De-banking questions

Question 1: Does de-banking happen globally in other jurisdictions? How do we prevent de-banking from happening in Australia?

As we have noted in our submission, de-banking continues to be a considerable issue across the entirety of the Australian fintech market. New and innovative businesses are unable to start and grow in Australia, due to de-banking acting as a steep barrier to entry. If we continue to allow de-banking to occur, we may see that companies could choose to do business in foreign jurisdictions, taking jobs and innovation with them.

De-banking happens in many jurisdictions, but the cause of de-banking differs across jurisdictions. For example, in China, cryptocurrency businesses have recently been banned and de-banked due to a policy decision in relation to cryptocurrency. In Australia, the primary reason for de-banking seems largely due to the major bank's fear of fines and other regulatory penalties. This fear stems from recent money laundering breaches by the banks and the resulting fines from the regulator, the Australian Transaction Reports and Analysis Centre (**AUSTRAC**). Fines are given under our Anti-Money Laundering and Counter-Terrorism Financing (**AML/CTF**) legislation and supported by the Financial Action Task Force (**FATF**), the global group that sets international AML/CTF standards. The secondary reason for de-banking seems to be the banks' anti-competitive conduct. De-banking is a commercially convenient reason for banks to slow down new competition. This competition concern has been identified by the Australian Competition and Consumer Commission (**ACCC**) in its response to Treasury's Payment Systems Review, as set out in the report *Payment Systems Review: From system to ecosystem*, August 2021. In contrast to Australia, one member noted that international money transfer businesses find it very easy to open and maintain accounts in Europe, whereas in Australia they have been de-banked multiple times.

Regardless of whether and why de-banking occurs overseas, the most important focus for the government should be the prevention of de-banking within Australia. As noted, the cause of de-banking is primarily the bank's concerns around possibly breaching money laundering compliance obligations. This results in an unnecessarily conservative approach to fixing the issue. These concerns stem in part from the need to monitor and report international money transfers (**IMTs**), where money received from and sent overseas, to AUSTRAC and AUSTRAC's scrutiny of these transactions as well their sensitive risk perception. It is important to note that both traditional banks and many fintechs facilitate IMTs. Major banks incur an astronomical cost to process IMTs and processing such payments takes a long-time. In contrast, a third-party fintech is able to facilitate IMTs at a far lower cost and much more efficiently than the major bank's SWIFT network. It is also important to note that despite banks' large amounts of spending, they are still vulnerable to IMT-related money laundering breaches.

FinTech Australia poses the following question: "What is it that banks do that give them the license to operate despite contravening the law with respect to IMTs?" The answer is that banks have systems in place to mitigate money laundering risks and manage the consequences of any breach. These systems have become more important to banks following the large fines given out by AUSTRAC for breaches in recent years. However, by the same logic, a payments fintech that demonstrates that they are able to process IMTs with the same level of safety as a bank should be able to also process these transactions with the appropriate conditions.

It is critical to remember that fintechs in the payments space are the key to Australia remaining an innovator in the sector. The practice of de-banking continues to lead to a significant damper on competition. FinTech Australia acknowledges that while major banks have the advantage of being authorised deposit-taking institutions with an exchange settlement account with the Reserve Bank of Australia, fintechs in the payments sector will continue to play an essential supportive role for the major banks. It is the fintechs that will continue to improve efficiency in payments to the benefit of Australian consumers, merchants and businesses generally and push innovation into the local and global markets. Furthermore, preventing de-banking will enhance investment by enabling responsible fintechs to invest in Australia with operational certainty.

Prevention

In short, de-banking can be prevented by ensuring that major banks cannot break a contract or arrangement with a fintech on the basis of perceived AML/CTF risks without providing some form of natural justice to that fintech. Fintechs are regulated on the same terms for AML/CTF risks as the banks. Given the very strict regulations placed on many payments-sector fintechs, it is disappointing to see that complying fintechs are still being de-banked. An internal and opaque decision making process within a bank cannot be allowed to be the primary determinant for whether a fintech is to be debanked. FinTech Australia recommends that AUSTRAC should be required to release clearer guidelines to the industry to clarify the obligations of banks and the obligations of fintech businesses. A more transparent code of conduct will reduce the occurrence of de-banking to the benefit of banks and fintechs alike.

FinTech Australia argues that banks should be required to have valid reasons and be held accountable for the de-banking decisions they make. Banks must actively address risk and other commercial considerations with customers before a de-banking decision is made. Regulators should also address the issue of constructive de-banking, where banks either cap value limits to cap a customer's growth or increase pricing or security arrangements which effectively de-bank clients. Furthermore, to combat the frequent occurrence of de-banking, banks should be required to have a duty not to act uncompetitively. In turn, the AML/CTF Act or Rules should be amended to introduce a duty upon banks to act reasonably with regard to the interests of the customer and the stability of the financial system. Similarly, these same duties should apply to AUSTRAC in its enforcement activities.

It is also important to note that there is no uniform appeals process for fintechs that have been de-banked. Unlike elsewhere where complaints can be made to independent bodies such as ombudsman, or the Australian Financial Complaints Authority, that consider and resolve disputes, these bodies have not considered debanking. We suggest a uniform and binding appeals process where debanked customers can speak with a clearly identified regulator or ombudsman, who would then determine whether the de-banking was reasonable in the circumstances, would go far in solving some of the uncertainty and impacts of de-banking. A bank should have to justify why a de-banking decision is made. Upon review, a decision to debank should be overturned where a bank has not acted reasonably. This process could be supported by a voluntary self-reporting scheme, where a proposed regulatory body holds a database of debanked entities. This would enable regulators to identify patterns of de-banking behaviour and may assist in identifying systemic problems.

The process put in place by the United Kingdom's Financial Conduct Authority (**FCA**) as outlined in the Australian Competition and Consumer Commission's (**ACCC**) 2019 Foreign Currency Conversion Services report (which is explored further in response to the following question taken on notice) is instructive. This outlines a reasoning process for a bank to go through with a relevant authority when choosing to de-bank a fintech. This guide is not the limit for what standard should be set but it provides a great foundation.

Alternatively, where a fintech is already reporting to AUSTRAC directly, liability of the bank in respect of AML/CTF risks should shift to the fintech where that bank has made reasonable enquiries to confirm the fintech is complying with the requirements under the AML/CTF Act, including reporting to AUSTRAC. This would provide more comfort to banks that the fintech is subject to its own compliance obligations.

Additionally, reducing the reliance of fintechs on traditional financial institutions is another step towards the prevention of de-banking. This can be achieved through numerous ways, including lowering access requirements for direct access to payments architecture.

Question 2: What is our view on the ACCC's 2019 due diligence report on Foreign currency conversion services in Australia? The report found that de-banking was a significant issue for non-bank international money transfer suppliers.

In its 2019 report, the ACCC Foreign Currency Conversion Services Inquiry identified de-banking of non-bank IMT suppliers as damaging to both innovation and competition.[1] Although the ACCC did not find that the banks were engaging in anti-competitive behaviour, the ACCC recommended that banks and IMT suppliers engage in a due diligence scheme that involved a review process.[2] Similarly, in their submission to the Senate, ACCC representatives affirmed their support for a review or appeals process for debanked individuals or entities. As outlined in our previous question taken on notice, we support the proposal for a review process for de-banking and believe it would open communication and clarify compliance expectations from banks.

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[1] ACCC Foreign currency conversion services inquiry, Final Report, July 2019, p. 57.
[2] ACCC Foreign currency conversion services inquiry, Final Report, July 2019, p. 64.

However, we note that a due diligence scheme is likely to add additional cost to onboarding IMTs. Banks already conduct due diligence to satisfy themselves of the risks posed by banking with an IMT. An additional requirement for due diligence beyond a bank's investigation may prove to be repetitive for scaleups that already face certain resourcing constraints. Furthermore, imposing a due diligence scheme involving government prior to banking an IMT is unlikely to assist in solving de-banking. De-banking is more concerned with the actions of a bank after the engagement is entered into, rather than beforehand. In turn, a due-diligence scheme is likely to act as another hoop for IMTs to jump through.

In turn, instead of an up-front due diligence scheme, when a bank chooses to de-bank an IMT, the bank should be required to provide written reasons and indicate where the risk profile deviates from that of the banks. If AML/CTF is the reason given, then the bank should be required to provide notice to the IMT in writing and give an indication of where they believe the AML/CTF risk is that is distinguished between the activities of the IMT and the bank. If a bank provides this notice to the IMT, then the IMT should be able to have a period to rectify this perceived deficiency. If the IMT is unable or unwilling to rectify the issue then the bank can proceed with a de-banking. If the de-banking occurs on grounds which are unreasonable then the matter should be appealable to independent arbiters either in government or quasi-judicial or judicial authorities. In turn, the process of meeting AML/CTF obligations will be comprehensive, secure and fair.

Cryptocurrency questions

Question 1: Cryptocurrency in Australia may go down the path of requiring a market license, not an ASFL or self-regulatory alternative. If a market license approach is taken - what does the ideal market license look like for cryptocurrency?

The Australian Market Licence (**AML**) regime is not currently designed for large volumes of applicants. There have only been a small number of licences granted thus far and the process for obtaining an AML remains relatively bespoke depending on the nature of each business. The application process for an AML is known to be extremely complicated to apply for. It requires a business to have a comprehensive understanding of a range of principles as well as an understanding of how their company might meet those principles. In particular it imposes significant capital requirements to operate the market and maintain operations and procedures. It is clear these AML obligations are not designed for smaller businesses, like fintechs, due to the large capital requirements and procedural and operational requirements. In its current state, the market license approach would act as an unfair barrier to entry for fintechs and stifle innovation and growth in the crypto-asset sub-sector.

In contrast, the Australian Financial Services Licence (**AFSL**) is relatively easy to apply for as it is accompanied by a wide range of guides and resources provided by regulators such as ASIC to assist applicants. The AFSL regime is well understood within the industry, suitable for large volumes of applicants and can be tailored based on particular authorisations. For these reasons, FinTech Australia continues to maintain that an ASFL is an appropriate requirement for crypto-asset businesses looking to provide crypto-assets that fall within the definition of a financial product. Fintech Australia also supports statements made in the Payments Review Report that a “flexible framework” is required to “allows [sic] cryptocurrencies to be brought into regulation should there be a policy requirement to do so.”

FinTech Australia acknowledges that if cryptocurrencies were to become (or to be) financial products, a crypto-asset exchange would need to hold an AML under the current regulatory framework. However, for the reasons set out above, we consider the AML regime is not well adapted for this purpose as of the present. Instead we suggest providing further guidance and streamlining the process to obtain a market licence. This could be addressed by adapting a process more like the AFSL application process. This could be accompanied by strategies to improve industry understanding and ease of application.

Were crypto-asset exchanges required to hold an AML, FinTech Australia recommends that the government release additional guidance to support fintechs’ applications for licenses. Explicit regulatory guidance should be released to assist fintechs to apply for and attain their AML, as well as to assist the Australian Securities and Investments Commission (**ASIC**) to process and assess these applications. An increased level of guidance will reduce barriers to entry for fintechs and improve the standardisation and efficiency of license application approval processes. Standardisation provides certainty and may also improve compliance with general principles which are required to promote efficient and fair markets.

Alternatively, a new category of authorisation under an AFSL could be created. A new category would enable unique features of cryptocurrencies exchanges to be dealt with differently. This may reflect some over-the-counter markets, and may require compliance with other ASIC obligations. Introduction of a new regime, must be made following consultation with all Australian exchanges and platforms operating in this space, including in more traditional markets. Such a regime should not unnecessarily remove the availability of existing exemptions and should consider the interaction between the AFSL and AML regimes, including any effect on businesses which may currently be required to hold an AML.

However, the government must be careful to ensure that the obligations required for an AML are not watered down. Doing so may allow large international players in traditional markets to threaten the market share of Australian companies and start-ups if they were able to obtain an AML. We acknowledge that while there are currently a large number of cryptocurrency exchanges in the market we predict consolidation at least in the domestic market over time. Ultimately, a balance is required to ensure fintechs can more easily apply for an AML, without reducing the necessary protections to ensure efficient and fair markets, or enabling international players to dominate domestic players.

In respect of international regimes, we note that one of our members submitted that the Digital Payment Token (**DPT**) license in Singapore, a broader part of their Payment Services Act, provides clear and appropriate requirements around AML/CTF. Regarding international approaches, we would like to refer back to our third submission to the Committee, where we submitted on the regimes of Singapore, Hong Kong and New York.[3] Here, we commented on the market impact that such a regime has had in those jurisdictions. Companies in New York have considered the BitLicense to be overly burdensome, causing some to leave New York. Singapore and Hong Kong's regimes have suffered from a lack of consultation which has resulted in regimes that are not fit for purpose and hinder industry, rather than assist it. We also addressed concerns that were noted above that these regimes have inadvertently captured businesses which are not exchanges and which should not be subject to these requirements as they use blockchain as part of the technological stack. If these businesses were captured it would have a chilling effect on both the crypto-asset and blockchain industry. Further, we suggest any regime relating to markets, should not be based on requirements for payments, but on the principles of ensuring a fair and efficient market. Accordingly, this should refer to principles of traditional financial markets.

It is also essential that the government clarifies how a new regime will apply retrospectively for companies that hold a markets license. For example, it may be necessary to ensure there is sufficient time prior to commencement for existing markets operating in Australia to establish processes and systems which meet the compliance obligations, apply for and obtain licences.

[3] Submission page 11

The current AML/CTF compliance and reporting obligations that apply to registrable digital currency exchange services (**DCEs**), businesses that exchange cryptocurrency with fiat currency, do not take into account what we would usually expect a market operator to consider in any other sort of financial market. As such, merely bolstering AML/CTF obligations is unlikely to provide adequate protections to those accessing the market, or to ensure it's efficient operation. On the other hand, over-regulation of DCEs will lead to investors looking offshore to find friendlier jurisdictions. A careful balance must be struck in fostering a fair and proportionate regime which aligns with the principles of financial markets, protection of consumers and the flexibility of a growing data and technology enabled industry.

Additionally, while fungible crypto-assets may share certain characteristics of, or fall under the definition of financial products, non-fungible tokens (**NFTs**) rarely share these properties. NFTs is a description of the technology used where something unique or a record of something unique, is maintained on a blockchain or distributed ledger. What an NFT is, depends on the nature of the information that is provided when an NFT is transferred and recorded. For example, NFTs underpin many blockchain use cases, such as in relation to supply chain management to track the movement of a particular good at a particular time, or records of trademarks. Other NFTs exist purely in the digital realm, such as collectors items, such as jpeg images, or rights in those images. Accordingly, it is important to appreciate that given that an NFT is merely a description of the technology, any regime which relates to crypto-assets, and in particular one which treats them as, or akin to financial products, should not apply to NFTs.

Further, FinTech Australia submits that significant care should be taken to ensure that NFTs can be treated according to their use (such as an artwork, a register of a trademark, or title to goods) and are not unfairly disadvantaged as against other technologies. If a system with an NFT requires a certain license, or all disposals of NFTs trigger a CGT event, it is likely to negatively impact systems that use NFTs in their back-end, such as grain receipts in a farming management system. More generally, care should be taken when seeking to define crypto-assets under any regulatory or legislative framework.

In particular, where a broad approach to the definition of "crypto-asset" was taken in Singapore, this has captured a wide-range of crypto-assets within a regime which is structured for financial product and payments. In particular, the Singaporean regime does not adequately differentiate between asset classes or tokens under its regime. As such, there is concern that blockchain businesses using NFTs as part of their underlying technology are caught under this regime. Further, significant consideration should be given if existing financial products were to be caught under a new regime merely by virtue of also being a crypto-asset.

Any new laws, regulations or policies should adhere to technological neutrality principles so that they do not apply based on what technology underpins a given asset, but rather has regard as to the rights given to the recipient of the asset. Separately from these unintended consequences, such an approach may also entrench certain technologies, preventing the adoption of new technologies which are developed. These issues are explored further with respect to tax in the following question taken on notice.

Question 2: Currently, there are a range of capital gains tax (CGT) events that are triggered when selling and swapping cryptocurrency into other cryptocurrencies. What would the cost be to the ATO if we instead had only a single CGT event when converting back into the Australian Dollar / fiat currency?

During the most recent public hearing, the Committee put to the ATO a key industry proposal on the taxation of crypto assets, being one where crypto-to-crypto transactions are ignored for CGT purposes and CGT is only triggered when crypto assets are transferred to Australian dollars or fiat (**Alternative Taxing Point**). In the context of these discussions, the ATO took a question on notice about how much CGT revenue is being collected on crypto assets. Although this question would be difficult for FinTech Australia or any industry body to answer, we have outlined below our thoughts on the Alternative Taxing Point and additional issues that it raises.

We note that based on the ATO's appearance before the Committee, the proposed Alternative Taxing Point, seems targeted at cryptocurrency trading transactions only (with the ATO using share trading as the appropriate non-crypto asset equivalent), without considering broader crypto asset transactions. While the Alternative Taxing Point is a welcomed approach in respect of crypto trading, we would encourage further discussion surrounding tax solutions to transactions beyond crypto trading as we believe that this proposal cannot be applied uniformly to all transactions involving crypto assets.

Focusing on the Alternative Taxing Point as it has currently been proposed, we would support a proposal in this nature with respect to cryptocurrency trading transactions, on the basis that the current tax treatment of crypto asset transactions is a disincentive for taxpayers to invest in crypto assets. Under the current regime, tax liabilities arise for taxpayers in respect of transactions (i.e. crypto-to-crypto trading transactions) where the taxpayer does not receive cash to support payment of the actual tax liability. This is compounded by the fluctuating and sometimes volatile value of crypto assets which can result in potentially large tax liabilities. The proposed Alternative Taxing Point would decrease the compliance burden for taxpayers and it would drive revenue over time through increased trade volumes and increased participation in the crypto market, which would offset any short term loss of revenue as cost to the ATO.

In terms of implementing the Alternative Taxing Point, one option could be a CGT roll-over for crypto-to-crypto transactions, which could allow the transfer of like-for-like crypto currency without an adverse tax impact, by allowing any taxing point to be deferred until the disposal of the crypto currency for fiat or cash. This would have the effect of not eliminating the ATO's collection of revenue, but deferring the taxing point to a point in time where the taxpayer actually made a gain to enable them to cover any tax liability owing to the ATO. In light of the current Board of Taxation Review into roll-overs, this crypto roll-over could be included with any legislative amendments that come from this review.

As provided above, the Alternative Taxing Point seems to focus on crypto-to-crypto trading transactions. In terms of the characterisation of crypto assets for the purpose of tax law, all crypto transactions cannot be simplified as being the equivalent of traditional share trading as there are a range of crypto use-cases and asset types that expand beyond cryptocurrency trading and this is an area that is continuing to evolve. To date, the ATO guidance on the tax treatment of crypto transactions has focused on cryptocurrency trading (with the majority of its guidance being released in 2014). This contributes to significant uncertainty in the industry, especially as the current guidance does not distinguish between types of crypto asset transactions in determining tax outcomes. For example, NFTs are a type of crypto asset which have been utilised more broadly in recent years. As noted in our written submission, the ATO has only published a single private ruling[4] which is binding only for the intended recipient and provides that the taxpayer's specific NFT artworks are CGT assets. An NFT can be more than artwork, and clear guidance would assist to improve certainty in the market and ultimately increase use of crypto assets. NFTs are just one example of the new and emerging technologies that have been developed since the ATO last published its guidance in 2014. The industry is continuously developing new DeFi protocols that allow users to stake, lend, borrow, and generate interest in novel ways, such as yield farming. Given the pace of cryptocurrency innovation, we would support the establishment of a cryptocurrency working group by the ATO to assist it in issuing guidance on the taxation of cryptocurrency (including DeFi protocols) in a timely manner so as to provide greater certainty to the sector.

Mergers & Acquisitions (M&A) Question

Question 1: Our thoughts and feelings on the ACCC's proposed changes to the M&A sector?

1. **Accelerate innovation**

FinTech Australia is a strong proponent of strong competition in markets. Our members continue to accelerate innovation across a range of sub-sectors and disrupt incumbents in payments, banking, lending and many more areas. A healthy level of competition is critical for innovation, especially in a growth sector with many small high-growth companies like the fintech industry. Merger control changes must be implemented carefully to ensure that M&A activity is not reduced to the detriment of the sector. As a result, a careful balance is required.

We also expect there to be a degree of consolidation in many relatively novel areas of fintech, such as cryptocurrency exchanges. It is essential that M&A deals are not unnecessarily prevented to ensure we continue to drive innovation in the space. A key example of this is in the neo-banking sub-sector through the recent acquisition of 86 400 by NAB. As a result of the merger, 86 400 saw an expansion to their technology teams, which were limited by investment previously, enabling 86 400 to bring forward more smart products and features to their customers. Additionally, because of the larger customer base enabled via NAB's UBank, even more institutions will be willing to partner and grow with 86 400, encouraging growth in product and service innovation industry-wide. This is just one example of many deals and partnerships that will continue to promote innovation in the fintech space to the benefit of consumers while maintaining strong levels of competition.

2. **Capital flow impact**

Capital is a significant factor in the growth of technology scaleups that will power the Australian economy in the future. Without capital, companies are unable to scale and some may not survive. We require an ecosystem where there is a strong pool of investors and confidence that there will be a return on investment. A strong level of M&A activity promotes investor confidence as it proves that strong returns are possible within the industry. In contrast, preventing an upcoming business from selling to an incumbent within the industry may not only affect that businesses' future but also creates future uncertainty in regard to the ability of investors to receive capital upon their exit. This acts as a disincentive to invest in the Australian industry.

Additionally, reducing the number of acquisitions or increasing the difficulty of acquisitions may form a barrier to entry as capital will not be able to be recycled and reinvested in another innovative company. It is essential that capital is readily available and accessible to new entrants seeking to join the market and experience growth.

Furthermore, most founders are driven into business with a goal of seeking an exit. It is critical to prove to founders that they continue to have a viable option to seek an exit to ensure prospective founders remain motivated.

Ultimately, if acquisitions in the fintech space are blocked, fintech companies in the future will be provided with reduced opportunities to receive sufficient capital upon entry and exit, leading to increased barriers to entry and a reduction in innovation within the industry overtime. This may result in businesses establishing themselves offshore.