
B. Ontario Securities Commission

B.1 Notices

B.1.1 CSA Notice and Request for Comment – Proposed Amendments to National Instrument 81-102 Investment Funds Pertaining to Crypto Assets



Canadian Securities
Administrators

Autorités canadiennes
en valeurs mobilières

CSA NOTICE AND REQUEST FOR COMMENT

PROPOSED AMENDMENTS TO NATIONAL INSTRUMENT 81-102 *INVESTMENT FUNDS* PERTAINING TO CRYPTO ASSETS

January 18, 2024

Introduction

The Canadian Securities Administrators (the **CSA** or **we**) are publishing, for a 90-day comment period, proposed amendments (the **Proposed Amendments**) to National Instrument 81-102 *Investment Funds* (**NI 81-102**) and proposed changes (the **CP Changes**) to Companion Policy 81-102CP *Investment Funds* (**81-102CP**) (collectively referred to as the **Proposed Amendments and CP Changes**). The Proposed Amendments and CP Changes pertain to reporting issuer investment funds that seek to invest directly or indirectly in crypto assets (**Public Crypto Asset Funds**).

Substance and Purpose

The Proposed Amendments and CP Changes are intended to provide greater regulatory clarity with respect to certain key operational matters regarding these investments, such as:

- Criteria regarding the types of crypto assets that Public Crypto Asset Funds are permitted to purchase, use or hold;
- Restrictions on investing in crypto assets by Public Crypto Asset Funds or other types of reporting issuer investment funds; and
- Requirements concerning custody of crypto assets held on behalf of a Public Crypto Asset Fund.

The Proposed Amendments and CP Changes will codify practises of existing Public Crypto Asset Funds, developed mainly through the prospectus review process, as well as codifying exemptive relief previously granted to existing Public Crypto Asset Funds. The Proposed Amendments and CP Changes will provide investment fund managers greater regulatory clarity concerning investments in crypto assets. We think this can facilitate new product development in the space while also ensuring that appropriate risk mitigation measures are built directly into the investment fund regulatory framework.

Background

The Proposed Amendments are a key phase of the CSA's implementation of a regulatory framework for Public Crypto Asset Funds (the **Project**). The Project's objective is to review existing requirements, provide guidance, and then implement a regulatory framework relating to Public Crypto Asset Funds that ensures adequate investor protection and mitigates potential risks while providing greater regulatory clarity for product development and management. The Project is a recognition by the CSA that the existing regulatory framework in NI 81-102 needs to be adapted to properly account for the unique aspects of crypto assets as an investment product for publicly distributed investment funds.

The Project is being carried out in three phases.

Phase 1 – CSA Staff Notice

Phase 1 of the Project entailed communicating information to stakeholders on areas we believe required greater guidance regarding CSA staff expectations, and new developments relating to Public Crypto Asset Funds. Phase 1 was completed with the publication of CSA Staff Notice 81-336 *Guidance on Crypto Asset Investment Funds that are Reporting Issuers* (the **Staff Notice**) on July 6, 2023.¹

The Staff Notice provided guidance to stakeholders and outlined CSA staff's views and expectations regarding the operations of Public Crypto Asset Funds within the current framework of NI 81-102, including:

- Providing an overview of the Public Crypto Asset Funds market and clarifying the application of existing securities regulatory requirements to them;
- Discussing key findings from previous reviews conducted by CSA staff, and
- Communicating CSA staff expectations for stakeholders with respect to various matters related to Public Crypto Asset Funds, including key considerations for investing in crypto assets, expectations regarding custody of crypto assets on behalf of Public Crypto Asset Funds, issues concerning staking and other similar yield-generating activities, and reminding registrants of their know-your-product, know-your-client and suitability obligations concerning these types of funds.

Phase 2 – The Proposed Amendments

The Proposed Amendments and CP Changes are part of the second phase of the Project. As discussed in greater detail below, the purpose of this phase of the Project is to build on the guidance in the Staff Notice by focusing on targeted amendments that reflect priority issues regarding investment funds investing in crypto assets. This phase seeks to codify policies and practises of existing Public Crypto Asset Funds, many of which were developed and adopted through the prospectus review process and were also cited in the Staff Notice. Also, where appropriate, the Proposed Amendments seek to codify routinely granted exemptive relief for these products.

Phase 3 – Consultation Paper and Possible Future Amendments

Phase 3 of the Project will involve a public consultation concerning a broader and more comprehensive regulatory framework for funds investing in crypto assets.

Summary of Proposed Amendments

The following is a description of the Proposed Amendments and CP Changes.

Proposed Amendments to NI 81-102

(i) Part 1 – Definitions

“alternative mutual fund”

We are proposing to amend the definition of “alternative mutual fund” to also include a mutual fund that invests in crypto assets. This change is consistent with alternative mutual funds being permitted to have greater exposure to certain alternative asset classes or investment strategies compared to other types of mutual funds. This is also consistent with how Public Crypto Asset Funds currently offered in Canada as mutual funds are currently structured.

(ii) Part 2 – Investments

Section 2.3 – Restrictions Concerning Types of Investments

Restrictions on investing in crypto assets

We are proposing to amend the investment restrictions in section 2.3 to permit only alternative mutual funds and non-redeemable investment funds to buy, sell, hold or use crypto assets directly. This restriction would also apply to investing indirectly in crypto assets through specified derivatives. Mutual funds, other than alternative mutual funds, will only be permitted to invest in crypto

¹ See CSA Staff Notice 81-336 *Guidance on Crypto Asset Investment Funds that are Reporting Issuers*, available at <https://www.osc.ca/en/securities-law/instruments-rules-policies/81-336/csa-staff-notice-81-336-guidance-crypto-asset-investment-funds-are-reporting-issuers>.

assets by investing in underlying alternative mutual funds or non-redeemable funds that invest in crypto assets, subject to the fund of fund restrictions in subsection 2.5(2) of NI 81-102.

Additionally, we are proposing to limit the types of crypto assets that alternative mutual funds and non-redeemable investment funds can invest in. Specifically, we are proposing to restrict investment funds subject to NI 81-102 to investing only in crypto assets that are listed for trading on, or are the underlying interest for a specified derivative where that specified derivative trades on, an exchange that has been recognized by a securities regulatory authority in Canada. This proposed requirement reflects the concerns raised in the Staff Notice about determining the suitability of a crypto asset as a portfolio holding of a Public Crypto Asset Fund, such as market integrity and price discovery.²

As an additional restriction, Public Crypto Asset Funds would be prohibited from buying or holding crypto assets that are not fungible. Non-fungible assets, such as collectibles, may have characteristics that are incompatible with investment fund products offered to retail investors. For example, the non-fungibility of an asset generally creates additional liquidity and valuation risks, and the current regulatory framework may not have the parameters needed to mitigate these risks. Additionally, the markets for non-fungible crypto assets may have heightened risks regarding liquidity and valuation. Nonetheless, we welcome submissions regarding whether there are circumstances where it would be appropriate to allow investment funds to invest in crypto assets that are not fungible and whether there are specific regulatory parameters that should be outlined in the regulatory framework for investment funds to allow for this.

Section 2.12 – Securities Loans, Section 2.13 – Repurchase Transactions, and Section 2.14 – Reverse Repurchase Transactions

We are proposing to prohibit the use of crypto assets in securities lending, repurchase transactions or reverse transactions, as the loaned securities, transferred securities or collateral posted in connection with these transactions, as applicable. While we believe that the market characteristics of most crypto assets make them impractical for these types of transactions in an investment fund, we think it is important to remove any regulatory ambiguity.

Section 2.18 – Money Market Funds

We are proposing to clarify that a “money market fund” as defined in section 2.18 cannot buy or hold crypto assets. This is consistent with restrictions in section 2.18 of NI 81-102 that prohibit money market funds from engaging in activities or holding assets that are associated with alternative mutual funds and is intended to eliminate any regulatory ambiguity.

(iii) Part 6 – Custodianship of Portfolio Assets

We are proposing to include provisions specifically applicable to custodians and sub-custodians that hold crypto assets on behalf of an investment fund (a **Crypto Custodian**). These provisions primarily codify practises and policies in existing Public Crypto Asset Funds concerning custody, which act to mitigate some of the unique risks associated with funds holding these assets in their portfolios and are consistent with, and include:

- (a) a requirement, under section 6.5.1, for a Crypto Custodian to keep crypto assets in offline storage (usually referred to as “cold wallet” storage), except as needed to facilitate purchases and sales or other portfolio transactions in the fund. This is consistent with what is considered best practices of custody of crypto assets when they are not needed to facilitate transactions,
- (b) a requirement, under subsection 6.6(3.1), for a Crypto Custodian to maintain insurance regarding crypto assets it custodies for an investment fund that a reasonably prudent person would maintain. Recognising that commercial practises may vary and that there may be a need for flexibility, we are not proposing to require a specific type of insurance or minimum dollar amount to meet this standard, and
- (c) amendments to section 6.7 that would require a Crypto Custodian to obtain, on an annual basis, a report prepared by a public accountant assessing the Crypto Custodian’s internal management and controls relating to security, availability, processing integrity, confidentiality and privacy controls. An example of this would be a Service Organization Control (**SOC**) report prepared in accordance with the American Institute of Chartered Public Accountants although that will not be prescribed under the Proposed Amendments. The Crypto Custodian would be required to deliver that report to the fund. The annual compliance report to be prepared by a fund’s Crypto Custodian under subsection 6.7(2) would also include a requirement to confirm that it provided the report.

² In the Staff Notice, CSA staff expressed their view that the presence of a regulated futures market for a crypto asset provides support for the proper valuation of a Public Crypto Asset Fund that invests in that crypto asset, along with other operational benefits. CSA staff generally consider that the presence of a regulated futures market for a particular crypto asset offers an additional regulated market facility which provides a liquid market and promotes greater price discovery towards valuing fund assets and for disposing of the crypto asset to satisfy redemption requests. It may also better support the ability of authorized dealers and market makers to properly carry out their market making duties in respect to Public Crypto Asset Funds. CSA staff also noted that the presence of a regulated futures market for a given crypto asset generally correlates with institutional support for that particular crypto asset.

(iv) Part 9 – Sale of Securities of a Mutual Fund

We are proposing to codify exemptive relief that has been granted to existing Public Crypto Asset Funds that permit them to accept crypto assets as subscription proceeds under subsection 9.4(2). The relief was granted primarily to facilitate the functioning of exchange-traded mutual funds (**ETFs**), by allowing their designated brokers and other market makers to exchange crypto assets (specifically bitcoin or ether, in the case of the exemptive relief orders) they hold for “creation units” of the ETFs. Such arrangements are typical for ETFs that hold traditional assets. The exemptive relief addresses a technical issue in the existing provision which only allows a mutual fund to accept securities as subscription proceeds in lieu of cash. Paragraph 9.4(2)(c) would clarify that a mutual fund can accept crypto assets that are not securities as subscription proceeds under similar conditions, namely that:

- The mutual fund is permitted to purchase the applicable crypto asset, the crypto asset is acceptable to the fund’s portfolio advisor and it is consistent with the fund’s investment objectives, and
- The value of the crypto asset accepted as subscription proceeds is at least equal to the issue price of the securities of the mutual fund for which they are payment with the value calculated as if the crypto asset was a portfolio asset of the fund.

This will permit future Public Crypto Asset Funds that are ETFs to facilitate similar market making functions without the need for exemptive relief.

Proposed Changes to 81-102CP***Section 2.01 – Guidance on “Crypto Assets”***

We are proposing to add guidance relating to what we will generally consider to be crypto assets for the purposes of investment funds regulation. We believe the proposed guidance is consistent with terminology used in prior CSA publications and with the general understanding of what constitutes a crypto asset by market participants.

Section 3.3.01 – Investing in crypto assets

We are proposing to add section 3.3.01 which will provide guidance clarifying that the proposed requirement that funds only invest in crypto assets that are either listed for trading, or are the underlying interest in specified derivatives that are listed for trading, on a “recognized exchange” is not intended to restrict funds to only acquire crypto assets through a recognized exchange. In other words, funds can continue to acquire crypto assets from sources such as crypto asset trading platforms so long as the crypto asset the fund invests in meets the necessary criteria set out in subsection 2.3(1.3) of NI 81-102.

Section 8.1 – Custody Standard of Care

We are proposing to add subsection 8.1(2) which will expand on the guidance for meeting the standard of care requirement set out in section 6.6 of NI 81-102 in the context of Crypto Custodians. It includes guidance on what could be considered best practises for Crypto Custodians and primarily reflects current practices of Crypto Custodians of existing Public Crypto Asset Funds, which were also described in the Staff Notice. The guidance provided in this section includes:

- ensuring the Crypto Custodian has the requisite expertise to custody crypto assets;
- the use of segregated wallets or omnibus wallets visible on the blockchain, so long as the books and records of the Crypto Custodian confirm the fund’s ownership of the crypto assets;
- the use of multi-signature technology to limit the risk of a single point failure;
- the use of strong passwords, multi-factor authentication and encryption of client information to limit the risk of hacking, and
- the maintenance of robust cyber and physical security practices to ensure greater security of the crypto assets.

We are also proposing to add subsection 8.1(4) which will clarify the CSA’s expectations regarding the proposed requirement in subsection 6.6(3.1) for Crypto Custodians to obtain insurance with respect to crypto assets in its custody. It clarifies that this requirement is not intended to prescribe a minimum amount of insurance but rather sets out a “reasonably prudent” standard for determining whether the insurance is sufficient, taking into account different factors. It also reminds investment fund managers of their obligations to understand the material terms and conditions of such insurance, consistent with their fiduciary obligations to the investment fund.

Section 8.3

We are proposing to add subsection 8.3(2), which addresses the requirement that a Crypto Custodian obtain an assurance report of its processes relating to security and other measures pertaining to its custody obligations. It clarifies that the CSA will consider a Crypto Custodian obtaining a SOC-2 Type 2 Report, prepared in accordance with the framework developed by the American Institute of Chartered Public Accountants (a **SOC-2 Type 2**), to be the type of report that is contemplated for the purposes of complying with the requirements in section 6.7 of NI 81-102.

(v) Transition/Coming into Force

Subject to the nature of comments we receive on the Proposed Amendments, as well as any applicable regulatory requirements, we are proposing that, if approved, the Proposed Amendments would come into force approximately 90 days after the final publication date.

Local Matters

Annex C is being published in any local jurisdiction that is making related changes to local securities laws, including local notices or other policy instruments in that jurisdiction. It also includes any additional information that is relevant to that jurisdiction only.

Request for Comments

We are soliciting comments on the Proposed Amendments and CP Changes. While we welcome comments on any aspect of the Proposed Amendments and CP Changes, we have also identified specific issues for which we seek comment, which we have listed below:

Guidance on “crypto asset”

1. We are seeking feedback as to whether the guidance in the CP Changes provides sufficient clarity in understanding the type of assets that will be considered crypto assets for the purpose of NI 81-102.

Restrictions on investing in crypto assets

2. The Proposed Amendments contemplate restricting publicly distributed investment funds to only holding fungible crypto assets. We are seeking feedback on whether this is a reasonable restriction in light of the risks that are generally associated with holding non-fungible crypto assets in an investment context. If not, please be specific as to why you think the scope of permitted crypto assets should be expanded to include non-fungible crypto assets and what investor protection measures are appropriate for Public Crypto Asset Funds to hold these types of assets.
3. The Proposed Amendments also contemplate restricting publicly distributed investment funds to holding crypto assets that trade on, or are reference assets for specified derivatives that trade on, a “recognized exchange”. This reflects market integrity concerns with certain crypto asset markets and is intended to limit funds to holding those crypto assets for which spot prices can be derived through regulated sources that reflect institutional support and promote price discovery, which is not dissimilar to how more traditional fund portfolio assets trade. We are seeking feedback as to whether this is a reasonable qualifying criterion. If not, please provide feedback on what criteria may be more appropriate for determining when a crypto asset should be deemed an appropriate investment for an investment fund directed at retail investors.

Custody

4. The Proposed Amendments include a requirement that custodians or sub-custodians that hold crypto assets on behalf of an investment fund obtain an annual assurance report prepared by a public accountant that assesses the design and effectiveness of various internal controls and policies concerning their obligations to custody crypto assets. The CP Changes clarify that obtaining a SOC-2 Type 2 will be considered to comply with the requirement, without prescribing that specific report. We are seeking feedback regarding other assurance reports that may be comparable to a SOC-2 Type 2 that we should also consider sufficient for complying with this requirement. We are also seeking feedback regarding the appropriate scope of any reporting to be provided under this requirement.

Broader Consultation

5. We are seeking comments on other issues or considerations relating to investment funds that invest in crypto assets that the CSA should also be considering. This feedback will help inform the broader consultations for the third phase of the Project.

B.1: Notices

Please submit your comments in writing, by email, on or before **April 17, 2024**.

Please address your submission to the CSA as follows:

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumers Services Commission, New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Office of the Superintendent of Securities Service Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Superintendent of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Please send your comments only to the addresses below. Your comments will be forwarded to the other CSA members.

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor, Box 55
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
Email: comments@osc.gov.on.ca

Me Philippe Lebel

Secrétaire et directeur général des affaires juridiques,
Autorité des marchés financiers
Place de la Cité, tour Cominar
2640, boulevard Laurier, bureau 400
Québec (Québec) G1V 5C1
Fax: 514-864-6381
E-mail: consultation-en-cours@lautorite.qc.ca

We cannot keep submissions confidential because securities legislation in certain provinces requires publication of a summary of the written comments received during the comment period. All comments will be posted on the websites of the Ontario Securities Commission, the Autorité des marchés financiers, the Alberta Securities Commission and the British Columbia Securities Commission. Therefore, submissions should not include personal information directly in comments to be published. It is important you state on whose behalf you are making the submissions.

Questions

Please refer your questions to any of the following CSA staff:

James Leong
Senior Legal Counsel, Corporate Finance
British Columbia Securities Commission
jleong@bcsc.bc.ca

Chad Conrad
Senior Legal Counsel, Investment Funds
Alberta Securities Commission
chad.conrad@asc.ca

Cathy Tearoe
Senior Legal Counsel, Market Regulation
Alberta Securities Commission
cathy.tearoe@asc.ca

Michael P. Wong
Senior Securities Analyst, Corporate Finance
British Columbia Securities Commission
mpwong@bcsc.bc.ca

Ashlyn D'Aoust
Senior Legal Counsel, Market Regulation
Alberta Securities Commission
ashlyn.daoust@asc.ca

Heather Kuchuran
Director, Corporate Finance
Financial and Consumer Affairs Authority of Saskatchewan
heather.kuchuran@gov.sk.ca

Patrick Weeks

Deputy Director, Corporate Finance
Manitoba Securities Commission
Patrick.weeks@gov.mb.ca

Frederick Gerra

Senior Legal Counsel, Investment Funds and Structured
Products
Ontario Securities Commission
fgerra@osc.gov.on.ca

Bruno Vilone

Acting Manager, Investment Products Oversight
Autorité des marchés financiers
bruno.vilone@lautorite.qc.ca

Gabriel Vachon

Securities Analyst, Investment Products Oversight
Autorité des marchés financiers
gabriel.vachon@lautorite.qc.ca

Peter Lamey

Legal Analyst
Nova Scotia Securities Commission
Peter.lamey@novascotia.ca

Christopher Bent

Senior Legal Counsel, Investment Funds and Structured
Products
Ontario Securities Commission
cbent@osc.gov.on.ca

Michael Tang

Senior Legal Counsel, Investment Funds and Structured
Products
Ontario Securities Commission
mtang@osc.gov.on.ca

Philippe Lessard

Securities Analyst, Investment Products Oversight
Autorité des marchés financiers
philippe.lessard@lautorite.qc.ca

Moira Goodfellow

Senior Legal Counsel
New Brunswick Financial and Consumer Services
Commission
moira.goodfellow@fcnb.ca

Contents of Annexes

The text of the Proposed Amendments is contained in the following annexes to this Notice and is available on the websites of members of the CSA:

Annex A – Proposed Amendments to National Instrument 81-102 *Investment Funds*

Annex B – Proposed Changes to Companion Policy 81-102CP *Investment Funds*

Annex C – Ontario Rule-Making Authority

Annex D – Cost-Benefit Analysis

ANNEX A

PROPOSED AMENDMENTS TO
NATIONAL INSTRUMENT 81-102 *INVESTMENT FUNDS*

1. ***National Instrument 81-102 Investment Funds is amended by this instrument.***
2. ***Section 1.1 is amended in the definition of “alternative mutual fund” by adding “, crypto assets” before “or specified derivatives”.***
3. ***Section 2.3 is amended***
 - (a) ***in subsection (1) by adding the following paragraph:***
 - (j) purchase, sell, use or hold a crypto asset or a specified derivative of which the underlying interest is a crypto asset.,
 - (b) ***by adding the following subsections:***
 - (1.3) Paragraph (1)(j) does not apply to an alternative mutual fund with respect to the purchase, sale, use or holding of a crypto asset if
 - (a) the crypto asset is fungible, and
 - (b) either of the following apply:
 - (i) the crypto asset trades on an exchange recognized by a securities regulatory authority in a jurisdiction of Canada;
 - (ii) the crypto asset is the underlying interest of a specified derivative that trades on an exchange recognized by a securities regulatory authority in a jurisdiction of Canada.
 - (1.4) Paragraph (1)(j) does not apply to an alternative mutual fund with respect to the fund entering into a specified derivative transaction that trades on an exchange that is recognized by a securities regulatory authority in a jurisdiction of Canada., ***and***
 - (c) ***in subsection (2) by adding the following paragraphs:***
 - (d) purchase, sell, use or hold a crypto asset unless it is a crypto asset referred to in subsection (1.3);
 - (e) enter into a specified derivative transaction the underlying interest of which is a crypto asset, unless it is a specified derivative referred to in subsection (1.4)..
4. ***Subsection 2.12(1) is amended by adding the following item:***
 13. Neither the loaned securities nor the collateral delivered to the investment fund includes a crypto asset..
5. ***Subsection 2.13(1) is amended by adding the following item:***
 12. No securities transferred by the investment fund as part of the transaction are crypto assets..
6. ***Subsection 2.14(1) is amended by adding the following item:***
 10. No securities transferred as part of the transaction are crypto assets..
7. ***Subsection 2.18(2) is replaced with the following:***
 - (2) Despite any other provision of this Instrument, a mutual fund that describes itself as a “money market fund” must not use a specified derivative, sell securities short or purchase, sell, use or hold a crypto asset..
8. ***Part 6 is amended by adding the following section:***
 - 6.5.1 Holding of Portfolio Assets that are Crypto Assets**

Despite subsections (3) and (4) of section 6.5, a custodian or a sub-custodian that holds portfolio assets that are crypto assets must hold the private cryptographic keys to those assets in offline storage unless required to facilitate a portfolio transaction of the investment fund..

9. **Section 6.6 is amended by adding the following subsection:**

- (3.1) The custodian or sub-custodian of an investment fund that holds portfolio assets that are crypto assets must maintain insurance with respect to those crypto assets, of a type and amount that a reasonably prudent person would maintain..

10. **Section 6.7 is amended**

(a) **by adding the following subsections:**

(1.1) The custodian or sub-custodian of an investment fund that holds portfolio assets that are crypto assets must, on a periodic basis not less frequently than annually and within 60 days after the end of its most recently completed financial year, obtain a report prepared by a public accountant that expresses a reasonable assurance opinion concerning the design and operational effectiveness of the service commitments and system requirements set for the custodian or sub-custodian relating to security, availability, confidentiality, processing integrity and privacy controls with respect to its custodial or sub-custodial obligations during its most recently completed financial year.

(1.2) A custodian or sub-custodian referred to in subsection (1.1) must deliver a copy of the report referred to in subsection (1.1) to the investment fund, promptly after receipt., **and**

(b) **in subsection (2) by deleting “and” at the end of paragraph (b), replacing “.” with “; and” at the end of paragraph (c) and adding the following paragraph:**

(d) whether the custodian or each sub-custodian, as applicable, of an investment fund that holds portfolio assets that are crypto assets has delivered a copy of the report referred to in subsection (1.2)..

11. **Subsection 9.4(2) is amended by replacing “.” at the end of subparagraph (b)(iii) with “;” and adding the following paragraph:**

- (c) by making good delivery of crypto assets if
- (i) the mutual fund is an alternative fund,
 - (ii) the crypto assets are not securities,
 - (iii) the mutual fund would at the time of payment be permitted to purchase those crypto assets,
 - (iv) the crypto assets are acceptable to the portfolio adviser of the mutual fund and consistent with the mutual fund's investment objectives, and
 - (v) the value of the crypto assets is at least equal to the issue price of the securities of the mutual fund for which they are payment, valued as if those crypto assets were portfolio assets of the mutual fund..

Effective date

12. (1) This Instrument comes into force on [●].
- (2) In Saskatchewan, despite subsection (1), if this Instrument is filed with the Registrar of Regulations after [●], this Instrument comes into force on the day on which it is filed with the Registrar of Regulations.

ANNEX B

PROPOSED CHANGES TO
COMPANION POLICY 81-102 INVESTMENT FUNDS

1. **Companion Policy 81-102 Investment Funds is changed by this Document.**
2. **Section 2.01 is changed by adding the following subsection:**
 - (4) The term “crypto asset” is not defined in the Instrument, but for the purposes of the Instrument, the Canadian securities regulatory authorities will generally consider a crypto asset to include any digital representation of value that uses cryptography and distributed ledger technology, or a combination of similar technology, to create, verify and secure transactions..
3. **Part 3 is changed by adding the following section:**
 - 3.3.01 Investing in Crypto Assets**

Subsection 2.3(1.3) of the Instrument provides an exception to the general prohibition on mutual funds investing in crypto assets in paragraph 2.3(1.2)(j) to permit alternative mutual funds to invest in crypto assets provided the crypto asset is either (a) listed for trading or (b) is the underlying interest in a specified derivative that is listed for trading, on an exchange that has been recognized by a securities regulatory authority in Canada. Subsection 2.3(2) provides a similar exception for non-redeemable investment funds. For greater clarity, this is not intended to restrict investment funds to only purchasing crypto assets through a recognized exchange. It is meant to be the criteria to determine whether a fund can invest in a particular type of crypto asset. Funds will continue to be permitted to acquire crypto assets from other sources, such as crypto asset trading platforms, provided the crypto asset qualifies under the criteria set out in subsection 2.3(1.3) and subject to any other existing requirements that may impact how an investment fund acquires its portfolio assets..
4. **Section 8.1 is changed:**
 - (a) **by renumbering it as subsection “8.1(1)”, and**
 - (b) **by adding the following subsections:**
 - (2) The Canadian securities regulatory authorities expect that custodians and sub-custodians responsible for the custody of portfolio assets that are crypto assets implement policies and procedures that address the unique risks concerning safeguarding of crypto assets compared to other asset types. We would expect these policies and procedures to include:
 - (a) having specialist expertise and infrastructure relating to the custody of crypto assets;
 - (b) storing private cryptographic keys in segregated wallets or in an omnibus wallet visible on the blockchain so that unique public and private keys are maintained on behalf of an investment fund, so long as in each case the custodian or sub-custodian’s books and records clearly reflect the investment fund’s ownership of the crypto assets held by it;
 - (c) using hardware devices to hold private cryptographic keys that are subject to robust physical security practices, with effective systems and processes for private key backup and recovery;
 - (d) using signing approaches, such as the use of multi-signature technology, that minimise single point of failure risk;
 - (e) maintaining robust systems and practices for the receipt, validation, review, reporting and execution of instructions from the investment fund;
 - (f) maintaining website security measures that include two-factor authentication, strong password requirements that are cryptographically hashed, encryption of user information and other state-of-the-art measures to secure client information and protect the custodian and sub-custodian’s website from hacking attempts;
 - (g) maintaining robust cyber and physical security practices for their operations, including appropriate internal governance and controls, risk management and business continuity practices.

- (3) For the purposes of section 6.5.1 of the Instrument the Canadian securities regulatory authorities generally consider offline storage to mean the storage of private cryptographic keys in a manner that prevents any connection to the internet.
- (4) Subsection 6.6(3.1) of the Instrument requires the custodian or sub-custodian of an investment fund that holds crypto assets on behalf of the investment fund to maintain insurance with respect to its custody of crypto assets of a type and in an amount that a reasonably prudent person would maintain. The Canadian securities regulatory authorities expect this to include using their best judgement, consistent with their custodial or sub-custodial obligations and standard of care to the fund to determine whether the insurance maintained by the custodian or sub-custodian is sufficient or appropriate in the circumstances, including taking into account how the insurance compares to industry standards. The Canadian securities regulatory authorities also remind investment fund managers of the need to understand the material terms and amounts of such insurance coverage and make their own determination of whether they consider the insurance sufficient considering the relevant circumstances, consistent with their fiduciary obligation to the investment fund..

5. Section 8.3 is changed by renumbering it as subsection 8.3(1) and by adding the following subsection:

- (2) Subsection 6.7(1.1) of the Instrument requires a custodian or sub-custodian of an investment fund that holds portfolio assets of that investment fund that are crypto assets to obtain a report prepared by an external auditor to assess its internal management and controls. The provision does not specify the exact report that must be obtained. However, it is the view of the Canadian securities regulatory authorities that a Service Organization Control 2 Type II report, generally referred to as a “SOC-2 Type II” report, prepared in accordance with the framework developed by the American Institute of Chartered Public Accountants, will satisfy this requirement, though other comparable reports may also be considered from time to time..

6. These changes become effective on [●].

ANNEX C

ONTARIO RULE-MAKING AUTHORITY FOR THE PROPOSED AMENDMENTS

The following provisions of the *Securities Act* (Ontario) (the Act) provide the Commission with authority to adopt the Proposed Amendments:

Paragraph 143(1)31 of the Act authorizes the Commission to make rules regulating investment funds and the distribution and trading of the securities of investment funds, including

- making rules prescribing permitted investment policy and investment practices for investment funds and prohibiting or restricting certain investments or investment practices for investment funds (subparagraph (ii));
- making rules prescribing requirements for investment funds in respect of derivatives (subparagraph (ii.1));
- making rules prescribing requirements governing the custodianship of assets of investment funds (subparagraph (iii));

Paragraph 143(1)34 of the Act authorizes the Commission to make rules regulating commodity pools.

Paragraph 143(1)49 of the Act authorizes the Commission to make rules permitting or requiring, or varying the Act to permit or require, methods of filing or delivery, to or by the Commission, issuers, registrants, security holders or others, of documents, information, notices, books, records, things, reports, orders, authorizations or other communications required under or governed by Ontario securities law.

ANNEX D
COST BENEFIT ANALYSIS

Background

- The current regulatory regime for publicly distributed investment funds does not fully account for the unique nature of crypto assets as an investment holding for investment funds.
- Much of the framework that has developed around investment funds holding these assets has been through the prospectus review process. Codifying this framework through rule amendments would provide greater clarity and consistency for market participants and investors.
- The proposed action is to introduce targeted amendments to National Instrument 81-102 *Investment Funds (NI 81-102)* that would specifically account for investment funds investing in crypto assets.

Stakeholders affected by the proposed Instrument/Rule

- Investment Fund Managers (IFMs) – any IFM of an investment fund that seeks to invest in crypto assets (**Impacted IFM**) would be affected by this proposal as it sets out the regulatory framework under which their investment funds could invest in this asset class. See the Appendix for a breakdown of the Canadian crypto asset investment fund market, as of June 30, 2023.
- Dealers – rules governing funds investing in crypto assets could impact the scope of products available for dealers to distribute. There are approximately 168 investment dealers that are able to distribute crypto asset investment funds.¹
- Investors – any current or potential investors who may seek to hold investment funds will be impacted as the rules will have an impact on product selection.
- Service Providers – service providers to funds such as custodians and sub-custodians will be impacted by having a clear framework for how crypto assets are to be handled on behalf of an investment fund. There are currently 5 custodians and 3 sub-custodians who provide custodial services on behalf of crypto asset investment funds.

Anticipated costs and benefits

- (a) Benefits to stakeholders
- IFMs – Impacted IFMs benefit from having clear and consistent rules around when an investment fund can invest in crypto assets. This allows for better planning and can encourage new product development and foster greater competition in this space. In addition, Impacted IFMs will benefit from cost and time savings as a result of not having to navigate an uncodified regulatory regime when seeking to launch a crypto asset investment fund. Furthermore, Impacted IFMs will also realize added benefits as previously granted exemptive relief in connection with crypto asset investment funds will be codified resulting in cost savings to the industry.²

Table 1 – Estimated cost savings per Impacted IFM that decides to issue an investment fund with crypto assets

Activity	Staff category	Hourly rate	Total hours per activity	Total cost per activity
Labour costs associated with applying for exemptive relief under current framework per Impacted IFM	External Lawyer	\$243 ³	25	\$6,075
Filing fee per Impacted IFM				\$4,800
Total potential savings per Impacted IFM				\$10,875

¹ CIRO FY24 Q1 Quarterly Report Summary For the period April 1, 2023, to June 30, 2023.

² There are approximately 8 IFMs who have received exemptive relief from subsection 9.4(2) of NI 81-102 that permits a crypto asset investment fund to accept crypto assets as subscription proceeds. The relief was granted primarily to facilitate the functioning of ETFs by allowing their designated brokers and other market makers to exchange crypto assets they hold for "creation units" of ETFs, similar to the functioning of ETFs that hold traditional assets. There were approximately 126 IFMs registered in Ontario that offered prospectus-qualified funds as of December 31, 2022 (2023 OSC Investment Fund Survey). Although there are approximately 118 IFMs that currently do not offer crypto asset investment funds, we do not have a reasonable estimate of how many will choose to do so in the future. Likewise, it is not possible to estimate how many IFMs might seek exemptive relief in the future. Table 1 sets out the potential estimated cost savings on a per firm basis for illustrative purposes.

³ Estimate based on the national average hourly rate of \$243.12 for a lawyer with approximately 2 to 5 years' experience. See Bruineman, Marg. ["The right price: Canadian Lawyer's 2018 Legal Fees Survey shows some bright spots for law firms despite a highly competitive market" Canadian Lawyer, April 2018](#)

B.1: Notices

- Dealers – potential wider scope of products in which to offer to clients for their investing needs.
 - Investors – potentially greater product selection for their investing needs as evidence suggests crypto assets may offer potential diversification benefits to more traditional asset classes.⁴ Also provides a means of investing in the crypto asset space through a regulated investment vehicle with the applicable regulatory safeguards.
 - Service providers – a potential market for offering services relating to investment funds investing in crypto assets, such as custodians and sub-custodians.
- (b) Costs to stakeholders
- IFMs – costs are expected to be nominal since the basic investment fund framework is substantially unchanged. Existing investment funds holding crypto assets will not be materially impacted since proposals are consistent with what they already do. Furthermore, any costs incurred would **only** be limited and applicable to Impacted IFMs that would seek to launch a crypto asset investment fund.⁵
 - We estimate that each Impacted IFM will incur approximately \$1,080⁶ in initial costs associated with reviewing and learning about the proposed amendments to NI 81-102 and updating existing policies and procedures. The estimated costs are based on the following assumptions:
 - All Impacted IFMs will undertake the same activities and incur the same initial compliance costs. We do not anticipate any significant costs associated with IT/systems modification as a result of the proposed amendments.
 - We do not anticipate there will be any significant ongoing costs associated with the proposed amendments as the crypto asset investment fund industry is already operating with the proposed amendments.

Table 2 – Estimated initial compliance costs per IFM

Activity	Staff category	Hourly rate ⁷	Total hours per activity	Total cost per activity
1. Learning about the regulation	Compliance Analyst	\$60	2	\$120
	Senior Compliance Analyst	\$77	2	\$150
	Chief Compliance Officer	\$133	1	\$130
2. Updating policies and procedures	Compliance Analyst	\$60	3	\$180
	Senior Compliance Analyst	\$77	3	\$230
	Chief Compliance Officer	\$133	2	\$270
			Total cost per firm	\$1,080

- Dealers – no additional costs. Dealers are already obligated to engaged in “know your product” analysis with respect to any new investment fund offerings. Proposal does not change that.
- Investors – no direct cost impact. Investment funds will be offered and sold in the same distribution channels. However, investors may incur non-monetary opportunity costs associated with learning about crypto asset funds, but these costs would not be directly attributable to the proposed amendments.
- Service providers – proposed requirement to obtain an assurance opinion report, such as a SOC-2 Type 2 report, could impose costs on “new” potential custodians/sub-custodians holding crypto. However, this would be comparable to what is happening with existing investment funds, as all custodians/sub-custodians that service existing investment funds have a SOC-2 Type 2 report.

⁴ <https://blogs.cfainstitute.org/investor/2022/11/16/how-do-cryptocurrencies-correlate-with-traditional-asset-classes/>.

⁵ See footnote 2.

⁶ There were 126 IFMs registered in Ontario that offered prospectus-qualified funds as of December 31, 2022 (2023 OSC Investment Fund Survey) of which 8 IFMs have issued prospectus-qualified funds with crypto asset holdings.

⁷ All hourly rates are obtained from the Robert Half 2023 Salary Guide.

Summary comparison of costs and benefits

Benefits:

- Greater clarity for investment funds investing in crypto assets including a clearer path for launching product. Clearer rules can result in a more level playing field and encourage new entrants due to more regulatory certainty.
- Greater regulatory consistency and certainty – less reliance on prospectus review process to develop appropriate policies. Proposals largely codify existing practices.
- Stronger investor protection – rules have stronger force of law than staff comments on a prospectus review. Proposals are focused primarily on investor protection concerns such as custody and nature of assets that can be held.

Costs

- Costs are limited and applicable only to Impacted IFMs.
- Costs are minimal since the substantive regulatory framework is unchanged. Existing investment funds holding crypto assets will be unaffected since no new requirements are being introduced beyond what they already do.
- We estimate that each Impacted IFM will incur approximately \$1,080 (Table 2) in initial costs associated with reviewing and learning about the proposed amendments to NI 81-102 and updating existing policies and procedures.
- Based on the estimated potential savings and initial compliance costs per IFM, the net benefit to each new IFM that decides to issue prospectus-qualified investment funds with crypto asset holdings is approximately \$9,795⁸ under the proposed amendments.

Impact of the proposed amendments on the OSC's mandate

- Given that the purpose of the proposed amendments is to codify existing practices that have developed through staff reviews of crypto asset funds, the amendments would further foster fair, efficient and competitive capital markets, and confidence in capital markets by ensuring there is clarity and consistency amongst IFMs who currently manage crypto asset investment funds and those who intend to in the future.
- The proposed amendments would also help foster capital formation as crypto asset IFMs would be provided with a regulatory framework that would reduce regulatory burden given that the staff prospectus review process would be more efficient and timelier.
- Lastly, the proposed amendments would contribute to the stability of the financial system and the reduction of systemic risk as they would establish a regulatory framework for the fund industry for a novel and evolving asset class such as crypto assets.

Description of alternatives considered

- The only alternative considered was status quo (i.e. no proposed amendments). We determined that the benefits of rules that also codify current practices and offer greater clarity, relative to the minimal costs were superior to status quo.

Appendices and references

Appendix – Canadian Crypto Asset Investment Fund Market Data as of June 30, 2023.

⁸ This estimate nets the potential savings of approximately \$10, 875 per IFM and potential initial compliance costs of \$1,080 per firm.

Appendix**Canadian Crypto Asset Investment Fund Market Data – as of June 30, 2023****By Fund Structure**

Fund Structure	No. of Funds	Net Assets (Millions)
Non-redeemable investment fund	2	\$455
ETFs	11	\$2,578
Open-ended mutual fund ¹	8	
Total	21	\$3,033

By Crypto Asset Type

Crypto Asset	No. of Funds	Net Assets (Millions)
Bitcoin	10	\$2,090
Ether	9	\$943
Bitcoin and Ether	2	n/a
Total	21	\$3,033

By Fund Strategy

Strategy	No. of Funds	Net Assets (Millions)
Direct Investment	12	\$3,010
Fund of Fund	8 ²	
Investments in listed futures	1	\$23
Total	21	\$3,033

¹ The open-ended mutual funds invest their securities of one or more of crypto asset investment funds that are ETFs. As such, their net assets are part of the total assets under management for the ETFs listed above.

² The crypto asset investment funds that employ a fund of fund strategy invest their assets in one or more of the "direct investment" crypto asset investment funds structured as ETFs or Directly holding bitcoin or ether in a "buy and hold" strategy. The net assets of the "fund of fund" strategies are therefore included as part of the net asset of the "direct investment" funds.