Crypto asset trading platforms – Terms and conditions for trading VRCAs (stablecoins)

October 17, 2023

On Oct. 5, 2023, the Canadian Securities Administrators (CSA) published Staff Notice 21-333 *Crypto Asset Trading Platforms: Terms and Conditions for Trading Value-Referenced Crypto Assets with Clients* (the Staff Notice), which expands on the CSA's views in the staff notice from Feb. 23, 2023 (CSA SN 21-332) that "Value-Referenced Crypto Assets" or "VRCAs", crypto assets that are designed to maintain a stable value over time by referencing the value of a fiat currency or any other value or right (or a combination of both), may constitute securities and/or derivatives in several jurisdictions.

In CSA SN 21-332, the CSA acknowledged that, despite the prohibition on the trading of crypto contracts in respect of crypto assets that are securities and/or derivatives, there may be uses for VRCAs by clients of registered crypto asset trading platforms (CTPs), including CTPs that provided a pre-registration undertaking (PRU) to the CSA in accordance with CSA SN 21-332. Additionally, the CSA provided guidance on the CSA's expected interim approach to permit CTPs to continue trading certain VRCAs that seek to replicate the value of a single fiat currency. Under this approach, the CTPs will need to agree to certain terms and conditions before obtaining the CSA's consent, and the issuer of each accepted VRCA will be required to file an undertaking with the CSA.

The Staff Notice expands on the CSA's previously announced interim approach in respect to VRCAs and sets out the form of the CTP's terms and conditions (the Terms and Conditions) and the VRCA issuer's form of undertaking. Note that the CSA also confirms that any new VRCAs that a CTP wishes to offer at a date after the publication of CSA SN 21-332 are not covered by this interim approach and are instead expected to follow alternative regulatory approaches to be developed through discussions with the CSA.

Summary of interim approach

Below is a summary of the interim approach to permitting the trading of VRCAs:

Terms and Conditions – The Terms and Conditions developed by the CSA require, among other things, that:

- the following conditions be met:
    - the VRCA reference, on a one-for-one basis, the value of a single fiat currency (either Canadian dollar or United States dollar only);
    - the VRCA entitles the holder of such asset a right of redemption, subject only to reasonable publicly disclosed conditions, on demand directly against the issuer of the VRCA or against the reserve of assets;
    - the issuer of the VRCA maintain a reserve of assets that is in the reference fiat currency and is comprised of: (i) cash; (ii) investments that are evidence of indebtedness guaranteed by the Canadian or United States governments; (iii) securities issued by money market funds (within the meaning of National Instrument 81-102 or Rule 12d1-1 of the United States *Investment Company Act of 1940*, as applicable); and (iv) such other assets that the principal regulator of a CTP and other members of the CSA have consented to in writing;
    - the assets that comprise the reserve of assets are: (i) measured at fair value; (ii) held with a qualified custodian (as defined in National Instrument 31-103), in an account clearly designated for the benefit of the VRCA holders or in trust for such holders, and held separate and apart from the assets of the issuer of the VRCA and its affiliates and from the reserve of the assets of any other crypto asset; and (iii) not encumbered or pledged as collateral at any time; and
    - the fair value of the reserve of assets is at least equal to the aggregate nominal value of all outstanding units of the VRCA at least once each day;
- the issuer of the VRCA make certain information publicly available, including, among other things, the following: (i) details of each type, class or series of VRCA; (ii) the quantity of all outstanding units of the VRCA and their aggregate nominal value once per business day; (iii) the names and experience of persons or companies involved in the issuance and management of the VRCA; (iv) details on the redemption rights (including restrictions on redemption) and rights against the issuer of the VRCA in the event of insolvency or winding up; (v) the fees charged by the issuer of the VRCA for distributing, trading or redeeming the VRCA; (vi) details on any revenue entitlement; (vii) an assurance report from a public accountant (authorized under the laws of Canada or the United States, as applicable); and (viii) annual financial statements that comply with the terms set out in the Terms and Conditions;
- the CTP prepare a Crypto Asset Statement for the VRCA that includes the specific disclosure described in the Terms and Conditions, which expands on what is typically required of the CTP under the terms of the CTP's exemptive relief decision or the PRU, as applicable;
- as part of the CTP's know-your-product policy, the CTP assess whether the VRCA or the issuer of the VRCA satisfies the specific criteria in the Terms and Conditions applicable to the VRCA and the issuer of the VRCA on an on going basis; and
- the CTP establish and maintain policies and procedures to facilitate halting or suspending deposits or purchases of VRCAs, or crypto contracts in respect of VRCAs, as quickly as is commercially reasonable, if the VRCA no longer satisfies the specific criteria in the Terms and Conditions applicable to the VRCA.

In addition, under the Terms and Conditions the issuer of the VRCA must file an undertaking (the Issuer Undertaking) acceptable to the CSA that is substantially in the form of Appendix B to the Staff Notice (and also file a submission to jurisdiction and appointment of agent for service in the form of Appendix C to the Staff Notice).

Implementation

Unless a registered CTP does not intend to allow clients to continue to buy or deposit VRCAs or enter into crypto contracts to buy or deposit VRCAs, the CSA expects the CTP to take the following steps:

- as soon as possible, contact the principal regulator to discuss the process for implementing the Terms and Conditions;
- **by Dec. 29, 2023**, no longer allow clients to buy or deposit VRCAs, or to enter into crypto contracts to buy or deposit VRCAs, that are not VRCAs that satisfy certain of the conditions in the Terms and Conditions; and
- **by April 30, 2024**, no longer allow clients either to buy or deposit VRCAs, or to enter into crypto contracts to buy or deposit VRCAs, that do not comply with all of the Terms and Conditions.

A CTP that provided a PRU is expected to comply with similar requirements.

The CSA expects issuers of VRCAs to provide the Issuer Undertaking by **Dec. 1, 2023**. The Staff Notice confirms that this deadline does not preclude an issuer of a VRCA from giving an undertaking at a later date; however, if the issuer has not provided the Issuer Undertaking by the deadline, registered CTPs and CTPs that provided a PRU will be required to cease making the VRCA available to clients by Dec. 29, 2023, or April 30, 2024, as described above.

Alternative regulatory approaches

The CSA confirms that they remain open to submissions from market participants regarding the appropriate longer-term regulation of VRCAs that would address the investor protection concerns identified in CSA SN 21-332 or alternative criteria for trading of other VRCAs by CTP. Accordingly, the CSA invites both CTPs and VRCA issuers to contact their principal regulator or other members of the CSA to discuss further.

Our commentary

While the Staff Notice provides a possible path forward for CTPs and VRCA issuers, it is important to the digital asset market in Canada that at least one VRCA be permitted to be traded on CTPs. Unlike other crypto assets, VRCAs play an important operational role on many platforms, notably for those entities that continue to face obstacles in establishing traditional banking relationships, and they are an integral part of the digital asset space as a whole. In addition, the CSA has not yet addressed how VRCAs can be used by platforms that offer only the immediate delivery of crypto assets to their clients and are not, therefore, subject to securities laws.

How BLG Digital Assets can help

BLG's Digital Assets team helps clients to determine their regulatory status and to work closely with the regulators to obtain appropriate registrations or exemptions. We understand the digital asset business and we work with our clients to put into place a plan that balances investor protection concerns with the need for innovation while

securing a feasible business model. We are also aware that domestic and global participants may be faced with different challenges and obstacles and need to plan accordingly.

For more information on the digital assets industry, reach out to any of the key contacts listed below.

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