



STABLECOIN

HKMA to Adopt Licensing Regime for Stablecoins in 2023/24

On 31 January 2023, the Hong Kong Monetary Authority (**HKMA**) published its [Consultation Conclusions](#) on its [proposals for regulating payment-related stablecoins](#) set out in its [Discussion Paper on Crypto-assets and Stablecoins](#) published a year earlier. Noting generally positive feedback from respondents, the Consultation Conclusions summarise the feedback received and set out the key parameters of a proposed regulatory regime for stablecoins (**HKMA's Proposed Stablecoin Licensing Regime**).

The HKMA observed that, since January 2022, the crypto-assets market has seen rounds of price volatility with its market capitalisation having shrunk by more than half by the end of December 2022. Stablecoins' market capitalisation managed to maintain growth until April 2022 but declined from May 2022 along with the wider crypto-assets market. Events such as TerraUSD's stabilisation mechanism's break down and losing its peg to the US dollar (triggering a fall in the price of Tether (USDT) to US\$0.95 before recovering its US\$1.00 peg), and FTX's bankruptcy filing in the US, the subsequent discovery of its operational and governance failures and the collapse of its native token - FTT, have spurred international organisations, standard setting bodies and other major jurisdictions to propose various policy developments to address the potential risks of virtual assets. See Annex 1 and Annex 2 of the Consultation Conclusions for the policy developments since January 2022.

Stablecoins within the scope of the HKMA's Proposed Stablecoin Licensing Regime

The HKMA will adopt a risk-based approach to regulation and prioritise the regulation of payment-related stablecoins (i.e. stablecoins that reference one or more fiat currencies and have the potential to become a widely acceptable means of payment) that present greater risks to the monetary and financial systems, while retaining flexibility to adjust the scope of regulated stablecoins as necessary in the future.

Stablecoins will be required to be fully backed and redeemable at par: the reserve assets will need to correspond to the value of the outstanding stablecoins at all times and the reserved assets themselves should be of "high quality and liquidity". Significantly, stablecoins that derive their value based on arbitrage or algorithm will not be regarded as fully backed and will not be accepted. Holders of stablecoins should be able to redeem their stablecoins into the referenced fiat currency at par within a reasonable period.

Activities to be regulated under the HKMA's Proposed Stablecoin Licensing Regime

The HKMA is proposing a licensing regime with different types of regulated activity covered by different licences, rather than a single licence covering a number of activities. The mandatory licensing regime will apply to the following regulated activities:

- a) governance – the establishment and maintenance of the rules governing an in-scope stablecoin arrangement;
- b) issuance – the issue, creation or destruction of in-scope stablecoins;
- c) stabilisation – the stabilisation and reserve management arrangements of an in-scope stablecoin, regardless of whether these arrangements are provided by the issuer; and
- d) wallets – the provision of any service allowing users to store their cryptographic keys which can be used to access users’ holdings of an in-scope stablecoin and the management of such stablecoins.

The new regulatory regime will however incorporate flexibility to allow the HKMA to broaden the scope of regulated activities to address risks that unregulated stablecoin activities may present in the future.

Under a proposed “principal business restriction”, licensed entities (other than authorised institutions) will be prohibited from conducting activities that deviate from the principal business permitted under their licence. For example, a licensed wallet operator will not be allowed to conduct lending activities.

Who will need a licence under the HKMA’s Proposed Stablecoin Licensing Regime?

An entity will need to be licensed by the HKMA if:

- a) it conducts a regulated activity in Hong Kong;
- b) it actively markets a regulated activity to the Hong Kong public;
- c) it conducts a regulated activity involving a stablecoin that references the value of the Hong Kong dollar, regardless of whether the relevant regulated activity is conducted in Hong Kong or actively marketed to the Hong Kong general public; or
- d) the HKMA believes that it should be regulated having regard to “matters of significant public interest”.

Regulatory requirements for licensed entities

The regulatory framework will be comprehensive and include regulatory requirements on matters such as ownership, governance and management, financial resources requirements, risk management, anti-money laundering and counter-terrorist financing, user protection, regular audits and disclosure requirements. The HKMA is continuing its formulation of the detailed regulatory requirements that will apply to licensed entities and will conduct a further consultation with more granular information on the regulatory regime in due course.

Who can issue Stablecoins under the HKMA’s Proposed Stablecoin Licensing Regime?

Under the HKMA’s Proposed Stablecoin Licensing Regime, both authorised institutions and non-authorised institutions who satisfy the relevant licensing and regulatory requirements will be permitted to issue stablecoins. In line with the “same risk, same regulation” principle, the HKMA will tailor the regulatory requirements applicable to authorised institution and non-authorised institution issuers according to the risks presented by each type of issuer to the financial system.

The HKMA’s Proposed Stablecoin Licensing Regime Target Implementation Date and the HKMA’s Next Steps

The target date for putting in place the HKMA’s Proposed Stablecoin Licensing Regime is 2023/24. As noted above, the HKMA will conduct a more detailed consultation, with more granular information, in due course. This will cover issues such as: (i) whether the HKMA’s Proposed Stablecoin Licensing Regime should be introduced under new legislation or through the amendment of existing laws; (ii) minimising regulatory overlaps; (iii) addressing risks that may be posed by affiliated entities’ provision of multiple or bundled financial services; and (iv) whether licensed entities should be required to be incorporated in Hong Kong.

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