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Me Anne-Marie Beaudoin
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**Re: Proposed Framework for Crypto-Asset Trading Platforms**

Dear Madams or Sirs:

State Street Corporation ("State Street") appreciates the opportunity to respond to the joint Canadian Securities Administrators ("CSA") and the Investment Industry Regulatory Organization of Canada's ("IIROC") Consultation Paper on a Proposed Framework for Crypto-Asset Trading Platforms ("consultation paper").[1] Specifically, the CSA and IIROC seek feedback as they begin to establish a regulatory framework for platforms facilitating the buying and selling of crypto-assets. This includes requirements regarding the custody of such assets.

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[1] See *https://www.osc.gov.on.ca/documents/en/Securities-Category2/csa_20190314_21-402_crypto-asset-trading-platforms.pdf.*

Headquartered in Boston, Massachusetts, State Street specializes in the provision of financial services to institutional investor clients, such as pension plans, mutual funds, alternative investment funds, central banks, charitable foundations and endowments. This includes the provision of investment servicing, investment management, data and analytics, and investment research and trading. With $32.643 trillion in assets under custody and administration and $2.805 trillion in assets under management, State Street operates in more than 100 geographic markets globally.[2]

State Street is organized as a United States ("U.S.") bank holding company, with operations conducted through several entities, primarily its wholly-insured depository institution subsidiary, State Street Bank and Trust Company ("SSBT"). In Canada, State Street provides global custody and local financial services through State Street Trust Company Canada, a Canadian federal trust company and wholly-owned subsidiary of SSBT, the Canadian branch of SSBT and State Street Global Markets Canada Incorporated.

State Street supports the development of a proper regulatory regime for digital assets, such as crypto-assets (including crypto-currencies, utility tokens and security tokens, hereinafter referred to as "digital assets") which will assist platforms that facilitate the buying and selling, or the transferring, of digital assets. In our view, the participation of institutional investors in this new asset class will only materially develop to the extent that the market structure for digital assets improves and the regulatory framework is clarified.

As described in more detail below, we strongly believe that custody banks should be involved in ensuring the proper safekeeping of digital assets; that minimum safeguards and standards should be established for platforms engaged in the buying and selling of digital assets; and efforts should be made to expand the availability and affordability of insurance for digital assets.

## I. <u>Use of Regulated Custodial Entities</u>

State Street recommends that the custody of digital assets should be limited to regulated custodial entities, such as banks and trust companies. As emphasized in the consultation paper, some digital assets platforms are hybrid in nature and perform several functions similar to those of various market participants, including custodians. This includes the self-custody of investors' assets or systems which give the platform control over investors' assets. We are concerned that platforms that engage in the buying or selling of digital assets may not have sufficiently robust systems in place to mitigate risks and ensure the safety and soundness of assets. Most notably, some digital asset platforms may not segregate investor assets from their own, a practice that is central to the proper safekeeping and control of assets.

Regulated custodial entities, such as State Street, specialize in the safekeeping and administration of investment assets, and already have well established processes and controls in place to safeguard assets. Similarly, custodial entities have the necessary experience and expertise to develop policies, procedures and controls for digital assets as the regulatory regime evolves. Moreover, regulated custodial entities routinely segregate investors' assets from their own, and perform in-depth know-your-customer and anti-money laundering assessments. We believe that there should be no exceptions from these core practices when guarding against the misappropriation of digital assets.

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[2] As of March 31, 2019.

In our view, key areas of consideration required for the custody of digital assets include: (1) information systems and technology; (2) the operating model; and (3) the manner in which digital assets are reflected in the underlying distributed ledger technology ("DLT") and the requisite controls over DLT. For example, to mitigate the risk of misallocation and malicious transfers, controls should be put in place to approve transactions which are appropriately managed via either infrastructure and/or layers of software. The operating model should, in turn, delineate responsibilities, escalation procedures and business continuity plans. It also should control what final users/beneficial owners are permitted to do with digital assets (*e.g.* prevent the selling or transferring of digital assets to facilitate illicit activities).

As such, regulated custodial entities are, in our view, better positioned to support the custody of digital assets than other market entities, such as trading platforms.

## II. Establish Minimum Standards for the Custody of Digital Assets (Question 4)

As a threshold matter, we believe that platforms for digital assets that engage in custody should be subject to the same regulations and principles which apply to other financial market infrastructures, as outlined by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions.[3] This includes principles around: credit and liquidity risk management; settlement and settlement systems; default management; operational and business risk management; access; efficiency; and transparency.

In addition, State Street recommends the establishment of minimum operating standards for the custody of digital assets. As mentioned in the consultation paper, a significant risk to digital assets is that they are not adequately safeguarded in today's operational environment. We therefore support the adoption of a set of minimum standards which address:

- Segregation of assets;
- Data privacy and cybersecurity;
- Verification of assets, including multi-signature authorizations for transactions, with rotating permissions; hyper-secure (*i.e.* complete end-to-end) encryption of private keys; and enhanced control protections, including physical access to wallets and security protocols for private keys; and
- Development of a standardized settlement cycle, reconciliation requirements and dispute adjudication procedures.

## III. Minimum Insurance Coverage Availability (Questions 16, 17, and 18)

Finally, State Street strongly supports efforts to promote the availability of more affordable, minimum insurance coverage for digital assets. The consultation paper discusses the difficultly and high costs for platforms to obtain insurance due to the lack of consistent regulatory guidance around the custody of digital assets, the limited number of insurance providers and the high risk of cyber-attacks.

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[3] Committee on Payment and Settlement Systems Technical Committee of the International Organization of Securities Commissions- Principles for financial market infrastructures. April 2012. Available at *https://www.bis.org/cpmi/publ/d101a.pdf.*

State Street agrees with this assessment. The lack of transparency and the difficulty in assessing security of digital assets drives increased costs which are exponentially higher than insurance rates for traditional assets. We suggest that the CSA and IIROC encourage the development of innovative insurance solutions for digital assets.

For example, insurance intermediation platforms have been recently introduced to the market which could provide a unique solution for crypto-assets. Platforms can offer these products which permit the use of digital tokens for premiums, thus allowing the platform itself to provide insurance to its clients. In effect, the insurance platform acts an intermediary between clients and the traditional insurance market, leading to decreased insurance costs for users and increased levels of protection.

Furthermore, we recommend, that all insurance products for digital assets cover the following:

- Third-party hacking and the theft of private keys;
- Insider (*i.e.* employees) hacking and theft of private keys;
- System breakdowns; and
- The death or incapacity of a keyholder.

**Conclusion**

Thank you once again for the opportunity to respond to the consultation paper. We appreciate the CSA's and IIROC's engagement on this matter and look forward to the opportunity to serve as a resource as the regulatory regime for digital assets evolves to support the needs of the Canadian market.

Please feel free to contact me at JBiancamano@StateStreet.com should you wish to discuss State Street's submission in further detail.

Sincerely,

James J. Biancamano