$$R_{\mu\nu} - \frac{1}{2}Rg_{\mu\nu} + \Lambda g_{\mu\nu} = \kappa T_{\mu\nu}$$

Response to Public Consultation on Legislative Proposal to Regulate Dealing in Virtual Assets

Hong Kong Institute of Physics Limited

Business Registration No: 71858488

Contact person Dr. Joseph C Wang (joequant@hkphysics.hk)

- (phone/whatsapp) +852 6352 9195
- (telegram) joequanthk
- (wechat) joequant

Contact address 22/F Room 2202 Kaiser Centre 18 Centre Street Sai Ying Pun

The Hong Kong Institute of Physics Limited is pleased to respond to the request for public consultation on the legislative proposal to regulate dealing in virtual assets. Our research institute is a small boutique research institute involved in developing supercomputing and blockchain computation systems in support of global physics efforts such as the Circular Electron-Positron Collider and the International Lunar Research Station as well as working on projects for web3 and blockchain development.

These efforts come in a critical period of human history. Within the period of 15th Five-Year Plan from 2026 to 2030, humanity will again set foot on the moon after an absence of two generations. As a science research institute, we are committed to ensuring that when humanity returns to the moon, this will be merely the first step in further colonization of the solar system.[1]

We intend that history take a different course than the one that occurred in 1971, when President Richard Nixon cancelled much of the post-Apollo programs of the United States or in 1433, when the Ming Dynasty ended the maritime exploration voyages of Zheng He. We believe that the cessation of maritime exploration activities by China when taken with the continued exploration by Prince Henry and the European powers put China on a historical path to economic and social ruin with the Opium Wars and the century of humiliation. It has taken several centuries for the Chinese nation to finally overcome this mistake, and the past few centuries have given China painful lessons on the need to develop science and technology, that we shall not easily forget.

Published Aug 27, 2025

The development of science and technology is not merely a project of building machines, but it is also a project of building institutions and of mobilizing social and

[1] We choose to go to the moon in this decade and do the other things, not because they are easy, but because they are hard, because that goal will serve to organize and measure the best of our energies and skills, because that challenge is one that we are willing to accept, one we are unwilling to postpone, and one which we intend to win, and the others, too. - President John F. Kennedy

financial capital. As the capitalist region and “financial sandbox” for the People’s Republic of China, the Hong Kong Special Administrative Region has a sacred responsibility to play a positive role in creating the financial infrastructure necessary for the People’s Republic of China to fulfil its duty in advancing the humanity’s efforts to advance the colonization of space and come in peace for all mankind.

In both the space race and in the world of international finance, we consider that competition with other powers can be a positive thing, and competition produces excellence among all competitors. In these efforts, we wish rival centers great success, as their success will push Hong Kong to do better, and this positive competition will result in benefits for all mankind.

It is therefore with great frustration that we have seen Hong Kong unable to live up to its potential in financial, web3, and blockchain technologies. Hong Kong **invented** stablecoins and perpetual futures, and yet these technologies have withered on the vine in Hong Kong while being developed elsewhere. In a world of intense geopolitical and commercial competition, why are we followers when we should be leaders? Why are we so behind? As patriots who love Hong Kong and love China, we find this situation intolerable.

It is with this context, that we are pleased to offer constructive suggestions on the upcoming legislation. Our suggestions are based on the basic constitutional principles of Hong Kong, namely Articles 109, 112, 115, and 118 of the Basic Law.

Basic Law Articles 109, 112, 115, 118

> **Article 109** The Government of the Hong Kong Special Administrative Region shall provide an appropriate economic and legal environment for the maintenance of the status of Hong Kong as an international financial centre.
>
> **Article 112** No foreign exchange control policies shall be applied in the Hong Kong Special Administrative Region. The Hong Kong dollar shall be freely convertible. Markets for foreign exchange, gold, securities, futures and the like shall continue.
>
> The Government of the Hong Kong Special Administrative Region shall safeguard the free flow of capital within, into and out of the Region.
>
> **Article 115** The Hong Kong Special Administrative Region shall pursue the policy of free trade and safeguard the free movement of goods, intangible assets and capital.
>
> **Article 118** The Government of the Hong Kong Special Administrative Region shall provide an economic and legal environment for encouraging investments, technological progress and the development of new industries.

1. Q1. Do you agree with the proposed definition and scope of VA dealing services? Are there any potential exemptions which you consider appropriate?

Yes We are in general agreement with the proposed definition and scope of the VA dealing service

Yes There are potential exemptions which we believe are appropriate. This consist of

- exemptions arising from the definition of virtual asset and stablecoins and
- exemptions on the persons and activities to be subject to licencing

We believe that Hong Kong has made some critical but not fatal missteps in developing its virtual asset policy and has moved from a leader in this field to a follower.

In developing the capitalist system of Hong Kong, patriotic forces should strive to emulate best practices from other capitalist jurisdictions. Due to Hong Kong's history under British administration, its administrative practice has been to model its financial regulation on that of the United Kingdom and the European Union. However, we believe this to be unwise. As many in the industry have noted, there is a lack of dynamism in the development of science and technology in the United Kingdom and the European Union[2]. This lack of dynamism is in contrast to that of other capitalist jurisdictions such as the United States, Dubai, and Singapore, and we believe that much of the problem with Hong Kong's virtual asset environment lies in it having copied worst practices of the United Kingdom rather than best practices from other capitalist jurisdictions.

We are concerned that a regulatory framework based on United Kingdom or European Union practices has led Hong Kong to a path of overregulation and when combined with local business pressures has resulted in rent-seeking, local protectionist, monopolistic behaviour. We are concerned that copying worst practices rather than best practices has led to local market actors seeking to create what is known in India as a "licence raj" and to attempt to create local cartels to monopolize virtual asset and stablecoin trading. Due to the open and borderless nature of virtual assets and stablecoins, this has left Hong Kong at a competitive disadvantage against other financial centers, resulting in rent seekers getting a local monopoly on nothing.

Going forward, we believe that the HKSAR should correct this mistake developing regulations based on Hong Kong's own historical capitalist traditions of market-driven innovation and positive non-interventionism and oppose rent-seeking, regulatory capture, and local protectionism, as well as taking note of movement in other capitalist jurisdictions, particularly the United States and bipartisan efforts there via the GENIUS Act and Project Crypto toward less regulation.

[2]The difficulties faced by the European Union are based summarized in the The future of European competitiveness: Report by Mario Draghi (https://commission.europa.eu/topics/eu-competitiveness/draghi-report_en)

We note that with the new administration under Donald Trump, both his supporters in the Make American Great Again ("MAGA") movement and his critics in the anti-MAGA movement have cooperated to fundamentally change the direction of virtual asset and stablecoin policy in the United States toward a new philosophy of market-driven light-touch regulation, that going forward Hong Kong must respond to this efforts, by drafting regulations which avoid the mistakes of the United Kingdom and at previous efforts at virtual asset regulation in Hong Kong.

The provisions of the Basic Law are critical in this effort, because the Basic Law limits the powers of the administration, and allows for regulatory space in which market actors may grow and flourish. We believe in maintains and expanding this space for market driven growth.

As we believe in a light-touch minimal regulatory system in which the capitalist market leads innovation in Hong Kong, we therefore focus our remarks on limiting the scope of the proposed legislation, and our comments can be divided into exemptions arising from the definition of virtual asset and stablecoin and exemptions on the persons and activity to be subject to licencing

1.a. Exemptions arising from the definition of virtual asset and stablecoin

We begin with the definition of "virtual asset" as defined in the Anti-Money Laundering and Counter-Terrorism Finance Ordinance (Cap. 615) s. 53ZRA and the definition of "stablecoin" in the Stablecoin Ordinance (Cap. 656) s. 3.

Anti-Money Laundering and Counter-Terrorism Finance Ordinance (Cap. 615) s. 53ZRA

- (1) In this Ordinance— VA or virtual asset (虛擬資產), subject to subsection (2), means—
  - (a) a cryptographically secured digital representation of value that —
    - (i) is expressed as a unit of account or a store of economic value;
    - (ii) either—
      - (A) is used, or is intended to be used, as a medium of exchange accepted by the public, for any one or more of the following purposes—
        - (I) payment for goods or services;
        - (II) discharge of a debt;
        - (III) investment; or
      - (B) provides rights, eligibility or access to vote on the management, administration or governance of the affairs in connection with, or to vote on any change of the terms of any arrangement applicable to, any cryptographically secured digital representation of value;

        - (iii) can be transferred, stored or traded electronically; and
        - (iv) satisfies other characteristics prescribed by the Commission under subsection (3)(a); or
    - (b) a digital representation of value prescribed as a virtual asset by notice published under subsection (4)(a).
- (2) A digital representation of value is excluded from the definition of VA in subsection (1) if—
    - (a) it—
        - (i) is
            - (B) issued by a government of a jurisdiction, or by an entity authorized by the government of a jurisdiction and acting pursuant to an authority to issue currency in that jurisdiction;

Stablecoins Ordinance (Cap. 656) s. 3

- (1) For the purposes of this Ordinance, a stablecoin is a cryptographically secured digital representation of value that—
    - (a) is expressed as a unit of account or store of economic value;
    - (b) is used, or intended to be used, as a medium of exchange accepted by the public for any one or more of the following purposes—
        - (i) payment for goods or services;
        - (ii) discharge of a debt;
        - (iii) investment;
    - (c) can be transferred, stored or traded electronically;
    - (d) is operated on a distributed ledger or similar information repository; and
    - (e) purports to maintain a stable value with reference to—
        - (i) a single asset; or
        - (ii) a pool or basket of assets.
- (2) However, a digital representation of value is not a stablecoin if—
    - (a) it is issued by—
        - (i) a central bank;
        - (ii) an entity that performs the functions of a central bank;
        - (iii) an entity authorized by a central bank on the central bank's behalf;
        - (iv) a government of a jurisdiction; or
        - (v) an entity authorized by a government of a jurisdiction that is acting in accordance with an authority to issue currency in that jurisdiction;

We presume that the term "the public" refers to the Hong Kong public as the Hong Kong Special Administration Region being a local government of the People's Republic of China can only exercise powers granted to it by the Basic Law and has no

authority to legislate restrictions on persons that do not have a nexus with Hong Kong and its authority to regulate cross-border transactions are limited by the Basic Law Articles 112 and 115.

We note that there are two classes of commonly used tokens that would not be subject to the virtual asset dealer licensing assuming that the Legislative Council were to take the existing definition of "virtual asset" or "stablecoin"

- a) tokens that are used or intended to be used solely by professional investors or through private placements. This definition excludes most RWA tokens as they are intended for professional investors or through private placements and are not used or intended to be used by the Hong Kong public.
- b) tokens issued under the authority of the United States GENIUS Act (Public Law 119-27) as they they are issued by an entity authorized to do so by the Congress of the United States acting pursant to its authority under Article I, Section 8, Clause 5 of the Constitution of the United States to coin money and regulate the value of money and foreign coins and Article I, Section 8, Clause 18 to make all laws necessary and proper for carrying out these foregoing powers.

With respect to the impact of recent legislation from the United States, we note that both the amendments to the Anti-Money Laundering and Counter-Terrorism Finance Ordinance and the new Stablecoins Ordinance were passed before the US GENIUS Act was enacted, and did not foresee that the United States would engage in a wide project of virtual asset and stablecoin liberalization under the administration of President Donald Trump and a bipartisan legislative coalition led by Democratic Senator Kirsten Gillibrand from New York and Republican Senator Cynthia Lummis from Wyoming.[3]

We note that any tokens issued under the authority of the GENIUS Act are unregulated under current or anticipated legislation, and would not require a virtual asset dealing licence to transact in, assuming that the enabling legislation uses the existing definitions of virtual asset and stablecoin. This consequence may have been unforeseen, but we consider this a natural consequence of Hong Kong having copied "worst practices" of the United Kingdom and the European Union rather than the "best practices" of the United States, Singapore, and Dubai.[4]

[3]We note, in passing, that Senator Gillibrand is an outspoken opponent of the "Make America Great Again" or MAGA movement led by President Donald Trump while Senator Lummis is an outspoken supporter of the MAGA movement, and we would like to take the efforts of Senators Lummis and Gillibrand to work with each other on the GENIUS Act as an inspiration for patriotic forces in Hong Kong as to how patriots from different social sectors and with different views can work with each other for the common good.

[4]We note that while Hong Kong remains in active and healthy competition with financial centers in New York City, Singapore, Dubai, San Francisco, as well as upcoming centers in Austin, Texas, and Miami, Florida, London has not been seen as a viable financial center for virtual asset development. We attribute this to regulatory missteps by the United Kingdom, which have been worse than those made in Hong Kong.

Regarding Footnote 25[5] of the Public Consultation document, we note that although the Stablecoin Ordinance (Cap. 656) may place limitations on the offering of stablecoins, that there are no legislative limits on offering to buy stablecoins, nor are there limits on offering to sell Hong Kong dollar or any other goods and services with stablecoins as payment. And in any event, the fact that tokens issued under the GENIUS Act, being authorized by the government of the United States acting under the authority to issue currency, fall outside the definition of virtual asset or stablecoin and are not regulated and cannot easily be constitutionally regulated, thereby rendering these restrictions moot.

Although the HKSAR may choose to expand or modify the definition of virtual asset or stablecoin either through new legislation or subsidiary legislation, we believe that this course of action would be unwise, and we see it as unlikely that any definition that would seek to restrict the use of GENIUS Act tokens in Hong Kong could be written without grave conflict with Basic Law Articles 112 and 115.

One could also argue that tokens issued by the United States under the GENIUS Act are not currencies and do not fall under the limitations of existing legislation. We believe that these efforts are likely to fall as we see and we believe that Hong Kong courts will see no legal difference between the United States Congress authorizing the Federal Reserve Banks to print Federal Reserve Notes or issue central-bank digital currencies, and Congress authorizing private issuers to mint government approved payment tokens.[6]

We note in closing that there is a bipartisan consensus that the United States should liberalize crypto regulations both among supporters of President Donald Trump and his MAGA movement as well as with some of his most bitter opponents in the anti-MAGA movement. We believe that the GENIUS Act and Project Crypto will be merely the first of many initatives originating in the United States to liberalize regulations in virtual assets, stablecoins, and blockchain, and that this will continue regardless of what party is in power in the United States.

It would be bitterly ironic if, with the passage of the GENIUS Act and future legislation from the United States, businesses attempting to operate in Hong Kong find themselves under onerous regulations and regulatory overreach, while businesses operating from the United States find no restrictions in operating in Hong Kong. This naturally would lead to the perverse result that the regulatory structure of Hong Kong restricts the development of the Hong Kong virtual asset industry while encouraging the use of non-Hong Kong products. The Basic Law was drafted

[5]Footnote 25 states "After the regime comes into effect, stablecoins can only be offered by permitted offerors. Stablecoins issued by entities not licensed by the HKMA may only be offered to professional investors in view of the risks involved." We have pointed out in earlier consultations that the term "offering" used in this legislation is extremely narrow

[6]We believe that it would be a fruitful area of study to compare the GENIUS Act with the recently adopted Stablecoin Ordinance, as we believe that the GENIUS Act avoids many of the issues associated with financial regulatory practice derived from the United Kingdom.

specifically to avoid this result, and this is why we are focusing on the constitutional principles within that document.

We leave this as a matter for the FSTB and Legislative Council to consider more fully.

1.b. Exemptions on the persons and activities to be subject to licencing

With respect to the persons and activities to be licencing, we are pleased to see that the FSTB and SFC appear to share our concerns on regulatory overreach and have limited licensing only to VA OTC dealers, which are engaged in OTC activities "by way of business". We are also pleased that FSTB and SFC have stated in the public consultation proposal that the definition of "by way of business" will exclude peer-to-peer trading of virtual assets between individuals where no intermediary is involved. We note that as this statement is a statement of legislative intent that will be considered for judicial and administrative interpretation under the Interpretation Ordinance (Cap. 1) s. 19.

We believe that the HKSAR would best be served if the limitation "by way of business" were interpreted so as to limit the entities and person subject to licensing.

Therefore, in order to reduce regulatory uncertainty, we propose that the following should be included in the legislation under the ``same activity, same risk, same regulation'' principle

- Safe-harbour exemptions to encourage the use of virtual assets in the ordinary and usual course of business for the purpose of trading goods and services or to undertake funding, repayment, or collateralization of loans
- A "no-action letter" mechanism similar to the regulatory process used by the United States Securities Exchange Commission in addition to the power to publish codes and guidelines.
- Exemptions to provide for consistency with the Securities Futures Ordinance (Cap 572) with respect to professional investors and market contracts

We shall now describe our proposals in detail.

1.b.i. *Exemptions to allow to provide a safe-harbour for the use of virtual assets in the ordinary and use course of business for the purpose of goods and services trade or loans:*

Proposed Exemption 1

We propose to exclude from the definition of dealing in virtual assets activities where a person

- as principal performs the act in the ordinary and usual course of business
  - to facilitate a transaction incidental to the trade of goods and services
  - to use a virtual asset for the purpose of the funding, repayment, or collateralization of a loan"

Virtual assets are used in business contexts much broader than the use of traditional securities, and under the ``same activity, same risk, same regulation'' principle, where a virtual asset is used in a manner that is not currently subject to securities regulation, it should be exempt from such regulation.

Imposing securities-style regulation in contexts where the virtual asset is not used as a security imposes regulatory uncertainty, and it is in the public interest that the Legislative Council create regulations that encourage the use of virtual assets in the ordinary and usual course of business.

While it may be argued that the limitation of "by way of business" would exclude these activities from the scope of licensing, we believe that it is not in the interests of Hong Kong to leave this matter to interpretation, but rather that there be a bright line statutory exemption to very clearly exempt the use of virtual assets in the ordinary and usual course of business from regulations on dealing virtual assets.

Not providing a safe-harbour exemption would discourage the use of virtual assets in the ordinary and usual course of business, and would place Hong Kong at a competitive disadvantage with respect to other capitalist jurisdictions such as the United States and Singapore that are encouraging the use of virtual assets for business. In the United States, Paul Atkins the new Chairman of the United States Securities Exchange Commission has stated in his speech announcing Project Crypto[7] has stated the policy to aggressively establish safe harbours as part of Project Crypto.

In Singapore, the scope of the Payments Services Act has been limited by the High Court in the case of *Rio Christofle v Tan Chun Chuen Malcolm. [2023] SGHC 66*, in which the High Court limited the application of the Payment Services Act to remove the types of activities envisaged under these exemptions from the scope of licensing in Singapore.

In doing so, the court noted that if a business was engaged in unlicenced transactions involving cryptocurrency that these would be illegal and hence contracts related to such transactions would be null and void as a matter of public policy. In the absence of regulatory clarity, this would allow persons involved in a cryptocurrency contract to make frivolous claims to impede the operation of such contracts. We believe that an exemption such as the one we have proposed would prevent misuse of the legislation.

In conclusion, Basic Law Article 109 mandates the maintanece of Hong Kong as an international financial center, and Basic Law Article 115 mandates the free movement of goods, intangible assets and capital. These mandates will best be implemented by promoting the use of virtual assets in the ordinary and usual course of business, and the proposed exemptions will best achieve these objectives in a "same activity, same risk, same regulation" framework.

[7] https://www.sec.gov/newsroom/speeches-statements/atkins-digital-finance-revolution-073125

1.b.ii. *Inclusion of a code and guideline provision as well as a no-action letter mechanism based on practices of the United States Securities Exchange Commission to define the scope of regulation:*

Proposed Addition 1

We propose to add a provision to allow the SFC or HKMA to publish codes and guidelines by copying the language of the Securities Futures Ordinance (Cap. 571) s. 112Z

Proposed Addition 2

We propose to add the following provision

No action letters

1. In response to an inquiry concerning a specific action or proposed transaction its jurisdiction, ether the Commission or the Monetary Authority (‘’the issuing body’‘) may at its sole discretion issue a formal letter (``no action letter’‘) that it has been advised by its staff that the issuing body take no action against the person making the inquiry for that specific action or proposed transaction based on the facts and representations described in the inquiry.
2. A no-action letter may contain an expiration date and may be conditional to actions and commitments by the applicant and subject to limitations issued by the issuing body.
3. A letter issued under Section 1, shall be made available for inspection and copying by any person as soon as practicable after the response has been sent or given to the person requesting it.
4. The issuing body may amend or withdraw the no-action letter at any time.
5. A no-action letter published under subsection (1) and all amendments made to it are not subsidiary legislation.

Effect of No-Action letter

1. The contents of a non-action letter shall have no precedential value and shall not bind the issuing body to take or refrain from taking any enforcement or regulatory action. However, compliance with the terms of a no-action letter shall be taken as evidence of good faith and may be used to determine whether a person is fit and proper in any administrative or judicial proceeding.

The inclusion of a “no action” mechanism has been a long standing desire of financial professionals in Hong Kong, and we would recommend that the Legislative Council

use this opportunity to include a “no-action letter” provision analogous to the “no action letter” procedure used by the United States Securities Exchange Commission.

As the virtual asset industry is dynamic and fast moving, we believe that it is in the public interest for the SFC and HKMA to have a mechanism that would provide regulatory clarity and allow the SFC and HKMA to dynamically and quickly adjust regulations for the public good. Under current legislation, there are three mechanisms for adjusting the scope of regulation:

- judicial interpretation
- subsidiary legislation
- codes and guidelines

The use of subsidiary legislation is unwieldy and unsuitable for a dynamic environment, and the use of judicial interpretation is difficult because Hong Kong is a small market with a limited number of precedential cases, and the Hong Kong judiciary prefers not to involve itself in issues involving the social balancing of interests.

We note that the use of no-action letters is familiar to financial lawyers in the United States as the Hong Kong Special Administrative Region of the People’s Republic of China finds itself in both geopolitical and commercial competition with financial centers in the United States, we believe that adopting some of the tools available to securities regulators in the United States is essential to maintaining Hong Kong’s geopolitical and commercial advantages.

Finally, we intend that a no action letter mechanism allow greater regulatory dialogue between the SFC and HKMA and market actors both inside and outside of Hong Kong. As an international finance center, we believe that SFC and HKMA must be vigilant against efforts, whether intentional or unintentional, to create a “licence raj” to encourage regulatory capture, rent seeking or local protectionism. Greater dialogue between the SFC and HKMA and a broader spectrum of market actors both within and outside of Hong Kong is in the public interest but also in the commercial interest of market actors in Hong Kong.

1.b.iii. *Exemptions from the Securities Futures Ordinance to be included under the “same activity, same risk, same regulation” principle:*

Proposed Exemption 2

We propose to exclude from the definition of dealing in virtual assets activities by persons who

- as principal—
  - performs the act by way of dealing with a person who is a professional investor (whether acting as principal or agent);
- enters into a market contract

> and that the terms “professional investor” and “market contract” have the same meaning as found in the Securities Futures Ordinance (Cap. 571) Schedule 1.
>
> see Securities Futures Ordinance (Cap. 571) Schedule 2 dealing in securities (v-vi)

We hope that these exemptions would be uncontroversial and would provide the consistency in the regulation of different asset types in Hong Kong.

2. Q2. Do you have any comments on the proposed scope of allowed activities?

Yes We have comments on the proposed scope of allowed activities arising from the statutory definition of virtual assets and stablecoins and from the prohbition of foreign exchange controls in Basic Law Article 112

We wish to note the implications of the Basic Law Article 112 prohibition against foreign exchange controls and its requirement of that Hong Kong dollar shall be freely convertible. Furthermore, we would point out the limitations on the definition of virtual assets that we noted in the previous question.

We wish to point out that some forms of virtual assets such as “stablecoins” have the functional characteristics of currency and foreign exchange rather than that of securities. Therefore, both the SFC and HKMA must be careful not to impose limits on the dealing of foreign stablecoin by licenced dealers which would constitute an unlawful foreign exchange control.

Specifically, the United States has as a result of the GENIUS Act has created a general regulation allow for the issuance of payment tokens. We note that these tokens are excluded from the definition of virtual asset by the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) s. 53ZRA(2)(a)(i)(B) and the definition of stablecoin under the Stablecoin Ordinance (Cap. 656) s. 3(2)(a)(v) as tokens issued under the GENIUS Act are issued by an entity authorized by a government of a jurisdiction that is acting in accordance with an authority to issue currency in that jurisdiction.

We note that even if the Legislative Council were to attempt to change the definition of virtual assets, that Basic Law Article 112 forbids the Hong Kong Special Administrative Region from using its virtual asset OTC regulatory powers to limit spot conversion of these and other stablecoins issued outside of Hong Kong to and from Hong Kong dollar by the Hong Kong public. In addition to violating the Basic Law, misapplying rules which are appropriate for the regulation of securities to the regulation of foreign exchange and currency products contradicts the “same activity, same risk, same regulation” principle.

Finally, we note that Basic Law Articles 109 and 115 mandate that Hong Kong maintain Hong Kong’s status as an international financial centre and safeguard the free movement of capital. In developing policy, we are concerned that the policies of the FSTB, SFC and HKMA may be subject to pressure toward regulatory capture and rent-seeking by local businesses that have a financial interest in setting up a ``licence raj’‘ or to encourage local protectionist measures.

We therefore urge that in developing policy, the FSTB, SFC and HKMA consult a broad spectrum of opinions both within and outside Hong Kong, from not only virtual asset dealers but also technology professionals, business users, industry thought leaders, and the general public, and take care not to place undue weight on

the concerns of local virtual asset dealers where these concerns promote local protectionism. We believe that the FSTB, SFC, and HKMA should particularly seek the views of virtual asset companies which have either left Hong Kong or have decided to base themselves in other jurisdictions.

In a previous question, we proposed creating a no-action letter mechanism, and we have done so specifically to encourage regulatory discussions that would reduce the impact of rent-seeking and regulatory capture.

3. Q6. Do you agree with the proposed transitional arrangement?

No We do not agree with the proposed transitional arrangements.

We are extremely concerned about the proposed transitional arrangement as without a deeming arrangement, it is impossible for existing businesses to comply with new licensing requirements without knowledge of what those requirements are. Having businesses attempt to apply for licenses before the legislation has been enacted puts the cart before the horse, and is likely to lead to administrative confusion and chaos.

We believe that this transitional arrangement would have the effect of forcing a great many businesses to immediately shut down, and we would ask FSTB and the Legislative Council to consider if this is in the public interest of Hong Kong, or and if this conforms with directives from the Central Government to expand Hong Kong's to create a strong impetus for growth and to maintain social stability by increasing high quality employment.[8]

We believe that there is tension between these objectives of the Central Government along with its national security goals of ensuring that China is immune to Western blockades and sanctions, versus the objectives by the Hong Kong regulators of investor production as well as local market participants who may wish to set up a cartel of virtual asset providers, and that these competing objectives must be managed and resolved in the course of deliberations over this legislation.

At a minimum, we believe that the FSTB and the Bills Committee should insist that HKMA and SFC explain their regulatory philosophy. It may appear that HKMA and SFC intend a massive and disruptive purge of the virtual asset and stablecoin OTC market in Hong Kong, and it is essential for FSTB and the Bills Committee to ascertain if this is the intention of the administration, and if so, to have the administration justify this regulatory vision as being in the public interest, and if not, to explain what is the regulatory vision of the financial regulators.

[8] See Points 2 and 4 of Xi Jinping's address at the meeting celebrating the 25th anniversary of Hong Kong's return to the motherland and the inaugural ceremony of the sixth-term government of the Hong Kong Special Administrative Region

4. Q7. Do you agree with the expedited licensing or registration arrangement?

No We have grave concerns over an expedited licensing or registration arrangement.

In conjunction with Q6, an expedited licensing or registration arrangement would result in a large number of businesses closing, and massive disruption to the virtual asset industry in Hong Kong, and would furthermore result in a lack of transparency and encourage rent-seeking, regulatory capture, and local protectionism behaviour which has been detrimental to Hong Kong as an international financial centre.

To an outside observer, these measures can appear to be a heavy-handed effort to allow local cartels to shut down new business or prevent external competition; this is hardly conducive to attracting external investment or talent.

Given the failure of initiatives such as the Virtual Asset Trading Platform legislation to attract overseas companies to Hong Kong or develop a healthy ecosystem of local innovators, we share global industry skepticism of the ability of regulators to administer these measures in ways that encourage market development.

In order to improve transparency and accountability we believe that at a minimum it should be a requirement that the SFC and HKMA must be required to publish either the names of the businesses eligible for expedited licensing or alternatively to set up legislative or regulatory criteria by which any business which complies with that criteria would be eligible for expedited licencing.

5. **Q9. Do you agree that, for the purpose of protecting the investing public, persons not licenced by or registered with the SFC should not be allowed to actively market VA dealing services to the public of Hong Kong?**

Yes. We believe that the VA dealing services regulation should follow the same "active marketing" standard in force with the Securities Futures Ordinance.

We note that, as with the analogous provision in the Securities Futures Ordinance, the active marketing rule allows companies to conduct virtual asset technology and financial operations in Hong Kong in support of virtual asset activities that do not involve the Hong Kong public. Moreover, the active marketing rule in the Securities Futures Ordinance avoids regulatory conflict with Basic Law Articles 109, 112, and 115, by allowing Hong Kong persons to access financial products and services outside of Hong Kong through ``reverse solicitation'', where these services are not actively marketed to Hong Kong persons.

We note that the active marketing rule will force Hong Kong virtual asset dealers to compete with offshore dealers, and we consider this competition is essential in preventing local protectionism, rent-seeking, regulatory capture, and the creation of a "licence raj."

Therefore, we support using the same regulatory standards as the Securities Futures Ordinance, we believe that this will increase regulatory certainty and transparency, thereby enhancing Hong Kong's role as an international financial center.

6. **Q11. Do you agree that a review tribunal mechanism should be put in place to handle appeals against the decisions to be made by the SFC or the HKMA in implementing the licensing regime?**

Yes. We believe that a review tribunal mechanism should be put in place, but this mechanism must be effective and aligned with regulatory practice and should not be a pro-forma mechanism as are the existing appeals mechanisms.

We wish to bring to the attention of the FSTB, the negative reputation that Hong Kong has developed in the global virtual asset community because of regulatory practice. The Legislative Council enacted a statutory framework for the issuance of Virtual Asset Trading Platforms, and to the frustration of licence applicants, the actual process used was very different from the statutory framework enacted by the Legislative Council.

Specifically, much of the negative reputation that Hong Kong has developed in the global virtual asset community because of regulatory practice on appeals, as regulatory practice in Hong Kong has made the statutory framework of appeals ineffective. A legally problematic practice has developed among financial regulators in Hong Kong to circumvent the appeals process by refusing to accept applications to avoid creating reviewable decisions. Moreover, a practice has also developed to place pressure on applicants to withdraw applications so as to circumvent the appeals process.

We note that with the introduction of the Virtual Asset Trading Platform licence, all unsuccessful applications were withdrawn, and no application was formally rejected. However, because of this regulatory practice of "constructive denial," the Hong Kong virtual asset ecosystem is unable to understand the reasons for the unsuccessful applications, and it becomes impossible effectively exercise legislative, judicial, or administrative oversight over the financial regulators, and to make necessary policy corrections.

We note that the recent move toward liberalization in virtual asset and stablecoin policy in the United States was catalyzed by dissatisfied industry participants appealing decisions by the Securities Exchange Commission under the direction of its former Chairman Gary Gensler. The general dissatisfaction with the policies of the SEC under Gensler produced a constructive policy dialogue that resulted in the current policy changes. Without effective appeals and grievance mechanisms in Hong Kong, the dialogue proves to be more difficult, and unlike the United States market, which is large enough so that people dissatisfied with its administrative policy stay and fight, in Hong Kong, the talent and capital move to other competing financial centers.

We believe that the experience of the global virtual asset industry with the Hong Kong regulatory system in the context of the Virtual Asset Trading Platform licence has left it with a highly negative perception of Hong Kong's regulatory system. The

mere fact that current regulatory practice is unaligned with the statutory framework is itself problematic. Hong Kong prides it devotion to the rule of law, and this misalignment leads to regulatory confusion and disillusionment with Hong Kong as a financial center.

We believe that a policy dialogue between regulators and industry as to how best to resolve this situation is essential. Our first response, as we have outlined above, is to reduce the scope of regulation. We believe it is also essential to align the statutory framework with actual regulatory practice, and this is a matter that FSTB and the Bills Committee must also deliberate. To further the discussion we propose the following ideas for debate and comment.

Proposed ideas to align statutory framework with regulatory practice

- **A two stage licencing process** by which an applicant submits a brief statement notifying the regulator of an intent to file a licence and requesting feedback on the likelihood of success, with an adverse decision that a licence is unlikely to be granted being appealable to the tribunal. This would formalize the current regulatory practice of having pre-licence discussions before the actual licence application is accepted, but would do so in a way that allows for greater oversight and transparency.
- **A remedy of appeal in cases of constructive denial** In this remedy, any communication from the financial regulators that a licence is unlikely to be granted will enable the applicant to withdraw the licence application and file an appeal or grievance with the review tribunal. The financial regulators will also be required to notify applicants that this remedy exists.
- **Legal protection in exercising the right of appeal** A rule that a filing of an appeal in response to a communication that a licence is unlikely to be granted shall not be considered negatively in future licencing decisions or on decisions of fit and properness.