Charltons - Hong Kong Law - 01 November 2024

[online version](https://www.charltonslaw.com/growing-hong-kongs-virtual-asset-market-hk-fintech-week-2024)

Growing Hong Kong's Virtual Asset Market: HK Fintech Week 2024

Dr. Eric Yip, Executive Director, Intermediaries at the SFC, outlined the current landscape and the future direction of the virtual assets market in Hong Kong in his opening speech, [Charting a Regulatory Roadmap for Hong Kong's Virtual Asset Market](https://www.sfc.hk/-/media/EN/files/COM/Speech/HKFTW-Speech-FINAL-EN.pdf?rev=25c208b36b0944caa4309f4738ec7820&hash=344AD2882BA4452AFF3FCFDDD79B8302), at Hong Kong FinTech Week 2024, held on 28-29 October 2024 at the AsiaWorld-Expo, Hong Kong. Noting the unprecedented year-on-year growth in Hong Kong virtual asset trade volumes, Dr. Yip stressed the need for a robust regulatory framework to protect investors and market participants while fostering innovation and further developing Hong Kong's virtual asset market. The SFC's key initiatives, as described by Dr. Yip, are also the subject of the SFC's publication “[SFC sets out vision to foster a vibrant fintech ecosystem in Hong Kong](https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=24PR180)” of 28 October 2024.

**The Current Licensing Regime for Virtual Asset Trading Platforms (VATPs) in Hong Kong**

There are currently three SFC-licensed VATPs in Hong Kong and 14 licence applicants undergoing the vetting process. The SFC's main focus now are the 11 so-called “deemed to be licensed” applicants. These are VATP licence applicants that operated in Hong Kong before the implementation of the VATP licensing regime in June 2023 that are “deemed to be licensed” under the regime's transitional provisions until their licence application is approved, rejected or withdrawn.

As highlighted by Dr. Yip, the SFC has changed its vetting approach for these “deemed to be licensed” applicants, replacing a document-based vetting process with risk-based on-site inspections, concentrating on specific areas such as safe keeping of client virtual assets, cybersecurity and the applicants' anti-money laundering (AML) and know-your-client (KYC) procedures. The SFC has now conducted on-site inspections for all 11 “deemed to be licensed” applicants and given them feedback.

For new applications, the SFC is adopting a three-pronged approach:

1. the VATP licence applicant agrees to rectify issues raised in the SFC's feedback following its on-site inspection;
2. the SFC grants a licence permitting the applicant to operate a restricted scope of business after rectification of the identified issues; and
3. completion of a review by a third party after which the restrictions on the scope of business will be lifted.

**Establishment of Consultative Panel for Licensed VATPs**

Dr. Yip's speech also noted the SFC's plan to set up an official consultative panel for licensed VATPs in early 2025. The panel will include senior management members from all SFC-licensed VATPs whose perspectives will be taken into account in the SFC's policy making. The consultative panel will contribute to a virtual asset white paper to be published by the SFC outlining a development roadmap for virtual asset products and services and potential improvements to compliance and risk management.

**Hong Kong's Virtual Asset Market Development**

Dr. Yip identified three key drivers behind the rapid development of Hong Kong's virtual asset market, namely:

* **Talent Pool**: A wealth of talent and expertise is driving the virtual asset market's growth.
* **Economic Potential**: The sector's high economic potential.
* **Younger Demographics**: Studies show that market participants involved in trading crypto assets are younger on average than those trading traditional stocks, highlighting the shift in investor demographics.

The SFC has also noted two emerging trends supporting the SFC's drive to regulate virtual asset-related activities: (i) virtual asset practitioners are facing increasing scrutiny from law enforcement agencies and regulators globally, prompting many market participants to reassess their previously unregulated operations; and (ii) the increasing participation of traditional finance (Tradfi) in the virtual asset market has introduced valuable compliance concepts such as anti-money laundering and conflict checks, client suitability assessment and measures to ensure the safe custody of assets.

**Establishing a Robust Virtual Asset Regulatory Regime in Hong Kong**

As noted by Dr. Yip, the SFC is working with the Hong Kong Government and other regulators in developing further regulation for the provision of virtual asset trading services and virtual asset custody services and public consultations on new licensing regimes for these activities will be conducted in due course. To this end, the SFC has been working with Hong Kong's virtual asset community to understand their business models and operating procedures for ensuring efficient and AML-compliant on- and off-ramping.

More generally, the SFC and Hong Kong Government are seeking to put in place a comprehensive regulatory framework for virtual assets in Hong Kong to assure Hong Kong's status as an international crypto hub. Hong Kong's Chief Executive, John Lee, announced in his 2024 Policy Address delivered on 16 October 2024 a range of virtual asset-related initiatives including the promotion of real-world asset tokenisation and development of a digital money ecosystem and digital securities market. For further details of the Chief Executive's 2024 Policy Address, please see our [October 2024 newsletter](https://www.charltonslaw.com/the-hong-kong-chief-executives-2024-hong-kong-policy-address-key-business-points/).

**Tokenisation, Project Ensemble and Stablecoins**

Hong Kong is seeing progress in the implementation of tokenisation-related initiatives. The SFC issued two circulars - the [Circular on Tokenisation of SFC-authorised Investment Products](https://apps.sfc.hk/edistributionWeb/api/circular/openFile?lang=EN&refNo=23EC53) and [Circular on Intermediaries Engaging in Tokenised Securities-related Activities](https://apps.sfc.hk/edistributionWeb/api/circular/openFile?lang=EN&refNo=23EC52) in November 2023, and is co-leading tokenisation initiatives for the asset management industry with the Hong Kong Monetary Authority (**HKMA**) through Project Ensemble. In August 2024, the HKMA launched the Project Ensemble Sandbox which allows participating financial institutions to trial interbank settlement of tokenised asset transactions using tokenised money.

Hong Kong is additionally planning to implement a new regulatory regime for fiat-referenced stablecoin issuers in Hong Kong. According to the [Consultation Conclusions](https://www.hkma.gov.hk/media/eng/doc/key-information/press-release/2024/20240717e3a1.pdf) published jointly by the Financial Services and the Treasury Bureau (FSTB) and the HKMA on 17 July 2024, a stand-alone piece of Hong Kong legislation implementing a Hong Kong regulatory regime for fiat-referenced stablecoin issuers in Hong Kong will be introduced, and the bill to implement that regime will be presented to the Legislative Council this year. For further details of the proposed regulation of fiat-referenced stablecoin issuers, please see our [October 2024 newsletter](https://www.charltonslaw.com/hong-kongs-proposed-regulation-of-fiat-referenced-stablecoin-issuers/).

**Commitment to Investor Protection**

The SFC considers “education” to be a key focus area in its efforts to enhance investor protection. The SFC has invested in multiple initiatives to educate investors about virtual assets, which include expedited information dissemination, developing a proactive alert system, promoting via TV drama series, commercials and other media outlets to raise awareness of scams and unregulated platforms.

**International Collaboration on Virtual Asset Regulation**

In closing, Dr. Yip highlighted the importance of international collaboration when establishing a robust regulatory framework, noting the SFC's continued collaboration with other international regulators in monitoring trends and sharing best practices and experiences.

This newsletter is for information purposes only.

Its contents do not constitute legal advice and it should not be regarded as a substitute for detailed advice in individual cases.

Transmission of this information is not intended to create and receipt does not constitute a lawyer-client relationship between Charltons and the user or browser.

Charltons is not responsible for any third party content which can be accessed through the website.

If you do not wish to receive this newsletter please let us know by emailing us at unsubscribe@charltonslaw.com

Charltons - Hong Kong Law - 01 November 2024