

A new regime for Hong Kong's Virtual Asset Service Providers is coming. Beosin will support its implementation.



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**This article was co-authored by Beosin guest authors, lawyers Wang Liao and Jiening Gu.*

In response to the “Policy Statement on the Development of Virtual Assets in Hong Kong” issued in October 2022, promoting the development of Hong Kong as an international virtual asset center, the latest amendments to the Anti-Money Laundering and Terrorist Financing Ordinance 2022 (AMLO) were passed by the Hong Kong Legislative Council on 7 December 2022. This means that Hong Kong’s new licensing regime for Virtual Asset Service Providers (VASP regime) will come into force on 1 June 2023.

On 20 February 2023, the Hong Kong Securities and Futures Commission (SFC) released the VASP Consultation Paper, and then the VASP Consultation Summary was issued on 23 May, which clarifies that the Guidelines Applicable to Operators of Virtual Asset Trading Platforms (VASP Guidelines) will come into force on 1 June 2023. This marks the Hong Kong government’s proactive approach in welcoming the new VASP regime with an open attitude towards the virtual asset market through more than half a year of planning.

When the policy comes into effect:

All centralized virtual asset exchanges operating in Hong Kong or actively promoting their services to Hong Kong investors, whether or not they offer securities-based token trading services, will be required to be licensed and regulated by the SFC.

SFC will follow through on allowing licensed virtual asset exchanges to offer services to retail investors in the second half of the year, but only tokens that are not securities and are highly liquid in one of the traditional financial indices can be offered to retail investors.

The regulatory arrangements for stablecoins will be implemented in 2023/24 and a licensing and permitting regime for stablecoin-related activities will be established. Until stablecoins are regulated, SFC believes that stablecoins should not be included in retail trading.



This article will help you better understand the upcoming VASP licensing regime for virtual assets in Hong Kong that will be implemented on June 1.

Background of the Revision of the VASP Regime

SFC is ahead of other jurisdictions, having gradually established a “voluntary licensing” regime for security-based token virtual assets as early as 2018. **This regime explicitly excludes SFC from regulating platforms that only trade in non-securities-based virtual assets or tokens.** Under the “voluntary licensing” regime, virtual asset trading platforms that engage in non-securities-based tokens are not required to be licensed. Only two virtual asset exchanges have been licensed to trade under the “voluntary licensing” regime: OSL Digital Securities Limited, a subsidiary of BC Technology Group, and Hash Blockchain Limited, a subsidiary of HashKey Group were

awarded a Type 1 (dealing in securities) licence and a Type 7 (providing automated trading services) licence.

Today, the virtual asset industry has undergone a dramatic transformation, and the original “voluntary licensing” regime no longer covers today’s market, which is dominated by retail investors and mainly deals in non-securities based tokens. In order to comprehensively regulate all centralized virtual asset trading platforms in Hong Kong and to implement the latest Financial Action Task Force (FATF) standards, the Hong Kong government has amended the Anti-Money Laundering Ordinance and established a new VASP “mandatory licensing” regime to strike a balance between investor protection and market development. **Upon the implementation of the VASP regime, all centralized virtual asset exchanges operating in Hong Kong or actively promoting their services to Hong Kong, whether or not they offer securities-based token trading services, will be required to be licensed and regulated by the SFC.**

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	旧制度	新法规
法规文件	《立场书：监管虚拟资产交易平台》 附录《适用于虚拟资产交易平台营运者的发牌 条件和条款及条件》	《2022 年打击洗钱及恐怖分子资金筹集条例》 《适用于虚拟资产交易平台营运者的指引》
牌照类型	1号牌 + 7号牌（证券型代币）	1号牌 + 7号牌（证券型代币） VASP 牌照（非证券型代币）
发牌制度	自愿发牌	强制发牌
持牌主体	仅针对提供证券型代币交易服务的 中心化虚拟资产交易所	所有在港或离岸运营， 针对香港用户的中心化虚拟资产交易所 （不限于证券型代币）
交易所客户	仅限专业投资者	SFC 将于下半年落实向零售投资者提供服务细则
监管重心	反洗钱、反恐怖主义融资	反洗钱、反恐怖主义融资、 投资者保护

Compliance Requirements for Exchanges

According to the VASP Guidelines, a centralized virtual asset exchange needs to meet the following compliance requirements in its operations:

A. Keep Customer Assets Safe

The platform operator shall hold customer monies and customer virtual assets in trust (TCSP trust license) through a wholly owned subsidiary (i.e., an “associated entity”). The Platform Operator shall ensure that no more than 2% of the Customer’s Virtual Assets are stored in the Online Wallet.

In addition, since access to virtual assets requires the use of a private key, safekeeping of virtual assets is basically about secure management of relevant private keys. The Platform Operator shall establish and implement written internal policies and governance procedures for private key management to ensure that all cryptographic seeds and keys are securely generated, stored, and backed up.

In addition, the Platform Operator shall not deposit, transfer, lend, pledge, re-pledge or otherwise deal in or create any encumbrance on the title of the Customer’s Virtual Assets. It shall also maintain insurance that covers the risks involved in the safekeeping of the Customer’s Virtual Assets.

B. Know Your Customer (KYC)

The Platform Operator shall take all reasonable steps to establish the true and full identity, financial status, investment experience, and investment objectives of each of its customers. In addition, the platform operator shall ensure that the customer is fully aware of the virtual assets (including awareness of the risks involved) before providing any services to the customer.

C. Anti-money laundering/countering terrorist financing

Platform operators shall establish and implement adequate and appropriate anti-money laundering/terrorist financing policies, procedures, and controls. Platform operators may use virtual asset tracking tools to trace the transactions of specific virtual assets.

D. Prevention of Conflicts of Interest

Platform operators should not engage in proprietary trading or proprietary bookmaking activities and should have policies in place to manage internal employee transactions in virtual assets to eliminate, avoid, manage, or disclose actual or potential conflicts of interest.

E. Inclusion of Virtual Assets for Trading

The platform operator shall establish a function responsible for establishing, implementing, and enforcing guidelines for the inclusion of virtual assets and guidelines for the termination, suspension, and withdrawal of trading in virtual assets, together with the options available to customers.

In addition, the Platform Operator shall conduct a reasonable due diligence review of any Virtual Assets to ensure that such Virtual Assets continue to meet all guidelines.

F. Prevention of Market Manipulation and Irregularities

The Platform Operator shall establish and implement written policies and monitoring measures to identify, prevent and report any market manipulation or irregular activities on its Platform. Such measures shall include the restriction or suspension of trading upon detection of manipulative or irregular activities. The Platform Operator shall use an effective market surveillance system provided by a reputable independent vendor to identify, monitor, detect, and prevent such manipulative or irregular trading activities and provide SFC with access to this system.

G. Accounting and Auditing

The platform operator should select auditors with appropriate skill, care, and diligence and consider their experience and ability to conduct audits for the virtual asset-related business and the platform operator. In addition, the platform operator should submit an auditor's report each fiscal year containing a statement of whether there has been a breach of applicable regulatory requirements. In addition, the SFC requires the platform operator to provide monthly reports on its business activities to the SFC within two weeks after the end of each month or upon request by the SFC.

H. Risk Management

Platform operators should have a robust risk management framework in place to enable them to identify, measure, monitor, and manage all risks arising from their business and operations. Platform operators should also require customers to pre-fund their accounts and shall not provide any financial facilities to customers for purchasing virtual assets.



Conclusion

With the imminent implementation of the VASP regime, VASP license applicants should prepare in advance for business compliance and the associated license application, whether they are: (1) virtual asset exchanges already operating in Hong Kong; (2) virtual asset exchanges operating offshore that actively promote their services to Hong Kong; (3) virtual asset exchanges that intend to operate in Hong Kong; or (4) traditional financial institutions that intend to venture into virtual asset exchanges.

We can see that a change of era is inevitable. With the fall of FTX, the tightening regulation, and political games in the U.S., Hong Kong will regain its glory as a “crypto center” based on its traditional financial foundation and perfect law system, as well as the solid resources of the full stream of service and product support from the mainland.

Beosin is a leading global blockchain security company co-founded by several professors from world-renowned universities and there are 40+ PhDs in the team. It has offices in Singapore, South Korea, Japan, and other 10+ countries. With the mission of “Securing Blockchain Ecosystem”, Beosin provides “All-in-one” blockchain security solution covering Smart Contract Audit, Risk Monitoring & Alert, KYT/AML, and Crypto Tracing. Beosin has already audited more than 3000 smart contracts including famous Web3 projects PancakeSwap, Uniswap, DAI, OKSwap and all of them are monitored by Beosin EagleEye. The KYT AML is serving 100+ institutions including Binance. You are welcome to contact us.

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Reference:

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