

CRYPTOCURRENCIES AND DIGITAL ASSETS: BACK TO SCHOOL UPDATE ON RECENT DEVELOPMENTS IN CANADA

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It may be hard to imagine a world without cryptocurrencies, yet Bitcoin was first launched only a little over a decade ago. Since then, blockchain, digital assets, cryptocurrencies, and related technologies have developed at explosive rates and continue to pervade more and more of our everyday life - from El Salvador becoming the first sovereign nation to adopt Bitcoin as legal tender – to the landmark sale in March, 2021 by Christie's auction house of an entirely digital artwork in a US\$69 million transaction in Ether, a cryptocurrency.

As summer vacation comes to an end, this bulletin provides a “back to school” refresher on recent highlights and developments in Canada in this fast-paced and innovative industry.

Bitcoin ETFs

Canada has continued to keep up with the innovative trends in the cryptocurrency industry. Earlier this year, the world's first Bitcoin exchange-traded fund (ETF) began trading on the Toronto Stock Exchange: the Purpose Bitcoin ETF, soon followed by the Evolve Bitcoin ETF. Although there are retail-level Bitcoin exchange-traded products available in Europe, this was the first vehicle of its kind in North America, and the first globally to be designated as an “ETF”.

Securities Regulatory Developments

Cryptocurrencies and digital assets are a key focus for the Canadian securities regulators, and the Canadian Securities Administrators (CSA) have in place a three year business plan to modernize the regulatory regime for crypto trading and crypto assets in Canada.

On March 11, 2021, the CSA published Staff Notice 51-363 – *Observations on Disclosure by Crypto Assets Reporting Issuers*, summarizing the regulators' observations and recommendations with respect to disclosures by reporting issuers (excluding investment funds) that are materially engaged in the business of holding, trading, or mining cryptocurrencies and other digital assets.

On March 29, 2021, the CSA and the Investment Industry Regulatory Organization of Canada (IIROC) published Staff Notice 21-329 – *Guidance for Crypto-Asset Trading Platforms: Compliance with Regulatory Requirements*,

which sets out how securities legislation applies to crypto asset trading platforms that facilitate the trading of crypto assets that are securities and instruments or contracts involving crypto assets. For more details, please see our separate bulletins [on this Staff Notice](#) and on [previous developments in the Canadian securities regulatory space in respect of crypto asset trading platforms](#).

The Ontario Securities Commission (OSC) concurrently issued a press release notifying all crypto asset trading platforms that they must bring their operations into compliance with Ontario securities laws, with a deadline of April 19, 2021 to contact OSC staff to initiate compliance discussions. The OSC's threat of potential regulatory enforcement was followed with swift action, with statements of allegations published against Polo Digital Assets, Ltd. (Poloniex), Mek Global Limited and PhoenixFin Pte. Ltd. (KuCoin), Bybit Fintech Limited (ByBit), and Aux Cayes Fintech Co. Ltd. (Aux Cayes). As of June, 2021, over 70 platforms had initiated compliance discussions with the Canadian securities regulators, with almost one quarter of them based outside of Canada. McMillan has acted in both publicly disclosed and non-publicly-known settlements with the OSC involving a range of client-focused outcomes. Indeed, McMillan represented clients in the very first public settlement with the OSC regarding such platforms.

On August 10, 2021, the OSC published OSC Staff Notice 33-752 – *Summary Report for Dealers, Advisers and Investment Fund Managers*. This Staff Notice noted that compliance review activity of the OSC will prioritize “Registration as the First Compliance Review” for crypto asset trading platforms.

Consistent with this focus, the OSC released its 2021 – 2022 Statement of Priorities for the fiscal year ending March 31, 2022, which includes strengthening oversight of crypto asset trading platforms and other dealers as a component of its goal to promote confidence in Ontario's capital markets.

Other Regulatory Developments

In addition to securities regulatory developments, other recent regulatory developments in Canada include:

- [Office of the Superintendent of Financial Institutions \(OSFI\)](#): A public consultation paper on the prudential treatment of crypto asset exposures was released by the Basel Committee on Banking Supervision on June 10, 2021. This was followed by a letter published by OSFI on July 5, 2021 requesting feedback from Canadian federally regulated financial institutions on the consultation questions raised in the paper. In addition, earlier this May, the Bank of Canada noted that volatility in cryptocurrency assets is an emerging vulnerability to the country's financial system, noting that although crypto markets are not yet of systemic importance as an asset class or method of payment, this could change if a large technology firm (or “Big Tech”) with a sizeable user base decided to issue a cryptocurrency that became widely accepted as a means of payment.
- [Financial Transactions and Reports Analysis Centre of Canada \(FINTRAC\)](#): Updates to the *Proceeds of*

Crime (Money Laundering) and Terrorist Financing Act and associated regulations took effect June 1, 2021 and extended various compliance obligations with respect to transfers exceeding C\$10,000 and know-your-client recordkeeping to “virtual currencies”.

- Canada Revenue Agency (CRA): In March, 2021, the Federal Court authorized the CRA to issue an “unnamed persons requirement” (UPR) to Coinsquare Ltd. for information and documentation relating to users of Coinsquare, a cryptocurrency exchange operating in Canada. This is part of an ongoing CRA project, led by the CRA’s specialized “Cryptocurrency Section” of the CRA’s Digital Compliance and Audit Support Division, which focuses on taxpayers who have failed to properly report income from cryptocurrency transactions.

Crypto and ESG

A significant issue facing cryptocurrencies with respect to ESG (environmental, social, and governance) is the concern with respect to the energy consumption required to fuel certain cryptocurrency activities, such as mining certain cryptocurrencies. Famously, the annual energy consumption of Bitcoin has been cited as rivaling or exceeding the annual energy consumption of entire countries, such as the Netherlands or Argentina. The price of Bitcoin crashed by more than fifty percent during one week in May, arguably fueled by a tweet from Elon Musk citing concerns around the fossil fuel energy consumption of Bitcoin.

Some claim that the benefits of cryptocurrencies could outweigh this problem, or point to other cryptocurrencies that use different technologies that arguably use less energy. For example, some argue that cryptocurrencies present social advantages (the “S” in ESG) by democratizing financial markets by removing intermediaries or by reducing the cost of remittance corridors between richer and poorer countries through which, for example, migrant workers can send funds home to their families.

The industry continues to grapple with this issue, including the launch of new products that aim to address this concern, such as through the purchase of emission offsets or wrapping cryptocurrencies with carbon credits that trade together as a single asset. Government action may also affect how this area develops. For instance, in March, 2021, the provincial government of Inner Mongolia, where a large amount of cryptocurrency mining was conducted, announced that it would ban all cryptocurrency mining operations in a bid to achieve carbon-reduction targets set by the central government. As both ESG and cryptocurrencies develop, it will be interesting to see how the market responds to these concerns.

The Rest of 2021 and Beyond

As the cryptocurrency and digital assets industry marches forward, it will continue to grapple with existing and new issues, including bridging the gap between crypto securities and crypto commodities, the potential development of central bank digital currencies (CBDCs), and how jurisdictional matters for an intangible

product without borders can or should be addressed. It is clear that this industry is and will continue to be a key priority for the regulators, and that addressing the unique issues raised will continue well beyond 2021.

McMillan has been a market leader in the cryptocurrency and digital asset space and our team has the experience and expertise to explore with technology clients how the Canadian legal landscape may apply to their business.

by [Jennie Baek](#)

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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