used outside the system. They provide users with access to a product or service. Frequently the product or service is already in existence. Some examples are tokens which act as a discount coupon to use a network, pre-payment for a service such as the right to use a decentralized cloud storage space

⁹ See section 173(1), Corporations Act.

¹⁰ See section 172(1)(c), (1A)(c), Corporations Act.

¹¹ Note that this may need to be considered further.

¹² Senate Economics Reference Committee, Digital Currency – game changer or bit player (Commonwealth, 2015) (available online at http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Digital_currency/Report/) (**Senate Inquiry**); ASIC, Submission 44 to the Senate Inquiry [5], [44], [51]. Note that at [50] ASIC’s submission provides that digital currencies such as bitcoin are ‘more akin’ to commodities.

¹³ See Senate Inquiry, paras 2.20, 5.15 and 5.27. See also footnote 3 above.

¹⁴ Note that these definitions are slightly different as each was designed to fit with the requirements of the relevant Act.

	using unused computer hard drive space, membership of a network or (provided it complies with the relevant regulatory requirements) loyalty points.
2.1 What is the effect and importance of secondary trading in the ICO market?	<p>The primary market is required to raise capital and gain the network effect. The secondary provides an opportunity to expand that network and the business to access further capital if required.</p> <p>That being said, the secondary markets have be subject to market misconduct, including manipulation due to discounts provided to early purchasers of tokens or pump and dump schemes by so called ‘whales’ or ‘influencers’ through a variety of social media channels.</p>
2.2 What will be the key drivers of the ICO market going forward?	<p>Regardless of whether a token is regulated under chapter 7 of the Corporations Act, the value of a token will be connected to the market as a whole, the demand for the network or product created, security of the network or product and, in some cases, an intrinsic value that derives from its ability to ‘connect’ investors with an instrument linked to a blockchain. For example a token might be linked to gold production and the token be ‘paid’ when each gold sale contract is settled (although this token may be a financial product in and of itself).¹⁵</p> <p>With respect to the market more broadly, there may be a correlation between the success of distributed ledger technologies, smart contracts and tokens, and TGE.</p> <p>Nevertheless, it is important to note that the market has been partially driven by speculation and manipulation which may continue.</p>
3.1 How can ICOs contribute to innovation that is socially and economically valuable?	<p>Work has already begun to transform traditional financial markets using smart contracts and distributed ledger technologies. For instance the ASX is currently replacing CHESS with distributed ledger technology developed by Digital Asset.¹⁶ Similarly, ISDA has been investigating the use of smart derivatives contracts.¹⁷ Outside financial markets, blockchain technologies are considered in use cases such as supply chains, provenance, and monitoring water rights.</p> <p>However it remains to be seen whether a token is necessary to achieve this functionality. Even if required,</p>

¹⁵ Note that in this example the token is likely to be a financial product as it gives a right to a future revenue stream from a pool of assets managed by another, or the price of another asset. This ability to link the asset to the financial product through a smart contract and blockchain technology continues to evolve and may even be subsumed into traditional financial markets as the products being provided (in token form) will be financial products themselves. See for instance work undertaken by ISDA with respect to legal smart derivatives contracts available online at <https://www.isda.org/tag/smart-contracts/>.

¹⁶ ASX, CHESS Replacement, <https://www.asx.com.au/services/chess-replacement.htm>.

¹⁷ ISDA’s publications are available online at <https://www.isda.org/tag/smart-contracts/>.

	<p>the token may simply by a technological mechanism by which the distributed ledger operates and not a separate legal right in and of itself. Care must be taken to ensure that the use of a smart contract alone does not require a person to comply with a regulatory regime above and beyond that which regulates the thing being built itself.¹⁸</p>
<p>3.2 What do ICOs offer that existing funding mechanisms do not?</p>	<p>Based on our experience, TGE offer a method of raising capital that is sometimes cheaper, quicker and (supposedly) has less regulatory hurdles (licensing and disclosure obligations) than traditional initial public offering or issuance of other financial products.</p> <p>TGE allow the public (retail clients) to invest small sums of money in an early stage of a venture no matter where they are in the world. Each of these features – international reach, small investment parcels, and early stage ventures – are not always present in traditional avenues for raising funds.</p> <p>From a business perspective, the person engaging in a TGE is usually looking to implement innovative technology to gain some network effect. At the early stages of the TGE market, this network was united by an appreciation for new technology. This may or may not still be the case depending on the nature of the token being sold.</p> <p>TGE may also provide the opportunity to pre-sell products or develop a network before the product is rolled out, providing early capital to the business and future clients.</p>
<p>3.3 Are there other opportunities for consumers, industry or the economy that ICOs offer?</p>	<p>See our response to question 3.1 above.</p>
<p>3.4 How important are ICOs to Australia's capability to being a global leader in FinTech?</p>	<p>The token market globally is looking for a safe home. Whether Australia should lead the way and what path that may take are matters which remain to be seen. Australia should not be concerned with anecdotal evidence that entrepreneurs are moving to more 'favourable' and less regulated jurisdictions. Instead it should recognise that it has an opportunity to leverage its existing position as a well-respected, sensible and appropriately regulated country and welcome similarly minded projects. Any path</p>

¹⁸ Smart contracts enabled by blockchain technology are programmable applications that manage exchanges of value conducted online. Those exchanges would usually be an asset in exchange for value (but could be an asset in exchange for another asset, or one value for another value that is in a different currency). In the case of blockchain technology that value may also be represented by a digital token. Ryan, P.A., 'Smart Contract Relations in eCommerce', *Australian Journal of Corporate Law* (2017) 7(10) *Technology Innovation Management Review* 10.

	<p>which undermines the robustness of our current regime should be avoided.</p> <p>That being said, as highlighted in responses to question 3.1, distributed ledger technology does not always require a token or a TGE. Similarly, as set out in the response to question 1.1 not all tokens are, or should be unregulated.</p> <p>In this context, Australia’s opportunity is likely to arise from its ability to embrace distributed ledger technology. Australia has a history of leading the field in embracing this technology. In 2017 CSIRO’s Data61 produced two reports for Treasury that examine the risks and opportunities of blockchain technology in Australia.¹⁹ Further initiatives such as these should be encouraged.</p>
3.5 Are there other risks associated with ICOs to raise with policymakers and regulators?	<p>The primary risks associated with TGE identified by the Financial Stability Board are market liquidity, volatility, leverage and technological and operational risks including cyber security risks.²⁰</p> <p>Other key issues (aside from investor protection and illegal offers of financial products) include anti-money laundering and counter-terrorism financing, the impact of sanctions against individuals, privacy, data retention, and taxation (including anti-avoidance) and a need to avoid circumvention of capital controls.</p>
4.1 Is there ICO activity that may be outside the current regulatory framework for financial products and services that should be brought inside?	<p>The Committee suggests that the existing regulatory framework for financial products should, for the most part remain, as is. Unlike elsewhere, the Australian definitions tend to be principles based and technology neutral. This encapsulates most products issued by means of TGE and there is little need to further expand these categories further.</p> <p>Additional discussion regarding amendments to this regime are set out in the response to questions 4.3, 4.5 and additional information in ‘Other issues on the regulation of token offerings and managed investment schemes and ‘Investor protection for products which are not regulated under chapter 7 of the Corporations Act’ below.</p>
4.2 Do current regulatory frameworks enable ICOs and the	<p>See Other issues on the regulation of token offerings and managed investment schemes and ‘Investor protection for products which are not regulated under chapter 7 of the Corporations Act’ below.</p>

¹⁹ Data61, *Distributed Ledgers: Scenarios for the Australian economy over the coming decades*, May 2017, and Data61, *Risks and opportunities for systems using blockchain and smart contracts*, May 2017, both available online at <https://www.data61.csiro.au/en/our-work/safety-and-security/secure-systems-and-platforms/blockchain>.

²⁰ Financial Stability Board, *Crypto-asset markets: Potential channels for future financial stability implications*, 10 October 2018, available online at <http://www.fsb.org/wp-content/uploads/P101018.pdf>.

creation of a legitimate ICO market? If not, why and how could the regulatory framework be changed to support the ICO market?

4.3 What, if any, adjustments to the existing regulatory frameworks would better address the risks posed by ICOs?

The existing regulatory framework creates broad categories of regulated products. For the most part these are well understood and designed with investor protection in mind. However there are instances where the definition of certain financial products when applied to a TGE may no longer be appropriate.

It is apparent from ASIC's INFO 225 that there are circumstances where tokens issued will not be considered to be financial products. It goes without saying that where the token is a product which falls within a category exempted from the definition of a financial product²¹ the existing exemption should still be available. Similarly where the token is merely a receipt for ownership of a physical good, such as an artwork, this too should remain outside the regulated regime.

In other cases the distinction may be a little less apparent. In particular, given the broad definition of 'interest in a managed investment scheme' it is difficult to ascertain when a token may not be a financial product. The Committee recommends providing further guidance regarding where a product which may have certain features of a financial product is not likely to be considered one. This may include examples where a token may be considered to be one of the three categories identified in response to question 1.1 above.

In addition, where a token is designed to operate in a particular industry, the laws which would otherwise apply to that industry remain. For instance, an ICO which focusses on logistics and supply chain management will need to comply with customs requirements and any applicable restrictions on transfers of illegal or controlled goods.

See Other issues on the regulation of token offerings and managed investment schemes and 'Investor protection for

²¹ For example certain products such as loyalty points are excluded from the definition of a non-cash payment facility under ASIC Corporations (Non-cash Payment Facilities Instrument 2016/211).

	products which are not regulated under chapter 7 of the Corporations Act' below.
4.4 What role could a code of conduct play in building confidence in the ICO industry? Should any such code of conduct be subject to regulatory approval?	ASIC has the power to approve a code of conduct in the financial services sector. ²² A code of conduct must not be inconsistent with the Corporations Act or any other law ²³ and should do at least one of the following: (a) address specific industry issues and consumer problems not covered by legislation; (b) elaborate on legislation to deliver additional benefits to consumers; and/or (c) clarify what needs to be done from the perspective of a particular industry, practice or product to comply with legislation. ²⁴ Given the nature of a code of conduct, it cannot be used to amend or provide guidance regarding interpretation of law. There are only narrow circumstances where this may be appropriate and it is not apparent that they exist in these circumstances.
4.5 Are there other measures that could be taken to promote a well-functioning ICO market in Australia?	See response to 4.1 and 4.3 above.

Other issues on the regulation of token offerings and managed investment schemes

As it stands today, a vast majority of token offerings will fall within the gamut of the managed investment scheme (**MIS**) rules. An MIS is deliberately defined widely within the Corporations Act.²⁵ The provisions were designed to regulate a panoply of

²² Corporations Act, s1101A.

²³ Corporations Act, s1101A, and RG 183, [RG 183.28] – [RG 183.34].

²⁴ RG 183, [RG183.5].

²⁵ Defined as:

managed investment scheme ' means:

(a) a scheme that has the following features:

- (i) people contribute money or money's worth as consideration to acquire rights (**interests**) to benefits produced by the scheme (whether the rights are actual, prospective or contingent and whether they are enforceable or not);
- (ii) any of the contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the people (the **members**) who hold interests in the scheme (whether as contributors to the scheme or as people who have acquired interests from holders);
- (iii) the members do not have day-to-day control over the operation of the scheme (whether or not they have the right to be consulted or to give directions); or

(b) a time-sharing scheme;

but does not include the following:

...

(k) a barter scheme under which each participant may obtain goods or services from another participant for consideration that is wholly or substantially in kind rather than in cash;

...

(m) the provision of a crowd-funding service (as defined in section 766F);

(n) a scheme of a kind declared by the regulations not to be a managed investment scheme

collective investments. The breadth of these provisions can be seen in the *Multiplex* decision²⁶. In that case the Court held that a litigation funding arrangement constitutes a managed investment scheme.²⁷ The basic indicators of whether an arrangement is an MIS are as follows:

- people contribute money or money's worth (such as digital currency) as consideration to acquire an interest in benefits produced by the scheme;
- the money or money's worth is pooled together with contributions from one or more other contributors or used in a common enterprise, to produce financial benefits or benefits consisting of rights or interests in property, for the people (the members) who hold interests in the scheme (which includes the contributors or any person who acquired the rights from a contributor); and
- the contributors (or any person holding the rights) do not have day-to-day control over the operation of the scheme but, at times, may have the right to be consulted or to give direction such as through voting or similar rights.²⁸

The breadth of the provision is clear and intentional.

Background

The MIS regime was designed in 1993 and whilst designed to be flexible did not contemplate a bundle of rights that may have no legal structure, operates on a self-executing smart contract running on a peer-to-peer platform and incorporates computer code that can immutably execute certain rules and check for compliance.²⁹

While it had its origins in both CAMAC's [Collective Investments: Other People's Money](#), Report No. 65 and recommendation 89 of the [Financial System Inquiry Final Report](#) the 'collective investment vehicle' was a model designed for a unit trust structure. This structure provides that property is held by a trustee, managed by a management company, and the beneficial interest in the trust fund is divided into units evidenced by certificates held by investors. This does not easily fit with the offer of tokens to subscribers.

The current MIS regime contemplates enterprise schemes where contributions by members are to be 'used in a common enterprise'.³⁰ An offeror must comply with the applicable managed investment, AFS licensing, anti-hawking and product disclosure provisions if offers or issues are made to other persons.³¹ At its heart the MIS regime contemplates a model that includes:

²⁶ [Brookfield Multiplex Limited v International Litigation Funding Partners Pte Ltd](#) [2009] FCAFC 147.

²⁷ See also [Initial coin offerings](#) – ASIC

²⁸ Corporations Act, s9 'managed investment scheme'.

²⁹ Instead, the model was built around the public unit trust. The proposal could have gone further and recommended a broader range of legal structures such as corporate vehicles and limited partnerships. A Corporations and Markets Advisory Committee 2012 report ([CAMAC Report](#)) outlines some of the existing shortcomings of the current legal framework for Australian managed investment schemes and proposes that schemes be established as a separate legal entity. The CAMAC Report illustrates that what is needed to develop a genuine and workable alternative to the use of trust or contract based structures in a managed investment scheme context is a coordinated response from Government

³⁰ Section 9 (a)(ii) of the definition of 'managed investment scheme' - that has been used for other schemes like film finance

³¹ Unless those offers, invitations or issues are excluded offers, invitations or issues although RG 80 does hold out some hope of better treatment when it says at RG 80.30:

- interests being issued by a regulated responsible entity;
- an issuer with material financial and capacity requirements including prescribed minimum capital requirements;
- a constitution that is required to be registered with ASIC and must address certain matters and imposes responsibilities on the responsible entity; and
- the ‘unavoidable overlay of trust law’³² meaning that there is a trust relationship between the issuer and members even if the parties never contemplated that to be the case.

Clarification of application of MIS to TGE

The Committee suggests that this does not satisfy the requirement that rules are no more onerous than they reasonably need to be as issuers and parties purchasing tokens would expect that the rights and obligations the parties have with respect to each other are intended to be contractual, and not fiduciary. Again, this depends on the nature of the token and the nature of the relationship and dependence of the token holder on the issuer’s efforts.

As stated above, where the tokens represent interests in property or some other pooling of assets, this token is highly likely to be considered to be an interest in a managed investment scheme and its issuance must comply with the Corporations Act. Similarly, where the token holder expects the issuer to take into account the interests of the token holder there may be a fiduciary relationship.

However the fringe models of token where the relationship is purely contractual, and the benefits received by the token holder are independent of the future efforts of the token issuer, should be clarified as falling outside the definition of a managed investment scheme.

The Committee would welcome the opportunity to work with Treasury to provide guidance to the industry regarding the delineation between products regulated under chapter 7 of the Corporations Act, such as managed investment schemes and financial products for making an investment, and products which should remain under the general consumer law. This delineation should take into account the differing nature of the rights, obligations and relationships between the person issuing the tokens, purchaser of the tokens and the use of the tokens by the purchaser.

However, a promoter who believes that there are grounds on which we should exercise our discretion may still apply for individual relief. We may grant relief from requirements under the Corporations Act, including the requirement that a managed investment scheme be registered under Ch 5C, on a case-by-case basis in certain circumstances: see Regulatory Guide 51 *Applications for relief* (RG 51).

³² *Investa Properties Ltd v Westpac Property Funds Management Ltd* (2001) 187 ALR 462 see also R. I. Barrett [Insolvency of registered managed investment schemes](#) July 2008.

Investor protection for products which are not regulated under chapter 7 of the Corporations Act

Nevertheless, as investor protection is paramount, further guidance might be provided for sale of tokens which are not financial products. The Committee suggests this might include minimum disclosure requirements which might follow those required for financial products.³³ The standard of information required may depend on the sophistication of the persons eligible to receive product and the nature of the product itself. Some of these requirements may be as follows:

- include the following information in a disclosure document:
 - date of issuance;
 - name and contact details of the issuer;
 - listing affiliates and providing details of its affiliates;
 - dispute resolution mechanism;
 - cost of the product and any ongoing fees;
 - significant characteristics or features of the product; and
 - the rights, terms, conditions and obligations attaching to the product;
- assurance by the issuer to the token holders (present and future) that the terms and conditions are a true and accurate reflection of the way the token functions at the date of issuance. This would include with respect to the smart contract and the underlying distributed ledger;
- require the issuer to consider whether the product is otherwise regulated under the Australian Corporations Act;
- the purchaser must receive all information that a person would reasonably require for the purpose of making (or be expected to reasonably influence) a decision to acquire the product offered in connection with a TGE;
- the issuer must not act in a way that would diminish the rights of investors, manipulate the price of a product or act contrary to the security of the market as a whole; and
- ASIC should have a mechanism to take action against those involved in the sale process including by issuing stop notices, including where the products are not regulated under chapter 7 of the Corporations Act.

Regulatory oversight

With respect to regulatory oversight, since May 2018, ASIC has had a delegation of power from the ACCC to take action with respect to ICOs where there is potential misleading or deceptive conduct. This delegation effectively permits ASIC to act as the relevant regulator with respect to all products issued by way of TGE. The Committee submits that where regulatory oversight is necessary for TGEs, ASIC should retain this position.

Technologically neutral

As noted above any regulatory response, including with respect to classification of a token as a financial product or otherwise, must be technology neutral. Instead, it should take into account the differing nature of the rights, obligations and

³³ In particular it may follow the requirements for disclosure under a FSG (see s942B of the Corporations Act) or a PDS (see s1013D of the Corporations Act).

relationships between the person issuing the tokens, purchaser of the tokens and any use of the tokens.

Similarly, where a product uses a distributed ledger, blockchain or smart contract in its technological architecture, this should not necessitate compliance with any regulatory regime or guidance. Care must be taken by Treasury when providing guidance that it does not inadvertently require those undertaking normal business processes with new technologies to comply unnecessarily. Such a requirement would also be contrary to the principle that regulation is no more onerous than reasonably necessary.

If you have any questions in relation to this submission, please do not hesitate to contact Chair of the Committee, Shannon Finch, (slmf2497@gmail.com or 0400 442 991).

Yours sincerely,

A handwritten signature in black ink, appearing to read 'R Maslen-Stannage', with a long horizontal flourish extending to the right.

Rebecca Maslen-Stannage
Chair, Business Law Section