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Outlook 2020: Artificial Intelligence Activity on the Enforcement Front

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Artificial Intelligence ("AI") is clearly on the horizon of the regulatory landscape. Alongside the use of technology to assist with navigating the regulatory process, regulators are now digitizing their enforcement efforts. The Canadian Securities Administrators ("CSA")[1] have approached this challenge head-on.

Market Analysis Platform

In 2018, the CSA put the capital markets on notice that they were strengthening their technological capabilities to assist in fighting securities misconduct.[2] The CSA confirmed they would rely on AI technology to analyze large data sets, allowing them to detect misconduct faster and earlier, through the Market Analysis Platform ("MAP"), an automated centralized solution that the CSA believed could handle the size of the current market practices.

The CSA's 2019 Enforcement Report, released in June 2020, confirmed that it was preparing to launch the MAP in the near future.[3] It has been two years since the CSA selected Kx, a division of First Derivatives plc, to build and manage the MAP platform. The Kx platform provides some insight into the CSA's potential uses for the MAP. Kx allows for custom real-time and historical data analysis that features redundancy, alerting, and reporting for stock market analysis and algorithmic trading.[4]

Expertise and Working Groups

The role of big data and the ability to process massive datasets will allow CSA Members to focus limited staff resources on reviewing possible violative conduct in the market. The CSA have confirmed that alongside emerging technology, CSA Members will deploy dedicated teams with established new roles, including data scientists, analysts, and blockchain specialists.[5]

The allocation of these dedicated teams indicate that CSA Members are planning on relying more heavily on AI in enforcing regulatory compliance. Although the power of AI is obvious, its effective use requires experienced staff to examine and evaluate the output of the advanced analytics.

Cassels

Good Data = Intelligence

In November 2018, the Ontario Securities Commission ("OSC"), a CSA Member, formed the Burden Reduction Task Force ("Task Force"). The Task Force focused on implementing initiatives to keep Ontario's capital markets competitive, but also took note of the importance of collecting good data over more data. In November 2019, the OSC released the Task Force's report.[6]

Among other things, the Task Force's report considered the potential use of Regulatory Technology ("RegTech") in the OSC's regulation of Ontario's capital markets. RegTech is the use of machine-learning software or other technology in the management of regulatory processes. It has been seen as a disruptor to the current regulatory landscape and an influencer in the modernization of securities regulation. Ultimately, the Task Force's report did not recommend incorporating RegTech based solutions into the OSC's regulatory enforcement processes.

Where regulatory processes were considered burdensome, the OSC opted to consider technology-based solutions to simplify the regulatory requirements. For example, the OSC was willing to consider technological alternatives to the delivery of notices under sections 11.9 and 11.10 of NI 31-103[7] where it could reduce the burden without compromising the underlying objective of that national instrument.[8]

Into the Sandbox

The Task Force also discussed the expansion of FinTech firms and the concerns raised with their novel business models. The Task Force reinforced the use of initiatives such as the OSC Launchpad (discussed below) to assist in navigating compliance with terms and conditions imposed with registration.

In Canada, regulators have created a number of initiatives including the OSC Launchpad and the CSA Regulatory Sandbox, allowing registrants to operate innovative business models that don't fit the traditional mould.

The two initiatives are distinct. The OSC Launchpad is an arm of the OSC; the CSA Regulatory Sandbox is a pilot environment where firms can operate in a limited commercial setting – often on a time-limited basis. Some recent firms to use the OSC Launchpad and the CSA Regulatory Sandbox are TokenGX Inc. ("TokenGX") and Wealthsimple Digital Assets Inc. ("Wealthsimple").

In late 2019, TokenGX was granted time-limited exemptive relief from the OSC to pilot test a secondary trading marketplace for crypto-assets (tokens). The trading marketplace is powered by blockchain technology and allows investors to buy and sell private market securities between themselves.[9] The OSC restricted the annual investment limit ($10,000 to $30,000) and has significant oversight of the firm while the

Cassels

pilot test is ongoing.

Wealthsimple obtained OSC registration in August 2020 (subject to numerous conditions) to operate a platform where clients could buy, hold, and sell crypto-assets. Wealthsimple filed an application for time-limited relief from certain registrant obligations, including prospectus and trade reporting requirements.[10] Similar to TokenGX, the OSC has capped the amount investors can fund at $30,000.00 per annum.

The approvals of TokenGX and Wealthsimple signal the beginning of a new framework whereby Canadian regulators are able to simultaneously promote innovation and market confidence while keeping Canada competitive in global financial markets.

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[1] The members are the securities regulatory authorities in Alberta, British Columbia, Manitoba, New Brunswick, Nova Scotia, Ontario, Québec, and Saskatchewan ("CSA Members").

[2] CSA, "Canadian Securities Regulators Announce Agreement with Kx to Deliver Advanced Post-Trade Analysis", September 13, 2018, online: <https://www.securities-administrators.ca/aboutcsa.aspx?id=1735>.

[3] *Collaborating to Protect Investors and Enforce Securities Law*, FY2019/2020, at p. 5, online: <http://www.csasanctions.ca/assets/pdf/CSA-Enforcement-Report-English.pdf>.

[4] Kx Platform, online: <https://code.kx.com/platform/>.

[5] *Evolving Securities Enforcement for a Digital World*, CSA, FY2018/2019, at p. 11, online: <https://www.securities-administrators.ca/uploadedFiles/General/pdfs/CSA-Enforcement-Report_FINAL201819.pdf>.

[6] *Reducing Regulatory Burden in Ontario's Capital Markets*, OSC, 2019, online: <https://www.osc.gov.on.ca/documents/en/20191119_reducing-regulatory-burden-in-ontario-capital-markets.pdf> [*Reducing Regulatory Burden*].

[7] NI 31-103, Registration Requirements, Exemptions and Ongoing Registrant Obligations, ss. 11.9-11.10.

[8] *Reducing Regulatory Burden* at p. 68.

[9] *TokenGX Inc., Re*, 41 OSCB 8511, online: <https://www.osc.gov.on.ca/documents/en/ord_20191023_tokengx.pdf>.

[10] *Wealthsimple Digital Assets Inc., Re*, 43 OSCB 6548, online: <https://www.osc.gov.on.ca/documents/en/ord_20200807_wealthsimple-digital-assets.pdf>.

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