May 19, 2023

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Email: economics.sen@aph.gov.au

Dear Sir or Madam,

Ripple Labs Inc. ("Ripple") welcomes the opportunity to comment on the consultation on the Digital Assets (Market Regulation) Bill 2023[1] (the "Digital Assets Bill") referred to the Economics Legislation Committee by the Australian Senate on March 30, 2023.

Ripple would like to thank the Senate Standing Committees on Economics (the "Senate Standing Committees") for the in-depth and comprehensive analysis that has been undertaken in drafting the Digital Assets Bill, as well as the opportunity to provide our comments. We respectfully request you take them into consideration as you consider the policy direction and scope of intended regulation for the digital assets sector. We welcome the opportunity for further engagement on the Digital Assets Bill, and any other related consultations as may be appropriate.

Ripple is also appreciative of 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 Senate Select Committee") on May 18, 2021.[2] Ripple responded to the Discussion Paper ("Ripple Senate Select Committee Response") on June 30, 2021,[3] and we thank the Senate Select Committee for considering our feedback in the final report published in October 2021.[4]

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[1] *See* https://parlinfo.aph.gov.au/parlInfo/download/legislation/bills/s1376_first-senate/toc_pdf/23S1220.pdf;fileType=application%2Fpdf, Digital Assets (Market Regulation) Bill 2022.
[2] 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.
[3] *See* https://ripple.com/files/Ripple_Australia-Senate_Third-Issues-Paper_May-2021_final.pdf, Ripple response to Senate Select Committee on Australia as a Technology and Financial Centre Third Issues Paper.
[4] *See* https://parlinfo.aph.gov.au/parlInfo/download/committees/reportsen/024747/toc_pdf/Finalreport.pdf;file

1. Introduction

Using blockchain technology, Ripple allows financial institutions to process payments instantly, reliably, cost-effectively, and with end-to-end visibility anywhere in the world. Our customers are financial institutions and other corporations that want tools to effect faster and less costly cross-border payments, as well as to eliminate the uncertainty and risk historically involved in moving money using interbank messaging alone.

Some customers, in addition to deploying Ripple's blockchain solution RippleNet, leverage the digital asset known as XRP for an On-Demand Liquidity ("ODL") capability. Just as Bitcoin is the native asset to the open-source Bitcoin ledger, and Ethereum is the native asset to the open-source Ethereum ledger, XRP is the native asset to the open-source XRP Ledger. XRP, given its unique design, can serve as a near instantaneous bridge between fiat currencies (or any two representations of value), 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 operates on what is known as a "consensus" protocol. While there are well over a hundred known use cases for XRP and the XRP Ledger, 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 efficiency, all of which benefits the customer and helps reduce friction in the market for cross-border payments.

As highlighted in the Ripple Senate Select Committee Response,[5] these products and features can help reduce friction in the market for cross-border payments, thereby removing barriers to Australia's growth as a technology and finance centre.

2. Cross-border Payments using RippleNet & ODL

Ripple believes that blockchain technology demonstrates the potential to transform many sectors of Australia's economy, including in cross-border payments. However, we also believe that for any technology, success is based on its use cases and ability to solve real-world problems.

Cross-border payments are costly, full of friction and slow. Much of this friction is the result of processes followed in cross-border payments, until now the domain of incumbent banks (referred to as correspondent banks). A definition cited by the Bank for International Settlements defines correspondent banking as *"the provision of current or other liability account and related services to other financial institutions (including affiliates), used for the execution of third-party payments and trade finance as well as its*

Type=application%2Fpdf, Senate Select Committee on Australia as a Technology and Financial Centre Third Issues Paper Final Report.

[5] *See* Ripple Senate Select Committee Response, page 2.

own cash clearing, liquidity management, short-term borrowing and investment needs in a particular currency."[6]

As this definition highlights, banks use correspondent relationships - a network of bilateral accounts-based relationships - spread across the world to process payments. Although widely proliferated, the market structure of correspondent-banking injects significant friction, delays, and costs in processing payments for the respondent banks, primarily due to the need to prefund accounts.[7]

RippleNet, the cross-border payments solution offered by Ripple, connects hundreds of financial institutions around the world via a single API which makes transferring money faster, cheaper, and more reliable. It also helps to reduce, and even eliminate, the need to prefund accounts with ODL, a service that uses the digital asset XRP to source liquidity during cross-border transactions as an alternative to traditional funding mechanisms. RippleNet customers can use XRP to bridge two currencies in a matter of minutes, ensuring payments are quickly sent and received in local currency on either side of a transaction. The broad ODL flow is outlined in Figure 1 below.

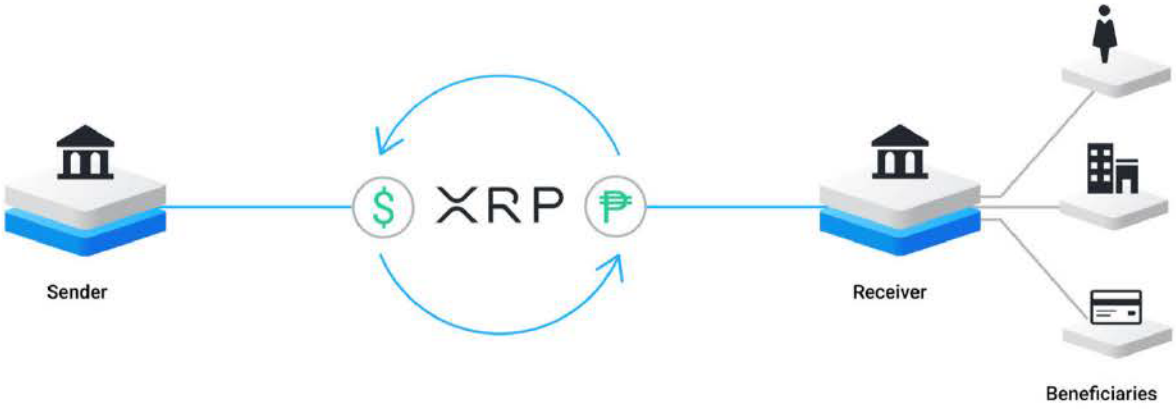

Figure 1: ODL Flow

Digital assets issued on blockchains that serve the same end-use as the incumbent correspondent banking model can offer a compelling alternative for end-users while still being compliant with anti-money laundering ("AML") and countering the financing of terrorism ("CFT") requirements. Global multilateral bodies have also recognized the potential digital assets and blockchain technology have in facilitating faster cross-border payments.[8]

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[6] *See* https://www.bis.org/cpmi/publ/d147.pdf, Committee on Payments and Market Infrastructures – Correspondent Banking.
[7] *See* https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf, BIS Quarterly Review March 2020, page 31.
[8] *See* https://blogs.worldbank.org/psd/paying-across-borders-can-distributed-ledgers-bring-us-closer-together, World Bank blog.

3. General comments and policy considerations

We respectfully submit that any regulatory framework for digital assets should encourage responsible innovation by service providers and intermediaries while also ensuring appropriate risk management. In doing so, the Senate Standing Committees will not only promote the strengthened operational resilience of the digital asset ecosystem, but also transform the way digital asset services are provided. This will ultimately benefit both industry and end-users, and encourage investment in new technologies and innovation. We therefore believe it is imperative that the Senate Standing Committees take into account the following guiding principles as it develops a regulatory framework for digital assets, or determines where digital assets best fit into existing frameworks. Taken together, these principles will encourage the potential of blockchain and digital asset technology, while also establishing important consumer and market protections that ensure global alignment and reduce the risk of regulatory arbitrage.

Principle 1 - Adopt a globally consistent taxonomy

It is important to note that there is no single or generally recognised definition of digital assets in Australia at present. Ripple respectfully submits such assets should not solely be defined relative to a specific technology (e.g., cryptography), but, for purposes of regulation, should instead fall under a broader heading such as "digital assets" and subsequently be 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, but rather on the inherent characteristics of a token and the rights that attach to it.

Therefore, we respectfully request that the Senate Standing Committees consider adopting a taxonomy for digital assets consistent with global best practices to provide clarity as to the legal character of such assets in Australia. Additionally, Ripple recommends that there be a clear distinction between payment tokens, utility tokens, and security tokens, as outlined below:

- *Payment 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.

Principle 2 - Implement a risk-sensitive regulatory framework

We are supportive of the Senate Standing Committees applying effective regulation, supervision, and oversight to digital asset activities and markets in proportion to the financial stability and consumer protection risks they pose (or potentially pose), in line with the principle of "same activity, same risk, same regulation." We also recommend that the regulatory framework should also align with the following principles to be truly risk-sensitive:

- 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 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 and unwittingly increasing financial stability risk through 'business-model herding'.[9] Therefore, we recommend that the Senate Standing Committees consider a **principles-based** regulatory framework that is drafted in a way to steer market participants to specific regulatory and policy objectives while maximizing flexibility and breadth of application; and

- The regulatory framework should use a **risk-based** approach to identify digital asset services that pose sufficient risk to warrant regulation. A simple, and obvious initial distinction in risk-profile should be between digital asset intermediaries that provide services to consumers ("B2C") and those that only provide enterprise services to businesses ("B2B").[10]

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 policy goals of encouraging innovation and growth of digital assets in Australia.

Principle 3 - Foster innovation sandboxes

Innovation sandboxes for market participants to test new and innovative products, services, and business models with end-users in a controlled environment while being

[9] That is, the implicit market bias towards certain business models due to the regulatory requirements attached to given financial activities rather than to the behaviour of the market and fundamentals. This can reduce financial stability by undermining actor diversity and hence overall resilience within a financial system.

[10] Regulation has often drawn distinctions between B2B and B2C business models given the inherent differences between retail consumers and more sophisticated market actors. Examples include, but are not limited to, the European Union's Second Payment Services Directive and Markets in Financial Instruments Directive.

subject to regulatory oversight have been set up in multiple jurisdictions. However, while some regulators have set up successful sandboxes, many regulators currently do not offer any opportunity for such experimentation. This could lead to a potential divergence between jurisdictions in their expertise of supporting the digital asset sector with the likelihood of regulatory fragmentation, and potentially even regulatory arbitrage, arising.

In order to incentivise innovation and inform the development of clear and consistent regulatory frameworks for digital assets, we believe innovation sandboxes should be encouraged in Australia, at the very least for specific use cases such as cross-border payments. For example, the Monetary Authority of Singapore has a FinTech Regulatory Sandbox[11] which allows market participants to experiment with innovative solutions in a live environment, but within a well-defined space and duration.

However, it is important to note that innovation sandboxes will only be useful if there are clear entry and exit criteria defined, as well as parameters to measure the success of the sandbox.

Principle 4 - Encourage public-private collaboration

Any policy framework intended to regulate digital assets should promote an active dialogue between regulators and market participants. Such public-private collaboration will lead to more appropriate and effective policy outcomes for the industry and consumers alike. A collaborative forum that brings regulators and industry stakeholders together to build a rational and holistic framework for blockchain and digital assets would represent a substantial step forward toward achieving regulatory clarity in Australia.

We welcome the opportunity to provide feedback to the Senate Standing Committees on the Digital Assets Bill as well as the related consultations, and recognise this is an important step in furthering public-private collaboration.

Principle 5 - Ensure global consistency and comparability

Lastly, given the cross-border nature of digital asset markets, Ripple supports having minimum global standards, supported by cross-border cooperation and information sharing across jurisdictions, to help ensure an approach that is consistent and comparable.

However, Ripple posits that a framework that supports mutual recognition of licenses across jurisdictions could also lead to a level playing field globally, thereby supporting the sustainable growth and development of the digital assets ecosystem.

[11] *See* https://www.mas.gov.sg/development/fintech/regulatory-sandbox, Overview of Regulatory Sandbox.

Such mutual recognition decisions exist for traditional financial institutions and infrastructures, which can be used as a template for digital asset service providers and intermediaries. Many of the regulatory and supervisory institutions for digital asset companies would be the same as those for the traditional financial sector, which should foster trust and ease communication between jurisdictions. However, Ripple would like to highlight that in making such a determination, a principles-based approach should be followed (in line with Principle 2 noted above). An overly prescriptive process for a mutual recognition determination could disincentivize global firms from exploring this option.

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With this overview, Ripple respectfully submits the following feedback to the Digital Assets Bill in the Appendix.

Ripple appreciates the opportunity to provide feedback on the Digital Assets Bill as you study 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

Sincerely,

Ripple Labs Inc.

APPENDIX

Ripple respectfully submits the following feedback to the proposals set forth in the Digital Assets Bill[12].

1. Part 1, Section 5 - Definitions (Digital Assets)

Ripple is supportive of the Digital Assets Bill using the term digital assets, as we believe that such assets should not be solely defined relative to a specific technology (e.g., cryptography). However, the existing definition of digital assets in the Digital Assets Bill is far too broad to give the market comfort as to the legal nature of such assets. As highlighted in Principle 1 of Section 3 (General comments and policy considerations) and in the Ripple Senate Select Committee Response, there is no single or generally recognised definition of digital assets in Australia at present.

Therefore, for the purposes of regulation, Ripple respectfully submits that digital assets should subsequently be classified and defined 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 such classifications. We have summarised the taxonomies for the UK[13] and Singapore respectively in Figure 2 & Figure 3 below.

Regulated Tokens

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.

b. E-money tokens: These are tokens that meet the definition of e-money under the Electronic Money Regulations. These tokens fall within regulation.

Unregulated Tokens

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.

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.

Figure 2: Summary of the UK Financial Conduct Authority taxonomy for digital assets

[12] Unless otherwise defined, all terms in this section use the definitions provided in the Digital Assets Bill.
[13] It should be noted here that the Financial Conduct Authority taxonomy will clarify, for regulatory purposes, the broader legislative definition of a 'cryptoasset' proposed in the Financial Services and Markets Bill which is currently being debated in the UK Parliament. *See* https://bills.parliament.uk/publications/50528/documents/3210, Financial Services and Markets Bill.

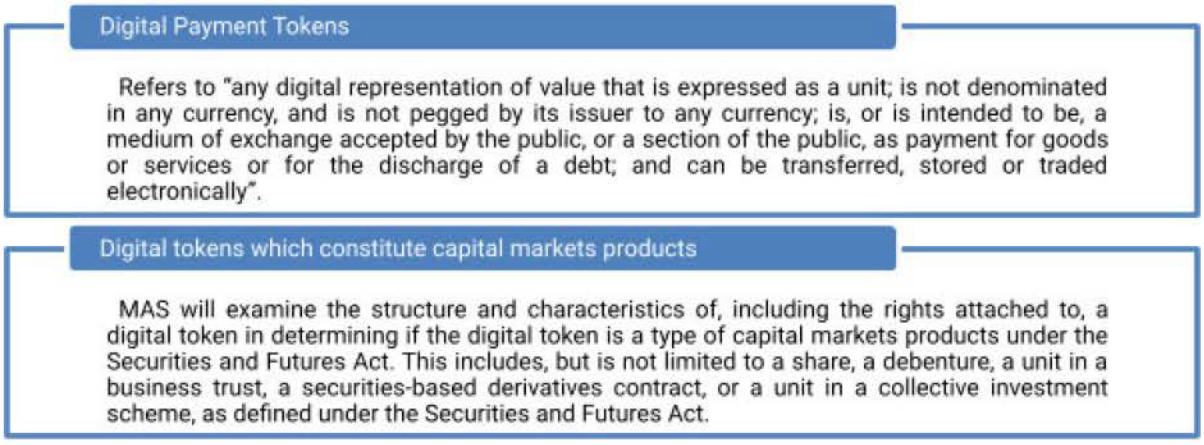

Figure 3: Summary of the Monetary Authority of Singapore taxonomy for digital assets

As highlighted in Principle 1 of Section 3 (General comments and policy considerations) and in the Ripple Senate Select Committee Response,[14] we recommend that there be a clear distinction between payment tokens, utility tokens, and security tokens, in line with global practices 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.

Ripple also respectfully submits that one definition of digital assets (and the categories of tokens) be developed to apply across all Australian regulatory frameworks. Accordingly, since digital assets that fall within the definition of a financial product (i.e., security tokens) under the financial products regime are already regulated by the Australian Securities and Investments Commission ("ASIC"),[15] any such amendments should also be made to the relevant ASIC regulations. Similarly, the Anti-Money Laundering and Counter-Terrorism Financing Act, 2006[16] defines digital assets as digital currencies, and will similarly need to be amended.

Ripple believes that such an approach will help provide clarity as to the legal character of digital assets in Australia.

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[14] *See* Ripple Senate Select Committee Response, page 7.
[15] *See* https://asic.gov.au/regulatory-resources/digital-transformation/crypto-assets/, Information Sheet 225: Crypto-assets.
[16] *See* https://www.legislation.gov.au/Details/C2021C00243, Anti-Money Laundering and Counter-Terrorism Financing Act, 2006.

2. Part 1, Section 5 - Definitions (Digital Asset Exchange)

Ripple believes that, as currently drafted, the definition of Digital Asset Exchange is far too broad as it could include digital assets a party trades for its own account. We believe that the policy intent here is not to capture such activities, as they are technically not that of an exchange. However, such activities could fall within the definition of *"exchanges of regulated digital assets for currency (whether Australian or not); (b) exchanges of regulated digital assets for other regulated digital assets; and (c) exchanges of currency (whether Australian or not) for regulated digital assets."*[17]

Ripple respectfully requests that the definition of Digital Asset Exchange be amended to carve out digital assets that a party trades for its own account (for currency or for other digital assets) to ensure that the definition aligns with the policy intent of exchanges that act as intermediaries between third party buyers and sellers.

This approach is consistent with that taken by Singapore, where the definition of Digital Asset Exchange in the Payment Services Act, 2019 (the "PS Act") specifically carves out digital asset trades done on one's own account[18]:

"does not include a place or facility (whether electronic or otherwise) that is used exclusively by one person to do only either or both of the following things:
(i) to make offers or invitations to buy or sell any digital payment token in exchange for any money, or any digital payment token (whether of the same or a different type);
(ii) to accept any offer to buy or sell any digital payment token in exchange for any money, or any digital payment token (whether of the same or a different type)"

3. Part 2, Division 3 - Digital asset custody services and Part 7, Section 52 - Application to digital asset custody services

As currently drafted, the provisions of Part 2, Division 3 (Digital asset custody services) when read with Part 7, Section 52 (Application to digital asset custody services) appear to indicate that the Digital Asset Custody Service License requirement does not apply to those providers who provided Digital Asset Custody Services before commencement of the Digital Assets Bill. We therefore welcome clarification around the grandfathering of the Digital Asset Custody Service License.

4. Part 2, Division 5, Section 31 – Recognition of foreign licenses etc.

Ripple is supportive of the proposal to recognise foreign licenses in the Digital Assets Bill, and we believe this aligns with Principle 5 of Section 3 (General comments and policy considerations). We also believe such recognition will make Australia an attractive destination for global firms, thereby supporting the growth and development of the Australian digital assets and payments ecosystem.

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[17] *See* Digital Assets Bill, Page 4.
[18] *See* Payment Services Act 2019, First Schedule, Part 3.

However, as also highlighted in Principle 5 of Section 3 (General comments and policy considerations), we respectfully request that the Minister follow a principles-based approach in making an equivalence decision for recognition of foreign licenses. An overly prescriptive and onerous process for an equivalence determination could disincentivise global firms from entering the Australian market, and thereby have the unintended consequence of moving this growing market offshore.

5. Part 2, Division 2, Section 12 – ASIC to supervise digital asset exchanges

Ripple is supportive of ASIC supervising digital asset exchanges in Australia. However, as highlighted in our comments on Part 1, Section 5 (Definitions) of the Digital Assets Bill, we respectfully request that one definition of Digital Assets (and the categories of tokens) be developed to apply across all Australian regulatory frameworks, including the financial products regime, and any such amendments be made to existing ASIC regulations as needed.

6. Part 7, Section 51 – Transition period

Ripple is supportive of a transitional period to allow digital asset exchanges and digital asset custody services sufficient time to make an application for the relevant licenses.

Ripple also respectfully requests that in addition to a transition period, an exemption regime also be considered for digital asset exchanges and digital asset custody services, and such exemption should be valid until the license application is approved, rejected, or withdrawn. It would also be beneficial for the list of exempted entities to be made public, to ensure consumers and end-users have a ready reference as to which entities are covered under the exemption regime.

One example of a jurisdiction with such an exemption regime is Singapore, where under the Payment Services (Exemption for Specified Period) Regulations 2019,[19] certain entities are granted an exemption until the date that the application is approved, rejected, or withdrawn.

An exemption regime, as outlined above, will ensure minimal disruption to digital asset services while license applications are being processed, and will therefore minimise disruptions to consumers and end-users during the transition to a licensing regime.

[19] *See* https://sso.agc.gov.sg/SL/PSA2019-S809-2019?DocDate=20191205, Payment Services (Exemption for Specified Period) Regulations 2019.