

July 19, 2023



Director
Payments Licensing Unit
Financial System Division
The Treasury
Langton Crescent
Parkes ACT 2600

Email: paymentslicensingconsultation@treasury.gov.au

Dear Director,

Ripple Labs Inc. ("Ripple") welcomes the opportunity to comment on the consultation paper on Payments System Modernisation (Licensing: Defining Payment Functions) (the "Consultation") published by the Australian Government Treasury (the "Treasury") on June 7, 2023.¹

Ripple would like to thank the Treasury for both the in-depth and comprehensive analysis that has been undertaken in the Consultation, and for the opportunity to provide our comments. We respectfully request you take them into consideration as you consider the policy direction and scope of intended licensing requirements for payments services in Australia, specifically payment stablecoins. We welcome the opportunity for further engagement with the Treasury on this Consultation and any other related consultations as may be appropriate.

1. Introduction

Ripple's software products allow financial institutions to send money globally, on a real-time basis, at a fraction of the cost of traditional services available to market participants. Using blockchain technology, Ripple allows financial institutions to process payments instantly, reliably, cost-effectively, and with end-to-end visibility anywhere in the world.

¹ See <https://treasury.gov.au/sites/default/files/2023-06/c2023-403207-cp.pdf>, Australian Government Treasury consultation paper on Payments System Modernisation (Licensing: Defining Payment Functions).

Ripple's aim is not to replace fiat currencies, but rather to enable a faster, less expensive, and more transparent method of making cross-border payments that is in the public's best interest.

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 the dated 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 own cash clearing, liquidity management, short-term borrowing and investment needs in a particular currency."*²

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.³

RippleNet, the cross-border payments solution offered by Ripple, connects hundreds of financial institutions around the world via a single application programming interface ("API") which makes transferring money faster, cheaper, and more reliable. It also helps to reduce, and even eliminate, the need to prefund accounts with On-Demand Liquidity ("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.

² See <https://www.bis.org/cpmi/publ/d147.pdf>, Committee on Payments and Market Infrastructures – Correspondent Banking.

³ See https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf, BIS Quarterly Review March 2020, page 31.

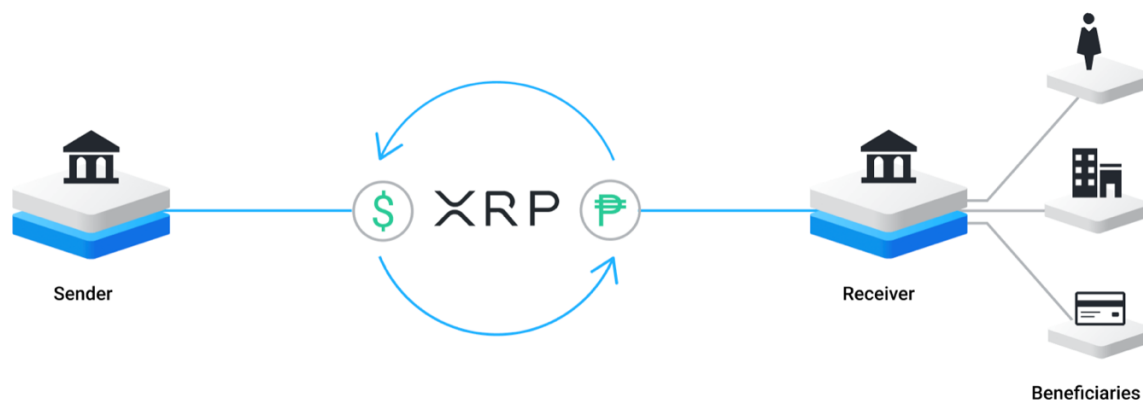


Figure 1: ODL Flow

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.⁴

3. Interoperability

Ripple believes that interoperability - achieved through alignment of national payment protocols and adoption of international standard protocols - will ultimately be core to the successful adoption of crypto-assets and stablecoins.

Ripple itself applies protocols to drive the efficient globalization of value through multiple initiatives with financial services and open-source communities. RippleNet is powered by a standardized API (“API”) and built on the market-leading and open standard Interledger Protocol, enables financial institutions to facilitate faster and less costly cross-border payments. RippleNet demonstrates that deep interoperability between commercial financial institutions can make payments truly efficient, particularly in eliminating the uncertainty and risk historically involved in moving money across borders using interbank messaging alone.

Protocols used by global, cross-border payment networks and decentralized tools that support them should be considered and supported in this new age of domestic networks. Embracing the capabilities of these global networks, and better enabling domestic institutions to connect their individual capabilities with other systems and markets, will enable optimized outcomes for their respective domestic needs as well as fulfil the potential that globalization of value holds.

⁴ See <https://blogs.worldbank.org/psd/paying-across-borders-can-distributed-ledgers-bring-us-closer-together>, World Bank blog.

4. Issuing Stablecoins on the XRP Ledger

The XRP Ledger can also be used to support the issuance of stablecoins with a unique, fungible token functionality called Issued Currencies.⁵ Issued Currencies is designed to be the ideal stablecoin platform, providing simple but rich management functionality for the issuer that makes it easy to create, issue and manage any asset - including stablecoins.

The XRP Ledger has an integrated decentralized exchange (“DEX”) that allows neutral, counterparty-free crypto-assets like XRP to be seamlessly exchanged to and from “issued assets” including stablecoins. Among the unique features is its payment interoperability, which enables payments among those holding and receiving assets to minimize costs and work seamlessly when sufficient liquidity is available.

While neutral assets such as XRP and stablecoins alike can be used to settle a payment, stablecoins have an issuer as the counterparty that does not allow them to interoperate across payment networks. XRP, on the other hand, can be sent directly without needing a central intermediary - making it best-suited to bridge two different currencies quickly and efficiently.

In terms of initiatives in this space, Ripple announced a partnership with the Republic of Palau on November 23, 2021, which will initially focus on developing strategies for cross-border payments and a USD-backed digital currency for Palau.⁶ This could see the implementation of the world’s first government-backed national stablecoin. Additionally, STASIS, an established leader in Euro-backed stablecoin production, announced on February 16, 2022 that it will issue the EURS stablecoin on the XRP Ledger due to its scalability, speed, low cost and carbon neutrality.⁷ In Australia, Novatti announced on June 9, 2022 that it will issue the Australian Dollar-backed stablecoin AUDC on the XRP Ledger.⁸

⁵ See <https://xrpl.org/issued-currencies-overview.html>, Issued Currencies Overview.

⁶ See <https://ripple.com/insights/featured/republic-of-palau-partners-with-ripple-to-develop-digital-currency-strategy/>, Republic of Palau Partners with Ripple to Develop Digital Currency Strategy.

⁷ See <https://ripple.com/ripple-press/stasis-to-issue-euro-stablecoin-on-the-xrp-ledger/>, STASIS to Issue Euro Stablecoin on the XRP Ledger.

⁸ See <https://novatti.com/wp-content/uploads/2022/06/Novatti-to-issue-Australian-Dollar-backed-stablecoin-on-XRP-Ledger.pdf>, Novatti to issue Australian Dollar-backed stablecoin (AUDC) on XRP Ledger, with partnership support from Ripple.

With this overview, Ripple respectfully submits the following responses to the discussion questions set forth in the Consultation in the attached Appendix.

Ripple appreciates the opportunity to provide feedback on the Consultation as the Treasury studies 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 radvani@ripple.com.

Sincerely,

Ripple Labs Inc.

APPENDIX

Ripple respectfully submits the following responses to discussion questions 4, 5, and 6 set forth in the Consultation.

Question 4:

Does the term ‘payment stablecoins’ accurately describe the types of stablecoins this paper seeks to capture for regulation or are there other terms that may be more appropriate?

Ripple believes that the term ‘payment stablecoins’ accurately describe the types of stablecoins that are intended to be regulated. However, it’s worth noting that there is no consistent global term for such stablecoins, and various jurisdictions use differing terms.

For example, under the European Union’s (“EU”) Markets in Crypto Assets (“MiCA”) regulation, such stablecoins are referred to as ‘electronic money token’ or ‘e-money token’, which are considered to be *“a type of crypto-asset that purports to maintain a stable value by referencing the value of one official currency”*.⁹

The amended Payment Services Act in Japan defines a new term, ‘electronic payment method’, which covers ‘digital money-like type’ instruments, i.e., payment stablecoins, which fall under the category of ‘currency-denominated assets’.¹⁰

While Singapore and Hong Kong currently don’t have a regulatory framework for payment stablecoins, the Monetary Authority of Singapore (“MAS”) proposes to use the term ‘single-currency pegged stablecoins’ (“SCS”)¹¹ while the Hong Kong Monetary Authority (“HKMA”) proposes to use the term ‘payment-related stablecoin’.¹²

However, regardless of the term used to describe the types of stablecoins this Consultation seeks to capture for regulation, it is worth noting that Australia currently does not have any taxonomy to identify payment stablecoins, or more broadly, payment-related crypto assets in general.

⁹ See

<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32023R1114&qid=1689583589207>, Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, Article 3(1)(7).

¹⁰ See <https://www.japaneselawtranslation.go.jp/en/laws/view/4395>, Payment Services Act (Act No. 59 of 2009), Chapter 1, Article 2, Paragraph 5(i). Translated on May 12, 2023.

¹¹ See

https://www.mas.gov.sg/-/media/mas-media-library/publications/consultations/pd/2022/consultation-on-stablecoin-regulatory-approach_finalised.pdf, Consultation Paper on the Proposed Regulatory Approach for Stablecoin-Related Activities, Paragraph 3.5(a).

¹² See <https://www.hkma.gov.hk/media/eng/doc/key-information/press-release/2022/20220112e3a1.pdf>, Discussion Paper on Crypto-assets and Stablecoins, Chapter 5.

Ripple respectfully submits that such crypto assets should not be solely defined relative to a specific technology (e.g., cryptography), but, for the purposes of regulation, should instead fall under a broader heading such as 'digital assets', and subsequently 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.

For ease of reference, we have summarised the taxonomies for the UK and Singapore respectively in Figure 2 & Figure 2 below.

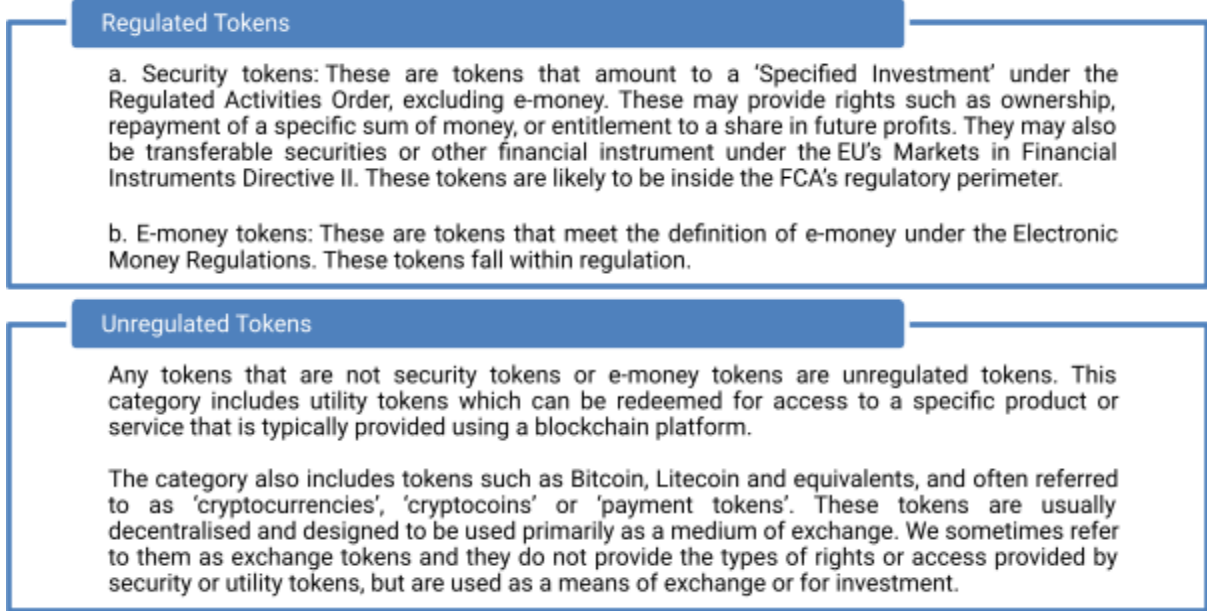


Figure 2: Summary of the UK Financial Conduct Authority taxonomy for digital assets

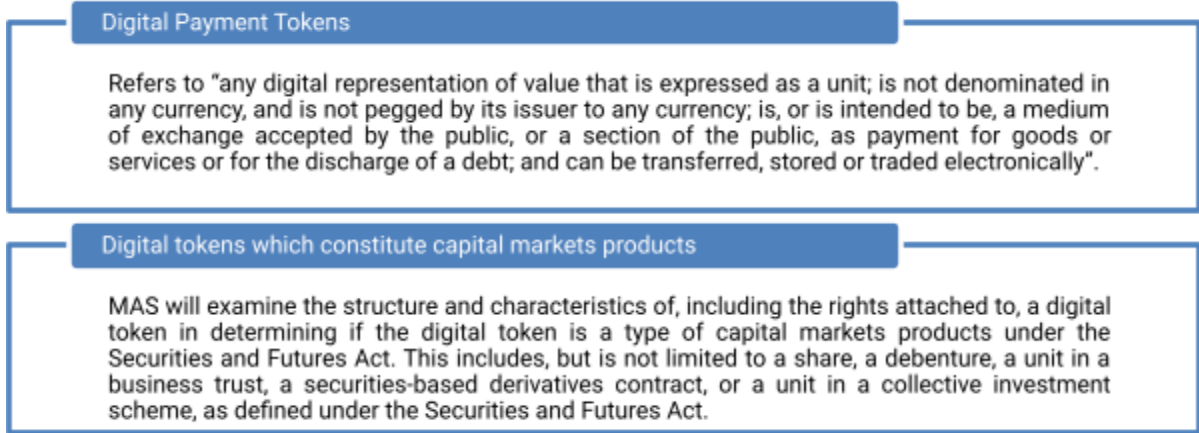


Figure 3: Summary of the Monetary Authority of Singapore ("MAS") taxonomy for digital assets

Taking into account the taxonomies of the UK and Singapore discussed above, Ripple respectfully recommends that the Treasury consider adopting a taxonomy consistent with such global practices, thereby providing clarity to the legal character of crypto assets, including payment stablecoins, in Australia.

In line with global practices, we recommend that there be a clear distinction between payment tokens, utility tokens, and security tokens, 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.

While we understand the scope of this Consultation isn't intended to cover crypto assets,¹³ for the reasons enumerated above we respectfully recommend that Treasury follow global best practices and provide a clear taxonomy for crypto assets, including payment stablecoins.

Question 5:

Does the proposed definition of 'payment stablecoins' adequately distinguish itself from other stablecoin arrangements?

Ripple believes that the proposed definition of 'payment stablecoins' adequately distinguishes such stablecoins from other stablecoin arrangements.

Question 6:

Is regulation as an SVF an appropriate framework for the regulation of payment stablecoin issuers? If not, why? What would be an appropriate alternative?

Ripple believes that regulation as a stored value facility ("SVF") is not an appropriate framework for the regulation of payment stablecoin issuers.

SVF are considered to be facilities that allow a holder of stored value to make a payment to another person on behalf of the user of the facility, and are currently regulated as purchased payment facilities ("PPF") under the Payment Systems (Regulation) Act 1998 ("PSRA").¹⁴ We understand that the regulatory framework

¹³ See Consultation, Section 3, Page 12.

¹⁴ See <https://www.legislation.gov.au/Details/C2020C00336>, Payment Systems (Regulation) Act 1998.

proposed for SVFs in the Consultation is based on the recommendations of the Council of Financial Regulators (“CFR”) report on the Regulation of Stored-value Facilities in Australia published on November 6, 2020.¹⁵

We appreciate that the intent of these recommendations is aimed at modernising the regulatory arrangements for SVFs, and to simplify the existing regulatory framework in a way that would be conducive to innovation while providing appropriate consumer protections.

However, under the PSRA, PPFs are defined as -

“A facility (other than cash) in relation to which the following conditions are satisfied:

- a. the facility is purchased by a person from another person; and*
- b. the facility is able to be used as a means of making payments up to the amount that, from time to time, is available for use under the conditions applying to the facility; and*
- c. those payments are to be made by the provider of the facility or by a person acting under an arrangement with the provider (rather than by the user of the facility).”¹⁶*

While payment stablecoins could meet the above definition, a key differentiating factor is that the exchange rate of the payment stablecoin to the fiat currency is not fixed, and can vary when traded on exchanges. This characteristic of payment stablecoins has been highlighted in footnote 17 of the Consultation,¹⁷ and has also been noted by the Bank for International Settlements.¹⁸

The certainty with which payment stablecoin holders are able to redeem for fiat currency may also vary - in times of crisis, market liquidity to redeem for fiat currency may tighten.

Additionally, it’s also important to note that holders can often use the payment stablecoin through third-party service providers such as exchanges or private wallets, without the payment stablecoin issuer being involved. This is unlike holders of SVFs who will have contractual relationships and accounts with the SVF issuer, and can only use the SVF through the SVF issuer.

Therefore, payment stablecoins are unlike SVFs in that the liability of the payment stablecoin issuer and the ability of payment stablecoin holders to redeem for fiat currency can vary. For example, payment stablecoin issuers may be able to secure trust

¹⁵ See

<https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2020/regulation-of-stored-value-facilities-in-australia/pdf/report.pdf>, Council of Financial Regulators, Regulation of Stored-value Facilities in Australia.

¹⁶ See PSRA, Part 2, 9(1).

¹⁷ See Consultation, Section 3, Page 13.

¹⁸ See <https://www.bis.org/publ/work905.pdf>, Bank for International Settlements, BIS Working Papers No. 905 - Stablecoins: risks, potential and regulation, Page 8 (Graph 2).

even without the payment stablecoin holders having a claim on the issuer or redemption rights, by ensuring that a market always exists for holders to redeem for fiat currency.

To summarize, payment stablecoins exhibit the following characteristics that differ from SVFs:

- a. the exchange rate of the payment stablecoin to the fiat currency it references may vary when used, traded or offered by third-party service providers; and
- b. a holder of the payment stablecoin need not have a contractual relationship or an account with the issuer of the payment stablecoin in order to use the payment stablecoin.

This makes the risks of a payment stablecoin very different to that of an SVF, and therefore regulating payment stablecoins as SVFs will not align with the risk-based regulatory approach outlined in the Consultation. Therefore, Ripple believes that given these differing characteristics and risks, regulation as an SVF is not an appropriate framework for the regulation of payment stablecoin issuers.

Instead, Ripple respectfully requests that the Treasury consider implementing a clear taxonomy for crypto assets, including payment stablecoins, as outlined in our response to Question 4 above. Doing so will mean that payment stablecoin issuers can be regulated as a type of payment or exchange token issuer, which will provide clarity to the legal character of payment stablecoins in Australia and will facilitate the development of a risk-based regulatory approach to regulate payment stablecoins.