May 15, 2019

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To Whom It May Concern:

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

The following comments are submitted in response to Consultation Paper 21-402 (the "**Consultation Pape**r"), the joint consultation paper and request for comments published by the Canadian Securities Administrators (the "**CSA**") and Investment Industry Regulatory Organization of Canada ("**IIROC**") on March 14, 2019, with respect to the establishment of a regulatory framework for platforms that facilitate the buying and selling or transferring of crypto assets ("**Platforms**").

Thank you for the opportunity to submit the following comments on the Consultation Paper. I am writing this letter in my personal capacity. My perspective is derived from my experience in legal, regulatory and business consulting in the crypto assets industry, as a core focus area,

and my active engagement in the industry, including through roles at a high tech consultancy and as an independent consultant. I also sit on the Advisory Committee for the Blockchain Program at George Brown College. My perspective is further derived from my professional experiences as a General Counsel in financial services in wealth management, including traditional funds as well as crypto asset investment funds. Given my perspective and professional experience in law, securities regulation, financial services and crypto assets, my goal is to offer a neutral perspective based on an appreciation of the issues and the various stakeholder perspectives involved.

OVERVIEW

I commend the CSA and IIROC on their efforts to facilitate innovation that benefits investors and the capital markets, keep pace with evolving markets, provide regulatory clarity to crypto asset businesses, while addressing investor risk and market integrity. I appreciate the consideration given in the Consultation Paper to the existence of novel features in relation to crypto assets, the desirability of industry tailored rules and the acknowledgement of the existence of operators who would like to comply, who have approached the regulators and who welcome some form of regulatory framework to legitimize their businesses and to help their businesses grow.

There is no shortage of opinions on crypto assets. Some see the industry as defined by investment scams. Others see it as revolutionary, efficient, and more technologically advanced, with significant potential across business and human rights. The underlying distributed ledger technology holds promise also, specifically, for regulators, including in enabling transparency with the future potential to avert or mitigate systemic and other risks.

Notwithstanding the above, the promise of innovation should warrant a balanced and thoughtful approach, but not a complete regulatory free pass particularly where retail investors are involved. Policy-maker consensus, for example, according to the Financial Stability Board, is that financial stability is not a current risk in light of industry size, volume and financial system interconnectedness, at least at this time. However, investor protection objectives and concerns are understandably paramount, including in the aftermath of Quadriga CX.

I am of the view that it is in the best interests of the crypto assets industry and investors for industry to collaborate with regulators and to work towards an appropriate regulatory, governance and accountability framework. I agree that it is necessary to consider appropriate governance models for Platforms and to examine ways to address the risks and governance gaps in the current framework. At the same time, I would urge the CSA and IIROC to consider alternative models for a regulatory framework, including of self-regulation combined with industry certifications.

GENERAL RECOMMENDATIONS

The following represent several general recommendations.

- **Learn from the experiences of other jurisdictions** - The fragmentation of regulatory rules in the United States, for example, between states and between regulators has caused so much frustration that the Token Taxonomy Act has been proposed (and reintroduced) as a solution. It is authored and sponsored by members of Congress, and it appears to have some level of support from blockchain technologies, Washington, D.C.-based think tank, Coin Center. The Token Taxonomy Act seeks to roll back and wipe off the books state cryptocurrency laws including a significant amount of work that was already accomplished to create state legislative regimes, such as the New York State BitLicense (which has been referred to as heavy handed) and the five bills passed in the more permissive state of Wyoming. Canada would not necessarily be invulnerable to similar potential problems arising. There is currently some absence of harmonization in traditional Canadian securities regulatory rules, for example, in the exempt market. Also, such regulatory areas as anti-money laundering could result in confusion where we currently see FINTRAC and the securities regulators all simultaneously enacting or proposing new rules, each of which will implicate business classifications and KYC/ AML expectations. Lack of clarity around business classification under securities regulatory rules could, for example, result in confusion around categorization and compliance with FINTRAC expectations. Problems could arise with inconsistent rules across geographic lines, within Canada as well globally given the global nature of this technology and business economy, or between and amongst regulators within the same jurisdiction (such as the CSA, IIROC, FINTRAC and CRA). A multi-constituent, collaborative dialogue and approach, with the objective of advancing harmonized, clear and consistent rules, will help to avoid problems with incompatible or fragmented rule-making.

- **Consider intervention and/or education in the broader business ecosystem** - As a matter of investor protection, and as a matter of enabling compliance with potential new rules, certain products or services normally required by traditional securities regulatory rules may not be attainable, or reasonably and feasibly attainable, by Platforms. For example, if certain insurance coverage isn't available to Platforms, or is only available to a few of the very largest entities, the rendering of this industry non-compliant, or monopolistic, or pushing business underground, all constitute potential consequences which would be unintended and undesirable. France, as one example, decided that it would be good public policy to require that its banks bank blockchain companies, in a fashion that bears similarity to a comply or explain model. Similar tactics could be considered in Canada for certain critical services. Consideration and investigation of the gaps and deficiencies within the broader business infrastructure and ecosystem, combined with thoughtful and balanced rules, can help to achieve regulatory objectives.

- **Consider the potential for creative alternatives in order to fill business and ecosystem gaps -** On May 7, 2019, Binance, a global cryptocurrency exchange and one of the largest exchanges in the world by trading volume, suffered a large scale hack worth around $40 million USD in bitcoin, as a result of what was apparently a well orchestrated attack. Binance has confirmed that it will compensate investors fully for all moneys stolen as a result of the attack using the Binance Secure Asset Fund. In July of 2018, Binance announced the creation of its Secure Asset Fund for Users (SAFU) as insurance to protect users in the event of such potential situations. It explained its intention to self-fund the SAFU using 10% of all trading fees earned by Binance. That plan has presumably been effective as it is enabling the full reparation of investors, as a thoughtful and considered solution selected by Binance, amongst several alternatives that it considered. This case could be used to set an example for others to follow, or for industry to implement in an organized and enforced fashion, such as through a third party agency that could establish a similar emergency investor fund, funded by industry, for use in specified emergency cases and where insurance isn't otherwise available to step in.

- **Consider, as an alternative model, formation of a dedicated third party agency -** Illustrations and variations of this concept include Osgoode's Professor Allan Hutchinson discussion, in his response letter, of what he refers to as a QUANGO. He describes and proposes a quasi-autonomous non-governmental organization to function separate from government but have ties to and representation from government, and to have primary and sole responsibility for regulating cryptocurrency.

  The Japan model is notable in this regard. Japan granted to the cryptocurrency exchange industry self-regulatory status. Japan provided authority to the self-regulatory body, the Japan Virtual Currency Exchange Association, over rule-making, policing and sanctioning of cryptocurrency exchanges.

  There are several reasons why this model - a separate, dedicated agency - would be more beneficial than the traditional regulatory model. A dedicated and specialized entity can stay close and connected to the industry, the technology and the international developments, which is necessary in this evolving, nascent, fast moving and high tech space. If primary authority was instead retained with the CSA and IIROC, will the regulators have adequate resources (including financial and specialized, multi-disciplinary and technical personnel with specific expertise in crypto assets) in order to effectively carry out all initial and ongoing obligations, including monitoring? As noted by Neil Gross in the Comments of the Investor Advisory Panel to the Consultation Paper, regulators will be required to "continually build knowledge and capacity to stay on top of technological innovation and understand its potential impact on investor outcomes and vulnerabilities". The combination of the technical complexity, industry nuances, speed of change and global scale could prove to be very onerous in the context of limited, partial or split resources. And although in terms of size the industry is not systemically

important yet, it is quickly growing. Establishing an appropriate dedicated, self-regulatory body sooner than later would help to stay ahead of market and regulatory needs.

On vision and reasoning, I also agree, in particular, with the comments of James Herhaw on behalf of Crowdmatrix Inc. within their response letter, including but not limited to the following proposal reasoning in advancing the concept of a dedicated federal taskforce and industry specific laws:

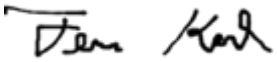
> "A federal taskforce to address all the Digital Assets issues would likely be more focused, better funded and better able to interact with other global leaders than the CSA coalition and the IIROC SRO that is funded by an existing subset of private Canadian registrants in the capital markets ecosystem. Developing new federal legislation can utilize existing principles but also consider new approaches to regulation."

- **Consider including in any new industry regulatory framework relevant reforms that are being implemented or accepted in traditional financial services -** For example, in accordance with the OSC Regulatory Burden Reduction Roundtable, a chief compliance officer ("CCO") should be allowed to work part-time for more than one smaller firm, so that several firms may share a single experienced CCO. I commend the OSC for engaging in this reform. This is beneficial to any industry and particularly to newer industries, such as crypto assets, which could benefit from flexibility in retaining experienced compliance and regulatory personnel. The alternative, i.e. prior model, can often result in an inferior outcome, not specific to the technology sector but also in financial services. It is not infrequently the case that a CEO, who is also the CCO, and who might have significant business experience but negligible compliance experience, wears multiple hats and must balance the internal conflict in being concurrently, effectively, the "Chief Sales Officer" and the "Chief Compliance Officer". The foregoing is not intended as a generalization about all CEOs but rather a commentary on the unintended consequences of the traditional one registrant rule and the rule's not too uncommon impact. Advancing this more innovative and flexible approach can be of great benefit to many industries, including crypto assets.

CONCLUSION

I commend the CSA and IIROC for their community outreach with this Consultation Paper. I support the CSA's objectives in investor protection, market integrity and reducing regulatory uncertainty as articulated in the Consultation Paper. I welcome any opportunities to assist and I am appreciative of being afforded this opportunity to comment. If you require any further information, please do not hesitate to contact me at fern@fernkarsh.com.

Yours truly,



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