

The Secretary  
Ontario Securities Commission  
20 Queen Street West  
22nd Floor, Box 55  
Toronto, Ontario M5H 3S8  
comments@osc.gov.on.ca

Me Anne-Marie Beaudoin  
Corporate Secretary  
Autorité des marchés financiers  
800, square Victoria, 22e étage  
C.P. 246, tour de la Bourse  
Montréal (Québec) H4Z 1G3  
Consultation-en-cours@lautorite.qc.ca

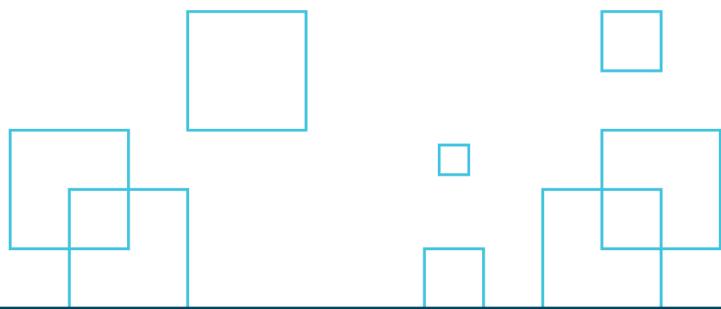
IIROC  
Victoria Pinnington  
Senior Vice President, Market Regulation  
Investment Industry Regulatory Organization of Canada  
Suite 2000, 121 King Street West  
Toronto, Ontario M5H 3T9  
vpinnington@iirc.ca

May 15, 2019

Dear Madams and Sirs:

**Re: Joint Canadian Securities Administrators/Investment Industry Regulatory Organization of Canada - Consultation Paper 21-402 - Proposed Framework for Crypto-Asset Trading Platforms**

We would like to thank the Joint Canadian Securities Administrators (CSA) and the Investment Industry Regulatory Organization of Canada (IIROC) for preparing the Proposed Framework



---

for Crypto-Asset Trading Platforms<sup>1</sup> and for inviting industry stakeholders to participate in this important consultation.

The Chamber of Digital Commerce Canada (the “Chamber”) represents Canada’s blockchain ecosystem. Our mission is to promote the acceptance and use of digital assets and blockchain-based technologies in Canada. Through education, advocacy, and working closely with policymakers, regulatory agencies, and industry, we are helping develop an environment that fosters innovation, jobs, and investment. As such, the Chamber has a significant interest in this Consultation that directly impacts a number of our members.

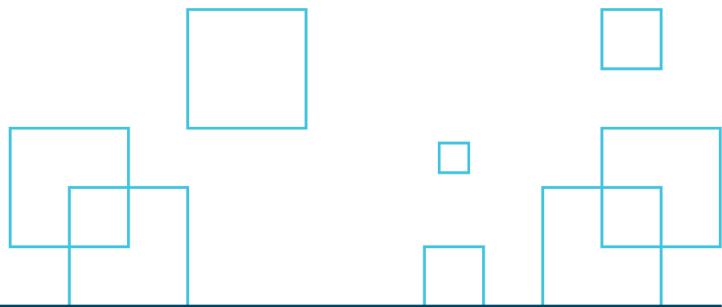
The transformative potential of digital assets, blockchain, and distributed ledger technologies (“DLT”) presents tremendous cross-sectoral and economic advancement opportunities that have been recognized globally by government and industry alike. Fundamentally, these technologies reshape the ownership of assets, how we interact with each other digitally, and how we transfer value. As a result, the ways in which companies across many sectors conduct business - from financial services, digital identity and privacy, healthcare, insurance, intellectual property, real estate, commerce, and supply chain management, among others - are being rapidly transformed and establishing a new Internet infrastructure dedicated to the digital exchange of value.<sup>2</sup>

This shift, as Canadian regulators know, is causing challenges for current regulatory and policy frameworks. While there are aspects of the digital asset and blockchain landscape that might fit under existing law, policy, and regulation, it remains the case that the broader systemic shift and innovation that is occurring, and in particular with regard to “crypto-asset trading platforms,” or what we refer to as “digital asset trading platforms,” demands holistic study and review with industry experts at the table. In reviewing the existing legal and regulatory framework, policymakers must take into account the innovative aspects of these technologies, which transcend the current regulatory frameworks applicable to financial services, securities and commodities. It is imperative that policymakers carefully evaluate the

---

<sup>1</sup> Canadian Securities Administrators, Joint Canadian Securities Administrators/Investment Industry Regulatory Organization of Canada Consultation Paper 21-402 Proposed Framework for Crypto-Asset Trading Platforms, [https://www.osc.gov.on.ca/documents/en/Securities-Category2/csa\\_20190314\\_21-402\\_crypto-asset-trading-platforms.pdf](https://www.osc.gov.on.ca/documents/en/Securities-Category2/csa_20190314_21-402_crypto-asset-trading-platforms.pdf).

<sup>2</sup> Deloitte, The Internet of Value-Exchange, <https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/Innovation/deloitte-uk-internet-of-value-exchange.pdf>.



---

extent to which it is appropriate to base new policy responses on traditional models, such as the Proposed Platform Framework.

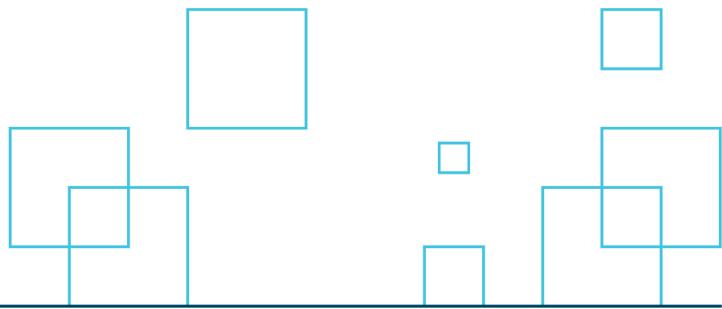
Regulators must be cognizant of the potential unintended consequences that could result from over-reaching terminology and interpretation. Such consequences could be harmful not only to industry by creating confusion and red tape that would stifle innovation and drive business out of Canada, but also to regulators by creating an unworkably broad mandate, or a mandate that directly conflicts with other Canadian legislation (such as the anti-money laundering legislation expected later this year). Consumer and commercial interests alike suffer where there is a misalignment of incentives and a lack of education. Such pitfalls can best be avoided through ongoing dialogue, which may take the form of a task force of experts to work with government policymakers and regulators to fully study and review each distinct aspect of digital asset trading platforms and the broader global blockchain regulatory frameworks and objectives. Where appropriate guidance is established, it should be published in a timely and transparent manner, as well as coordinated with other policymakers, legislation, and guidance.

The Chamber has prepared the following response to the Consultation with input from our members, which includes financial services companies, technology companies, law firms, multinational consulting firms, digital asset trading platforms, startups, and academics. We suggest ongoing and collaborative dialogue as we carefully work with Canadian regulators to establish a path forward that is in the best interest of Canadian blockchain investors, innovators, and the general public who stand to benefit from participation in the rapidly growing global blockchain ecosystem.

For the purposes of this Consultation reply, the Chamber has prepared a set of general comments and recommendations that should be considered throughout. Further, we respond directly to the questions raised in the Consultation Paper and have highlighted some specific challenges that deserve further consideration.

### **General Consultation Comments**

As a matter of general comment, the Chamber offers the following feedback in an effort to assist regulators and policymakers as they move through the work ahead in relation to digital asset trading platforms.



## 1. Not All Digital Assets Are Securities

At its heart, blockchain is a database technology. As with any database technology, it can be used to create and track digital representations of assets (including natively digital goods). The financial services applications of blockchain include value transfer and the creation of digital tokens<sup>3</sup> that may be used to represent traditional securities and other traditional financial instruments. It would be too limiting, however, to only consider these applications of the technology. Any consideration of digital assets, DLT, and blockchain technology must recognize the broad array of uses for tokens as well as assets that can be digitized and transacted on blockchains. Simply creating a digital representation of an asset does not change the asset's character or nature, nor should it change the asset's treatment under law. The Consultation assumes, in some respects, that all participants in this ecosystem are "investors". They are not, nor will they be, as the ecosystem evolves beyond its current applications. While some holders of digital assets do so for investment or speculative reasons, many also use digital assets to access and utilize software programs. These types of users are expected to increase in number as the blockchain ecosystem continues to grow and evolve.

***Recommendation: Recognize that not all digital assets or digital asset trading platforms should be considered within the reach of securities, commodities or derivatives regulatory frameworks.***

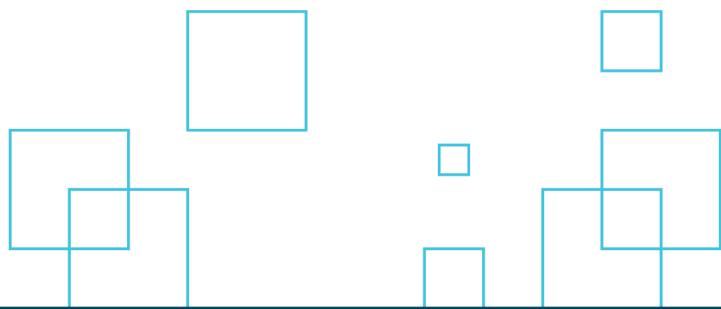
## 2. Regulatory Clarity for Digital Assets That Are Securities and Those That Are Not Is Essential

One of the most striking developments in the blockchain ecosystem is the emergence of tokenized networks. While exponential applications for digital assets are emerging, the versatility of digital assets has proved a challenge for regulators globally. The sheer number of unique characteristics that digital assets may represent means that much work remains to be done to understand their potential applications and functionality.

In the current blockchain ecosystem, digital assets can represent numerous things, from a currency to a commodity, a security, title to property, identity, provenance, and many other

---

<sup>3</sup> Digital tokens are transferable units generated within a distributed network that tracks ownership of the units through the application of blockchain technology. Chamber of Digital Commerce, Understanding Digital Tokens: Market Overviews and Proposed Guidelines for Policymakers and Practitioners, <https://digitalchamber.org/token-alliance-whitepaper/>.



assets. Further, a digital asset may initially represent one functionality, such as a security, and then shift and represent another, such as a commodity. When it comes to the regulatory treatment of a digital asset, this very versatility can be confounding. The fact that other countries are recognizing the potential of this technology, and developing regulatory systems to support it, renders the problem even more urgent if Canada wants to ensure it remains globally competitive.

Terminology and function-based assessment is critical when establishing any policy and regulatory framework relating to digital assets. Put another way, there is still no agreed upon nomenclature or framework that clearly establishes what is absolutely inside or outside the scope of securities and financial services regulation and policy, causing difficulty for all stakeholders that want to assess compliance and trust factors associated with digital asset exchange platforms and issuers.

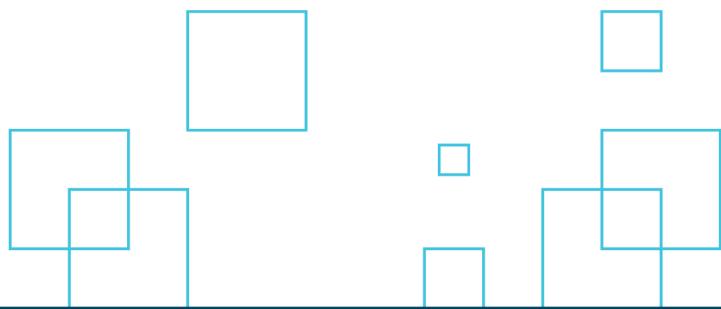
The Consultation does not squarely address the issue of how to characterize digital asset uses nor does it establish the distinction between different types of digital asset platforms.<sup>4</sup> For example, people who buy different types of digital assets and use them as currency are not investors, and would not be considered investors if they were to do the analogous act of exchanging common Canadian dollars for foreign currency. Clarity will be beneficial to the ecosystem as a whole, however, the benefit of such clarity will be lost if the positions are overly restrictive or likely to be challenged on the basis of being an incorrect application of law. Guidance relating to whether or not a digital asset is a security must recognize the breadth of possible permutations that exist, as well as other potentially applicable laws.

The importance of appropriate guidelines that take into account the myriad of applications for digital assets has been raised in numerous global fora. For example, the Chamber and its members have produced several resources in this regard, including "[Understanding Digital Tokens: Market Overviews and Proposed Guidelines for Policymakers and Practitioners](#)".<sup>5</sup> This resource, developed within the Chamber's Token Alliance, consisting of more than 450 participants, makes clear that there is a need to recognize the myriad of tokens that exist and

---

<sup>4</sup> Legal expert Addison Cameron-Huff articulates this point well. Cameron-Huff further brings forward inherent assumptions, and the challenges and risks that are related to these assumptions, as drafted into the narrative of the CSA -IIROC Consultation Paper: <http://www.cameronhuff.com/blog/csa-iiroc-consultation-2019-assumptions/index.html>.

<sup>5</sup> Chamber of Digital Commerce, Understanding Digital Tokens: Market Overviews and Proposed Guidelines for Policymakers and Practitioners, [https://digitalchamber.org/token-alliance-whitepaper/..](https://digitalchamber.org/token-alliance-whitepaper/)



that will emerge beyond securities tokens, such as utility tokens and other types of digital assets that are not securities.

As CSA and IIROC are aware, digital assets are used for:

- Identity verification;
- Payment for services and goods;
- Crowdfunding purposes, and may represent a right in a future product, but do not represent an interest in the underlying company;
- Video game platforms (in-game gold, armour, etc.) which can often be bought and sold on secondary markets or transferred between players; and,
- Access to membership or loyalty program benefits, and effectively replace a membership card to serve as proof of payment for access to services or perks.

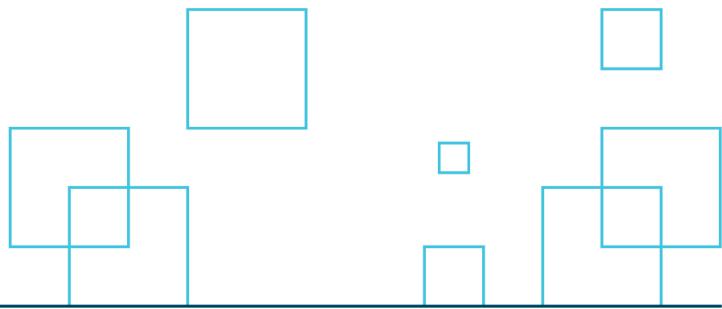
In cases where a digital asset is not a security, the Chamber has made specific recommendations for policy guidelines and governance, including the types of information that should be disclosed and when, and practices that should be clearly prohibited (for example, promises of financial return).<sup>6</sup> We believe that Canadian securities regulators should continue the publication of relevant policy positions and decisions, similar to those that have been published by the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC).<sup>7</sup> In each case, they consider the facts, context, and legislation at the time, and provide their analysis publicly.

We have seen government policies have profound effects on the development of digital asset exchange platforms and digital asset innovation and adoption. The Chamber recommends that policymakers and regulators across Canada aim to advance the development of supportive policy and regulatory guidance so that businesses in Canada focusing on digital asset innovation can confidently develop their business strategies and compliance roadmap and stay competitive globally.

---

<sup>6</sup> Chamber of Digital Commerce, Understanding Digital Tokens: Market Overviews and Proposed Guidelines for Policymakers and Practitioners, [https://digitalchamber.org/token-alliance-whitepaper/..](https://digitalchamber.org/token-alliance-whitepaper/)

<sup>7</sup> FINTRAC, FINTRAC interpretation notices and policy interpretations, <http://www.fintrac.gc.ca/guidance-directives/overview-apercu/FINS/1-eng.asp>.



***Recommendation: Publish frequent, timely and transparent guidance on digital assets, digital asset trading platforms including guidance related to digital assets that are and are not considered to be securities, commodities, or derivatives.***

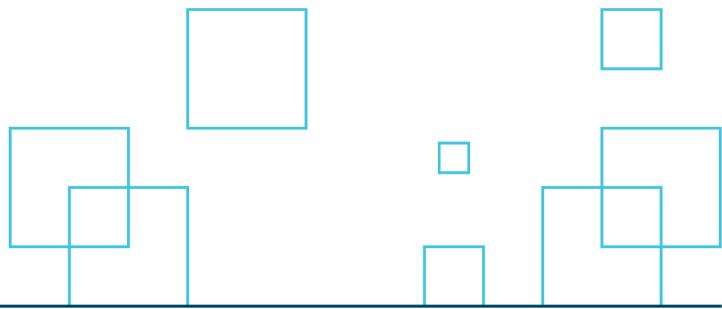
***Recommendation: Coordinate with other policymakers and regulators, including the Department of Finance, FINTRAC, and the Canada Revenue Agency, to ensure that regulations are aligned, consistent, and not confusing or overly burdensome to industry.***

***Recommendation: Take a principles-based, technologically-neutral approach to regulation and policy to foster innovation.***

3. Establish Meaningful Industry Dialogue, Input, and Collaborative Consultations to Create Effective and Appropriate Regulatory Regimes

Canadians have pioneered some of the most widely used and exciting digital asset projects to date, including Ethereum, a platform on which many other digital assets have been built. As early as 2014, the Canadian government was conducting in-depth analyses of emerging digital asset classes. In their 2015 report, the Standing Senate Committee on Banking, Trade, and Commerce recommended that “the federal government, in considering any legislation, regulation and policies, create an environment that fosters innovation for digital currencies and their associated technologies. As such, the government should exercise a regulatory “light touch” that minimizes actions that might stifle the development of these new technologies” and aim to “reduce red tape.”<sup>8</sup>

Blockchain technology has the potential to streamline transactions and regulatory burdens by reducing the need for certain intermediaries which creates greater efficiencies and promoting increased transparency. The key to the success of such initiatives is industry consultation to assist with the evaluation of the effectiveness and potential impact of regulation in advance of its drafting and implementation. As with all transformative technological innovation, it can be difficult to determine what aspects of the innovation to promote, as well as the appropriate regulatory scope, fit, and strategy. Global policymakers are actively considering a variety of ways to approach digital assets and their trading platforms. Striking an appropriate balance between protecting consumers and investors on the one hand, while allowing them access to new and highly innovative emerging markets on the other hand, is challenging. The risk



related to an error in regulatory judgement is also high - overregulation will stifle or displace blockchain innovators and investors in Canada, and ineffective regulation, and regulation with unintended harmful consequences for industry innovators and investors, will also do the same.

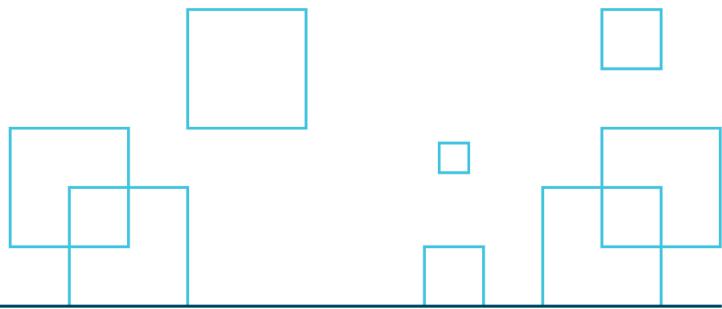
It is critical that policymakers and regulators understand blockchain technologies in an expert capacity. Achieving such an understanding will take time and will require regulators and policymakers to establish transparent, meaningful, multi-stakeholder working groups and collaborative dialogue to ensure that they are informed and working in a proactive manner to support both the growth of this highly valuable innovative sector, and to help guide the sector to embed best practices and standards into everyday operations. Meaningful consultation with industry players must occur on an ongoing basis, and not only as “point in time” or procedural exercises.<sup>9</sup>

The Chamber respectfully submits that the most effective regulatory results will be achieved through ongoing supportive and collaborative dialogue, rather than through a process that attempts to overlay or extend rules designed for an incumbent paper-based system onto new systems born in the digital age. We strongly encourage provincial policymakers, the CSA, IIROC, and its members to establish regular dialogue with industry, working groups, and a collaborative study of core questions, concerns and interests of all stakeholders in the digital-asset, and more broadly blockchain, technology industries to ensure the right regulatory balance is struck.

***Recommendation: Establish meaningful industry dialogue and collaborative consultations to create effective and appropriate policy, regulatory and legislative regimes for the global, digital marketplace.***

***Recommendation: Establish a task force of experts to work with federal and provincial government policymakers and regulators to fully study and review each***

<sup>9</sup> For example, the Office of the Privacy Commissioner (OPC) has been widely recognized for their success engaging industry, setting early standards and balanced regulation. The Canadian approach to data and privacy law was foundationally established with businesses at the table. More recent revisions to privacy laws and regulations in Canada are showing the long-term benefit of such a committed and engaged process, as awareness for privacy best practices is reasonably widespread across sectors, and there continues to be ongoing and meaningful dialogue with industry and Canadians. Heavy-handed, prescriptive regulation was not implemented at the outset of big data technology innovation, but rather, a relationship and respectful dialogue between industry, regulators and policymakers was established and has subsisted for the last 15 years serving all stakeholder interests.



*distinct aspect of digital asset trading platforms alongside broader global regulatory frameworks and objectives.*

#### **4. Investor and Consumer Education is Needed**

Investor, consumer, and public education in relation to innovative new technologies and platforms, including digital asset trading platforms, is needed, regardless of which stakeholder group is being considered in this process. By working with industry to gain a deeper understanding of emerging platforms, policymakers and regulators will be able to better support and provide principles-based public and consumer education tools.

Objective public education is particularly important in the case of nascent industries such as blockchain because the pace of change is rapid. It is noteworthy that education in this regard may diverge from traditional investor education. While providers, including the Canadian Securities Institute, have demonstrated an interest in digital assets,<sup>10</sup> most course materials, including materials related to advisory designations, have not been updated to include training related to digital assets.

We applaud efforts taken by the securities regulators to date to educate consumers, which have included engaging websites.<sup>11</sup> We encourage continued efforts in this regard, including educational materials designed to assist financial and investment advisors who may be answering questions about digital assets. The Chamber would be pleased to assist with these efforts.

***Recommendation: Develop objective investor and consumer education tools to help inform the public about digital asset trading exchange platforms.***

#### **5. Further Research and Review is Necessary to Develop Comprehensive Standards**

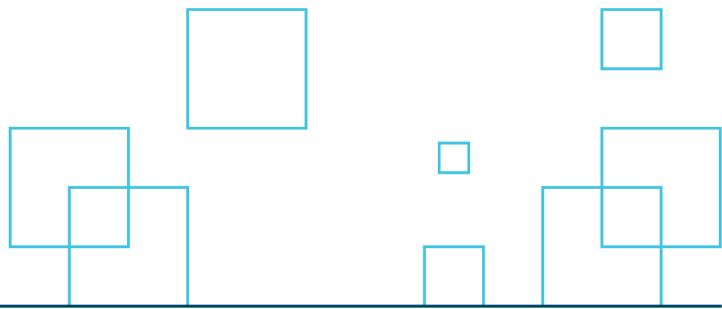
In the Consultation paper, it is noted, “although DLT may provide benefits, global incidents point to digital assets having heightened risks related to loss and theft as compared to other

---

<sup>10</sup> Canadian Securities Institute Research Foundation, Haskayne’s Alfred Lehar awarded professorship to study the impact of blockchain technologies on capital markets,

[https://www.csi.ca/student/en\\_ca/news/news/pdf/NR-CSIRF-Lehar\\_Press-Release-February.pdf](https://www.csi.ca/student/en_ca/news/news/pdf/NR-CSIRF-Lehar_Press-Release-February.pdf).

<sup>11</sup> Ontario Securities Commission, Get Smarter About Crypto, <https://getsmarteraboutcrypto.ca/>.



assets.”<sup>12</sup> The Consultation goes on to warn of “novel features that create risk to investors and our capital markets that may not be fully addressed by the existing regulatory framework.” The greater concern we see is that there has been one platform in Canada, Quadriga CX, that was ill-managed and caused harm to its users due to improper corporate governance and poor business decisions. Companies, regardless of sector, must have systems in place to mitigate risk to their stakeholders and ensure appropriate governance measures are in place. However, we caution against developing a new and broad regulatory framework in response to risks alone. Further establishing regulatory framework, ahead of holistic study of the cumulative legal, regulatory, policy, and economic landscape relating to the digital asset and blockchain ecosystem in Canada stands to introduce significant risk of industry and ecosystem disruption and interference. The risk of taking steps toward regulation without adequate evidence or policy to support these steps, impacts those who want to participate in the digital asset market - whether as innovators, purchasers, investors, or other industry participants that stand to benefit from new forms of commerce and digital engagement.

In February 2019, the Bank of Canada released a Staff Discussion Paper entitled, “Crypto “Money”: Perspective of a Couple of Canadian Central Bankers,” which discusses a number of important questions regarding the risk versus benefit assessment from the perspective of a central bank.<sup>13</sup> The Paper highlights the importance of the contemplative discourse in relation to monetary policy in Canada and states that there is no clear threat level to address, but rather significant research and broad policy work to complete to establish a clear path forward. The paper expressly states that, “while cash is a public good, a number of important policy and design questions need to be answered [to assess what would] be in the public interest. Clearly the implications for the broader financial system, especially deposit-taking institutions, need to be assessed in conjunction with other benefits and risks...”<sup>14</sup> Of note, on May 2, 2019, the Central Bank of Canada and the Monetary Authority of Singapore successfully completed the first ever cross-border and cross-currency payments using central bank-issued digital currencies.<sup>15</sup>

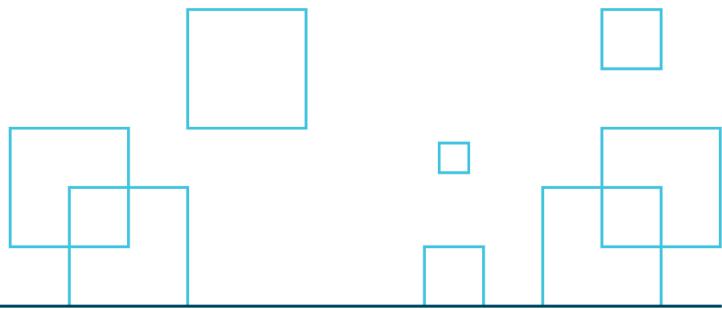
---

<sup>12</sup> Investment Industry Regulatory Organization of Canada, IIROC Notice: Joint CSA/IIROC Consultation Paper 21-402 Proposed Framework for CryptoAsset Trading Platforms, [http://www.iroc.ca/documents/2019/196069ad-9053-4d8b-8022-a8e11a6c4385\\_en.pdf](http://www.iroc.ca/documents/2019/196069ad-9053-4d8b-8022-a8e11a6c4385_en.pdf).

<sup>13</sup> Staff Discussion Paper 2019 - 01: Crypto “Money”: Perspective of a Couple of Canadian Central Bankers (February 2019): <https://www.bankofcanada.ca/wp-content/uploads/2019/02/sdp2019-1.pdf>.

<sup>14</sup> P.23, Staff Discussion Paper 2019 - 01: Crypto “Money”: Perspective of a Couple of Canadian Central Bankers (February 2019): <https://www.bankofcanada.ca/wp-content/uploads/2019/02/sdp2019-1.pdf>.

<sup>15</sup> Coindesk, “Central Banks Settle Cross Border Payments with Blockchain for the First Time” (May 2, 2019): <https://www.coindesk.com/central-banks-settle-cross-border-payments-with-blockchain-for-first-time>.



The Chamber is a strong proponent of engaged policy dialogue and research designed to help advance policy relating to digital assets, the platforms upon which they are exchanged, and how they fit into existing systems. The Chamber suggests that the CSA/IIROC takes a similar, measured approach to Platform regulation as the Bank of Canada is taking toward monetary policy applicable to digital assets. Risk should be assessed alongside reward and regulatory overreach should be avoided to minimize future jurisdictional challenges, stifling innovation and market chill.

***Recommendation: Take the time necessary to research and review the global blockchain ecosystem, considering all policy and legislative perspectives, to design and support a competitive blockchain ecosystem in Canada.***

### **Responses to Specific Consultation Questions**

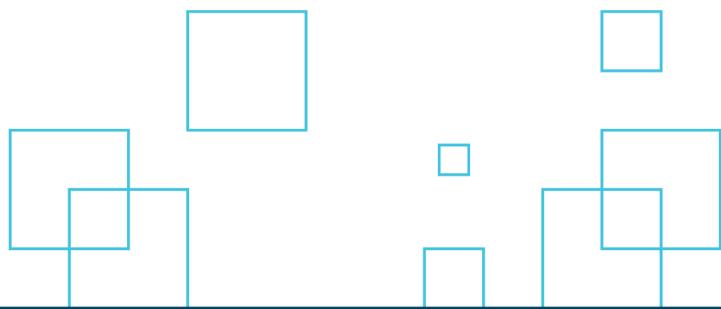
The general comments should be considered in relation to the questions below, in addition to the specific responses to each.

#### **1. Are there factors in addition to those noted above that we should consider [relating to digital-asset exchange platforms]?**

Definitions and terminology, such as “platform” for example, need to be clearly and contextually defined in all consultations, policy, and proposed frameworks going forward to mitigate the risk of establishing unclear and overly broad rules that may discourage innovation and/or result in unintended damage to businesses that should not be targeted.

Establishing regulation too early in an innovative sector also presents a risk. The industry is working hard to establish its own best practices, not least given the significant financial investments that have been made to drive progress to date. If the CSA moves forward to crystalize today’s best practices prematurely, they may be out of date in short order.

The Consultation acknowledges that “at least some of the well-established digital assets that function as a form of payment or means of exchange on a decentralized network, such as bitcoin, are not currently in and of themselves, securities or derivatives. Instead, they have certain features that are analogous to existing commodities such as currencies and precious metals.” We note that the Consultation stops short of exploring transactions that function as a “form of payment or means of exchange” - we believe these transactions require further clarification.

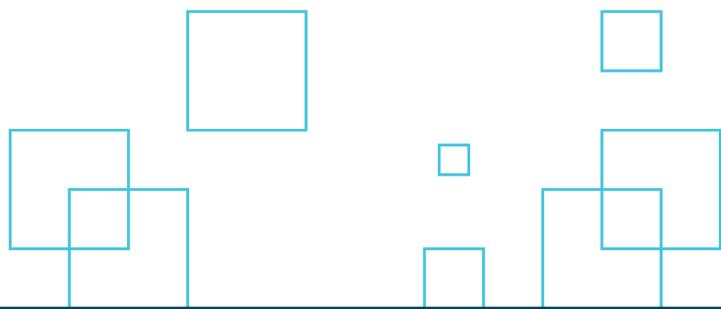


The Chamber's members submit that most Canadian Platforms do not offer trading in security tokens, but rather sell bitcoin and ether which are not securities in spot transactions. These types of Platforms are Money Services Businesses (MSBs) and should be regulated as such. The federal Department of Finance recognized this in 2014 when Bill C-31 proposed to amend the PCMLTF to add definitions for "virtual currency" and "dealers in virtual currency" and to regulate dealers in virtual currency as MSBs. It took the Department of Finance four years to publish the draft regulations in early 2018, and the final regulations which were scheduled to be adopted in the fall of 2018 are still on hold. Many Canadian Platforms have applied to FINTRAC for registration as MSBs but have been turned down or have had to change their business model to include fiat currency trading to be subject to MSB regulation. For the vast majority of Platforms, MSB regulation is appropriate and should address many investor protection concerns regarding digital assets, including ensuring that purchasers of cryptocurrencies are subject to identity verification requirements and transactions in cryptocurrencies are subject to reporting and recordkeeping requirements under Canadian anti-money laundering laws.

The Chamber proposes that exchanges dealing in virtual currencies should be considered Money Services Businesses, and not Brokers or Dealers in securities, a position that seems to have growing support in Canada.

There are several factors, beyond investment contracts, that should be assessed to determine what may constitute a security in the tokenized world. The definitions section in the *Ontario Securities Act* lists many factors that may not be appropriate or suited to determine what qualifies as a security or activities regulated by securities regulation. Coordinated industry discussions are necessary to determine the depth and breadth of applicability of current definitions in the *Ontario Securities Act*. We encourage coordination between federal and provincial policymakers and regulators to ensure that the industry does not receive conflicting guidance.

Finally, the Proposed Framework states, "the CSA wishes to remind market participants that any person or company advertising, offering, selling, or otherwise trading or matching trades in digital assets that are securities or derivatives, or derivatives that are based on digital assets to persons or companies in Canada, or conducting such activities from a place of business in Canada is subject to securities legislation in Canada." In Canada, we have seen a similarly proposed piece of regulation as part of the Proceeds of Crime Money Laundering and Terrorist Financing Act (the "PCMLTFA" or the "Act"). The particular regulation proposes that those "directing services" to Canadians will be considered foreign money services businesses, and



therefore captured under the Act and regulated. A business is seen to be “directing services” to persons or entities in Canada if it meets at least one of the following three criteria:

1. The business undertakes marketing and advertising directed at persons or entities in Canada;
2. The business maintains a Canadian website (e.g., with “Canada” in the name, a .ca domain name); or,
3. The business is listed on a Canadian business directory.

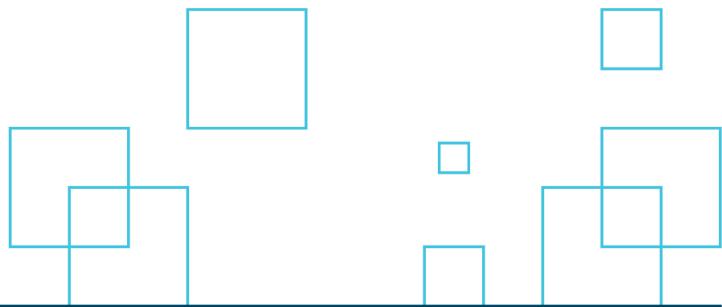
In the case of the Canadian regulatory environment, this leaves open a loophole for foreign entities operating in this space but “passively” providing services to Canadian customers (*i.e.*, through word of mouth and reputation). In the digital asset economy, direct advertising isn’t the norm. Customers are obtained through word-of-mouth and reputation rather than direct advertising in magazines, papers, and similar publications. As a result, this gives foreign entities an “out” from the regulation based on the current definition. It should be noted further that we are aware of many examples of Canadians using services or platforms that would not meet the proposed requirements based on the above. We acknowledge that Part 5.1 states that exemptive relief may be considered for those located outside of Canada and regulated by a foreign regulator “in a manner that is similar to domestic oversight.” Further discussion is required to understand what this would entail and how this would be assessed, particularly given the rapidly shifting regulatory environment we currently see across the globe, relative to the virtual asset space. It is imperative to ensure that Canadian exchanges and platforms are not disadvantaged by exemptive relief granted to foreign exchanges and platforms.

Finally, it is important for regulators to be aware that the vast majority of players in the blockchain ecosystem aren’t in Canada. Almost all of the exchanges cited in the Consultation operate abroad. If Canada creates rules that put Canadian exchanges or other businesses at a competitive disadvantage then not only will Canada have no exchanges, but Canadians will also be carved out of this market.

### Risks, Custody and Verification of Assets

**2. What best practices exist for Platforms to mitigate these risks? Are there any other substantial risks which we have not identified?**

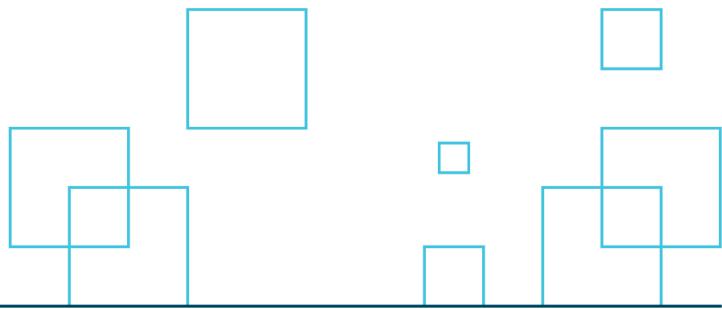
**3. Are there any global approaches to regulating Platforms that would be appropriate to be considered in Canada?**



---

There are no leading global approaches as of yet. Further study is required and the following regimes should be researched and considered as they demonstrate a nuanced approach to the classification of digital assets.

1. **Japan:** Japan requires that digital currency exchange businesses manage customer's funds or digital currency separate from their own. The state of this must be verified by CPAs or accounting firms. They must have a contract with a designated dispute resolution center with digital currency expertise. They must keep accounting records of digital currency transactions and submit a report of these transactions annually to Japan's Financial Services Agency. A group of exchange businesses formed a self-regulatory body that all registered exchange businesses must now join.
2. **Switzerland:** Switzerland has defined tokens into three categories: i) payment tokens (digital currencies) which are used as a means of payment or value transfer; ii) utility tokens which provide digital access to applications or services through the blockchain; and, iii) asset tokens which are assets such as a debt or equity claim and are analogous to equities, bonds and derivatives. Tokens received in an "ICO" generally qualify as securities. They define securities as certified or uncertified securities, derivatives and intermediated securities that are capable of mass standardized trading.
3. **Bermuda:** Bermuda is working to develop itself as a destination for utility tokens, tokenized securities, and coin offerings. They are creating a digital currency association with a defined code of conduct and rules of operation. The group will be self-governing. Utility tokens are not securities unless there is a promise of future value. There is a working group directed by the Minister of National Security which is tasked with ensuring that Bermuda's regulations are conducive for the development of digital currencies. The group's members include individuals from a variety of government ministries, a bank, a law firm, the National AML Committee, and the Bermuda Business Development Agency. The group is self-governing. They have previously consulted the public for opinions on digital asset regulation and what those regulations should be.
4. **Australia:** INFO 225 provides guidance on a number of aspects considered in this Framework. Guidance is given around the legal status of ICOs and digital-assets, considerations for when an ICO could be an offer of a financial product, when a platform for secondary trading of ICO tokens or other digital-assets could become a financial market, and guidance around how prospective ICO issuers and digital-asset businesses can obtain informal assistance from the Australia Securities and Investments Commission.



Members also note Malta, Gibraltar, and Mauritius are demonstrating global leadership through its standards-setting approach to digital assets and digital asset exchange platforms.<sup>16</sup>

**4. What standards should a Platform adopt to mitigate the risks related to safeguarding investors' assets? Please explain and provide examples both for Platforms that have their own custody systems and for Platforms that use third-party custodians to safeguard their participants' assets.**

Many platforms are taking proactive measures to ensure they can mitigate risk and build successful and sustainable businesses. As business needs have evolved, so too have the number of custody solutions, which we see as a very positive advancement that will attract institutionally managed digital assets that will advance blockchain adoption globally. Industry is demonstrating its commitment to improving innovation at a rapid pace. We encourage regulators and policymakers to acknowledge and applaud positive steps forward.

With digital tokens, there is no object stored physically anywhere in the world; rather records are maintained on an immutable blockchain showing transactions and transfers of ownership that have occurred by sending and receiving tokens via a software wallet using public-private key encryption. The technologies and methods used to maintain ownership and to safeguard these assets are constantly evolving. For example, the application of multi-signature<sup>19</sup> technology adds a layer of complexity to custody requirements for these assets because the keys necessary to execute a transaction may be in multiple physical locations.

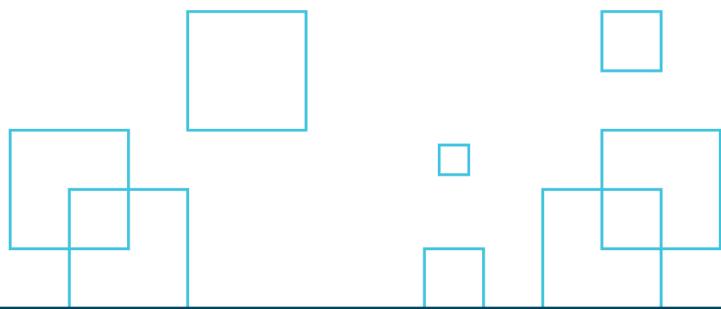
Public and private keys are analogous to a user name and password where the public key, like a user name, may be viewed by anyone and the private key, like a password, is stored privately and is used in conjunction with the public key to access the software. Regulators and policymakers will need to understand how ownership of these new assets is currently reflected and be mindful of the evolution of the technologies as they consider guidance to market participants on the application of existing regulatory requirements surrounding custody<sup>20</sup> to innovative technologies.

This changing technology is moving faster than regulatory infrastructure and decision-making. Investment advisers, lawyers, independent auditors, and others have spent

---

<sup>16</sup> Regulatory Framework for Custodian Services (Consultation Paper):

[https://www.fscmauritius.org/media/67493/consultation-paper-custody-of-digital-assets\\_final.pdf](https://www.fscmauritius.org/media/67493/consultation-paper-custody-of-digital-assets_final.pdf).



countless hours at a significant cumulative cost to try to fit rules written for physical and book-entry securities to the blockchain environment. Nevertheless, the market needs more definitive guidance for participants to move forward in light of regulatory and litigation risk.

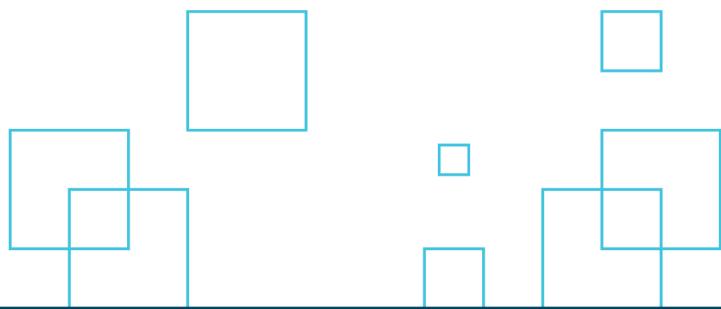
Any possession or control standards for digital assets need to take into account the technological reality of how these assets are managed, and satisfactory control should focus, for example, on whether the digital asset is properly cryptographically protected and that adequate cybersecurity practices, specific to DLT, are maintained. The Chamber encourages regulators and policymakers to be open-minded as to what can constitute possession or control and who can provide custody of digital assets, and for the government to foster a pro-growth environment when interpreting these and other issues that arise as blockchain technology develops.

There are varying schools of thought on the degree to which specific security measures should be known/shared outside of strictly controlled and vetted parties. The argument against a broader sharing of security parameters is the possibility that doing so may expose the platform to an attack vector via a vulnerability made apparent to a potential attacker via descriptions of the security measures in place. Further discussion with industry is required to fully address any new or proposed standards.

**5. Other than the issuance of Type I and Type II SOC 2 Reports, are there alternative ways in which auditors or other parties can provide assurance to regulators that a Platform has controls in place to ensure that investors' crypto-assets exist and are appropriately segregated and protected, and that transactions with respect to those assets are verifiable?**

It is important that the regulators work with industry to establish expectations regarding the scope of high-level control objectives or system requirements that may be relevant for a securities-specific digital asset platform. Some basic controls may include those that would manage and mitigate the custodial risks, including the safeguarding of private keys and ensuring that investors' digital assets exist and are appropriately segregated, protected, and that transactions for those assets are verifiable.

In many cases, public blockchains are fully transparent and may be auditable in relatively novel ways that are not possible with traditional assets. Assets in wallet addresses can be viewed at any time. Even in the case of assets that have been designed to be privacy intensive, audit keys can be built into the design of the digital asset to allow a type of "view



---

only” access on an as-needed basis. These types of features must be taken into consideration when designing audit processes. In some cases, it may be possible to automate most audit functions relating to the issuance and custody of digital assets.

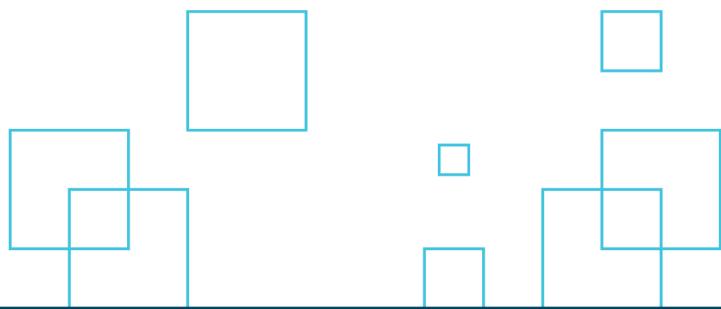
Many platforms pool assets. It is often impractical and expensive for the platform to create separate digital asset wallets for each user that hold only that user’s assets and confirm any transaction activity to the asset’s underlying blockchain. In such cases, transactions would only be visible on a public blockchain when the platform receives custody of a digital asset, transfers custody of a digital asset, or transfers a digital-asset between different wallets that are controlled by the platform. In other instances, it may be practical for platform operators to maintain segregated wallets for each user and/or to conduct transactions in a manner that is always confirmed to the blockchain of the digital-asset affected by each transaction.

Further, as noted by the CPA, regardless of whether a SOC 1 or SOC 2 report is provided, it is not possible to provide a Type II report (e.g., SOC 1 Type II or SOC 2 Type II) until the Platform has been in operation for a reasonable period of time (e.g., 6 months). Consideration should be given when a Type I report will be accepted and what the maximum period of time is that the Platform can operate until a Type II report is required.

The Consultation also notes that Platforms seeking registration as an investment dealer and IIROC membership that plan to provide custody of digital assets will not only need to satisfy existing custody requirements but may be expected to meet other yet-to-be-determined standards specific to the custody of digital assets. Should there be additional standards required it is important that these are addressed appropriately through focused consultation and in a manner that balances the protection of the public interest and the ability for organizations to innovate in Canada. The Chamber recommends that options to provide assurance over the design and operating effectiveness of and any controls should be explored with industry at the table, and that the Chamber and its members would welcome the opportunity to participate in these discussions.

## **6. Are there challenges associated with a Platform being structured so as to make actual delivery of crypto assets to a participant’s wallet? What are the benefits to participants, if any, of Platforms holding or storing crypto assets on their behalf?**

Best practices for platforms that are considered regulated under securities laws, are still being defined by innovation and industry.

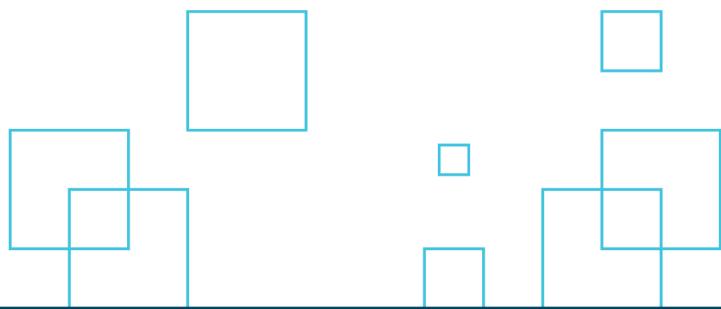


It is important to consider the innovations that are unlocked by technology, including the ability of owners to take full custody of digitally native assets, or to place such assets in a multi-signature smart contract, where both the platform operator and the owner of the asset would be required to sign a transaction in order to move an asset. Such innovation has the potential to greatly increase transparency, efficiency, and auditability. These innovations do carry risks as well, including the risk of loss of private keys used to sign transactions, and the risk that a smart contract does not function as intended or contains weaknesses in its code that can be exploited.

It is noteworthy that the use of technology can allow for more secure transactions without the use of intermediaries, or in some instances, using different types of intermediaries, including automated functions. For example, in a transaction that is conducted on a completely decentralized platform, it would be possible using digital signatures and other electronic controls to validate that certain conditions (cybersecurity-related controls, identification, KYC, etc.) are sufficiently met without necessarily exposing the users' personal information. Such models in which transactions are private but not anonymous should be explored and encouraged as they can play a significant role in protecting consumers from potentially harmful data and privacy breaches. The Chamber is concerned that the Proposed Platform Framework may stifle these innovations, which are designed to protect personal information and reduce transaction costs, by imposing a traditional model of financial regulation onto Platforms.

With regard to SOC Reports, members identified alternative options to SOC engagements which, depending on the ultimate audience of the results of such work, could serve as additional assurance that appropriate controls are in place. Establishing internal reporting protocol requirements may be useful. For example, internal controls over financial reporting and data provide factual accounts of performed procedures. Generally, they are used for management and have restrictions on public distribution. There are a variety of frameworks (COSO, CobiT, SOC 2, etc.) that can be utilized in guiding the above work and should be studied more carefully to assess applicability for platforms regulated by securities laws.

These disclosure principles apply to the parameters that exist when taking custody of their own digital assets. It is widely believed that the single greatest challenge to delivery and self-custody is user error. In some instances, it may be preferable for users that are not properly educated to have platforms remain in custody of their digital assets. In the meantime, risk-based education should continue. Where possible, platforms should implement real-time



safeguards, such as double-checking a wallet address, and displaying short and clear disclosures where a user requests to take custody of their funds.

### Price Determination

#### **7. What factors should be considered in determining a fair price for crypto assets?**

When considering price discovery, the activity that is confirmed to a digital asset's public blockchain should be taken into consideration where possible. This may include the volume of trading activity and the rates at which a digital asset has been traded for other digital assets (which is possible in some cases without the use of an intermediary). In such instances, the information is publicly accessible and easily verifiable. It may even be possible and desirable to automate some information aggregation and publication processes.

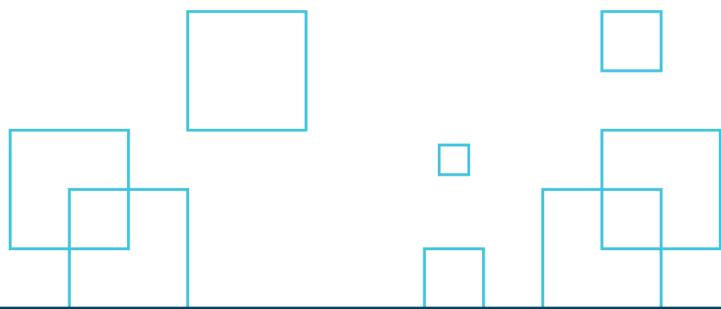
Where transactions or transaction information are not publicly available, clear guidelines should be developed to help platforms report complete and accurate information, including how such information should be calculated and disclosed. Here, again, it may be possible to automate many of the discovery functions based on predefined regular inputs from platforms at regular intervals.

We recommend working closely with the industry to understand the nuances of pricing and price disclosures. This may include transactions that take place via over the counter (OTC) units connected to platform providers, as well as the impact of platform providers in jurisdictions outside of Canada, as well as traditional futures markets that have implemented products related to digital assets.

#### **8. Are there reliable pricing sources that could be used by Platforms to determine a fair price, and for regulators to assess whether Platforms have complied with fair pricing requirements? What factors should be used to determine whether a pricing source is reliable?**

The fair and transparent pricing of digital assets continues to be the subject of much speculation and some academic study.<sup>17</sup> We agree that this is an important issue. We recommend that, rather than providing strict guidelines relating to how price discovery should/must be done, there be instead strict prohibitions against deceptive and manipulative

<sup>17</sup> For example, John M. Griffin and Amin Shams, Is Bitcoin Really Un-Tethered?, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3195066](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3195066).

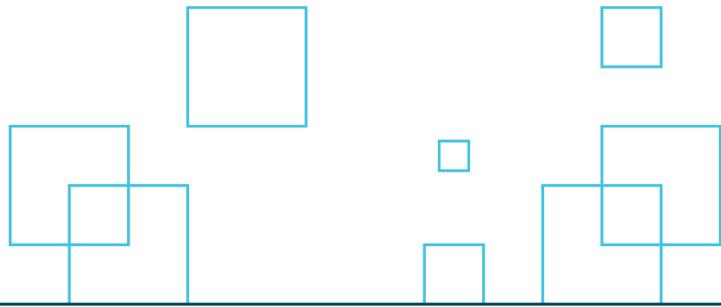


practices. We believe that this approach would continue to foster innovation while punishing “bad actors” within the ecosystem.

It was noted that where a tangible asset guarantees or is represented by a digital asset, there should be clear and timely financial audits related to the underlying asset (for example, real property). Material misrepresentations should have appropriate consequences, in particular where these meet the standard for negligence or malice. Finally, practices such as inflated or misleading transaction volumes on platforms should also be prohibited. Trading volume that represents trades made by the platform itself (and not by a user) should be explicitly excluded from the exchanges’ trading volume, as should trades conducted by third parties (including bots) for the sole purpose of creating volume on a platform and/or affecting prices on a platform.

Of note, price discovery, transparency, and lack of self-dealing are important, however, digital asset trading is a global activity. Pricing is not set by the Canadian marketplace but rather is set globally. Most exchanges make use of "liquidity pools" (*i.e.*, trading on their account with other exchanges to fulfill orders) or rely on people running arbitrage bots to ensure that large orders can be processed quickly without too much slippage. Users want this to happen because they want to be able to trade on Canadian exchanges, rather than using foreign exchanges that have substantially more volume. Unlike traditional exchanges, most digital asset trading being done by Canadians is not occurring in Canada and therefore cannot be regulated by Canadian regulators. Efforts to regulate extraterritorially is futile and more likely to result in an erosion of the competitive position of Canadian exchanges, further offshoring of digital currency trading activity.

As discussed above, the Proposed Framework may apply both to platforms that operate in Canada, and to those located outside of Canada that have Canadian participants. Clear guidance concerning any applicable exemptions/relief is required. If there is an expectation that exemptions will be granted to operators in jurisdictions that are deemed to have sufficient regulatory regimes in place in their home or operating countries, it would be desirable for Canadian regulators to publish and maintain an up-to-date list of such jurisdictions. The conditions under which exemptions/relief would be withdrawn from a particular platform operator should be clear (for instance, if there were egregious compliance issues in the home or operating country).



---

Finally, it would be imperative to ensure that Canadian exchanges and platforms can comply with these regulatory requirements to ensure Canada can maintain a competitive global position and participate in this growing and highly valuable marketplace.

#### Surveillance of Trading Activities

**9. Is it appropriate for Platforms to set rules and monitor trading activities on their own marketplace? If so, under which circumstances should this be permitted?**

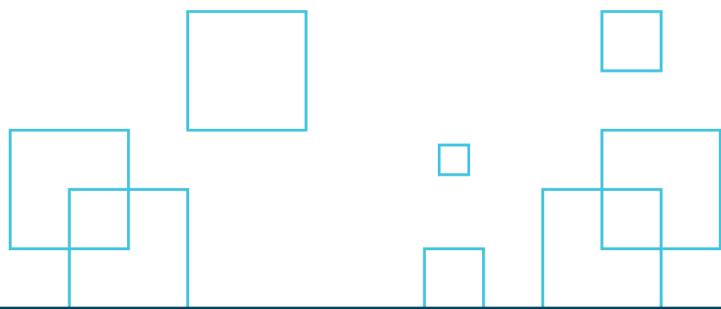
**10. Which market integrity requirements should apply to trading on Platforms? Please provide specific examples.**

**11. Are there best practices or effective surveillance tools for conducting crypto asset market surveillance? Specifically, are there any skills, tools or special regulatory powers needed to effectively conduct surveillance of crypto asset trading?**

**12. Are there other risks specific to trading of crypto assets that require different forms of surveillance than those used for marketplaces trading traditional securities?**

These questions can be addressed along two dimensions: the actions that platforms take in terms of monitoring and oversight, and the monitoring and oversight of the platforms themselves.

On the first dimension, the Chamber is aware that digital asset platforms are starting to monitor customer activity and monitoring for suspicious behavior. They are manually, or through combinations of manual and automated methods, identifying types of behavior and indicators of suspicion that require further consideration and engagement with regulators and other authorities. The typologies of what suspicious behavior looks like in the context of digital asset transactions is beginning to be better understood and documented. A number of these typologies are new and different to a fiat environment. While this monitoring activity is not currently a regulatory requirement in Canada, a number of platforms and companies are focusing their resources on such activities in an effort to proactively identify and mitigate the threat of their platforms being used for money laundering or illicit behaviour. Blockchain analytics tools created by companies such as CipherTrace and Chainalysis can be effective in tracing digital assets throughout the blockchain. The industry is anticipating federal regulations for anti-money laundering to establish surveillance requirements. The Chamber



recommends that provincial regulators align any surveillance requirements with the upcoming federal changes.

Once “virtual currency dealers” are regulated as MSBs, they will be subject to regulatory oversight by FINTRAC, which is expected to include reporting and surveillance measures appropriate for such Platforms. The Chamber expects that FINTRAC oversight will be sufficient for most Platforms that are not trading in securities.

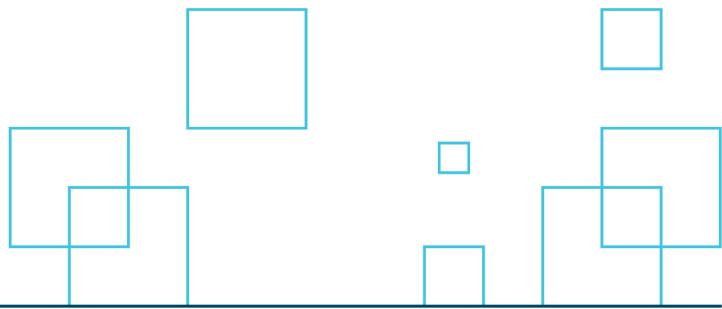
With respect to market manipulation, this responsibility currently sits with the Compliance Officer and is done on a proactive basis. Certain companies are building indicators and surveillance protocols into the training provided to members of their internal compliance team. There are also mainstream monitoring tools that provide surveillance capability to fiat financial organizations and are now increasingly turning their attention to FinTech and digital asset-related businesses, such as Irisium.

Chamber members felt that the scope of surveillance best practices should ideally include both functional activities and their supporting technology elements. For example, the scope should include the processing of transactions along with the systems (infrastructure, software, people, processes, data, procedures, etc.) that support the delivery of processing of transactions.

On the second dimension, the application of systems such as IIROC’s market surveillance system<sup>18</sup> may be useful in some instances, the development of such tools as they relate to digital assets should take into consideration the types of data that are publicly available, and the ability to automate certain oversight functions. Industry leaders in blockchain analysis technologies are already emerging, and it will be of great importance to work with such companies, as well as consult with the industry, to ensure that technologies are appropriately leveraged for efficiency. In order to be effective in this aim, there is a need to understand the current state of technology, as well as innovations which are continuously emerging. The ideal system must be robust and flexible enough to interface with data sets that are built in accordance with different technological standards.

---

<sup>18</sup> Investment Industry Regulatory Organization of Canada, IIROC and Nasdaq unveil state-of-the-art market surveillance technology to enhance oversight of Canada’s capital markets, [http://www.iroc.ca/documents/2019/0f12e531-e281-4fd7-8958-9ff0e6930037\\_en.pdf](http://www.iroc.ca/documents/2019/0f12e531-e281-4fd7-8958-9ff0e6930037_en.pdf).



It will be equally important to define the boundaries of the application of such oversight, which relates back to the need for comprehensive guidance in relation to the taxonomy of digital assets. Similarly, it will be important to clearly define exclusions, lest there be an expectation that provincial regulators are tasked with the monitoring of a volume of data that does not present a risk commensurate to such monitoring (such as in-game gold, or rewards points).

#### Systems and Business Continuity Planning

**13. Under which circumstances should an exemption from the requirement to provide an ISR by the Platform be considered? What services should be included/excluded from the scope of an ISR? Please explain.**

At this stage, it remains difficult to advise on this question as the level of decentralization of a given platform, for example if someone has a fully decentralized platform, it may mean that an ISR may not be feasible. The Chamber recommends that an industry and regulator working group be established to further discuss how to approach ISRs and the related questions regarding business continuity planning.

#### Conflicts of Interest

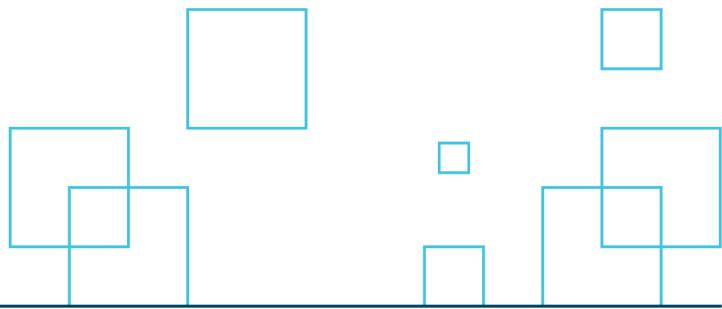
**14. Is there disclosure specific to trades between a Platform and its participants that Platforms should make to their participants?**

**15. Are there particular conflicts of interest that Platforms may not be able to manage appropriately given current business models? If so, how can business models be changed to manage such conflicts appropriately?**

Platforms should provide clear and concise real-time disclosures, whether or not these are related to any conflicts of interest. Clear guidance should be issued describing the circumstances that create a conflict of interest, as well as the expected resolution and disclosure. Chamber members did not believe that there were insurmountable conflicts of interest but did express a desire for clear guidance in this regard.

#### Insurance

**16. What type of insurance coverage (e.g. theft, hot-wallet, cold-wallet) should a Platform be required to obtain? Please explain.**



#### **17. Are there specific difficulties with obtaining insurance coverage? Please explain.**

We believe that the standards in this regard should be no greater than those established for traditional broker-dealers and custodians. Insurance in other industries (including the banking industry) does not provide full coverage for investors. The Canadian Deposit Insurance Corporation (CDIC) covers only the first \$100,000 in eligible deposits at any one member institution for any single depositor.<sup>19</sup> Significant exclusions from eligible deposits exist, including mutual funds, stocks, bonds, and accounts denominated in foreign currencies. In addition, some account types are exempt. It does not make sense to hold digital asset platforms to a higher standard than the standard that is applicable to Canadian banks. Finally, it is worth noting that in instances where a platform does not take custody of digital-assets on behalf of its users, insurance may not be necessary.

There is a relatively strong consensus that the challenges in the current environment would make it difficult to mandate insurance outside of a publicly administered insurance scheme.

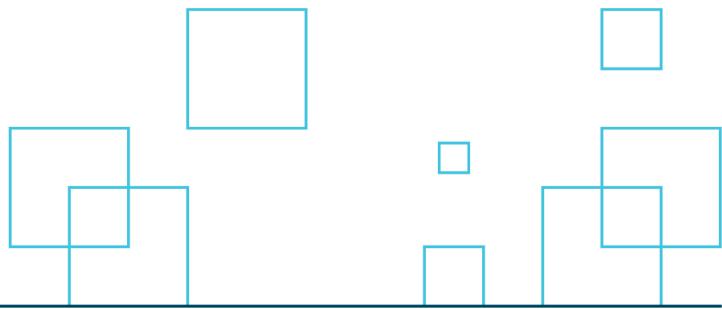
#### **17. Are there specific difficulties with obtaining insurance coverage? Please explain.**

Our members raised concerns over the fact that there are currently very few insurance providers willing to insure digital assets, or companies that deal in digital assets. Anecdotally, companies that deal in digital assets have reported significantly higher premiums, including premiums for insurance products (such as Directors' and Officers' liability insurance) that are unrelated to digital assets. Where insurance is obtained, buyers have expressed doubts about the nature of the coverage, and whether or not the insurer has understood the underlying digital assets sufficiently enough to allow appropriate insurance contract parameters. In short, the industry is not currently well-served. While we support insurance as a best practice, we recommend a cautious approach to requiring specific coverages, in particular where markets are limited and cost-prohibitive.

This is not a uniquely Canadian issue. Earlier this year, BitGo, a company that acts as a custodian (among other functions), announced that it had acquired insurance covering some of the digital assets that it holds at a significant expense.<sup>20</sup> This announcement quickly

<sup>19</sup> Canada Deposit Insurance Corporation, What's Covered?, <https://www.cdic.ca/about-deposit-insurance/whats-covered/>.

<sup>20</sup> <https://blog.bitgo.com/bitgo-sets-the-standard-for-insurance-coverage-and-transparency-4cf93446bbd7>.



---

attracted the ire of an underwriter, who went on to discuss in-depth the nuances of what may and may not be covered.<sup>21</sup>

**18. Are there alternative measures that address investor protection that could be considered equivalent to insurance coverage?**

Ideas proposed included devising an insurance scheme (similar to CDIC) in which platforms were required to participate, with reasonable premiums and strict parameters. This type of scheme may be useful, even if not mandatory, in the short term in order to provide insurance markets for digital asset platforms that are struggling to find market fit.

Further, it may be possible for platforms to instate a form of self-insurance by maintaining fiat balances in amounts equivalent to digital assets held on behalf of users in hot wallets (which are connected to the internet and can be used to conduct transactions) at all times.

Regulators should work with industry participants, both platforms and insurance companies, to better understand the types of risks that can be insured and those which cannot. Regulations should be tailored to meet the needs of investors, platforms and insurance companies in order to create standards that will reduce the cost of insurance in the overall industry. Without standards, platforms and insurance companies will have to engage in bespoke insurance policies that will be costly to obtain and require a lengthy underwriting process.

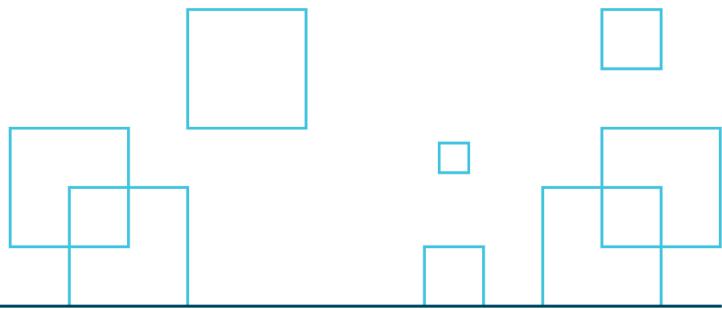
Clearing and Settlement

**19. Are there other models of clearing and settling crypto assets that are traded on Platforms? What risks are introduced as a result of these models?**

**20. What, if any, significant differences in risks exist between the traditional model of clearing and settlement and the decentralized model? Please explain how these different risks may be mitigated.**

---

<sup>21</sup> Ian Allison, Underwriter Claims Crypto Custodian BitGo Exaggerated Insurance Coverage, <https://www.coindesk.com/crypto-custodian-bitgo-exaggerated-insurance-coverage-underwriter-claims>.



Where transactions are confirmed on a blockchain, settlement can be automated and almost instantaneous, creating an immutable public record of the settled transaction, and allowing for transactions that involve fractions of a unit or share. Taken together, these characteristics indicate that there are significant advantages that can be offered over traditional settlement methods.

The Chamber recommends that an industry and regulator working group be established to further discuss how to approach related questions regarding settlement and clearing.

## **21. What other risks are associated with clearing and settlement models that are not identified here?**

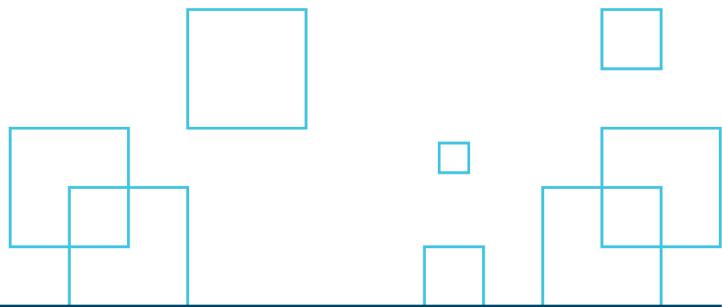
With regard to significant differences in risk that exist between traditional and decentralized clearing, members commented that decentralized exchanges should be subject to KYC/AML compliance measures that fit with and reflect their business models. The Chamber commented on Canada's proposed KYC/AML Proposed Regulations last fall and encourages the CSA and IIROC to review the comments submitted, as they provide relevant considerations at length in relation to this topic.<sup>22</sup>

It is also worth considering that new models for digital identity and digital transaction security will dramatically enhance the security for these types of trades. Decentralized exchanges should be encouraged to support a model where the trade instruction, which is digitally signed for all digital asset trades by the User's Private Key, also include:

1. Evidence in the form of a digital signature of a manifest of the system that protected the Private key, and support verification that the Cyber controls are operating correctly as part of the transaction execution. This attestation process will assure the controls required by the user are in place and working.

---

<sup>22</sup> Chamber of Digital Commerce, Comments of the Chamber of Digital Commerce on the Regulations Amending Certain Regulations Made under the Proceeds of Crime (Money Laundering) and Terrorist Financing Act, 2018 (the "Proposed Regulations") published in the Canada Gazette on June 9, 2018, [https://digitalchamber.org/wp-content/uploads/2018/09/Canada-AML-Proposed-Regulation-Comment-Letter\\_Chamber-of-Digital-Commerce.pdf](https://digitalchamber.org/wp-content/uploads/2018/09/Canada-AML-Proposed-Regulation-Comment-Letter_Chamber-of-Digital-Commerce.pdf).



2. Evidence in the form of a digital signature of a manifest of the compliance requirements is fully satisfied prior to the execution of a transaction. Third party compliance service providers could provide one-time use validation tickets that all of the steps for compliance were satisfied, and the compliance ticket could then be consumed by the execution of the trade.
3. Integration of privacy and protection of personally identifiable information. The new models should consider that it is possible to execute a private trade between known parties without the exchange knowing the parties, but trusting a third party service that “knows” the parties. Digital assets have the ability to enable a new model of private, but not anonymous, transactions that will meet the true needs of protecting customers and their PII.

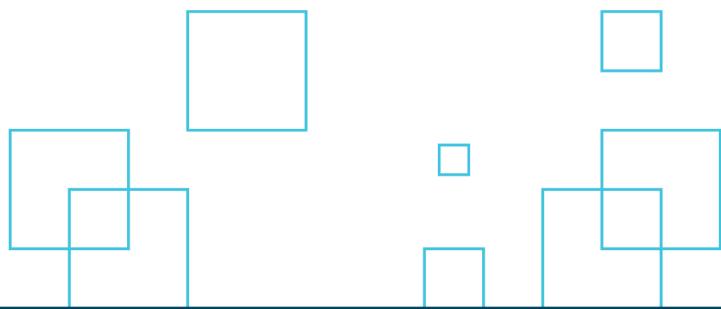
It is important that FinTech innovation is given space to evolve generally and specifically in relation to online transactions, as paper trade instructions are quickly becoming irrelevant and outdated.

Exchanges should be encouraged to support digitally signed instructions that are built on secure technology. This may include:

- Securely stored private keys in hardware with strong device controls;
- “What You See is What is Signed” technology such as global platform TUI 1.0 standard for trusted display;
- User consent using secure PIN or biometric authentication such as EU PSD2 Cyber security requirements for consumer e-commerce;
- Verified trust protocol attesting that systems are operational and working as expected.

Finally, platforms are currently unable to achieve Delivery vs Payment (“DVP”) settlement. DVP settlement is a requirement for many brokers, funds and other regulated investment entities to participate in trading on an Exchange or Marketplace. To date, there is no known system where digital assets can settle for fiat currency in a DVP fashion. The primary reason for this, correctly identified by the Consultation Paper, is a lack of clearing agents or clearinghouses with the technical capability to facilitate DVP settlement. This creates several risks not identified in the Consultation paper.

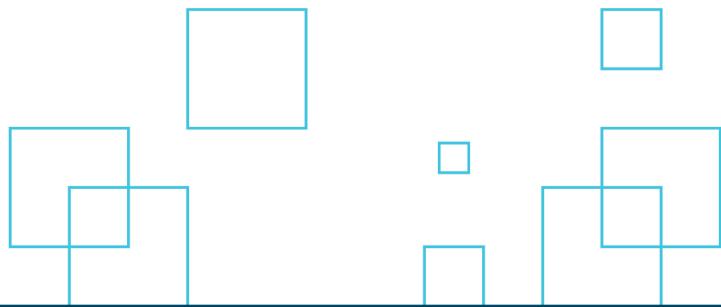
First, platforms, in their current configuration, require participant’s deposit fiat (or digital assets) on the Platform, or must setup margin facilities, prior to trading. This introduces counter-party risk and/or credit risk that does not exist today in regulated Marketplaces.



---

Second, the lack of DVP settlement precludes many brokers or trustees from participating on these platforms because they are prohibited from taking on this type of risk when dealing with client assets. This introduces an “opportunity cost” risk as many investors who choose to work exclusively with brokers would not be able to access digital assets on platforms. The lack of DVP also prevents pension funds and mutual funds from participating on the platforms, again excluding large segments of the Canadian investing public. Rather than relying on exemptive relief, regulators should form working groups with current market infrastructure participants to explore settlement systems. An example of how DVP settlement could be achieved is described below.

Certain digital assets, such as bitcoin, operate on a blockchain, (*i.e.* the Bitcoin blockchain,) that possesses the technical capabilities required to create a DVP-like settlement. However, key market infrastructure is required in order to create this system, chiefly banking and custody services that have access to the SWIFT payment system. In such a system, if the Platforms and the clearing agency had access to banking services, or even accounts at the same bank, the clearing agency could operate an escrow service to facilitate DVP settlement. The system would work as follows: Retail Investor could place an order through their registered representative, (*i.e.* their broker, who in turn would place an order to purchase bitcoin on a participating platform). Similar to today, during a “net settlement” period, typically between 4:00 PM EST and 6:00 PM EST, automated systems from both the platform and broker would match their trades and agree on an amount of fiat to be sent to the platform from the broker’s custodian and an amount of bitcoin to be sent to the clearing agent from the platforms custodian. Instructions would be sent to the clearinghouse via SWIFT or some other messaging service with the amounts, bank accounts and bitcoin wallet addresses participating in the transaction. The platform’s custodian would then initiate a multi-signature transaction and broadcast that transaction to the bitcoin blockchain. The clearing agent, having already received the instructions from the custodian, is able to “listen” to the Bitcoin blockchain (through their own node) and when the fiat funds arrive in the clearinghouse bank account, the clearing agent signs the bitcoin transaction and broadcasts the signed transaction to the Bitcoin blockchain. Simultaneously, the clearing agent releases the fiat funds to the platform’s custodian, achieving near DVP settlement as both participants receive their funds and digital assets simultaneously. If either party fails to deliver either fiat funds or digital assets the clearing agent cancels the transaction or delivers the missing asset to complete the trade. Regulators should form a working group to further explore such a solution with the aim of defining standards so that dealers, brokers, platforms, custodians and clearing agents could participate in roles similar to how they currently operate.



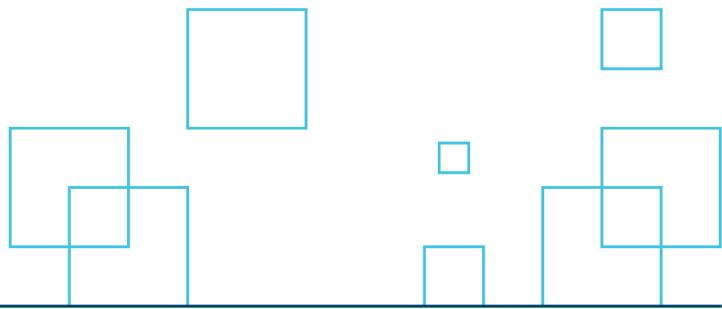
Underpinning many of the issues with clearing and settlement, however, is the inability for platforms to obtain access to banking services. So long as digital assets remain in regulatory limbo, banks will face significant difficulty providing banking services. Regulators should form a working group with both banks and digital asset industry stakeholders to develop operating standards for companies that wish to deal and/or accept payment in digital assets. Without such standards, banks will be unable to judge the risks that both platforms, as well as other digital asset participants, pose to their own operating model. Given the strict regulatory standards that oversee banks, it will continue to be extremely difficult to provide banking services. Banks must have clear regulatory guidance to know when a digital asset platform is operating in a manner that complies with rules and regulations. Banks cannot be making such assessments on their own because each bank will have to determine their own standards, resulting in a different set of rules for each institution. Ultimately, this will create even more challenges for other regulatory bodies, such as OSFI and IIROC, who would have to determine and review if each bank's unique set of guidelines is sufficient. Such a scenario appears contradictory to the public position of the Ontario government and the OSC which has been recently mandated to reduce regulatory burden, and even created the Burden Reduction Task Force.

#### Applicable Regulatory Requirements

#### **22. What regulatory requirements, both at the CSA and IIROC level, should apply to Platforms or should be modified for Platforms? Please provide specific examples and the rationale.**

In all instances, consultation with the industry should occur in order to ensure effective implementation. Particular care should be given to functionality that is enabled by technology, including:

- Users' ability to hold assets without a third-party custodian,
- The ability to automate audit-related functions,
- The ability to conduct testing and verification using publicly available data (in the case of public blockchains),
- Platforms' ability to deliver real-time disclosures and warnings, and
- Different types of digital assets and the suitability of requirements to each type.



Given the depth and breadth of potential digital assets a staged approach, which first provides clarity in relation to the expectations surrounding digitized or tokenized securities, and the platforms on which they are offered, may be the most useful.

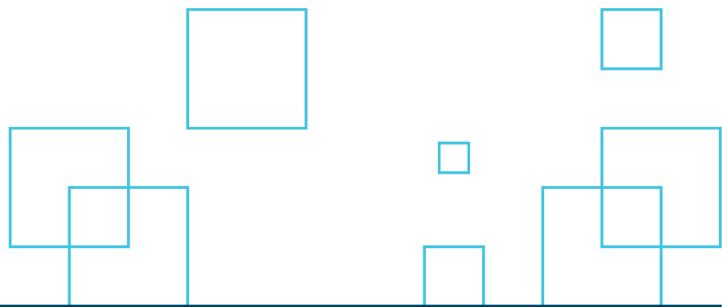
The Chamber recommends that an industry and regulator working group be established to further discuss how to approach related questions regarding regulatory requirements at the CSA and IIROC level.

### **Specific Industry Concerns That Require Attention and Consideration**

#### **Bank Accounts and De-risking**

For many businesses in Canada, the single greatest barrier to entry is not compliance, technology-related, or other deficiency in vital infrastructure, but instead is obtaining and maintaining a stable banking relationship. In one instance, a company obtained a large investment from a consortium which included banks as participant investors. When the investment consortium representative asked the company what they most needed to foster success, the company's CEO confided that they were in need of an operating account in which to deposit the cheque that they had just received. The bank members of the consortium stated that their banks would not open accounts for this type of company as it would contravene the bank's compliance and risk policies. In essence, the company was not so high risk that the bank would not invest, but it was too high risk to be able to offer access to a basic banking product. Months of perseverance were required before the company was able to establish a stable banking relationship.

The issue of access to banking is prevalent at both the federal and provincial levels. In some cases, provincial credit unions are prohibited by their service provider from sending electronic funds transfers or wires on behalf of any company that deals in virtual currency. The act of restricting access to stable banking services to these businesses (also known as derisking) creates significant barriers to functions such as audit, insurance, and price discovery. In addition, it may create additional risks for consumers, including the risk that funds become stuck or lost when a relationship is terminated, and the risk that transactions with suppliers in increasingly risky jurisdictions outside of Canada become the norm. In the recent bankruptcy case involving Quadriga CX, a popular Canadian digital currency exchange, the fact that the exchange was insolvent may have been apparent sooner if the exchange had not conducted its affairs through a complex web of payment processors and service providers that are neither as vigilant nor as well-regulated as the Canadian banking sector.



## Audits

In many ways, audit markets suffer from similar pitfalls to those suffered in insurance markets. There are not enough qualified personnel, and those that are willing to perform the work charge a premium under current market conditions. In addition, accounting professionals have expressed a need for clarity in order to establish appropriate standards related to digital-assets. We recommend that regulators work closely with one another, as well as with accounting and other relevant oversight bodies for professionals, in order to establish appropriate standards.

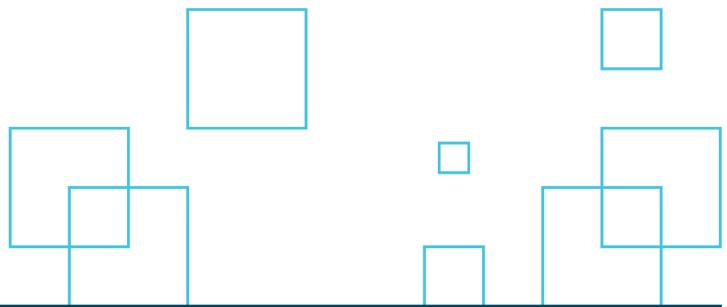
Where non-financial audits are being considered (for example security and compliance audits), we encourage clear guidance for service providers, including any relevant regulator expectations related to the scope, methodology, format and content of audit reports (where applicable). Such guidance is useful in helping professionals to set standards that will be useful to their clients.

## Conclusion

Providing the clarity required in conjunction with the flexibility to support rapidly-evolving technologies in a nascent industry will require a diligent and nuanced approach. Protecting consumers and the Canadian system are important goals. We should move swiftly to establish clarity and a viable regulatory and policy framework for digital assets and their trading platforms doing business in Canada. However, we should not rush to accomplish such goals at the expense of Canadian innovation or in any manner that would hinder Canadian access to the global digital asset market.

In all cases, we urge that policy, regulation and legislation be developed in close consultation with industry. Further, we ask that new policy, regulation and legislation include transparent guidance and policy interpretations that can be used by industry at all stages of business growth to ensure compliance requirements can be met.

The Chamber and its members look forward to working closely with policymakers and regulators across Canada to ensure that Canada's digital asset and blockchain ecosystem is safe, strong and globally competitive. We would be happy to provide additional information or answer any questions that you might have in relation to this submission. It is our sincere



---

hope that this consultation is the first in an ongoing dialogue with the industry and that we may serve as a valuable partner in this process and moving forward.

Sincerely,



Tanya Woods  
Managing Director  
Chamber of Digital Commerce Canada