

WeirFoulds Technology Insights: Canada's Crackdown on Crypto: An Overview of Cryptocurrency Regulation and Enforcement

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By James G. Kosa and Rapti Ratnayake, Student-at-Law

On November 21, 2022, the Canadian Securities Administrators (CSA) issued a [reminder](#), warning that trading in crypto assets “comes with elevated levels of risk”.^[1] The CSA noted that “the value and liquidity of crypto assets are highly volatile”.^[2] The CSA’s communication follows the statement of senior financial regulators on November 16, 2022, relating to entities engaged in crypto-asset activities or crypto-related services. The Office of the Superintendent of Financial Institutions (OSFI), the Financial Consumer Agency of Canada (FCAC) and the Canada Deposit Insurance Corporation (CDIC) issued a [statement](#) to regulated entities reinforcing the regulatory expectation that will take the appropriate measures to understand and properly address the risks of “crypto-asset activities”.^[3] Neither the CSA nor the federal agencies specifically mention the recent steep decline of the prices of crypto assets nor the dramatic bankruptcy of FTX, widely considered to be the world’s second-largest crypto exchange. It’s difficult to imagine that Canadian authorities are not closely following developments in this space, and not without considerable trepidation. The notices present an occasion to review the actions of the CSA and securities regulators with respect to the trading of cryptocurrencies and other crypto assets.

Since 2020, the CSA and the Ontario Securities Commission (OSC) have undertaken measures to protect investors from unregulated cryptocurrency trading platforms (CTPs). Coming on the heels of the CSA and OSC Staff Notices and publications,^[4] recent enforcement actions have signaled that regulatory actions will ensue if CTPs are found flouting Ontario securities laws.

In the last two years alone, the OSC has increased its enforcement efforts. In 2021, the OSC published a statement of allegations against Poloniex for failing to bring their operations into compliance with Ontario securities law.^[5] Similar allegations were raised in June 2021 against another group of CTPs for non-compliance.^[6] More recently, the OSC announced successful enforcement actions against two foreign non-compliant CTPs: one of which resulted in a settlement agreement, and the other in the disgorgement of substantial monetary sanctions and a permanent participation ban.^[7]

Given the significant penalties for non-compliance and the complex, shifting regulatory field, navigating securities laws can be a challenge for CTPs in or entering Canada.

BRIEF EVOLUTION OF DEVELOPMENTS IN CRYPTOCURRENCY REGULATION AND ENFORCEMENT

[1. CSA Staff Notice 21-327\[8\]](#) – *Guidance on the Application of Securities Legislation to Entities Facilitating the Trading of Crypto*

On January 16, 2020, the CSA issued a notice with guidance on whether securities legislation applied to transactions involving crypto assets. The CSA differentiated certain crypto assets as securities and others as derivatives. The CSA also suggested that certain crypto

platforms, being entities that facilitate transactions relating to crypto assets, fall within the ambit of securities legislation. The Staff Notice provides an in-depth breakdown of situations where securities legislation will or will not apply in the context of CTPs.

2. CSA Staff Notice 51-363[9] – Observations on Disclosure of Crypto Assets Reporting Issuers

In March 2021, the CSA released a report outlining several disclosure observations based on the first annual filings by reporting issuers that engage with crypto assets. The publication concluded that reporting issuers in the crypto asset industry are subject to the same disclosure requirements as other reporting issuers. The CSA acknowledged that novel issues may arise in the context of crypto assets, and as such, emphasis was placed on CTP's avoiding inaccurate or misleading disclosure. Further, crypto issuers considering filing a prospectus or contemplating other transactions to enter the Canadian public markets were advised to carefully consider their disclosure obligations concerning their business models to ensure that they are meeting regulatory requirements.

3. Joint Staff Notice 21-329[10] – Guidance for Crypto-Asset Trading Platforms: Compliance and Regulatory Requirements

The most recent publication was released on March 29, 2021. Here, the CSA and Investment Industry Regulatory Organization of Canada (IIROC) published detailed guidance on how securities legislation applies to platforms that facilitate the trading of cryptocurrency assets that are securities ("security tokens") and instruments or contracts involving crypto assets ("crypto contracts") (together "CTPs"). The registration process applicable to the CTP depends on whether the CTP operates as a Dealer Platform or a Marketplace Platform.

The characteristics below suggest that a CTP would be a Dealer Platform if:

- It facilitates the primary distribution of security tokens, and
- It is the counterparty to each trade in security tokens and/or crypto contracts, and client orders do not otherwise interact with one another on the CTP

Dealer Platforms could also be engaged in other activities that Marketplace Platforms do not undertake, including (i) onboarding of retail clients onto a CTP (ii) acting as agents for client for trades in security tokens or crypto contracts (iii) offering custody of assets, either directly or through a third-party provider.

The characteristics below suggest that a CTP would be a Marketplace Platform if it:

- Constitutes, maintains or provides a market or facility to bring together multiple buyers and sellers or parties to trade in security tokens and/or crypto contracts.
- It brings together orders of security tokens or crypto contracts of multiple buyers and sellers or parties to the contracts
- It uses established, non-discretionary methods under which orders for security tokens or crypto contracts interact with each other and the buyers and sellers or parties entering the orders agree to the terms of a trade.

The Notice recognizes that some Marketplace Platforms conduct activities similar to those performed by a Dealer Platform. In those instances, the Marketplace platform would be subject to the appropriate dealer requirements.

The publication provides a detailed breakdown of the application process for CTPs depending on whether they would be deemed a Dealer Platforms or a Marketplace Platform. The publication also acknowledges the need for an interim approach towards requiring CTPs to register as an investment dealer with IIROC.

4. CSA Staff Notice 330[11] – Guidance for Crypto-Trading platforms: Requirements relating to Advertising, Marketing

and Social media use

On September 23, 2021, the CSA and IIROC published a notice discussing advertising activities and marketing strategies by CTPs that have breached securities legislation or investor protection requirements and raised public interest concerns.

The notice provides guidance for CTPs on the prohibition of false and misleading statements in marketing materials, the use of improper “gambling style” promotions, and expectations for firms with respect to the use of social media.

LOOKING AHEAD

To date, the OSC has released periodic warnings and alerts against unregistered and non-compliant CTPs.^[12] This highlights the OSC’s strong stance towards protecting investors by curbing unfair, improper, and fraudulent practices. Moreover, the OSC’s has made efforts to work closely with international securities regulators and has extended its enforcement proceeding to target foreign non-compliant CTPs.

More than 70 CTPs were reported to have initiated compliance discussions with Canadian securities regulators in June 2021 and one crypto asset dealer has successfully been registered with Canadian securities regulators.^[13] It is an unsettled and unsettling time for participants in the crypto sector. The spectacular implosion of FTX and its affiliated hedge fund, Alameda Research, whose aftermath is very much unknown as of this writing, will almost certainly cause policy makers and regulators to pause and re-examine their prior assumptions. Whether the result is increased regulation coupled with more enforcement, or a more general and undifferentiated regulatory skepticism directed at the entire sector remains to be seen.

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The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

^[1] CSA News, “Canadian securities regulators remind investors about risks of trading crypto assets,” November 21, 2022. Online: <https://www.securities-administrators.ca/news/canadian-securities-regulators-remind-investors-about-risks-of-trading-crypto-assets/>

^[2] *Ibid*

^[3] OSFI, “Statement to entities engaging in crypto-asset activities or crypto-related services,” November 16, 2022. Online: https://www.osfi-bsif.gc.ca/eng/osfi-bsif/med/Pages/20221116_let.aspx?utm_source=osfi-bsif&utm_medium=email&utm_campaign=osfi-bsif-email

^[4] Staff Notices: 21-327 (SN 21-327), 21-329 (SN 21-329); 52-363 (SN 52-363); 21-330 (SN 21-330)

^[5] OSC, “OSC takes action against non-complaint international crypto asset trading platforms,” May 25, 2021. Online: <https://www.osc.ca/en/news-events/news/osc-takes-action-against-non-compliant-international-crypto-asset-trading-platform>

[6] OSC, "OSC takes action against second non-compliant international crypto asset trading platform," June 7, 2021. Online: <https://www.osc.ca/en/news-events/news/osc-takes-action-against-second-non-compliant-international-crypto-asset-trading-platform>

[7] OSC, "OSC holds global crypto asset trading platforms accountable," June 22, 2022. Online: <https://www.osc.ca/en/news-events/news/osc-holds-global-crypto-asset-trading-platforms-accountable>

[8] CSA Staff Notice 21-327, "Guidance on the Application of Securities Legislation to Entities Facilitating the Trading of Crypto," January 16, 2020. Online: https://www.osc.ca/sites/default/files/pdfs/irps/csa_20200116_21-327_trading-crypto-assets.pdf

[9] CSA Staff Notice 51-363, "Observations on Disclosure by Crypto Assets Reporting Issuers," March 11, 2021. Online: https://www.osc.ca/sites/default/files/2021-03/csa_20210311_51-363_observations-disclosure-crypto-asset.pdf

[10] CSA Staff notice 21-329, "Guidance for Crypto-Asset Trading Platforms: Compliance with Regulatory Requirements," March 29, 2021. Online: https://www.osc.ca/sites/default/files/2021-03/csa_20210329_21-329_compliance-regulatory-requirements.pdf

[11] CSA Staff Notice 21-330, "Guidance for Crypto-Trading Platforms: Requirements relating to Advertising, Marketing and Social Media use," September 23, 2021. Online: https://www.osc.ca/sites/default/files/2021-09/csa_20210923_21-330_crypto-trading-platforms.pdf

[12] OSC, "OSC investor warnings and alerts for June 21 – July 12, 2022," July 12, 2022. Online: <https://www.osc.ca/en/news-events/news/osc-investor-warnings-and-alerts-june-21-july-12-2022>

[13] OSC, "OSC takes action against non-compliant international crypto asset trading platform," May 25, 2021. Online: <https://www.osc.ca/en/news-events/news/osc-takes-action-against-non-compliant-international-crypto-asset-trading-platform>; Crypto asset trading platforms registered with securities regulators may be found here: <https://www.osc.ca/en/industry/registration-and-compliance/registered-crypto-asset-trading-platforms>

For more information or inquiries:



James G. Kosa

Toronto
416.947.5043

Email:
jkosa@weirfoulds.com

James Kosa is a partner at WeirFoulds with a practice focused on information technology and intellectual property law. He is the Co-Chair of the firm's Technology & Intellectual Property and Privacy & Access to Information Practice Groups, and Co-Chair of the Blockchain and Digital Assets Practice Group.



www.weirfoulds.com

Toronto Office

4100 – 66 Wellington Street West
PO Box 35, TD Bank Tower
Toronto, ON M5K 1B7

Tel: 416.365.1110
Fax: 416.365.1876

Oakville Office

1320 Cornwall Rd., Suite 201
Oakville, ON L6J 7W5

Tel: 416.365.1110
Fax: 905.829.2035