Question 1: Do you agree that licensed platform operators should be allowed to provide their services to retail investors, subject to the robust investor protection measures proposed? Please explain your views.

Answer:

1. We agree that cross-border hard limit (in terms of maximum dollar amount exposure to virtual assets) is not appropriate for retail investors.
2. It is advisable for the SFC to establish a guideline outlining the criteria for halting, suspending, and withdrawing a virtual asset from trading, as well as specifying the options available to clients holding that virtual asset. By doing so, the potential for abuse of discretion by licensed platform operators, particularly in times of liquidity crises, can be minimized. Clear guidelines from the SFC would promote a more consistent approach across platform operators, ensuring fair treatment for all parties involved and reinforcing the overall stability and integrity of the virtual asset trading environment.
3. In the absence of derivative or leverage features, policy of trading limit should be consistent with the on-going duty of Know-your-client by the licensed platform operators.
4. Given the potentially high volatility of virtual assets, mere notional dollar amount or number of units would not be appropriate. For example, the client bought 1 unit of certain virtual asset at US$ 10,000 which is exactly within the current dollar amount limit, say US$20,000. If the price of such virtual asset rises to US$30,000, the holding position of the client would obviously breach the pre-set dollar amount limit if marked-to-mark.
5. If derivative or leverage features are to be introduced, additional factors need to be considered by the licensed platform operators when setting the limit.
6. In conclusion, we suggest to keep the limit-setting as principle-based.

Question 2: Do you have any comments on the proposals regarding the general token admission criteria and specific token admission criteria?

Answer:

1. There is some confusion in the draft provision.

2. First, there is no definition of "Token" in the draft **Guidelines for Virtual Asset Trading Platform Operators (June 2023)** ("the Guidelines") but only "Virtual Asset" (or "VA") and "Security Token". In the Guidelines (Paragraph 1.1), Virtual Asset means any "virtual asset" as defined in section 53ZRA of the AMLO and the any security token.
3. Second, the "Token Admission" is referred in Paragraph 7.10 but the explanation in Paragraphs 38-42 makes no distinction between virtual asset in section 53ZRA and security token.
4. Third, it is indeed advisable for the SFC to consider establishing guidelines for dealing with "hard forks" in the context of virtual assets. While a virtual asset like Bitcoin may comply with the "General token admission criteria," its hard forks might not necessarily meet the same standards. Since hard forks are a common feature of virtual assets, it is essential for the SFC to develop guidelines addressing how licensed platform operators should handle them. This would ensure that potential risks associated with hard forks are adequately managed, providing greater investor protection and fostering a more secure and transparent trading environment.
5. Fourth, it is advised that Environmental, social, and governance (ESG) factors should be introduced into the evaluation process, considering the environmental impact, social responsibility, and governance structure of the virtual asset and its associated projects. This addition would align the policy with growing global concerns and investor expectations.
6. It is well-known that a general virtual asset, e.g., Bitcoin, shall be distinguished from a security token, in terms of admission. Security Token is a cryptographically secured digital representation of value which constitutes "securities" as defined in section 1 of Part 1 of Schedule 1 to the SFO (see Paragraph 1.1 of the Guidelines). Therefore, Security Token shall be subject to SFO accordingly when it is offered to retail clients.

Question 5: Do you have any suggestions as to how funds should be set aside by the licensed platform operators (for instance, under house account of the licensed platform operator or under an escrow arrangement)? Please explain in detail the proposed arrangement and how it may provide the same level of comfort as third-party insurance.

Answer:

1. We agree that as a supplement and/or alternative to the third-party insurance, the platform operator shall set aside certain funds on trust and designate for the purpose of appropriate level of coverage for risks associated with custody of client virtual assets.
2. We further suggest a 2-aspect approach as follows:
   (1) Legally, custody of client virtual assets should be covered with contract clauses which provide that such assets could not be traded with other platform operators which have been equivalent or similarly regulated as to Hong Kong in a "friendly jurisdiction". Such friendly jurisdiction would have in place relevant civil / criminal assistance protocols in Hong Kong. This would help reduce the enforcement uncertainty when following and tracing is necessary.
   (2) Commercially, the extent of the coverage as well as the necessary charging scheme by the platform operators should be disclosed mandatorily to all custody clients in prescribed form by the SFC and incorporated into the custodian agreement.
3. To ensure transparency and proper management of the reserve fund, periodic external audits should be conducted by independent auditors. This would provide an additional level of assurance that the funds are being managed according to the established guidelines.

Question 8: Do you have any comments on how to enhance the other requirements in the VATP Terms and Conditions when they are incorporated into the VATP Guidelines?

Answer:

See the answer at question 5.

Additional Comments to the Guidelines

Paragraph No.	**Current Version of Draft**	**Suggestion**	**Rationale**
7.5(a)	The background of the management or development team of a virtual asset;	The background of the management or development team of	E.g., there is no specific management team for Bitcion. Whether there is a reasonable expectation of profits derived

		a virtual asset where applicable;	from efforts of the management team? If such an expectation does not exist, this factor may appear irrelevant. In the U.S., extensive discussions on this aspect have taken place, as evidenced by the SEC's document titled "Framework for 'Investment Contract' Analysis of Digital Assets." More information can be found at the following link: https://www.sec.gov/files/dlt-framework.pdf It will provide a clearer guidance by stressing "where applicable".
7.5(c)	the supply, demand, maturity and liquidity of a virtual asset, including its market capitalisation, average daily trading volume, track record …. been made available for trading;	the supply, maximum supply, demand, maturity and liquidity of a virtual asset, including its market capitalisation, fully diluted market capitalisation average daily trading volume, track record (as well as the sources of such data) … been made available for trading;	It is recommended to also consider the maximum supply and fully diluted market cap. The reason for this addition is that the supply of a token is distinct from the concept of "maximum supply." Maximum supply refers to the total amount of coins that will exist for a specific token throughout its lifetime, as the token may generate a certain number of new tokens per year. On the other hand, the

			fully diluted market cap takes into account the maximum supply when calculating the overall market capitalization. By incorporating the maximum supply and fully diluted market cap into the evaluation, a more comprehensive understanding of a virtual asset's financial status can be obtained. To extend the duty of due diligence further level down expressly.
7.5(d)	… and especially how resistant it is to common attacks …	… and especially how resistant it is to common attacks where the Platform Operator decides to provide its opinion in this regard …	The current version put an onerous burden to the platform operator. It shall be at the Platform Operator's commercial decision to give such opinion or not.
7.10	… the Platform Operator should notify clients as soon as practicable, inform them of the options available to clients holding that	… the Platform Operator should notify clients as soon as practicable, inform them of the options available to clients holding that virtual asset, and ensure they	To give more protection to investors.

	virtual asset, and ensure they are fairly treated.	are fairly treated. In any event, the transition period before withdrawal of a virtual asset should not be less than 5 working days (except weekends or public holidays).	
7.12	… should implement appropriate access rights and controls …	… should implement appropriate policy and procedures ~~access rights and controls~~ …	Please refer to SFC v Pacific Sun Advisors Ltd and Another [2015] HKCFA 27[1]. It is submitted that the intention of the operators matters, not the format in terms of wording.
9.18	A Platform Operator should not post any advertisement in connection with a specific virtual asset		Advertisement is not defined. Further, there should be distinction between information posted to general public and those only available to existing clients (upon successful log-on / client identification)

(The End)

[1] See §§48: "on its proper construction, the exemption in section 103(3)(k) clearly applies to an advertisement of a relevant investment product that, as a matter of fact, is or is intended to be disposed of only to professional investors whether or not this fact is actually stated in the advertisement itself, it is not necessary for the appellants to invoke this principle in support of their appeal."