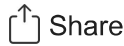


Learn about Hong Kong's VASP licence application details and get ready for the new regime



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

Over the past few years, Hong Kong has seen rapid development in FinTech, presenting a thriving virtual asset ecosystem. To promote the development of Hong Kong as an international virtual asset hub, the HKSAR Government has launched several documents to support Web3, such as the Policy Statement on Virtual Asset Development in Hong Kong published in October 2022. In a positive response to this policy, the Hong Kong Legislative Council passed the latest amendments to the Anti-Money Laundering and Terrorist Financing Ordinance 2022 (AMLO) on 7 December 2022, which means that Hong Kong's new Virtual Asset Service Provider licensing regime (VASP regime) will be officially implemented from 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:

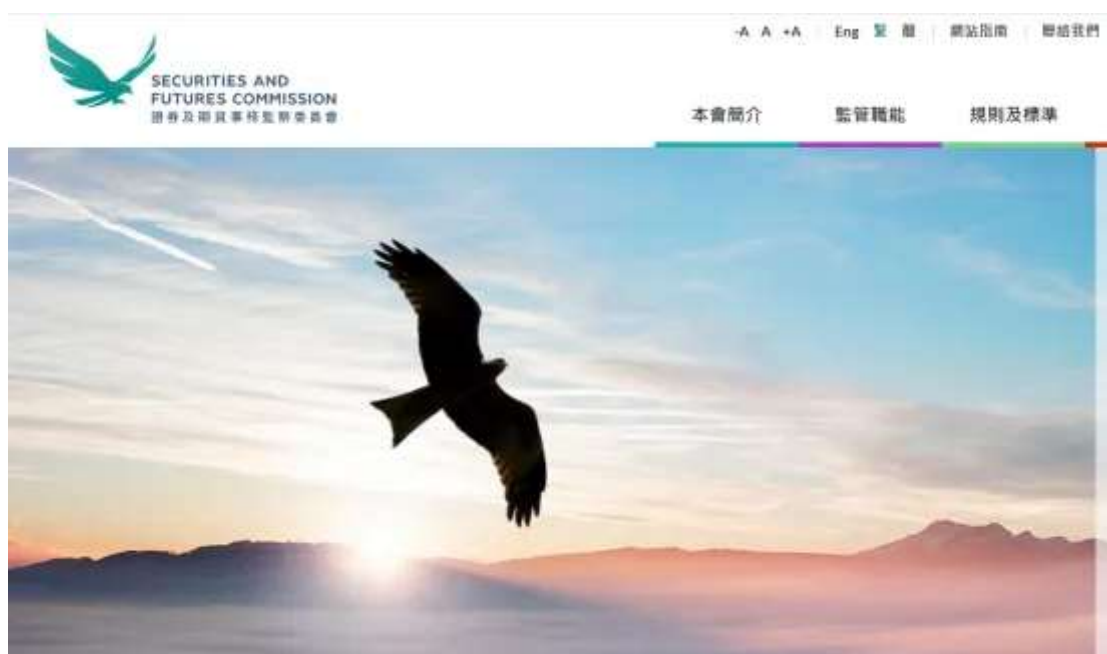
All centralized virtual asset exchanges operating in Hong Kong or actively promoting their services to Hong Kong investors, whether or not they offer securities-based token trading services, will be required to be licensed and regulated by the SFC.

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 take you through the application details of the upcoming Hong Kong VASP licensing regime that will be implemented on June 1.



Background of the revision of the VASP system

In the VASP Consultation Paper, SFC clearly explained the background of the revision of the new VASP regime: In the ongoing crypto winter, there have been a series of crashes, which have intensified the risks in the virtual asset market, especially the collapse of FTX, causing significant losses to millions of investors. The risks posed by the increasing integration of virtual asset markets with traditional financial markets highlight the importance and necessity of effective regulation of the virtual asset industry. Major jurisdictions around the world are shifting their regulatory approach from lax (i.e., regulation from an anti-money laundering and payments perspective) to more comprehensive (i.e., regulation from an investor protection perspective).

SFC took the lead over other jurisdictions by gradually establishing a regulatory framework for virtual assets back in 2018, primarily for virtual asset service providers offering security-based token services. Today, the industry has undergone a dramatic

transformation. In order to comprehensively regulate all centralized virtual asset trading platforms in Hong Kong and to implement the latest FATA standards, the Hong Kong government has passed the Amendment Ordinance 2022 by way of legislation and established a new VASP regime with a view to striking a balance between investor protection and market development.

<div><div><div>SECURITIES AND FUTURES COMMISSION 證券及期貨事務監察委員會</div></div><div>香港虚拟资产交易所 新旧两套发牌制度对比</div><div><div>BEOSIN Blockchain Security</div><div>Web3 小律</div><div>Meta 区块链</div></div></div>		
	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运营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运营者的指引》
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

Virtual Assets and Virtual Asset Services

In the context of the “mandatory licensing” of VASP, it is important to clarify what virtual assets and virtual asset services are.

What are virtual assets?

Under the AML Regulation53 ZRA and VASP guidelines, a Virtual Asset (VA) is broadly defined as

- (a) A representation of value in cryptographically protected digital form that meets the following descriptions:
- (1) Expression in the form of a unit of computation or a store of economic value;
 - (2) Meets one of the followings:
 - A. is or is intended to be used as a publicly accepted medium of exchange for one or more of the following purposes: (I) payment for goods or services; (II) liquidation of a

debt; (III) investment;

or B. to provide the right, entitlement, or means to vote on the management, operation, or governance of any matter relating to the cryptographically protected digital form value or any change in the terms of any arrangement applicable to the cryptographically protected digital form value;

(3) can be transferred, stored, or traded by electronic means;

(4) has such other characteristics specified by SFC by notice published in the Gazette;

(b) Representation of value in digital form as a virtual asset as prescribed by the Hong Kong Financial Services and the Treasury Bureau by notice published in the Gazette.

© Any security-based token that constitutes a “security” as defined in section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance.

Under the AMLO 53 ZRA, the following items are excluded from the definition of VA:

(1) Digital currencies (CBDC) issued by a central bank, an entity performing the functions of a central bank, or by an entity authorized by a central bank to issue on behalf of a central bank;

(2) Limited use digital tokens (non-transferable, non-exchangeable, and non-substitutable in nature, such as gift cards, customer loyalty reward programs, and electronic payment services);

(3) Stored value payment instruments (regulated by the Payment Systems and Stored Value Payment Instruments Ordinance);

(4) Securities or futures contracts (regulated under the Securities and Futures Ordinance).

The definition of VA in the AMLO will cover most of the virtual currencies in the market, including BTC, ETH, Stablecoin, Utility Token, and Governance Token. For Stablecoin, SFC also clearly stated in the Consultation Summary: HKMA has issued the Consultation Summary of the Discussion Paper on Crypto Assets and Stablecoin in January 2023, indicating that the regulatory arrangements for Stablecoin will be implemented in 2023/24, and a licensing and permitting system for Stablecoin-related activities will be

established. Until stablecoins are regulated, SFC believes that stablecoins should not be included in retail trading.

The attributes of NFT are tied to the properties of the asset behind it, which is not yet clearly defined under the VASP regime. In the June 6, 2022 release warning investors of the risks of NFTs, the SFC stated that if an NFT is a truly digital representation of a collectible (artwork, music, or film), the activity associated with it is not regulated by the SFC. However, some NFTs cross the line between collectibles and financial assets and may have the attributes of “securities” under the Securities and Futures Ordinance and will therefore be regulated.

What is a VAS

According to Schedule 3B of the AMLO and the VASP guidelines, activities related to Virtual Asset Services (VA Services) are defined as operating a virtual asset exchange, i.e:

(a) provides, using an electronic facility, a service that is consistent with the following descriptions:

(1) The service:

A. offers to buy or sell virtual assets are frequently made or accepted in a manner that creates a binding transaction or results in a binding transaction arising from the making or acceptance of such offers in such a manner

B. persons regularly introduce or identify themselves to each other with a reasonable expectation that they will negotiate or complete a sale or purchase of virtual assets in a manner that results in a binding transaction or causes a binding transaction to arise;

(2) In the case of the service, the customer’s money or the customer’s virtual assets are in the direct or indirect possession of the person providing the service; and

(b) any virtual asset trading activities and incidental services provided by the platform operator to its customers outside the platform, and any activities undertaken in connection with virtual asset trading activities outside the platform.

Therefore, for (1) a centralized virtual asset exchange operating in Hong Kong, and (2) a centralized virtual asset exchange operating offshore that actively promotes its services to investors in Hong Kong, engaging in the above-mentioned relevant activities would fall within the scope of virtual asset services. Under the AMLO 53 ZRD, any entity operating virtual asset services must obtain a VASP license from the SFC.

Currently, other businesses such as market makers, proprietary trading, futures contracts, and derivatives are not allowed to be conducted except for the above-mentioned virtual asset services, but we do not rule out that other virtual asset services will be included by the Financial Services and the Treasury Bureau of Hong Kong by way of gazettal in the future.

VASP License Application

Under the new VASP regime, applicants will be licensed and regulated by the SFC under the AMLO and the VASP guidelines. The application for a VASP license has very high requirements for companies and their personnel:

A. Company: 1. Have a company established in Hong Kong with a fixed office location; 2. Need to have a registered capital of no less than HK\$5 million and liquidity of HK\$3 million or more; 3. A subsidiary or affiliated company must have a Hong Kong Trust TCSP license for virtual asset custody.

B. Personnel: 1. The applicant, responsible officer, licensed representative, director and ultimate owner of the VASP must meet the SFC's fit and proper test; 2. At least 2 responsible officers (ROs) with experience in virtual asset services must be appointed and the following conditions must be met: at least one RO must be an executive director of the VASP, at least one RO must be habitually resident in Hong Kong, and at least one RO must be available at all times 3. At least one RO licensed representative; and 4. an auditor with experience in virtual asset operations.

C. Compliance requirements: In addition to meeting the company qualification and company personnel requirements, a series of compliance systems such as virtual asset trading business rollout assessment reports, AML/CTF, client asset management, etc. are also required to be met. According to the VASP Guidelines, the detailed requirements for these applications also include: fit and proper person requirements, competency requirements, ongoing training requirements, business conduct principles, financial soundness, operation of virtual assets on the platform, prevention of market manipulation and irregularities, trading with clients, protection of client assets, governance, supervision and internal controls, cyber security, avoidance of conflicts of interest, record keeping, auditing, ongoing reporting and notification responsibilities, etc.

Dual Licensing System

Under different regulatory authorizations, SFC will regulate securities-based token transactions conducted by virtual asset exchanges under the Securities and Futures Ordinance (Type 1 licence + Type 7 licence); and will also regulate non-securities-based token transactions conducted by virtual asset exchanges under the Anti-Money Laundering Ordinance (VASP license).

VASP 双重牌照制度			
	适用法规	发牌制度	举例
证券型代币交易所	《证券及期货条例》	1 号牌 + 7 号牌	代币化绿色债券
非证券型代币交易所	《2022 修订条例》	VASP 牌照	BTC / ETH / Solana 等

Considering that the nature of virtual assets may evolve over time, e.g. from non-securities based tokens to securities based tokens, in order to avoid any breach of the licensing regime, Virtual Asset Exchanges should obtain dual licensing and approval from SFC under both the SFO and AMLO (i.e. apply for both VASP licence and licence 1, licence 7).

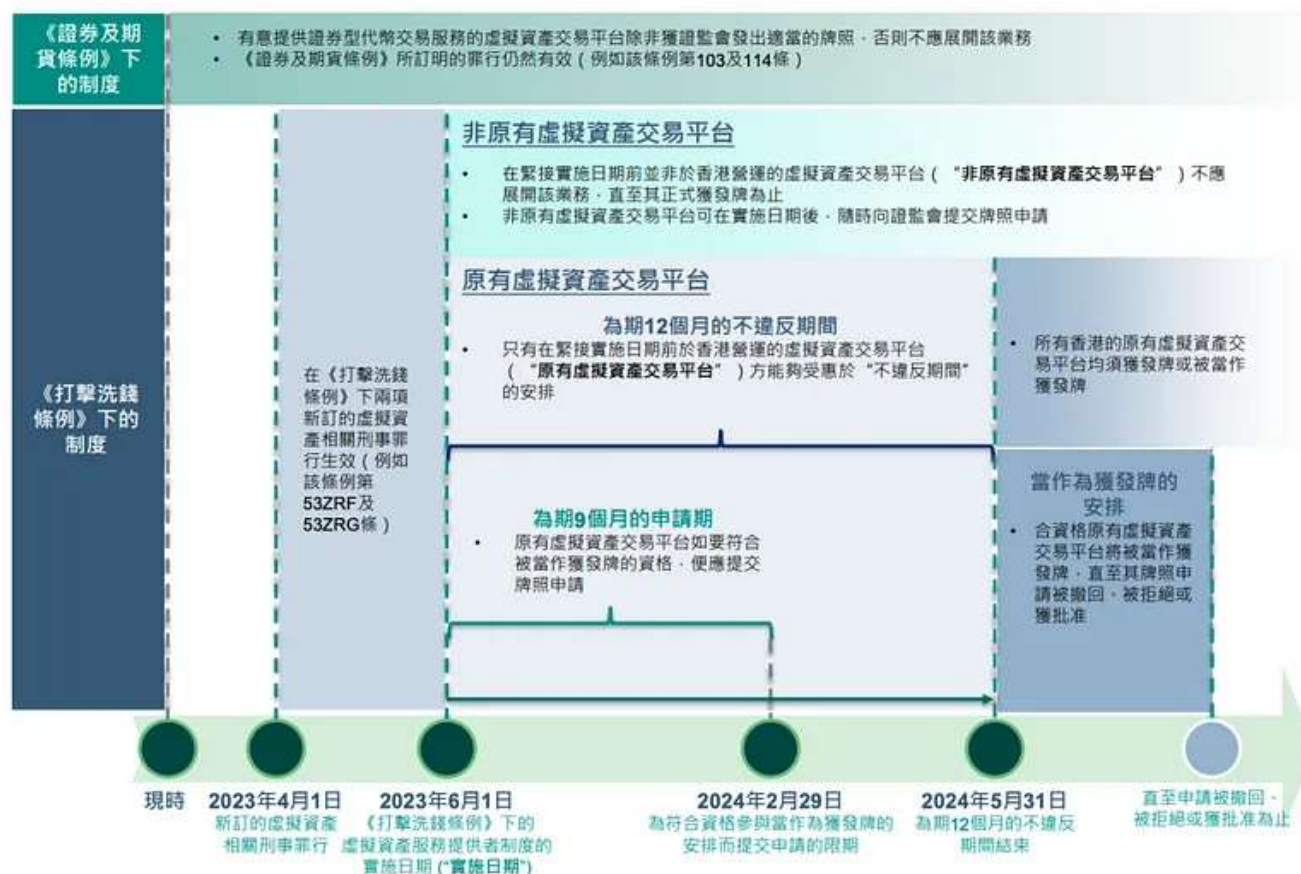
To simplify the dual licensing application process, applicants who wish to apply for a licence under both the current regime of the SFO and the VASP regime of the AML Ordinance will only need to submit a consolidated application form online and indicate that they are applying for both licences at the same time.

SFC expects that a dual-licensed platform operator will only need to make one submission to satisfy the licensing or notification requirements of both the current regimes.

Transitional Arrangements

The AMLO provides transitional arrangements for “pre-existing virtual asset exchanges” by setting a transitional period until June 1, 2024. Exchanges that are operating in Hong Kong and have a meaningful and substantial business prior to June 1, 2023, including (1) exchanges that have or are applying for a license under the SFO and (2) unlicensed exchanges that conduct business with non-securities tokens under the SFO, are eligible to participate in the transitional arrangements.

To be eligible to participate in the transitional arrangements, an exchange must meet the conditions set out in Schedule 3G to the AMLO in order to continue to operate in Hong Kong from 1 June 2023 to 31 May 2024 and will be subject to the VASP licensing regime from 1 June 2024.



If the operator applies to the SFC within 9 months of 1 June 2023 and confirms that it will comply with the regulatory requirements set by the SFC, the operator may be deemed to be licensed until the SFC decides on its licence application and will be able to continue to provide services during this period until (i) the end of the first 12 months, (ii) withdrawal of the application, (iii) rejection of the application by the SFC and (iv) the SFC grants a license, whichever is earlier.

If its application for a VSP license is denied by the SFC, it must terminate its VSP business within 3 months or by June 1, 2024, whichever is later. During this period, the operator may only take actions that are solely to shut down its services. The Operator may apply to the SFC for an extension of the closure period that the SFC deems appropriate.

For “non-existing virtual asset exchanges” that plan to offer virtual asset services in Hong Kong after 1 June 2023, they must apply to the SFC and be granted a VASP licence

in advance.

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.

The VASP regime is being implemented through licensed exchanges, and KYC and anti-money laundering compliance is a top priority in this context. After the first step of “channeling”, we will see a series of rules and regulations on opening up retail investors and protecting them in the second half of the year. Only based on meeting regulatory requirements can the exchanges participate in the distribution of this huge cake and promote the long-term development of the market.

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.

Introduction of two co-authors of this article:

Wang Liao , lawyer of Beijing Deheng (Hangzhou) Law Office,
liaowang@dehenglaw.com, Official Accounts: Web3 Small Law

Jiering Gu, Senior Counsel of Shanghai Mankun Law Office,
gujiening@mankunlaw.com, Official Accounts: Mankun Blockchain

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