

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

We agree that **licensed platform operators should be allowed to provide their services to retail investors**, given that robust investor protection measures are in place.

The **demand from retail investors** on virtual assets trading is **getting stronger**. With the changes in dynamics of virtual asset market, VA trading does not only attract institutional and professional investors per se, retail investors, especially the **younger generation** are also jumping into the bandwagon.

Allowing retail access would bring a number of benefits to investors. It does not only **provide a wider range of investment opportunities** with an expanded set of trading instruments and 24*7 trading, but also “fill the void” and **offer customer protection with more platform transparency**, enabling investors **peace of mind trading** and preventing them from deception by dubious unregulated platforms.

Having said that, given the high volatility in trading of VA and the novelty of the licensing framework, regulator should consider **to observe market development** on whether to fully extend VA trading to retail customers **at once or by phase**.

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

In order to establish a level playing field and a consistent investor protection regime, SFC should set up **minimum standards in terms of the criteria that Platform Operators (PO) should adopt** as part of their VA on-boarding criteria. Examples of required industry wide standard:

1. **Certification of resilience of the VA blockchain protocol:** In the consultation paper, it mentions the PO should take into account the resilience of the VA blockchain protocol (e.g. resistance to 51% attack). Those are technical and specialised topics that should require industry wide certification, as opposed to leaving it to each PO to assess, as it is expected that each PO may have different standards.
2. **Minimum market cap of admitted token:** In order to deploy an adequate and consistently applied investor protection regime, a number of such controls should be specified by SFC as minimum standards.
3. **Review committee requirement:** Product approval process should involve IT Risk / Cybersecurity as risk stewards.
4. **Conflict of Interest (COI):** Considerations to be given to any potential COI arising between the platforms’ activities and clients interests (e.g. house positions vs clients). For example regulations should specify minimum standards in terms of identification, inventory and mitigation of COIs
5. **Acceptable indices and white listed tokens:** It would serve as a guidance if SFC can provide a list of suggested indices and token to be admitted for PO to reference and follow, given the

interpretation of definition might differ across PO. For example, would “S&P Cryptocurrency LargeCap Index” be an acceptable index?

It is also suggested that **tokenized traditional asset (as opposed to genuine VA) could be subject to a more relaxed set of admission criteria for trading on VATP**, e.g. simplified background check, such to expedite the token onboarding process in terms of regulatory and internal approval.

Question 3 – What other requirements do you think should be implemented from an investor protection perspective if the SFC is minded to allow retail access to licensed VA trading platforms?

There are several requirements that we think should be implemented to ensure investor protection:

1. **Role & responsibility:** Platform operators (PO) should disclose clearly to investor their precise role and responsibility in the trades (e.g. Market maker) and in the custody role.
2. **Trading Process:** POs should disclose the detail trading process to clients, from order taking to execution, to settlement on blockchain. For example, where is the liquidity (price givers) sourced from for clients (price takers)? Who are the counterparties that the PO deals with? It is important be mindful of the cascading risks (i.e. the PO trades with a fraudulent counterparty and is affected by its subsequent failures).
3. **K&E checks:** Since VA custody relies on smart contracts entered in blockchain technology and the access to private keys, there is a strong technology, cybersecurity risks aspect to VA trading that clients should fully understand.
4. **Vulnerable Customer(VC):** Particular focus should be given to VC clients with consideration to suitability and protection. PO should be subject to a common set of minimum standards.
5. **Ongoing customer alert:** Regular reminder and quest for acknowledgement on the risk of investing in VA such as high volatility and over concentration.
6. **Investor education:** The platform should provide investor education and training to customers, helping customers understand the risks associated with investing in virtual assets and make more informed investment decisions.

With regard to the suitability assessment, we would like to clarify if there will be a clear regulatory protocol for PO to comply with the suitability obligations:

1. What level of **Product Risk Rating (PRR)** would be for VA investment products? Is there a standardized approach to derive the PRR? POs might find it difficult to include VA into **suitability assessment on a portfolio basis**. Is there any suggestion from SFC?
2. Any direction on whether **mismatch transactions are allowed for VA investments**?
3. Is an “**Execution only (EO)**” mode allowed if there is no standard PRR for VA products?
4. Is there clear protocol to distinguish an “**Execution only**” model with a “**Solicitation**” model?

Question 4 – Do you have any comments on the proposal to allow a combination of third-party insurance and funds set aside by the licensed platform operator or a corporation within its same group of companies? Do you propose other options?

No comment.

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.

No comment.

Question 6 – Do you have any suggestions for technical solutions which could effectively mitigate risks associated with the custody of client virtual assets, particularly in hot storage?

Hot wallet storage might impose security threats from hacking activities, below measures are potential mitigations the industry could consider:

1. **Multi-factor authentication (MFA):** using multiple forms of identification to grant access to hot wallets
2. **Encryption:** can be implemented using industry-standard encryption algorithms and protocols, using advanced cryptographic techniques to protect customer assets stored in hot wallets
3. **Regular audits:** help identify vulnerabilities and potential security threats, ensure that security measures are being properly implemented and that there are no vulnerabilities that could be exploited by attackers
4. **Automated risk detection:** monitor hot wallet activity and detect any unusual behavior that could indicate a security breach

We would also like seek SFC's clarifications on below questions:

1. **Any key considerations that Platform Operator and its Associated Entity should store 98% of client virtual assets in cold storage**, instead of 95% which better aligns with the common industry practice.
2. Will there be requirement on **maximum or minimum % of asset hold in hot wallet?**
3. Assuming customer can trade through hot wallet, is there **any guidance or SLA on the transfer between cold and hot wallets?**

Question 7 – If licensed platform operators could provide trading services in VA derivatives, what type of business model would you propose to adopt? What type of VA derivatives would you propose to offer for trading? What types of investors would be targeted?

Offering derivatives on VA to clients **may not necessarily mean more risk to clients**, as derivatives can offer protection in the form of put options or default swaps.

For retail investors, derivatives that **offer protection, act as risk hedging, and are fully funded** (ex: notes format) should be explored, with preference for centrally cleared derivatives (ex: futures or listed options) so as to ensure transparency and allow the exchange to centrally control trading activities and leverage (via margining mechanism).

From the Asset Management product manufacturers' perspective, it is always **preferable to have a larger set of tradeable instruments**. It is believed that VA derivative is not at the top priority when the spot market is still at the infant stage.

For the purpose of investor protection, VA derivatives could be **restricted to PIs or institutional investors at the initial stage**, and offer **simple and vanilla type of derivatives** to start with.

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?

No comment.

Question 9 – Do you have any comments on the requirements for virtual asset transfers or any other requirements in Chapter 12 of the AML Guideline for LCs and SFC-licensed VASPs? Please explain your views

From compliance perspective, we have concern on Section 12.7 “Ongoing monitoring in relation to virtual asset transactions and activities”, in particular **12.7.3 which requires FI to establish and maintain adequate and effective systems and controls to conduct screening of virtual asset transactions and the associated wallet addresses, as well as 12.7.5 which requires FI to monitor additional customer information including IP addresses with associated time stamps, geo-location data, and device identifiers**, etc. We would like to reflect the difficulties of establishing such capability on screening IP address with time stamps / wallet addresses – the same should apply to other POs/AIs. It is suggested that SFC can establish a centralized database for POs/AIs to access and utilize.

We would like to seek further guidance on the following sections from SFC:

1. Section 12.7.3 as to **whether pre-transaction due diligence shall be performed on risk based approach**, and if so further guidance on the risk-based approach (e.g. factors to be considered) is needed as to drive industry-wide standards
2. Section 12.11 **whether the CDD requirement on virtual asset transfers is also covering Virtual Asset to fiat currency conversion?**

Question 10 – Do you have any comments on the Disciplinary Fining Guidelines? Please explain your views.

No Comment.

Other Clarification:

Apart from above comments, we would also like to seek SFC's clarification on following areas:

(A) Competence criteria

- **Executive Officer/Responsible Officers/Licensed Representative for Registered Institutions:** Kindly provide competence criteria of approval of EOs/ROs, if any, on top of prevailing criteria currently stipulated for other regulated activities
- **Relevant individuals (RIs):** Kindly provide competence criteria of approval of RIs, if any, on top of prevailing criteria currently stipulated for other regulated activities, e.g. Will there be added regulatory requirements on licensed persons concerning VA product knowledge, enhanced suitability and sales process for a solicitation service?
- **Manager-in-charge (MIC):** On top of the current MIC roles for other regulated activities, will it be any new MIC role for the technical VA aspect

(B) Licensing/Other regulatory requirement

- **Licensing:** Understand the consultation is for "platform operator". With reference to a normal retail banks' business model to offer/distribute investment products, we would like to clarify whether a new license for regulated activities for distributions of VA is required if a bank is currently registered as Type 1, 4 and 7 regulated activities.
- **White Labelling of 3rd party VATP:** Any regulatory framework and requirement if FIs provide VATP service through white labelling of 3rd party solution.
- **Tokenisation of traditional assets and Issurance of genuine virtual assets:** Any new authorisation framework, if any, for tokenising traditional assets or issuing genuine virtual assets for trading on VATP?

(C) Other

- Any specific requirement on the VA's fee / benefit disclosure?