Article Information

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The wait is over: Australian government releases draft legislation for digital assets

The Australian government has opened its long-awaited consultation on exposure draft legislation to regulate digital assets under the Australian financial services regime (the *Treasury Laws Amendment Bill 2025: Digital asset, and tokenised custody, platforms*). The draft legislation proposes some big changes to the sector, outlining rules for digital asset licensing that would bring crypto-asset intermediaries within Australia's financial regulatory framework.

Announcing the draft legislation at the Digital Economy Council of Australia (DECA) Digital Asset Regulatory Summit, Assistant Treasurer Daniel Mulino stated that the regulation is:

"about legitimising the good actors and shutting out the bad, giving businesses certainty and consumers confidence, [and] working with industry, regulators and the broader community to make Australia a leader in the global digital asset ecosystem."

In line with an earlier consultation in late 2023, the draft legislation is targeted at addressing industry uncertainty, regulatory gaps, fostering innovation and enhancing competition and growth.

What is the approach of the draft legislation?

1. No definition of 'digital asset'

In its explanatory materials, the government has stated that the reforms will avoid using or defining the concept of a 'digital asset', rather the financial services laws' references to 'assets' will continue to cover bundles of rights, including rights that are "legally recognised as being held by a person who *in fact* possesses a digital token". Instead, the bill defines several related concepts discussed below, including digital tokens and digital objects.

2. Existing laws continue to apply unevenly and with targeted exemptions

Importantly, the draft legislation does not seek to implement a new test to determine whether activities involving digital assets are regulated under the existing laws. The regime as it stands continues to apply to the sector unless the reforms within the draft legislation expressly relieve entities from specific obligations.

Accordingly, important questions on the extent to which the financial product definitions under existing laws apply to digital assets will remain to be resolved ultimately by case law. While the explanatory memorandum acknowledges those challenges and the legislation attempts to side step these debates, it remains to be seen how ASIC continue to enforce existing laws and market conventions evolve between what is considered a financial product and a non-financial product digital token.

That being said, the draft bill aims to provide much needed clarity for certain activities such as intermediated staking, validation activities and potentially true DeFi.

3. Digital asset intermediaries identified as key risk area

The Treasury has identified custodial arrangements as a key source of risk in areas such as credit, liquidity, counterparty exposure, operations, fraud, and cyber security based on insights from previous public consultations. Since these digital custodial products closely resemble those already regulated under existing financial laws, the draft legislation proposes applying established regulatory frameworks such as those used for investor directed portfolio services, registered managed investment schemes, and managed discretionary accounts to digital asset intermediaries. This approach aims to proactively address potential financial stability risks and align Australia's digital asset regulatory framework with international standards, following the principle of "same activity, same risk, same regulation."

Meaning of digital token

The concept of a 'digital token' is introduced in the draft legislation, with the explanatory materials drawing on international work including the United Kingdom Law Commission's Final Report on Digital Assets, the International Institute for the Unification of Private Law Principles on Digital Assets and Private Law and the US Uniform Law Commission's Uniform Code Amendments 2022. The definition covers a digital object if one or more persons are capable of controlling that digital object.

Control is generally understood to be factual control rather than legal control. According to the draft bill, a person is considered to have control if they can:

1. Exclude others from controlling the digital object;
2. Use, transfer or dispose of the digital object; and
3. Identify themselves as the person capable of performing either of those actions.

An important related definition is "possession". Possession is equated with control but excludes negative control.

New financial products

The draft legislation proposes two new financial products, being a "digital asset platform" and a "tokenised custody platform".

1. Digital Asset Platform (**DAP**)

As anticipated, a key component of the draft legislation is the licensing of DAPs. A DAP is defined in the draft legislation as a non-transferable facility, where an operator possesses one or more digital tokens on trust for or on behalf of a client, or the client's nominee. A person becomes a client when they enter into the facility by accepting its terms an opening account. The definition is broad enough to cover platforms that solely provide custody of digital tokens, as well as those that enable operators or third parties to act on behalf of clients (e.g. using, transferring, or staking tokens), with the operator holding the underlying assets in a manner analogous to physical custody.

Under the proposed regime, a DAP is required to hold an Australian Financial Services Licence (**AFSL**) if it surpasses an asset holding threshold of more than $5,000 per customer and facilitates more than $10 million in transactions per year. This is a significant increase from earlier proposal thresholds of $1,500 per customer or $5 million in aggregate holdings, and the proposed volume test would apply on a rolling 12 month basis. However, any person seeking to rely on the exemption will also need to notify ASIC of the same.

2. Tokenised Custody Platform (**TCP**)

A TCP is defined as a non-transferable facility where the operator identifies specific real-world assets and creates a unique digital token for each one. Possession of the token gives the holder the right to claim or receive the actual asset it represents, which the operator holds on trust for the token holder. The operator may also be authorised to manage or take actions involving the asset on the holder's behalf. A person becomes a client of the platform by accepting its terms and opening an account, regardless of how they acquired the token. The definition is broad enough to include platforms that provide simple custody and tokenisation, as well as those that enable operators or third parties to act on behalf of client (e.g. buying, selling, transferring, staking with the underlying assets). It is anticipated that additional licence authorisations may be required to deal and provide other financial services in relation to an underlying financial product.

Compliance, Disclosure and Design and Distribution Obligations

A licensee that is authorised to issue a DAP or a TCP must comply with:

- general obligations under financial services laws;
- asset holding standards;
- obligations to implement platform rules;

- transaction and settlement standards;
- breach reporting; and
- design and distribution obligations.

In addition, licensees will be subject to disclosure obligations, including the issuance of a facility guide (dubbed a DAP/TCP Guide) similar to an IDPS guide. A DAP/TCP must also maintain a voting policy dealing with the exercise of token governance rights.

The application of design and distribution obligations and product intervention powers to DAP and TCP may become an important area of debate depending on ASIC's views of the suitability of these platforms for investment by retail clients. AFS licensees providing financial services related to the above will be exempt from certain other fundraising, disclosure, and anti-hawking requirements.

Carve-outs from definition of managed investment scheme

The extent to which the managed investment scheme (**MIS**) definition applies to crypto-asset related offerings has been an issue of considerable uncertainty as evidenced by the Block Earner litigation which is now before the High Court. The draft legislation proposes to exempt specific digital asset platforms or tokenised custody platforms from being captured as a MIS. It does not however address the fundamental question of whether an underlying digital token is or is not a MIS, which will fall to be determined at common law.

A digital asset platform will not be classified as a MIS if:

- Clients have the right to redeem or request delivery of the assets held on the platform;
- The platform operator can only act on lawful instructions from the client regarding acquisition, disposal or use of the assets; and
- The operator cannot materially negotiate or determine the rights attached to the assets held on the platform.

Similarly, a tokenised custody platform would not come under this definition of MIS if:

- Clients have the right to redeem or request delivery of the assets held on the platform; and
- The platform operator can only act on lawful instructions from the client regarding acquisition, disposal or use of the assets; and
- The operator cannot materially negotiate or determine the rights attached to the assets held on the platform; and
- All assets linked to tokens on the platform are of the same asset class; and
- Tokens are only divisible to the extent that the asset can be physically divided and delivered in the same way.

In that context, while the legislation contemplates the tokenisation of an asset itself will not create an MIS, the fractionalisation of interests in that asset will do. This may pose a considerable restriction on the development of tokenised assets markets for retail investors, given the onerous compliance obligations which apply to retail managed investment schemes.

Regulatory clarity

The draft legislation introduces targeted exemptions for blockchain infrastructure and activities. This exemptions are particularly helpful as they seek to provide regulatory clarity in several areas of the digital assets space, which do not fit neatly within existing laws.

Intermediated Staking Arrangement

An intermediated staking arrangement is proposed to be exempt from being classified as a financial product where:

- The client and the operator agree to an arrangement using a DAP;
- The operator is allowed to use the client's digital tokens for staking activities; and
- Any rewards earned from staking, after fees, are passed on the client.

Further, the arrangement must benefit the client in at least one of three ways:

1. The client can redeem assets earlier than if staking directly;
2. The client can participate in staking even if they don't have enough assets to do so on their own; and
3. The client is protected from or compensated for losses related to issues in the staking infrastructure.

Public Digital Token Infrastructure

Infrastructure used to support digital tokens may also be exempt from classification as a financial product or clearing and settlement facility if it meets the following conditions:

1. It is used for the transmission, processing or recording of data in relation to digital tokens;
2. Anyone can contribute to the system's integrity and functionality by contributing data without needing permission;
3. It operates with decentralised control;
4. No one person or group can unilaterally control the digital tokens; and
5. The rules governing the infrastructure are immutable.

This exemption would provide greater comfort to miners and nodes operators involved in securing blockchain networks by processing transactions. The explanatory memoranda suggests that the exemption could also apply to some decentralised applications providing some regulatory clarity for true DeFi.

Wrapped Tokens

In certain circumstances, tokens that grant a right to redeem another asset may be excluded from consideration when assessing whether a wrapped token qualifies as a financial product.

The exemption applies where:

1. A wrapped token is created in relation to another digital token (related asset);
2. The token is issued under a tokenised custody platform or similar facility; and
3. The holder of the token has a right to redeem or direct delivery of the related asset.

This exemption is intended to accommodate circumstances where smart contracts, rather than traditional operators, create and manage wrapped tokens.

For example, on the Ethereum network, an individual can use a smart contract to convert Ether (**ETH**) into wrapped ETH (**wETH**), which grants the holder the right to redeem it for the same amount of ETH held by the contract. Since ETH is not a financial product and wETH only provides a redemption right, the exemption ensures that wETH (and its entire arrangement) is not treated as a financial product. Whereas if a tokenised custody platform is operated by an entity that holds a native digital token to participate in staking activities the wrapped token issued may grant both a redemption right and also returns a share of the staking rewards. The additional rights to staking rewards in this circumstance may cause the wrapped token to be classified as a financial product, depending on the nature of the rights granted to the holder.

'Coffee shop' exemption

The insignificant part of business exemption is designed to exclude businesses from AFSL requirements when their involvement with DAPs or TCPs is incidental. It applies to entities that, in the ordinary course of a primarily non-financial services business, arrange for clients to use a DAP or TCP or advise them about its existence. This includes where a coffee shop offers asset transfers to a digital wallet as a payment method, or a wine business offering access to a third party TCP that tokenises wine for customer redemption. Since these activities are not a significant part of the business, they are not subject to the same regulatory obligations as financial services providers.

Ministerial powers

The draft legislation provides broad discretionary ministerial powers to deem a facility that is ordinarily a DAP to be instead classified as either a financial market or a clearing and settlement facility.

Specifically, the Minister may:

- extend the definition of financial market and clearing and settlement facility to include certain digital asset platforms;
- exempt specific DAPs from being classified as a financial market or a clearing and settlement facility; and
- prohibit certain activities that are authorised under an AFSL from being carried out via a DAP or a TCP.

These powers give the Minister and any delegate considerable discretion to adapt the regulatory regime as its develops. While intended as a flexible tool, these powers could also create a degree of uncertainty over how widely and in what context financial market licensing may be applied to a DAP.

Transitional commencement and application

The draft legislation states it commence 12 months after the legislation receives assent, with transitional rules allowing entities that do not have an AFSL or appropriate authorisation under an AFSL a 6-month grace period before compliance is

required. For financial-services related provisions, if an AFSL application is submitted during this period, an entity's obligations will begin either upon ASIC's determination or after the 12-month transition period ends.

This draft legislation is ambitious in scope and represents Australia's answer to comprehensive crypto-asset reforms already implemented in Europe under the Markets in Crypto-Asset Regulation and market structure legislation under review in the United States. While the draft legislation leaves considerable uncertainty over the interplay between existing financial product definitions and cryptocurrencies, and permits considerable Ministerial discretion in some areas, it is a potential game-changer for the future of Australia's digital asset industry. If implemented, the legislation will provide for financial services licensing for digital asset intermediaries and provide important clarity for a number of areas of digital asset related activity.

The consultation for the draft legislation will close on 24 October 2025.

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