

## Introduction

appreciates the opportunity to respond to the *Consultation Paper on the Proposed Regulatory Requirements for Virtual Asset Trading Platform Operators Licensed by the Securities and Futures Commission*.

believes that digital currencies and assets can play a positive role but are more likely to complement rather than replace traditional currencies and assets. We are engaging in global discussions on the potential of Central Bank Digital Currencies (CBDCs), stablecoins and cryptocurrencies, and the required regulatory arrangements for each. In this context, we have been closely following and strongly supporting the Hong Kong SAR Government's work to develop a vibrant sector and ecosystem for Virtual Assets ("VA") in Hong Kong.

We believe that it is critical that regulatory regimes encompass the full scope of digital currencies and assets to ensure the safety and stability of the financial system. In the case of many stablecoins and all cryptocurrencies, we view them as nascent, privately issued forms of digital money whose current behaviour and use are more aligned with speculative investments as opposed to a mechanism for safe and reliable payments. We also note the growth of both retail and institutional adoption of VA and the interest of some regulated financial institutions and service providers in entering the VA space. All of this should come with comprehensive and appropriate regulation.

At present, trading and custody of stablecoins and cryptocurrencies are outside 's risk appetite, and we continue to monitor the broader risks relating to them. Comprehensive and appropriate regulation is important to reduce these risks. Recent crypto volatility and exchange failures have sent waves through broader markets and drawn attention to the need for such wider regulation.

That said, we always support the role of Hong Kong as a leading international financial centre. In this context, we believe that it is preferable to allow retail investors access to VA services offered by onshore licensed platform operators rather than trade VA via unregistered platforms overseas, under the condition that a robust and comprehensive regulatory framework with appropriate safeguards will be in Hong Kong place to protect investors and ensure market integrity. This is consistent with the position we have expressed for other jurisdictions.

We note and support that the SFC's proposed regulatory framework is based on the "*same business, same risk, same regulation*" (sometimes more specifically termed "*same application, same risk, same regulation*"), and we think that it should particularly apply to the regulation applied across different forms of private money – commercial bank money, stablecoins and cryptocurrencies. We also note and support the SFC's focus on investor education. observes that many retail investors do not have adequate knowledge of virtual currencies and assets and

their inherent risks. This leads them to take higher risks than they would have been willing or can take.

Against this backdrop, we encourage the SFC to work with other regulatory authorities and all participants in the VA industry, such as financial institutions, IT firms, academia and industry associations, to promote investor education.        will support such initiatives.

Moreover, we support in principle the SFC's proposals, including the token admission criteria, disclosure and governance requirements, and we share our recommendations about how to improve them further. We also believe that critical to investor protection is the introduction of safeguards that would ensure, among others, safe custody of assets, operational resilience of virtual asset trading platforms (VATP), and compliance with anti-money laundering (AML) rules. At the same time, while we agree with the introduction of full coverage of investors via third-party insurance and house accounts, we find this to be the bare minimum for investor protection, and we encourage the SFC to introduce measures against additional risks from VA trading. Furthermore, we believe that the SFC should allow only the trading of VA derivatives listed on recognized exchange companies and classify them as complex products.

Last, we want to take this opportunity and share that the usage of public networks in a safe and controlled manner may be appropriate for VA development, in which case the payment of small amounts of "gas fees" to network validators for their services to the blockchain, in a safe and controlled manner, is appropriate. This case is very different from proprietary or customer-facing cryptocurrency trading.

We have responded to each question posed in the discussion paper below. We would welcome the opportunity to speak further on these issues and answer any questions the SFC may have.

**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.**

The financial system is rapidly evolving towards a more digital environment. It is, therefore, critical that regulatory regimes encompass the full scope of digital currencies and assets to ensure the safety and stability of the financial system. We pay close regard to developments in all forms of digital currencies and assets and update our position based on regulatory and market developments. The growth of retail and institutional adoption of VA has also resulted in increased sophistication of those providing VA services. However, as of now, VA exchanges are not covered by existing SFO or guidelines, except in relation to security token activities, and this can undermine market integrity, investor protection and eventually, financial stability.

As shared by the SFC, such risks include, among others, market manipulation, loss of money due to IT failures and fraud schemes, money laundering, terrorist financing, as well as increased volatility and liquidity concerns. Therefore, without appropriate regulation, VA could undermine confidence in the financial system. The risks that such VA pose to liquidity, credit and the money market could be serious and are, as of now, untested. A big step in addressing these risks would be ensuring that VA trading platforms are licensed, registered and supervised.

At the same time, a significant number of markets, such as the EU and Japan are currently in the progress of defining new rules to get virtual asset services in order. For example, the EU is very close to finalizing the new Markets in Crypto-Assets Regulation. As one of the leading international financial centres in the world, Hong Kong's prime position with a strong regulation standard around VA would set a new benchmark for the rest of the world.

Given the existing VA market landscape and the interest of the Hong Kong SAR Government to reinforce the status of Hong Kong as a VA hub, we believe that it is preferable to allow retail investors access to VA services offered by onshore licensed platform operators rather than trade VA via unregistered platforms overseas. Hence, we agree with SFC's proposal that licensed platform operators should be allowed to provide their services to retail investors subject to a comprehensive regulatory framework with appropriate safeguards in place to protect those investors.

Striking the right balance is vital, as VA market development should not compromise market integrity and investor protection. However, we also think the widely accepted principle of "*same application, same risk, same rules*" should apply. As noted in this consultation, adopting that principle would result in a regulatory approach for stablecoins and cryptocurrencies that matches that for commercial bank money, at a bare minimum. This is because stablecoins and cryptocurrencies, as private currencies and investments, create at least the same risks as

commercial bank money and, depending on their design, may create additional risks. In addition, many cryptocurrencies, as an investment, have features and risks that retail investors may not reasonably understand because of their complex nature.

As the new enhanced guidelines aim to protect the investors and further develop the market, as they reach retail players in the industry, we believe that they could ensure high confidence for investors and financial institutions. The ongoing work of the Financial Stability Board (FSB) on global regulatory coordination for stablecoins and cryptocurrencies is important to consider when shaping this regulation.        engages closely with the FSB to coordinate global regulation for stablecoins and cryptocurrencies and calls for these principles to be followed in all markets where we operate to ensure the safety of the global financial system. In the same context, we remain committed to working closely with SFC, HKMA and others in Hong Kong.

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

believes that introducing high eligibility standards can contribute to investor protection. Our position is clear: all forms of digital money should be regulated commensurate with the risks they create, including any market and financial crime risks. This is in line with the “*same application, same risk, same regulation*” principle that should apply across the spectrum enabling a level playing field for all market participants. We think that should particularly apply to the regulation applied across different forms of private money – commercial bank money, stablecoins and cryptocurrencies.

Also, given the broad definition of “virtual asset”, we would like to clarify whether stablecoins and, in particular, those who are not asset-backed would be in-scope. In light of the recently-published report of the HKMA on stablecoins and the plans to introduce a regulatory framework by 2023/24 that will prioritize asset-backed stablecoins, strongly recommends that non-asset-backed stablecoins are included in the regulations proposed in this consultation. This is because we think such stablecoins create additional risks that need to be regulated. In particular, we are wary of so-called “algorithmically backed stablecoins” and are not convinced that they form a legitimate category, as algorithms merely select markets to rely on, they are not a replacement for backing assets. They may therefore create particular consumer dangers.

During times of general market stress, such as the recent collapse of SVB, certain coins, despite being represented as highly safe and well backed, fell well below their intended level of 1:1 with USD. This would not be acceptable for commercial bank money and highlights the stark current differences between even the safer parts of the stablecoin market and commercial bank money. This regulatory arbitrage should be closed, as it is creating current risks. We encourage all regulators to learn lessons from this situation and ensure that coins are as thoroughly regulated as commercial bank money to ensure that they are usable, safe and of consistent value in all credible scenarios.

believes that the general token admission criteria are in the right direction. However, as the market has been evolving rapidly, we recommend that SFC reviews the general token admission criteria list periodically to assess whether they ensure market integrity and investor protection. Moreover, we would also ask for more clarity about the assessment process and, whether the SFC recommends that all proposed assessment criteria be weighted equally. Furthermore, it would be helpful if the SFC could share some examples of VA who did not meet the assessment criteria, as this would assist the VATP with their overall assessment process.

Moreover, we would like to share our inputs with regard to the token admission and review committee; under paragraph 7.1(d), the token admission and review committee will be

responsible for: *“establishing, implementing and enforcing the rules which set out the obligations of and restrictions on virtual asset issuers (for example, the obligation to notify the Platform Operator of any proposed hard fork or airdrop, any material change in the issuer’s business or any regulatory action taken against the issuer), if applicable”*. While sharing such information would contribute to investor protection, we would ask for additional details on implementing this requirement. In addition, we agree in principle with the proposal to introduce additional admission criteria for security tokens offered to retail customers. In this context, we agree that eligible large-cap VA should be included in at least two “acceptable indices” issued by at least two independent index providers, and we would welcome some additional information about how SFC would define and consequently assess the experience of the index providers, and the liquidity of the indices. To further facilitate the adoption of these criteria, we would invite the SFC to consider publishing a list of indices commonly approved by the vast majority of the industry participants, as this would enhance transparency and bring more predictability to the market.

Last, we would like to ask for more clarity about what liquidity levels are deemed sufficient and how the SFC would assess the index provider’s expertise and technical resources to construct, maintain and review the methodology and rules of the index. In this context, we would encourage the SFC to work with industry participants and introduce a related assessment template to facilitate consistency and robustness across the industry.

### **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?**

agrees with the approach of the proposed requirements, and we would like to share some additional recommendations on how to ensure investor protection while allowing retail access to licensed VA trading platforms.

Therefore, it is vital to ensure sufficient knowledge of retail investors in virtual assets, as proposed by SFC. Hence, we agree with the SFC proposal that licensed platform providers have a responsibility to ensure adequate levels of awareness among retail investors. If licensed platform operators assess that retail investors do not have sufficient knowledge of the above-mentioned risks, they should provide additional training by offering educational material, and in case such training does not bring the required results, decline to provide their services

To achieve this, it is critical that operators have a robust mechanism that would ensure client education. Hence, we would encourage the SFC to work with other regulatory authorities and all participants in the VA industry, such as financial institutions, IT firms, academia and industry associations, including the Hong Kong Association of Banks (HKAB) to create an industry-consistent education framework.

In addition to the proposed risk awareness assessment measures, we would like to add to the proposed risk awareness measures and recommend that VATP should assess the retail customer's knowledge of the inherent risks including:

1. price volatility of virtual assets and the subsequent risk of capital loss;
2. risks stemming from illiquid market conditions;
3. losses stemming from system outages, IT risks and fraud;
4. blockchain network fees deducted for each transaction, and that this may fluctuate depending on the volume of activity being processed through the blockchain at any given time.

We also encourage the SFC to draw lessons from international best practices, as presented by peers and international bodies such as FSB, the International Organization of Securities Commissions (IOSCO), and the Bank of International Settlements (BIS). For example, the FSB [recommends](#) the following policy recommendations for the regulation, supervision, and oversight of crypto-asset activities and markets, which cover VATPs as well:

1. robust frameworks for collecting, storing, safeguarding, and the timely and accurate reporting of data that will cover among others, their financial conditions and risk profiles;

2. mechanisms to identify and monitor the relevant interconnections, both within the crypto-asset ecosystem as well as between the crypto-asset ecosystem and the broader financial system;
3. requirements to separate certain functions and activities, as appropriate;
4. mechanisms that identify and monitor the risks associated with individual functions as well as the risks arising from the combination of functions such as custody, brokerage, and lending.

Regarding disclosure requirements, we believe that licensed platform operators should provide detailed disclosure of IT-related risks, other than fraud and cybersecurity, such as third-party risk, and share their operational resilience framework. In the same context, we propose that licensed platform operators should clearly specify to investors their appointed service providers and any associated transfer of risk from one entity to another.

Last, we would like to call out issues with the quality of the related information that will be disclosed. As quoted by the [US White House Releases](#) in September 2022, almost a quarter of digital coin offerings had disclosure or transparency problems—like plagiarized documents or false promises of guaranteed returns. Therefore, we encourage the SFC to provide specific guidelines on the quality of required disclosure.

We believe that licensed platform operators could also be required to periodically (e.g., monthly) disclose to the SFC the public blockchain address(es) used to hold clients' virtual assets, snapshot of the client virtual asset holdings as recorded on the public blockchain versus internal system records and rationale to be provided for any reconciliation difference.

Aside from the requirements mentioned in this section, we would like to share our feedback on the proposed financial resources and soundness proposals, according to which:

- *A Platform Operator should maintain in Hong Kong at all times assets which it beneficially owns and are sufficiently liquid, for example, cash, deposits, treasury bills and certificates of deposit (but not virtual assets), equivalent to at least 12 months of its actual operating expenses calculated on a rolling basis.*<sup>6.2</sup> *A Platform Operator shall at all times maintain paid-up share capital of not less than HK\$ 5,000,000 (referred to as "minimum paid-up share capital").*

agrees with the approach. At the same time, we note that the required paid-up share criteria are the same as the requirements for Type 1 intermediaries, and we wish to highlight that compared to the traditional Type 1-licensed companies, the VA sector is relatively nascent and therefore entails relatively higher risks. As a result, we find the proposed requirements too low,



and we recommend higher capital and liquidity standards on VATP as opposed to other trading platforms under the principle of the "*same application, same risk, same regulation*" principle. To this end, the SFC could draw lessons from Hong Kong's stored value facility ("SVF") regime, as well as existing research and international best practices to determine the required amounts.

We also agree that VATP should hold only high-quality and sufficiently liquid assets to ensure business continuity. To this end, we wish to highlight that the proposed assets (i.e. cash, deposits, treasury bills and certificates of deposit have varying degrees of value, liquidity and risk. In parallel, recent fiscal events in the UK have manifested that even high-quality liquid assets can suffer periods of illiquidity in market turmoil). Therefore, we would welcome additional guidelines on the composition of the required liquid capital.

It is also critical to mitigate the risk of misuse of reserve assets from commingling. To this end, we believe that the SFC should introduce requirements that will ensure the segregation of reserve assets from those used for operational, business, or other purposes. In light of reconciliation and validation requirements to ensure that assets are appropriately ring-fenced from insolvency at all times and capital and liquidity requirements to protect against residual risks, we welcome the SFC's effort to ensure safe custody of assets. At the same time, conventional custodians for intermediaries have been safekeeping for licensed corporations' assets pursuant to the current SFC client asset requirements.

Therefore, we do not believe that only associated entities of platform operators can provide custody to client money and virtual assets. Hence, we invite the SFC to apply existing practices in the traditional custody space and allow licensed platform operators to appoint third-party virtual asset custodians in addition to safekeeping the virtual assets under wholly owned subsidiaries. This could provide optionality for operators to appoint an independent service provider who could fulfill the investor protection requirements, re-enforcing investor protection through entity separation, particularly in the event of an insolvency of a platform operator.

Furthermore, to ensure investor protection even at times of extreme stress, we believe that the redemption of VA should be as timely as possible, and the goal should be real-time or at least near real-time redemption. At the same time, we acknowledge that there are certain limitations in the existing IT and broader infrastructure capabilities of companies. In this context, we note that in many instances, regulators ask that redemption is as timely as possible without prescribing a specific deadline.

As a result, we recommend real-time redemption, and if this is not immediately possible, then we propose an interim goal alongside a detailed strategy to eventually achieve real-time or near-real-time redemption. To further ensure investor protection, the SFC should consider introducing redemption risk tests. Last, we recommend that the SFC requires that licensed platform

operators offer their services on a continuous basis, as digital asset markets are also operating on a 24/7/365 basis. This should include several services, including trading, monitoring and surveillance, support in different languages, as well as live customer support services.

**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?**

shares the SFC's observation about the global VA insurance sector, as well as that premiums for insurance policies covering the risks associated with client virtual assets are at high levels. This, however, comes as no surprise, given the VA sector's high volatility and additional risks. Given that market integrity and investor protection is SFC's priority vis-à-vis the proposed VATP regulatory framework, we agree with introducing a requirement for full coverage via third-party insurance and other funds, but we also believe that this is the bare minimum to ensure investor protection. Hence, we strongly recommend that the SFC considers additional measures that would protect VA investors against additional risks. Furthermore, we would like to share additional options to enhance investor protection further. To begin with, the SFC might want to consider introducing a transaction levy to build up a compensation fund for the industry.

Hong Kong could also follow the example of the US market, where individual customers can purchase their own personal insurance to cover their virtual assets being stored in the exchange hot wallets. The amount paid for personal insurance could also be deducted from the transaction levy that was proposed above. Again, this could be an option to consider later in the VA market development in Hong Kong.

Furthermore, to reduce the overall size of virtual assets being stored in the hot wallet and, therefore the incurred risks and the required insurance premiums, the SFC could encourage or even incentivize the platform operators to explain to retail investors the security risks from storing their VA in hot wallets versus cold wallets and encourage them to move them to their own cold wallet if they do not intend to make any transactions in the foreseeable future.

We also encourage the SFC to explore additional policies to enhance investor protection. For example, since cold wallets have the form of physical hardware, specie insurance can provide coverage for this highly valuable and portable hardware. Therefore, the SFC could encourage retail investors to choose specie insurance to protect from risks incurred from cold wallet storage.

Last, we would like to ask for more information about the insurance requirements for VA held in hybrid/" warm" wallets.

**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.**

As mentioned in our response above, [redacted] agrees with the SFC's 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. To ensure the same levels of investor protection, however, it is critical to safeguard the proper management of the funds.

To this end, [redacted] supports any solution ensuring the safe custody of these assets. However, in this context, we want to stress that not all custody options are equally secure. In particular, house accounts entail higher risks of asset comingling than escrow or trust accounts. Consequently, it is critical that the SFC introduces specific requirements to ensure that funds will be ring-fenced and under safe custody, regardless of which approved option will licensed platform providers choose to use.

In addition, we encourage additional safeguards to ensure that funds are protected from comingling and are in safe custody. In particular, the SFC might consider requiring a standardised acknowledgement letter to be adopted when opening any account to hold assets on trust, similar to the requirement on intermediaries for opening an account for holding client assets with an authorised institution. The SFC could also draw examples from Hong Kong's SVF regime, and adjust accordingly under the "*same application, same risks, same rules*" principle.

Equally important is the composition of the funds, as we believe that VATP should hold only high-quality and sufficiently liquid assets to ensure business continuity. To this end, we wish to highlight that proposed assets usually described as such (e.g., cash, deposits, treasury bills and certificates of deposit) have varying degrees of value, liquidity and risk. Therefore, we would welcome additional guidelines on the composition of the required funds.

Moreover, we take note that under guideline 4.8, the SFC requires that licensed operators perform a daily reconciliation of all customers' assets. We welcome such a proposal and suggest that licensed platform providers perform the reconciliation using independent evidence such as online bank/custodian account statements.

**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?**

The nature of VA indicates that one of the most prominent risks for retail investors is associated to cybersecurity. Based on recent [research data](#), 2022 was the biggest year for crypto hacking, with \$3.8 billion stolen from cryptocurrency businesses, up from US\$3.3 billion in 2021 and only

US\$ 0.5 billion in 2021. Against this backdrop, custody of client virtual assets is of paramount importance, with incidents of hacking and theft, not being uncommon for virtual asset exchanges.

According to Global Digital Finance (GDF), an industry association for the blockchain technology, hackers often take one of the following main approaches:

- Gain access to accounts and closed-functionality through the hacking of the founders' accounts and then to use malicious programs from the arsenal of other known hacking attacks.
- Attack on the infrastructure of the trading platform/ exchange itself, through the hacking of a web application linking the customer to his money on the trading platform/ exchange servers or an attack on “hot wallets”.

We recommend that VATP be subject to the existing HKMA and SFC regulations and guidelines for Cybersecurity, Technology and Operational Resilience Risk, which is in line with the principle of "*same application, same risk, same regulation*". These should serve as a minimum requirement for licensed platform providers.

Moreover,        believes that storing virtual assets offline and inaccessible to third parties in cold wallets stands as the safest way of storage. Hence, we take note that the SFC requires licensed platform operators and their associated entities to store 98% of client virtual assets in cold storage except under limited circumstances permitted by the SFC, together with other requirements under 10.5 to 10.10. We agree with this proposal, and we also encourage the SFC to consider requiring that aside from internal audits, the licensed platform operators conduct periodical independent audits on the system and controls for managing the risks associated with the custody of virtual assets.

What is more, other than independent audit as post-event, SFC could also consider requesting licensed platform operators to conduct third party assessment with industry standards by certified technology security company prior to service onboarding as needed. The above requirements could provide objective assessment of the security protocols in managing client virtual assets.

In addition, we would encourage the SFC to adopt international best practices and tap into existing academic and industry research. Some examples are the 2021 [ASIFMA Best Practices on Digital Asset Exchanges](#) and the 2019 GDF [report on crypto-asset safe keeping](#).

**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?**

Derivatives are very important tools that help investors with hedging and other risk-mitigating activities. We also note the rapid growth of crypto derivatives, with recent [reports](#) suggesting that derivatives take a dominant position in the crypto space, representing in January 2023 70.3% of the entire crypto market, up from 68% in December 2022. Paragraph 4.9 of the VATP Terms and Conditions states, “*A Platform Operator should not conduct any offering, trading or dealing activities of virtual asset futures contracts or related derivatives*”. Moving forward, suggests introducing a principles-based approach rather than an outright ban, with specific conditions that ensure market integrity and investor protection. We think it is important to recognise that derivatives amplify certain risks and sometimes create new kinds of risk.

In this context, we recommend that the SFC allows licensed platform operators to provide only trading services in VA derivatives listed on regulated public exchanges. Moreover, given that VA derivatives are relatively nascent compared to the remaining derivatives market, we would invite the SFC to consider sharing a list of approved exchanges and jurisdictions with equivalent regulatory status.

We also believe that VA derivatives should be available only to experienced individuals or financial institutions who can use them for hedging purposes or as tools to optimize capital efficiency. Therefore, in line with the 2022 SFC [Joint Circular](#) on VA derivatives, we believe that VA derivatives should be classified as complex products and consequently offered only to professional investors.

In addition, such services should be offered exclusively on an execution basis, with platform providers not being allowed to conduct any solicitation of business or promotion of related activities. Moreover, trading should be conducted on an agency or riskless principal basis, and all trades must be cash-settled in fiat currency.

**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?**

takes note of the proposed adaptations to existing requirements to be incorporated into the VATP Guidelines and would like to share some additional suggestions on how to enhance the specific guidelines.

To begin with, we recommend that the requirements for customer complaints should be closely aligned with the HKMA SPM IC-4 Complaints Handling and Redress. This would ensure a level playing field between banks and other participating institutions.

Last, we believe that allowing proprietary trading through exceptions or on a case-by-case basis creates misguided incentives, and it is not in line with the “*same application, same risk, same rules*” principle. Therefore, we propose that the SFC introduces a blanket ban on proprietary trading.

**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.**

appreciates the guidance on the AML/TF risks concerning virtual assets and the AML/CFT regulatory requirements and standards for addressing such risks provided in Chapter 12 of the Guideline on Anti-Money Laundering and Counter-Financing of Terrorism. We believe that addressing AML requirements, the SFC needs to consider a typical flow of virtual asset trading involving all parties in a transaction, including (but not limited to) the identification and KYC of self-custody wallets, as well as the obligation of custody service providers, including that of VATP and all intermediaries.

Furthermore, we would like to share our feedback on the following sections:

- 12.3 'CDD – What CDD measure and when they must be carried out:
  - According to 12.3.1, occasional transactions (VA transfers and VA conversions) of less than HKD 8,000 do not require CDD or any onboarding review, while footnote 107 indicates “occasional transactions” do not apply to FIs that are LCs or SFC licensed VAS Providers. We want to clarify whether footnote 107 suggests that ‘FIs that are LCs or SFC-licensed VASPs’ may not allow occasional transactions.
  - Furthermore, we would like to ask for additional information about whether other requirements covered in Chapter 12, such as those covering unhosted wallets and other transaction-related due diligence, apply to occasional transactions.
- 12.6 CDD- Cross-border correspondent relationships.
  - Other than the cross-border component, we seek further guidance about differentiating between correspondent virtual assets services and the virtual transfer of a FI or VATP acting in the capacity of a “correspondent institution” or “Intermediary institution” to a VATP.
- 12.7 'Ongoing monitoring concerning virtual asset transactions and activities:
  - In 12.7.3, we seek further clarity on when the controls mentioned under 12.7.3 shall be performed - whether the expectation is to perform such post-transaction. We also ask for additional guidance on whether pre-transaction due diligence shall be conducted on a risk-based approach, further guidance on the expected risk-based approach, and examples of factors that should be considered in the risk-based approach.



- We recommend that the ongoing transaction monitoring requirements specified in 12.7.3 be included as one of the due diligence measures for cross-border relationships and VAS transfer counterparts (12.6) and included in the body content under section 12.6.
- Concerning 12.7.3(b), while we understand VATPs are required to maintain adequate and effective systems and controls to screen virtual asset transactions and the associated wallet addresses, we understand the capabilities of blockchain analytics providers are still under development. We seek steer from the SFC to drive the discussion for the industry, as well as industry standards, such as establishing a centralized database that the industry can access and utilize.
- 12.8 ‘Terrorist financing, financial sanctions and proliferation financing – Database maintenance, screening and enhanced checking’:
  - 12.8.3 suggests that a virtual asset transfer can be completed without prior screening or when any of the required originator/ recipient information is missing. While examples of risk mitigating measures were mentioned under footnote 123 (e.g., preventing the relevant virtual assets from being made available to the recipient or putting the receiving wallet on hold), we suggest including as a mandatory requirement that the transfer cannot be made available to the recipient until the missing information is made available to drive consistency across industry and require VATPs to make available the missing information within a reasonable timeframe to the counterparties.
- 12.11 ‘Virtual asset transfers’:
  - We seek clarification on whether this section only covers transactions involving a transfer of VA ownership.
  - We also seek confirmation on whether the due diligence requirements under this section also cover the conversion of VA to fiat transactions and VA to VA between the same owner.
  - Please also refer to the point raised in 12.6 above.
- 12.13 ‘VA transfer counterparty due diligence and additional measures:
  - We seek further guidance on the extent of due diligence to be performed over counterparties located in jurisdictions with no licensing regime to drive consistency across industry.

- We noted under Footnote 147 FI should “determine on a risk-sensitive basis the amount of information to collect about the VA transfer counterparty” and “endeavour to identify and verify the identity of the VA transfer counterparty”. We recommend Footnote 147 be incorporated into the main body of Chapter 12.13.7 and clarify whether SDD can be applied to licensed platform providers and the extent of EDD that shall be applied to them.
- 12.14 ‘Virtual asset transfers to or from unhosted wallets.’
  - We recommend 12.14.3(b) to be a mandatory requirement for the acceptance of unhosted wallets instead of being one of the examples of the risk mitigating measures that the VATPs can impose.
  - In the context of 12.6, the correspondent institution would indirectly facilitate VA activities of the non-resident customers of the respondent institution through an unhosted wallet. We would ask for additional guidelines to define “prohibited services” in the scope of wallet types, platforms, and ledger technology that could link to illicit behaviours.

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

does not have any comments on the Disciplinary Fining Guidelines.