

FINNOSpace Response to VATP consultation

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As a major player in cross-border fintech, FORMS Hong Kong would want to share our perspective on how Virtual Asset Trading Platform Operators regulation could foster the growth of the Digital Economy and establish Hong Kong as a center of Web3 Fintech innovation.

FORMS Hong Kong has reviewed the regulatory requirements for Virtual Asset Trading Platform Operators and welcome the proposals in principle. Overall, the proposed regime would strike a good balance between investor protection and market development.

While we support the proposed requirements in general, there are a number of issues that need be considered to guarantee the proposed regime are competitive among the competitors.

1. Regarding retail access to licensed VA trading platforms (Q1)

Under the proposed investor protection measures, we agree that licensed VA platform operators should be allowed to offer their services to retail investors. This is due to the fact that greater market involvement gives developers the required liquidity to buy the virtual assets they require to fuel their projects.

The ecosystem for virtual assets is seeing increased growth in decentralized applications (dApps). The functionality of these blockchain-based applications is frequently supported by the use of virtual assets. The market's increasing liquidity has made it possible for developers to test out new financial instruments and business models, which has contributed significantly to the rise of DeFi initiatives in the Web3 ecosystem.

For instance, to enable users to buy and trade NFTs, developers creating an NFT marketplace may need to invest in a range of virtual assets. To pay for gas fees on the blockchain, they could need to buy ETH or another virtual asset. They might also need to buy a stablecoin like DAI to enable consumers to buy NFTs at a fixed price. The difficulty of obtaining the required assets without access to these virtual assets through a trading platform could impede the developers' endeavor.

2. Regarding the general token admission criteria and specific token admission criteria (Q2)

We suggest that the needs of Web3 Fintech business be taken into account while determining the scope of permitted tokens for VATP.

For a Web3 organization to take part in a relevant Web3 project, they must employ certain Tokens or Coins. In addition to "Professional Investors," a "Web3 Professionals" category has to be created.

The goal is to create a controlled channel for Web3 Professionals and recognized Web3 Organizations to buy the coins they need to run their businesses. Thus, it is advised to set up a committee with a focus on

- evaluate and validate particular coins for use in the Web 3 ecosystem and approving the token admission.
- evaluate and certify Web3 experts and organizations to use digital assets (coins) as fuel.

Under controlled conditions, VATP will be a crucial component of the Web3 economy, providing "fuel" to the Web3 ecosystem.

While the current criteria do consider market capitalization, which might be indicative of maturity of certain tokens, other factors like user adoption and developer support could also be considered to further unlock economic value for their platform and users.

| Top ten cryptocurrencies ¹ | Market Capitalization | Developer support | Daily active address |
|---------------------------------------|-----------------------|----------------------------|----------------------|
| Bitcoin (BTC) | Over \$500 billion | Over 37,082 Github Commits | 851,151 |
| Ethereum (ETH) | Over \$200 billion | Over 14,087 Github Commits | 497,907 |
| Tether (USDT) | Over \$79 billion | - | 89,987 |
| Binance Coin (BNB) | Over \$48 billion | - | 71,328 |
| USD Coin (USDC) | Over \$33 billion | Over 800 Github Commits | 35,034 |
| XRP (XRP) | Over \$25 billion | Over 12,800 Github Commits | 47,978 |
| Cardano (ADA) | Over \$12 billion | Over 800 Github Commits | 55,810 |
| Dogecoin (DOGE) | Over \$9 billion | Over 14,000 Github Commits | 50,998 |
| Polygon (MATIC) | Over \$9 billion | Over 1,800 Github Commits | 5,803 |
| Binance USD (BUSD) | Over \$7 billion | 10 Github Commits | 1,381 |

¹Top ten cryptocurrencies based on market capitalization as of March 27, 2023, according to CoinMarketCap

3. Regarding technical solutions to effectively mitigate risks associated with the custody of client virtual assets (Q6)

An approval engine could be added as an extra layer of security and risk management to transactions on the platform. By requiring all transactions to be reviewed and approved by the engine before being signed on-chain, the risk of fraudulent or high-risk transactions can be reduced.

It could be accomplished by connecting three pieces:

- HSM (Hardware Security Module) hardware to ensure all transactions are hardware signed and secure, additionally reducing the risk of compromised private keys
- Approval Engine that reviews all transactions in advance of being signed, similar in concept to what card payment services may traditionally do for any transaction or institutional treasury management.
- Risk Module which will include outlier algorithmic detection, velocity checks and follow industry standard practices for identifying high risk transactions.

It may also connect with on-chain analytics and other industry standard services to incorporate their controls, compliance tools and analysis.

Overall, a layer of approval engine can help ensure that all transactions on the platform are secure, compliant, and low-risk, which can increase trust and confidence in the platform among users and stakeholders.