



FSTB Consults on Regulating OTC Virtual Asset Trading

On 8 February 2024, the Financial Services and the Treasury Bureau (**FSTB**) published a [Consultation Paper](#) seeking views on proposals to regulate over-the-counter (**OTC**) trading of virtual assets (**VA**) under a new licensing regime for providers of VA OTC services under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap.615) (the **AMLO**).

The FSTB welcomes public feedback on its proposals and the deadline for responding to the Consultation Paper is 12 April 2024.

Background

The Government initiated the development of a comprehensive framework to regulate VA in its Policy Statement on Development of VA in Hong Kong back in October 2022.¹ In June 2023, a licensing regime for operators of VA trading platforms (**VATPs**) came into effect under amendments to the AMLO requiring VATP operators to be licensed by the Securities and Futures Commissions (the **SFC**) and to comply with the anti-money laundering and counter-terrorist financing (**AML/CTF**) provisions set out in Schedule 2 to the AMLO. Currently, only two VATPs have been licensed by the SFC.²

In 2023, several cases emerged involving shops providing OTC VA trading services to retail investors making false or misleading claims as to their licensed status. This has prompted the Government to regulate VA OTC services.

The FSTB estimates that there are approximately 200 physical VA OTC shops (including ATMs) operating in Hong Kong and about 250 digital platforms or active online posts on VA trading services in Hong Kong.

Hong Kong Proposed Regulation of VA OTC Service Providers

Licensing Requirement

The FSTB proposes that any person operating a VA OTC business in Hong Kong, or actively marketing the provision of VA OTC services to the Hong Kong public, will have to obtain a licence issued by the Commissioner of Customs and Excise (the **CCE**).

A VA OTC business will be defined as: (a) by way of business, provision of service of spot trade of any VA; (b) irrespective of whether the service is provided through a physical outlet (i.e. including ATMs) or other (e.g. digital)

platforms; and (c) explicitly excluding the operation of a VATP as already covered under the VATP licensing regime.

The definition will exclude peer-to-peer trading between individuals, unless the trade constitutes the business activity of either party.

Applicants for VA OTC licensing will need to be:

- a Hong Kong incorporated company with a permanent place of business in Hong Kong; or
- a company incorporated overseas but registered in Hong Kong under the Companies Ordinance (Cap. 622).

Permitted Activities

Under the proposed regime, licensed VA OTC operators will be allowed to engage in spot trade of any VA for any money, or vice versa. However, licensees will be prohibited from providing VA-to-VA trading services which require a VATP licence. To remit fiat money to clients, the OTC will need to apply for a money service operator licence. If the licensee will transfer VA to clients after sale, it must transfer the VA from its wallet registered with the CCE to a wallet for which the client provides proof of ownership and/or control. Other services such as VA advisory or referral services, and offering VA derivatives or other financial products (including staking, lending and margin trading), will not be permitted.

Types of VA Allowed to be Offered for VA OTC Trading

VA OTC licensees will only be allowed to offer spot trading in:

- VA that can be traded by retail investors on at least one SFC-licensed VATP; and
- Stablecoins issued by issuers licensed by the Hong Kong Monetary Authority.

This will restrict considerably the types of VA that can be the subject of VA OTC licensees' spot trading.

Under the SFC's VATP Guidelines, licensed VATP operators can only offer retail trading in VA that are "highly liquid".³ For a virtual asset to be considered "highly liquid", it must be an "eligible large-cap virtual asset", which is defined as a virtual asset that is included in a minimum of two acceptable indices issued by at least two independent index providers. An "acceptable index" is an index with a clearly defined objective to measure the performance of the largest virtual assets in the global market (for example, an index which measures the top 10 largest virtual assets) which is: (i) investible, meaning that the constituent virtual assets should be sufficiently liquid; and (ii) objectively calculated and rules-based. In practice, only the very largest VA, such as Bitcoin and Ethereum meet the definition.

The FSTB is currently consulting on a proposed licensing regime for issuers of fiat-referenced stablecoins. The proposed licensing regime will not apply to issuers of stablecoins referencing other assets (e.g. gold). Nor will it apply to algorithmic stablecoins which will not satisfy the requirement that the stablecoins are fully backed by reserve assets.

Proposed Requirements for VA OTC Licensees

The proposed regime will require an OTC licensee to:

- observe the AML/CTF requirements set out in Schedule 2 to the AMLO;
- appoint a competent Compliance Officer and a Money Laundering Reporting Officer;
- have a proper corporate governance structure;
- operate its business in a prudent and sound manner;
- act honestly, fairly, with due skill, care and diligence and in the best interest of its clients and the integrity of the market;

- have appropriate risk management policies and procedures to manage ML/TF, cybersecurity and other risks; and
- to keep records of transactions and fund flows.

Licensing period

To adjust for the ever changing VA market, the FSTB proposes an initial licence period of two years, with the possibility of renewal for an additional two years upon application to and approval from the CCE. This will enable the CCE to regularly monitor the licensee’s competence and its capacity to effectively conduct business.

Transitional Period Options

The FSTB is proposing a six-month transitional period before the commencement of the new licensing regime for VA OTC businesses already operating in Hong Kong. It is seeking comments on two alternative options:

Option 1 – No Deeming Arrangement

Under Option 1, existing VA OTC service providers will be allowed to continue operating during the six-month transitional period, but will need to apply to CCE for a licence within the first three months of that period. If they fail to do so, they will need to shut down their business before the end of the fourth month of the transitional period.

Option 2 – With Deeming Arrangement

As under Option 1, existing VA OTC service providers will be allowed to continue operating during the six-month transitional period and will need to apply to CCE for a licence within the first three months of that period. Applicants meeting the licensing requirements will be granted a “deemed licence” allowing them to continue operating after the end of the transitional period until the CCE determines to grant or refuse a licence.

Prohibition on Marketing Activities

Similar to the VATP licensing regime, the FSTB proposes to prohibit the active marketing of VA OTC services, in Hong Kong or elsewhere, to the Hong Kong public, unless the person hold a valid licence as a VA OTC service provider.

Powers of the CCE

The CCE will act as the VA OTC licensing authority and will have powers to:

- impose licensing conditions, including add to, vary or modify existing conditions;
- supervise the AML/CTF conduct of VA OTC licensees;
- enforce the statutory and regulatory requirements;
- enter licensees’ business premises to conduct routine inspections;
- investigate suspected non-compliances and remove evidence of the commission of an offence;
- carry out arrest and search; and
- impose disciplinary sanctions for non-compliance.

Sanctions

The following outlines the proposed penalties, which will depend on the nature and severity of the offence:

Offence	Proposed fines
Any person conducting regulated activities without a licence	Fine of HK\$1 million and imprisonment for two years
Knowingly issuing an advertisement relating to an unlicensed person’s provision of VA OTC services	Level 5 fine of HK\$50,000 and imprisonment for six months

Non-compliance with the statutory AML/CTF requirements	Fine of HK\$1 million and imprisonment for two years
Misconduct (e.g. contravening any other regulatory requirements)	Suspension or revocation of licence, reprimand, remedial order and/or pecuniary penalty (not exceeding HK\$500,000)
Engaging in fraudulent or deceptive behaviour in transactions involving VA	Fine of HK\$10 million and imprisonment for 10 years
Any person to make a fraudulent or reckless misrepresentation for the purpose of inducing another person to engage in a transaction involving VA.	Fine of HK\$1 million and imprisonment for seven years

Responding to the FSTB Consultation

Interested parties can respond to the consultation by submitting a written submission to vaotc-consult@fstb.gov.hk or by mail to Division 5, Financial Services Branch, Financial Services and the Treasury Bureau, 24/F, Central Government Offices, Tim Mei Avenue, Tamar Central, Hong Kong by 12 April 2024.

[1] Policy statement on the development of virtual assets (VA) in Hong Kong. Available at [P2022103000454_404805_1_1667173469522.pdf](https://www.info.gov.hk/p2022103000454_404805_1_1667173469522.pdf) (info.gov.hk)

[2] List of virtual asset trading platforms. Available at <https://www.sfc.hk/en/Welcome-to-the-Fintech-Contact-Point/Virtual-assets/Virtual-asset-trading-platforms-operators/Lists-of-virtual-asset-trading-platforms>.

[3] Paragraph 7.7(b) of the VATP Guidelines.

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CHARLTONS
易周律師行

Hong Kong Office

Dominion Centre 12th Floor
43-59 Queen's Road East Hong Kong

enquiries@charltonslaw.com

www.charltonslaw.com
Tel: + (852) 2905 7888
Fax: + (852) 2854 9596