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Greetings:

I am Dr. Joseph Chen-Yu Wang, sole proprietor of Bitquant Digital Services and writing on behalf of my company in response to the public consultation request issued on 27 December 2023 by the Financial Services and Treasury Bureau and the Hong Kong Monetary Authority.

I am a computational astrophysicist who is currently developing supercomputing, web3, and blockchain projects which are intended to advance the goals of the Circular Electron-Positron Collider project which is scheduled to be included in the 15th Five-Year Plan, to be constructed during the 2030s. In addition, I am a contributor to many Web3 open source projects such as OpenCEX, an open source exchange platform, and am working to encourage talent and technology to come to Hong Kong.

I consider the research and programming work to develop new productive forces that I am doing here in Hong Kong to be critical to the national security and common prosperity of the Chinese nation and in the common interest of all nations in a multipolar world.

However, I am extremely dismayed at the direction of legislation in Hong Kong. Through well-meaning but misguided efforts previous efforts at legislation have reduced rather than enhanced Hong Kong's attractiveness as a virtual asset hub and a destination for virtual asset businesses and I believe this and the proposed virtual asset OTC legislation will have a strongly negative impact on Hong Kong's efforts to attract talent, and promote trade and technological innovation, and this will impact the efforts of the People's Republic of China to maintain economic growth and maintain national security in a very complex and difficult geopolitical situation.

It is with great frustration and disappointment that I am seeing other centers leap past Hong Kong and Hong Kong to lose their leadership position in the area of virtual assets at a time when Hong Kong as part of the Chinese nation needs new industries and innovation to meet global geopolitical challenges.

Hong Kong was a world leader in virtual assets. Stablecoins and perpetual futures were invented in Hong Kong, and I am amazed at some of the innovations that are occurring in Hong Kong right now in the informal markets. However, the innovation of Hong Kong has never occurred in the formal markets but rather in the informal markets, and rather than attempting to grow these informal markets, regulatory policy based on a well-meaning yet misguided policy of "same activity, same risk, same regulation" has had and will have the effect of limiting and destroying these markets rather than grow them.

**Q3. Do you agree with the proposed approach of introducing a new piece of legislation to implement the regulatory regime for FRS issuers, and potentially cover the regulatory regime for other VA activities as appropriate in the future?**

We strongly oppose any new legislation on virtual assets including this legislation on stablecoins and legislation on virtual asset OTC regulation. However, in this current bill, we find the proposed framework on

issuance to be “harmless” whereas we find the proposed limits on offering and the philosophy of preventing the circulation of unlicensed stablecoin among the general public to be particularly objectionable.

We have noted severe national security and constitutional problems with the proposed legislation which we will detail in our response to Question 8. The proposed limits on offering is such a disproportionate response to any possible public good and therefore so clearly violate the provisions of Articles 6, 112, 115, and 118 of the Basic Law that should these pass, I will personally file a judicial review to seek to get them overturned. Therefore, I welcome this public consultation as it is a less expensive and more efficient means for me to challenge the constitutionality of the proposed legislation and seek redress from the legislature and the administration before the legislation is enacted than to seek redress from the courts through judicial review after the legislation is enacted.

However, we are alarmed at the lack of consideration of the negative national security effects of this legislation. The major rationale for the introduction of new legislation is to comply with the “same activity, same risk, same regulation” framework of virtual asset regulation given by international standard bodies. This is shocking and absurd as many of the members of these organizations have used and have publicly stated their intention to use those regulations to specifically undermine the technological progress, national security, and economic prosperity of the People’s Republic of China and to destroy Hong Kong as an international financial center.

While Hong Kong as a part of the People’s Republic of China should follow a policy of dialogue, peace, and cooperation and attempt to cooperate with all nations, even those that wish it harm, we find it bizarre and unacceptable to base the regulatory framework on virtual assets on the recommendations of international organizations without considering these frameworks are being proposed to limit the economic and technological development of the People’s Republic of China and to prevent it from operating an independent foreign and trade policy.

Many members of these international organizations have adopted financial regulations specifically to limit Chinese economic and technological power and to prevent China from conducting an independent foreign and trade policy in a multipolar world. Anti-money laundering laws that have been proposed by these standards bodies have been misused to arrest and detain persons such as the Chief Financial Officer of Huawei, Meng Wanzhou, and to sanction senior members of the Hong Kong government, including the Chief Executive, the Secretary for Security, the Secretary of Justice, the Secretary for Constitutional and Mainland Affairs, and the Commissioner of Police.

Hong Kong itself is facing capital and talent outflows in part due to efforts of unfriendly foreign powers to “decouple” and “derisk” from China, and the need to develop new industries such as web3 and virtual assets exist in part to replace companies that are being coerced into leaving because of these pressures. Furthermore, the funding mechanisms and networks that were used to create Chinese tech industry such as Alibaba, Tencent, and Baidu as well as to finance the reform of state-owned enterprises such as PetroChina and Sinopec have been shut down. Silicon Valley VC and Wall Street bankers are now under tremendous pressure to economically isolate the People’s Republic of China and deny it technology and capital.

In this troubled environment, the Central Government has entrusted patriotic forces within Hong Kong with the sacred duty of using our knowledge and expertise of capital markets and our understanding of overseas business practices to create new economic systems to power the economic, social, and national security development for the good of the Chinese nation. In doing so we must seek the help of those in the international community including those who may be motivated toward commercial rather than patriotic goals to overcome the challenges that face the Chinese nation. In doing so, we must remove any barrier or any difficulty that is not essential for the national security and economic prosperity of the Chinese nation that would prevent others from doing business in Hong Kong.

Those that wish to see China economically isolated and Hong Kong destroyed as an international financial center are doing so by increase the regulatory difficulty of doing business with China through Hong Kong. To counteract these measures, Hong Kong must remove any legal or regulatory barrier that does not contribute to national security. There should be less legislation and fewer regulations on virtual assets, not more.

In addition, as we have argued in our response to Question 5 the public consultation shows absolutely no awareness of how stablecoins are used in Hong Kong, and no sense of how this legislation will impact the financial ecosystem of Hong Kong. Hong Kong has developed a vibrant and active stablecoin industry

which allows the People's Republic of China to be more resistant to efforts at sanctions and blockades. The goal of many members of these international bodies is to destroy this ecosystem with the intent of destroying Hong Kong. We should not help them.

In addition, we are asked to support new legislation concerning virtual assets without reviewing the impact of previous legislation. We believe that the virtual asset trading platform licensing system has been a massive failure. It has not served to promote the virtual asset industry in Hong Kong, while at the same time has done nothing to reduce fraud and bad behaviour. It is forcing regulated exchanges to adopt rules that make them uncompetitive with off-shore overseas exchanges, thereby limiting the attractiveness of Hong Kong as a virtual asset hub.

It has been argued that a light-touch regulatory regime in Hong Kong will attract bad actors who have been kicked out of other jurisdictions. The fraud associated with JPEX leads one to question that presumption. In a world connected to the internet, bad actors can cross borders and perform their fraud remotely. Reducing the number of good virtual asset businesses in Hong Kong creates a vacuum that makes it easier for bad actors to operate, whereas having a strong local ecosystem allows local businesses to self-police and report instances of fraud and abuse to the police, and have more presence in Hong Kong makes it easier for law enforcement to take action. It is our opinion that well-meaning but misguided efforts at regulation makes frauds like JPEX and cryptocurrency scams easier and not harder, and that banning and overregulation of good businesses will do nothing to harm bad businesses.

None of these factors appear to have been considered in the consultation request, and because these factors have not been considered, we believe that the current measures that are being proposed by the FSTB and HKMA in virtual asset regulation will have consequences that range from merely bad to catastrophic.

Finally, we note the slowness of the legislative and regulatory process. In a world and an industry that changes day by day, a regulatory framework that takes years may be problematic. The legislative program that this proposal is currently part of addresses issues that were adequately addressed by the market years ago and fails to consider issues such as geopolitics and national security which were not as acute when the program was initiated. What sense is there in regulating horse carriages when the world has moved on to airplanes, and why is the government insisting on forcing people to use well-designed horse carriages when the rest of the world has moved on? Not only is this a bad technology policy, but having only horse carriages when your geopolitical adversaries are flying airplanes poses grave national security risks, and if you are using horse carriages while fraudsters and criminals are using airplanes, you have no hope of protecting investors and consumers.

However, in this situation, slowness may be a benefit. Because we believe that the legislative program toward virtual assets is very flawed and should not be undertaken, we are glad that it is being taken slowly as this limits the damage of a flawed regulatory policy and allows reconsideration of the direction Hong Kong is moving in.

We see no reason that Hong Kong should pass legislation in this area, and we believe that Hong Kong will be a much more prosperous and secure without new legislation. If the Legislative Council passes the new legislation, it should be aware that the proposed arrangements on issuing are "bad but harmless" while the proposed arrangements on offering is catastrophic.

#### **Q8. Do you have any view on the proposed arrangements for the offering of FRS?**

Although much of the proposed legislation is "bad but harmless," the proposed restrictions on offering stablecoins are particularly catastrophic.

The definition of "offer" in the consultation is

"Offer" refers to the act, as a principal or an agent, of providing a channel for a person to acquire FRS, which includes but is not limited to distribution, providing trading or brokerage services for acquiring FRS, etc

The proposed legislation appears to ban the sale or use of stablecoin to all but a few entities in Hong Kong. In particular, the proposed language would appear to prohibit me from exchanging the stablecoins that I receive as salary for Hong Kong dollars or using unlicensed stablecoins to pay others. We are

particularly concerned with the use of “etc” in the proposal. Open-ended terms such as “includes but is not limited to” and “et cetera” are terms that simply do not belong in proposals that include possible criminal and civil sanctions.

We note that the definition of “offer” used in the language of the proposed legislation is very different from the term “offering” as it is typically used in securities regulation. In most cases, the term “offering” exists either in the context of an issue of shares or the process of advertising and soliciting buyers for shares. This has constitutional implications as the definition of offering is so broad and so far over the limits found in typical securities regulation as to be a disproportionate restriction on the free flow of capital guaranteed by the Basic Law.

The intent of these restrictions appears to be to ban the circulation of unlicensed stablecoin in Hong Kong among the general public. As such, these proposed restrictions on offering stablecoins have been very poorly considered and are blatantly unconstitutional under the Basic Law, against the public policy objectives of the National Security Law, and disastrous for Hong Kong’s competitiveness as an international financial center. The proposed regulations take concepts and regulations that are appropriate for securities regulation and misapplies them to payment tokens to create a draconian regulatory system that exists in no other capitalist jurisdiction and is wholly inappropriate for Hong Kong.

If the legislation limiting the general circulation of unlicensed stablecoins is adopted, their catastrophic effects would be limited by the fact that those provisions appear to be so blatantly unconstitutional that they would be struck down by the courts, and that if the proposed limits on offering are adopted we intend to personally file a judicial review against the legislation. Moreover, the genius of the capitalist system will find ways of circumventing the negative effects of the legislation. However, this will waste effort and resources at a time in which Hong Kong within the People’s Republic of China is facing severe geopolitical and economic challenges.

We shall now explain the severe constitutional and national security problems of the proposed arrangements for the offering of stablecoin.

### **Stablecoin policy in Hong Kong is of vital concern to the national security and future prosperity of the People’s Republic of China**

The issue of Hong Kong’s virtual asset regulation is not merely one of commercial interest but impacts the national security and future prosperity of the People’s Republic of China. As patriots, we have been given the sacred duty to develop the capitalist system of Hong Kong for the benefit of the Chinese nation. There may be substantial disagreement as to the means, and I look forward to a rational, civil, and democratic discussion on Hong Kong’s virtual asset policy.

As part of my work, I am focused on developing Hong Kong as a center for advanced science and technology, and stablecoins are a critical aspect of this effort. Certain foreign powers are attempting to prevent the Chinese nation from acquiring advanced technologies and to limit our ability to advance scientifically and technologically and in the name of “decoupling” and “derisking” are also attempting to prevent the Chinese nation from engaging in normal trade relations with other nations.

As such they have misused the international banking system and their hegemonic control over the issuance of reserve currencies to control the flow of funds. These economic efforts have made it impossible for me and those conducting similar research and technology development to operate within the traditional banking system, and like many others in Hong Kong who are involved in advanced technology to develop new productive forces I receive payment for my services from overseas using cryptocurrencies, specifically USDT and USDC.

Moreover, I routinely use USDT to pay for secretarial services in areas such as Tunisia, Libya, Kenya, Tanzania, Brazil, and the Democratic Republic of Congo. These services are typically for things such as filling out forms, doing internet research, or generating documents using AI, and I receive USDT from these areas to purchase items such as electronic equipment on Taobao. The low value of these transactions (typically in the 500 HKD) and the lack of a traditional banking system render stablecoin such as USDT the only possible payment mechanism for these activities. These microtransactions are as important as high-profile large investments for the success of the Belt and Road Initiative and China’s future economic growth.

My difficulties in accessing the traditional financial system are not unique among patriotic forces in Hong

Kong. Many senior members of the Hong Kong government including the Chief Executive, the Secretary for Security, the Secretary of Justice, the Secretary for Constitutional and Mainland Affairs, and the Commissioner of Police and it has been proposed that these sanctions be extended to include judges who hear national security cases.

Therefore we share a common interest in developing an alternative money system that allows us to undertake normal financial transactions, and the development of Hong Kong as a virtual asset hub is critical for these efforts. We are pleased that because of the ingenuity and innovation created by the capitalist system of Hong Kong, that Hong Kong has developed a mature and stable alternative money system through virtual assets which allows the Chinese nation to circumvent the limits imposed by unfriendly foreign powers, and we believe that many of the measures proposed by international standards bodies exist specifically to destroy this alternative money system.

We note that stablecoins and virtual assets by themselves do not pose a national security risk to the Chinese nation or a threat to the socialist system that is practiced in the mainland of China. Because the blockchain renders all transactions traceable and permanently recorded, any use of stablecoins that harm national security can be traced to persons either in Hong Kong or mainland China are subject to local laws and legal processes. Moreover, in a multipolar world, nations can control the use of stablecoins locally to meet their local economic systems. Because the mainland of China practices the socialist system, the use of virtual assets and foreign currency is heavily restricted locally as part of its policies of socialist economic management.

However, stablecoins are essential for the Chinese nation to defeat the efforts of certain foreign powers to maintain global economic and political hegemony and a unipolar system. Control over the global banking system, allows certain powers to control and limit economic flows globally, and these powers are being misused to limit the scientific and technological development of the Chinese nation. As an international financial center, Hong Kong is critical for developing technologies and financial services to circumvent these efforts.

Although a scientist or engineer in the mainland of China operates within the socialist system and has restricted access to foreign currency and stablecoins, the scientist or engineer may find it necessary to receive stablecoins from foreign sources or use stablecoins necessary to pay for foreign goods and services in order to circumvent efforts at “decoupling” or “derisking.” It would be critical for them to be able to convert those stablecoins into Renminbi in Hong Kong. Therefore under the one country, two systems policy it is critical for Hong Kong to maintain open markets in foreign currency and stablecoins for the benefit of the entire Chinese nation. Under the one country, two systems policy, there is absolutely no contradiction between the socialist system as practiced on the mainland and the capitalist system as practised in Hong Kong, and stablecoin and virtual asset policy illustrate how the two systems within one country form part of an integrated whole.

### **The role of stablecoins in the one country, two systems framework**

The mainland of China practices the socialist system in which basic economic decisions are undertaken within a socialist market economy under the leadership of the Communist Party of China. While this economic system has been successful for the Chinese nation over the previous few decades, one fundamental issue has arisen about how the socialist system of mainland China should interact with political and economic systems in other nations which for their unique historical differences do not follow the socialist system.

Moreover, most people in the world are not Chinese. While people have a natural love for the places that they are connected to, to function in a global world, one must work with people whose love is focused on different places and different things. How does the People’s Republic of China make use of the talent, energy, and expertise of people who are not Chinese patriots for the good of the Chinese nation?

One solution to this dilemma is to attempt to isolate China from the rest of the world, but this approach renders China technologically behind. Another possibility is to use global hegemony to enforce a single-world economic system. This again is unacceptable as it is the fundamental foreign policy goal of the People’s Republic of China to allow all sovereign nations to develop using whatever economic means they find appropriate.

In contrast to other powers who believe that their political and economic systems should be imposed on the entire world, the People’s Republic of China believes that it has no right to interfere in the internal

affairs of other nations and people in other nations should have the right to determine what economic and political systems should be appropriate for their nation, so long as it does not interfere with China's national interest.

However, this belief in non-interference poses a dilemma for the People's Republic of China. If each country has its own system and if China cannot isolate itself, how can the Chinese nation connect to the different political economic systems of other nations?

Hong Kong is the solution to this dilemma under the "one country, two systems" policy. By granting Hong Kong the ability to perfect the capitalist system in an environment of limited government, the central government can use patriotic forces within the Hong Kong Special Administrative Region to connect the socialist system of Mainland China to interact with whatever economic and political systems of other sovereign nations choose to institute for the mutual benefit of all parties.

Because the very existence of Hong Kong is to connect fundamentally different systems for the benefit of the Chinese nation, it must have maximum freedom to develop unique policies to link very different systems. Because there the Hong Kong government simply does not have the expertise and knowledge of the different financial systems of the world, the Basic Law places much responsibility in the capitalist markets of Hong Kong.

As such a regulatory policy that follows the principle of "same activity, same risk, and regulation" is fundamentally opposed to the constitutional framework of Hong Kong. Because the purpose of Hong Kong is to link the socialist system of the mainland of China with the financial systems of other jurisdictions, it would be absurd and self-defeating for Hong Kong to copy the socialist system of the mainland of China, and the fundamental constitutional principles of Hong Kong ensures that this does not happen. However, it would be equally absurd for either the mainland of China or Hong Kong to copy the financial systems of other jurisdictions, particularly when those jurisdictions are intent on harming the national security and future prosperity of the People's Republic of China, and the constitutional principles which prevent Hong Kong from copying the socialist system practised in the mainland of China or imposing the capitalist system on the mainland of China equally prevent Hong Kong from blindly copying the financial systems and practises of other jurisdictions.

The necessity of this system and the importance of stablecoins is more important than ever as we move to the next stage of China's technological development. Unfortunately, as China develops technology, there is additional interest on the part of outside foreign powers to limit China's economic and technological development, and one may expect that these pressures will increase over the coming years. To resist these pressures, it is essential for patriotic forces within the Hong Kong Special Administrative Region to use all possible economic and technological means to resist these efforts, and this calls for a legal system that allows for patriotic forces within the markets and civil society in Hong Kong to develop the means to resist technological limits through blockchain and stablecoins.

One can expect that in the name of decoupling and derisking, that scientists and engineers in the mainland of China may find it difficult or impossible to find funding and engage in cross-border economic transactions due to interference by foreign powers. In this situation it would be essential for Hong Kong to develop its markets and its capitalist system to allow stablecoins to freely flow into Hong Kong where they can be exchanged to and from Renminbi and then transmitted to the mainland in China where they would be under socialist economic management.

The fundamental constitutional basis of the Hong Kong Special Administrative Region has been to create a synergistic interactions between the socialist system and capitalist system, and to examine the proper treatment of stablecoins within a world of geopolitical strife we must examine the basic constitutional norms of the Hong Kong Special Administrative Region beginning with the Basic Law and the National Security Law.

**The proposed restrictions on offering stablecoins are an unconstitutional foreign exchange or capital control under Article 112 of the Basic Law**

The relevant sections of the Basic Law are

**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.

Because stablecoins are intended to be equivalent to cash and are used in cross-border capital exchange, excessive restrictions on the use of stablecoins would constitute an illegal foreign exchange and capital control, and limits that would prevent stablecoins from being exchanged to and from Hong Kong dollars would be a limit on the convertibility of the Hong Kong dollar. In determining whether these limits are acceptable, the courts will use the four-step proportionality analysis in *Hysan Development Co Ltd and Others v Town Planning Board* (FACV 21/2015)[2016]. We believe that a limitation on offering stablecoins as broad as that envisioned in the public consultation would be ruled as disproportionate and therefore unconstitutional under the Basic Law.

While Hong Kong has other regulations that regulate capital exchange such as the money services operator licensing system in the Anti-Money Laundering Ordinance, these regulations do not and cannot limit the types of foreign currencies that are undertaken by money service operators. While the Hong Kong government can and does regulate where and how foreign currency exchanges take place, it would be an unconstitutional foreign exchange and capital control to limit the types of currencies that an MSO operator can transact in or limit the convertibility of Hong Kong dollar into cash equivalents. These principles apply as much to stablecoins as they do to other forms of fiat money.

Although the Hong Kong government can and does limit consumer and investor access to other products such as securities and consumer goods, the very fact that the regulation is being issued by the Hong Kong Monetary Authority indicated that we are discussing flows and transfer of money and therefore the limits restricting Hong Kong government's ability to impose foreign exchange controls. The public consultation mischaracterizes users of stablecoins as "investors" or "consumers" when in fact one typically no more invest in stablecoins as anyone would invest in cash or banknotes. Because stablecoins are "money" and not "investments" they are subject to the prohibition against foreign and capital control policies and limits to convertability to and from Hong Kong dollars.

Although stablecoins are not "currency" and therefore are not subject to the restrictions regarding the licensing of money services under Part 5 of Cap 615, the very fact that the proposed regulation is placing authority under the Hong Kong Monetary Authority indicates that stablecoins are "money" and therefore constitutional norms that limit the Hong Kong government's ability to control the flow of money is applicable.

Given the strong national security and technology interests that we have noted earlier, we assert that vague appeals to "consumer or investor protection" would not be a reason to impose disproportionate foreign exchange capital controls. It may be unwise for a person to trade or hold Congolese Francs, but under the Basic Law, they have the right to do so, and people can and do have good reasons to exchange Hong Kong dollars to and from Congolese Francs, such as when I pay my secretary in the Democratic Republic of Congo or when he asks me to buy a laptop for him on Taobao.

Because I cannot find a liquid supply of Congolese Francs in Hong Kong and they cannot find Hong Kong dollars in the Democratic Republic of Congo, I buy USDT to transmit to the Democratic Republic of Congo where they are converted to Congolese Francs, and they buy USDT to transmit to Hong Kong where they are converted to either Hong Kong dollar or Renminbi. The ability to perform these transactions is so fundamental to the viability of Hong Kong as an international financial center that Article 112 specifically exists to protect my ability to engage in these transactions involving Hong Kong dollar, Renminbi, Congolese Francs, and USDT or USDC.

**The proposed restrictions on offering stablecoins are a disproportionate limit on the rights of private property, free movement of capital, and seeking technological progress**

The constitutional issues with limitations on offering stablecoins are not limited to foreign exchange and capital controls, but also are a disproportionate limitation of Basic Law rights indicated in Articles 6, 115, and 118.

**Article 6** The Hong Kong Special Administrative Region shall protect the right of private ownership of property in accordance with law.

**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.

In contrast to Article 112, which specifically concerns itself with the convertibility of money, Articles 6, 115, and 118 concern themselves with the protection of the free flow of goods, intangible assets, and capital. These provisions constitutionally protect the essence of the capitalist system, and they exist to implement the “one country, two systems” policy and ensure that Hong Kong continues to play its vital role as an international financial center in the service of the motherland under the capitalist system and not the socialist system.

We consider the proposed limits on the use of stablecoins, which effectively ban the circulation of unlicensed stablecoins among the general public, to be a disproportionate and unconstitutional limit on the free movement of intangible assets and against the public policy goal of encouraging investments, technological progress, and the development of new industries.

We note that although the language banning offering appears to use the language of securities regulation, it far exceeds any limitation that currently exists in Hong Kong or in any other jurisdiction that practices the capitalist system. In securities regulation, the term “offering” is typically used in the context of issuing new shares, which is not a constitutionally protected activity. Moreover securities regulation typically concerns itself with advertising and regulation of intermediaries such as brokers and exchanges. The restrictions envisioned in this proposal would cover principals and “include but are not limited to” brokerage and trading activities. The broad scope of the language creates extremely an disruptive ban on the use of unlicensed stablecoins, which is disproportionate to any possible public good that we can see with “investor and consumer protection”.

The logic of “investor and consumer protection” is such that investors and consumers will only be fully protected if there are no stablecoins or indeed no virtual assets or financial industry in Hong Kong at all. This is absurd, so one could call for balance, but then the question lies as to where this balance should be placed. The question is already answered in the Basic Law which provides an extremely high weight on the free flow of capital and is extremely skeptical toward limitations on anything which disturbs this flow. The Basic Law forces us to ask if there are any other mechanisms by which the vulnerable may be protected without threatening me with prison if I just attempt to cash my salary or pay my employees in Africa using stablecoin. These are the questions that can not be avoided as we can debate them now before the legislation is enacted, or later when it is challenged in court, and the proposed restrictions are so disproportionate to any public good that can be achieved that they are very clearly unconstitutional under the Basic Law.

### **The proposed restrictions on offering stablecoin contradicts the goals of the National Security Law**

As an international financial center, Hong Kong maintains a vital role in the national security of the Chinese nation as Hong Kong remains the location by which the People’s Republic of China can conduct trade and commerce with the rest of the world. As such, Hong Kong operates under special laws within the “one country, two systems” policy that are designed to protect the capitalist system of the Hong Kong Special Administrative Region. The content of the laws such as the National Security Law allows one to derive the public interest objectives of the legal system.

The National Security Law states

**Article 6** Any institution, organisation or individual in the Hong Kong Special Administrative Region shall abide by this Law and the laws of the Region in relation to the safeguarding of national security, and shall not engage in any act or activity which endangers national security.

**Article 29** A person who (...) directly or indirectly receives instructions, control, funding or other kinds of support from a foreign country or an institution, organisation or individual outside the mainland, Hong Kong, and Macao of the People’s Republic of China, to commit any of the following acts shall be guilty of an offense:

(4) imposing sanctions or blockade, or engaging in other hostile activities against the Hong Kong Special Administrative Region or the People’s Republic of China

The prohibition against foreign collusion to maintain a blockade or sanctions is unique to Hong Kong



and there is no analogous provision in Mainland law. This provision illustrates the importance of Hong Kong's role as an international financial center. As such, these provisions of the National Security Law indicate public interest principles that should be considered when drafting legislation and when deciding whether the law constitutes a disproportionate restriction on individual rights.

The public policy goals of the National Security Law create complexity in international trade and financial relations. The People's Republic of China is a peace-loving nation that desires cooperation and trade even with nations that have unfriendly policies toward the nation. Moreover, even when a government maintains unfriendly or even hostile relations with the Chinese nations, as a peace-loving people, the Chinese nation believes in developing strong business, trade, and social relations with people of other nations even in the face of unfriendliness and hostility by their governments.

To maintain these policies economic regulators in both Hong Kong and the mainland of China meet with their counterparts to standardize and harmonize practices in areas of financial regulation and anti-money laundering. Some harmonization of standards is beneficial as it increases the volume of financial and trade flows with other nations, and the Hong Kong Monetary Authority and the Securities Futures Commission like their counterparts in the mainland of China should be congratulated for working with their counterparts in other nations, even when those nations have policies that intend to impose technological and financial restrictions against China.

However, despite the benefits and harmonization of standards, these objectives are subordinate to the objectives of national security and the rights stated in the Basic Law, and it is important in considering stablecoin policy to place national security before harmonization of standards when those standards can be used to enforce economic sanctions and blockades against the People's Republic of China.

**No other financial center practising the capitalist system has proposed restrictions on the offering of stablecoins as draconian as those envisioned by this consultation**

The ability for Hong Kong to trade with and yet compete with other capitalist financial centers are an essential part of the Basic Law and the spirit of the National Security Law. Therefore we find it very odd that Hong Kong is proposing restrictions on the offering of stablecoin which is far in excess of any current or proposed regulation by other international financial centers which practice the capitalist system.

Specifically, Singapore classifies stablecoins as digital payment tokens under the Payment Service Act 2019 while Dubai regulates stablecoins under the Virtual Asset Law. In both cases, stablecoins and other payment tokens are regulated under anti-money laundering laws which treat stablecoins as separate from and not subject to offering restrictions associated with securities. In the United States, trading of stablecoins is regulated as commodities subject to the Commodities Futures Exchange Act, where the use of stablecoins for value transmission is regulated under various money services laws. The result of this is that while there are limits on how stablecoins are used, they are not subject to the offering restrictions of securities law. Similarly in Canada and the United Kingdom, stablecoins are regulated in a regime that is based on money services laws rather than securities laws.

Singapore, Australia, and the United Kingdom are considering new regulations on stablecoin, particularly focusing on the issuance of stablecoins. However, in no case that we are aware of is any capitalist jurisdiction considering regulating stablecoins under securities rules in which "offering" stablecoins are restricted, and no capitalist jurisdiction is considering rules on stablecoins that are as draconian as the regulations being considered in this consultation. In every other jurisdiction, stablecoins are subject to rules appropriate for money and not securities and while "issuance" may be highly regulated, "offering" stablecoins is not. Given that, no other capitalist jurisdiction plans to restrict the "offering" of stablecoins under securities rules, and we see no reason why Hong Kong should do so.

For Hong Kong to adopt restrictions on offering stablecoins that have not been envisioned or adopted by any other capitalist jurisdictions would harm Hong Kong's competitiveness as an international financial center and ability to attract talent and investment. Moreover, given that these proposed regulations are so unusual and draconian we believe that they are excessive and disproportionate and therefore unconstitutional under the provisions of the Basic Law which we have cited earlier.

**The Supreme Court of India has ruled similar restrictions to be unconstitutional under the Constitution of India for reasons which are relevant to Hong Kong**

One essential part of the "one country, two systems" policy is the use of common law in Hong Kong.

**Article 8** The laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene this Law, and subject to any amendment by the legislature of the Hong Kong Special Administrative Region.

As with the policies regarding foreign exchange and capital controls, the use of common law allows the Chinese nation to take advantage of new legal principles and new legal ideas throughout the world, and provides a framework by which other countries can use the common law system of Hong Kong as a connector to the system of socialist civil law practiced in the Mainland.

Although common law originated in the United Kingdom, it has spread to many jurisdictions, and as we move to a more multi-polar world, it is necessary for Hong Kong to look past traditional sources of common law and incorporate the legal thinking of common law jurisdictions in South Asia, the Middle East, and Africa.

Specifically, one case which we believe would be relevant to Hong Kong is the case *Internet and Mobile Association of India v. Reserve Bank of India* (MANU/SC/0264/2020) in which a three-judge panel of the Supreme Court of India quashed a circular by the Reserve Bank of India which banned cryptocurrencies. The Supreme Court of India has issued subsequent rulings on the role of cryptocurrencies in India, and Hong Kong should look at these rulings in developing the law of cryptocurrencies in Hong Kong.

In this case, the Supreme Court of India applied the proportionality principle to Article 19(1)(g) of the Indian Constitution which states

All citizens shall have the right- (g) to practise any profession or to carry on any occupation, trade, or business

and struck down the restrictions by the Reserve Bank of India on limiting the use of cryptocurrencies in India, and which appear to be precisely the same types of regulations that are being proposed in this consultation.

The courts in Hong Kong have adopted a more limited interpretation of Article 33 of the Basic Law, which is the analogous provision in concerning the right to an occupation (see *Leung Sze Ho Albert v Bar Council of the Hong Kong Bar Association* CACV No. 246 of 2015 and *GA v Director of Immigration* FACV No. 7, 8, 9 & 10 of 2013)

However, we note that many of the decisions regarding the limited applicability of Article 33 were made before the *Hysan* decision and involves legal arguments that the Court of Final Appeals may should reconsider in light of *Hysan*. Regardless, even taking a narrow interpretation of Article 33, we believe that the proportionality arguments in *Internet And Mobile Association of India v. Reserve Bank of India* would be persuasive in interpreting the restrictions on foreign exchange and capital controls in Article 112 as well as the rights associated with Articles 6, 115, and 118 of the Basic Law.

Although cases concerning common law in India are of course not binding in Hong Kong, we would ask the Legislative Council to examine these decisions for guidance as to how the law of Hong Kong should be structured, and we consider it very peculiar that in this public consultation, the Financial Services Treasury Bureau and the Hong Kong Monetary Authority is proposing that the Legislative Council grant them authority which the Supreme Court of India has struck down as being unconstitutional in India for the Reserve Bank of India to exercise, and which are not in effect or being proposed by any other jurisdiction that practices the capitalist system, and which we therefore consider to be unconstitutional under the Basic Law.

**The “same activity, same risk, same regulation” principle is fundamentally inconsistent with national policy**

One difficulty in public policy is that the regulators and the public often face competing objectives and the question arises as to how these objectives should be reconciled. Although Hong Kong practices the capitalist system, it is an integral part of the People’s Republic of China, and hence the objectives of the Hong Kong government should be as much as possible aligned with those of the nation as a whole as well as the policy priorities of the HKSAR.

One can see how competing objectives arise when examining the speeches regarding national priorities,

and how objectives communicated by the Central Government are implemented locally within Hong Kong. The following set of speeches illustrates this process and how different levels of government have different priorities

- President Xi Jinping address marking 25th Anniversary of Hong Kong's return to the China (1 July 2021)
- The Chief Executive 2023 Policy Address by John Lee (25 October 2023)
- Financial Secretary 2023 Policy Address by Paul CHAN
- Policy Statement of Development of Virtual Assets by Financial Services and Treasury Bureau (31 October 2022)

The main concerns of the Central Government consist of national security, technological progress, and social stability. The main concerns of the Hong Kong Special Administrative Region executive are economic growth and the attraction of talent. The main concerns of FSTB and HKMA are harmonization with international standards and consumer protection. What the FSTB and HKMA have attempted to do in this consultation is to take international regulatory principles such as “same risk, same activity, same regulation” and attempt to reconcile those with national policy goals.

However, in the present situation, we believe that these efforts are merely an effort to reconcile what cannot be reconciled. The goals of the Central Government are social stability, economic prosperity, and national security. The goal of many of the members of international organizations such as the Financial Stability Board is to introduce rules and regulations specifically to ensure that the People's Republic of China is cut off from global capital and to limit Chinese access to new technology. Hong Kong simply cannot have the “same regulation” as the powers who wish to use these regulations to destroy it, and attempting to use “same risk, same activity, same regulation” as a basis for regulation creates fundamental conflicts with the Basic Law and the National Security Law as well as national objectives, and is therefore untenable as a basis for virtual asset legislation in Hong Kong.

**There should be no restrictions on offering stablecoins and no restrictions on the ability of the general public to access unlicensed stablecoins**

If the Legislative Council insists on limiting the “offering” of stablecoins it must do so in the most limited way possible and consider the constitutional and national security implications of these limitations. It could in principle create a complex set of restrictions on offering stablecoin that would pass constitutional scrutiny. However, creating a complex set of restrictions would merely increase regulatory confusion and worse yet may be misinterpreted to make Hong Kong less attractive as a business destination for prospective businesses.

And rather than focus on the details of the legislation, we should focus on the intent of the restrictions. The goal of these restrictions appear to be to attempt to prevent unlicensed stablecoins from circulating among the general public in Hong Kong, and the Basic Law forces us to ask why this is a public policy goal and whether there are better ways of achieving the objectives of these measures.

In my attempts to attract talent to Hong Kong, we have found that many people are under the misconception that the Central Government intends to impose the socialist system on Hong Kong, and that the methods of socialist economic management concerning foreign exchange and virtual assets will be imposed on Hong Kong by the Central Government. Others are concerned that Hong Kong will simply adopt the same regulations as other capitalist jurisdictions and hence there is no reason to move to Hong Kong, particularly as many unfriendly governments are actively discouraging people from doing new business with any part of the People's Republic of China. Adding confusing new legislation will simply add to these confusions and misperceptions.

Still others are dealing with the regulations and restrictions that unfriendly foreign powers are imposing on trade with the People's Republic of China and are not interested in the time and expense of yet another regulatory regime.

In any event, should the Legislative Council pass legislation that impact my ability to conduct stablecoin transactions in furtherance of my technological research activities, then it would be my patriotic duty to limit the scope of the damage by seeking judicial review to overturn such restrictions. While the Hong Kong Monetary Authority may have expertise in banking regulation, they have demonstrated no special

expertise on issues of technology development, national security, or trade finance, we, therefore, believe that in any judicial analysis of these restrictions, that the HKMA would not be able to rely on “measure of discretion” and that in considering the third step of Hysan that that courts would hold that HKMA would hold only a narrow “measure of discretion” and that “reasonable necessity” would be the correct standard of review.

However, resolving these issues after the legislation has passed would be a waste of resources both on my part and on the part of the Hong Kong government. A contentious and highly public legal battle would expose Hong Kong to severe reputational damage and the very moment Hong Kong is attempting to attract talent and business to Hong Kong.

We therefore urge the Financial Services Treasury Bureau, Hong Kong Monetary Authority, and the Legislative Council to consider these constitutional and national security factors in the process of drafting legislation and to consult the Department of Justice, the Constitutional and Mainland Affairs Bureau and the Committee for Safeguarding National Security to examine the constitutional and national security impact of any limits on offering stablecoin before proceeding, and believe that the outcome of this review is that no such restrictions on the ability of the general public to have access to unlicensed stablecoins be instituted.

**Q5. Do you have any comments on the proposed licensing regime for FRS issuers?**

**Q6. Do you have any comments on the proposed licensing criteria and conditions?**

The constitutional and national security issues that we have raised impact only restrictions concerning the offering of stablecoins, and do not impact the proposed regulatory framework concerning the issuance of stablecoins. While the Hong Kong government is restricted in the measures it can take regarding the exchange and trading of stablecoins, there are few such restrictions regarding creating regulations on the issuance of stablecoins within Hong Kong.

While we are concerned with some aspects of the proposed regime on the issuance stablecoins we do not foresee any disastrous consequences to the level of the proposed limits on offering. However, we are very skeptical that the proposed licensing system will be successful for commercial and geopolitical reasons, and we believe that most stablecoin coin activity will go through unlicensed issuers.

Our main concern with the proposed limitations on issuance is the attitude of the consultation. Under the flawed “same regulation, same risk, same activity” principle, the consultation regards the stablecoin and virtual asset ecosystem as “abnormal” and the traditional banking system as the standard, and attempts to have the new system act like the old. What has not been considered is the fact that the traditional financial system has its problems and through the capitalist system of Hong Kong, the informal markets have developed solutions to issues that may be better than those of the traditional financial system. We note that the collapse of Lehman Brothers created widespread disruption in the global financial system due to financial contagion. By contrast, when FTX or 3 Arrows Capital collapsed, the cryptocurrency ecosystem continued to function and the disruption in the virtual asset world was limited.

The proposed regulations on the issuance of stablecoin, while facing no constitutional issues reveal a fundamental misunderstanding of how stablecoins and virtual assets are used in Hong Kong. Because stablecoins have uncertain reserves and are not backed by any government, they are unsuitable for the goal of value storage. Any person holding stablecoins on a long-term basis has a very strong risk of losing any value that exists in stablecoins. The proposed regulations on issuance appear to focus on this issue, but this reveals a fundamental misunderstanding of why stablecoins are used in Hong Kong.

One problem that the traditional financial system has is moral hazard. It is assumed that the regulators have created a safe environment, but this leads to catastrophe as actors assume greater risk and when the regulators are unable to provide the assurances expected by the markets. In the case of stablecoins, the holders of stablecoins understand their instability and have no reason (such as return on investment) to hold stablecoins for any longer than is necessary. This has created an infrastructure and ecosystem that has new and novel approaches to managing risk. Rather than eliminating the risk of a collapse of a stablecoin provider, the infrastructure is resilient against such instability.

In Hong Kong, stablecoins are not used for value storage, but for value transmission. The typical use case for USDT is for a person to convert local currency into USDT, transmit it cross-border, and then convert it back to local currency at the destination. Because the funds are only stored in USDT during

transmission, this limits the risk to the user of the USDT. This is particularly used for transmitting value to areas with limited banking infrastructure, in situations that benefit from instant settlement, or cross-border that are in the interests of Hong Kong within the People's Republic of China but which outside powers find objectionable.

To give an example, I pay secretaries in Libya and the Democratic Republic of Congo with USDT, and they pay me to buy laptops and USB cables on Taobao. Because we use USDT, we instantly know when a payment has been issued, and I can immediately ship a laptop to Libya or DR Congo, and send them the tracking number of the courier. We can immediately perform “delivery versus payment” transactions which would otherwise be impossible. Both I and my counterparty are aware that USDT may have unreliable reserves which means that as soon as we receive our USDT, we convert it to local currency which is more secure as a store of value.

I receive USDT and USDC as salary and because I cannot trust these coins to maintain their value, I immediately convert stablecoin into Hong Kong dollar. Because conversions to and from crypto are regarded with suspicion by banks, I must use local OTC brokers to convert these coins into paper fiat currency. I am skeptical that any stablecoin regulated by the HKMA would provide any advantages. Once the money is in Hong Kong, there is no reason why I would store the coins in stablecoins, and in any event, I could not force my overseas employers to pay me in a licensed Hong Kong stablecoin that they do not have access to. If my employers found it a legal requirement to pay me or others in my situation in licensed Hong Kong stablecoin, they would simply stop hiring people in Hong Kong.

Many of the users of stablecoins in Hong Kong are money service operator and precious metal and jewelry shops that use stablecoin to settle cross-border money transfers. These shops are regulated by Customs and Excise and because they are cash businesses, they rely very heavily on good relationships with Customs and Excise and the Hong Kong Police to provide security. Customs and Excise for many years maintained a negative attitude toward stablecoins being used in money services, but the industry was delighted in June 2023 when C&E issued the new AML guidelines for money service operators which relaxed AML requirements on money services operators and legitimized many off-bank operations. We also note that because these shops are regulated by bodies which report to the Security Secretary rather than the Financial Secretary they are particularly sensitive to issues of law enforcement and national security, particularly given that the officials who are regulating the informal sector are under sanctions by the United States Treasury.

For these uses, global convertibility and instant settlement are more important factors than secure reserves, as users of stablecoin typically only hold stablecoins for a few minutes while a transaction is being settled. However, because there is a large demand to convert USDT immediately to and from the local currency, this creates a strong demand for OTC shops at both ends of the transaction. Typically because stablecoins are very efficient at transmitting value, the margins on trading stablecoins are very low but this is compensated by the large volume of transactions.

The chief financial risk in the system is settlement risk as there is the risk that the stablecoin may lose value or undergo a demand shock. The market response to this is to have large numbers of shops, each with limited capital risk. A large number of OTC shops ensures that settlement risk is distributed among a large number of independent entities and also ensures that the transmission of value cannot easily be blocked by outside foreign powers.

The fact that money services and OTC shops have personal liability on illegal money flows also accounts for the small size of the shops. With institutional financial intermediaries, personal liability can often be removed simply by following procedures. However, this is not true for money services and OTC virtual asset companies, where filling out the right forms will not prevent you from criminal sanctions. Hence money services and OTC shops are relatively small so that the operators can personally vet employees and transactions. Because money services and OTC shops are cash businesses, they rely on good relationships with law enforcement authorities to operate safely.

The creativity of the market system can also be examined in the way that the ecosystem deals with systemic risk, a topic that is of major concern to the Hong Kong Monetary Authority. The current structure of virtual asset markets insulates the general financial system from shocks that occur with stablecoins. In particular, because people are well aware of the risks of the stablecoin, there is an infrastructure for using OTC shops to convert to and from fiat cash to avoid holding stablecoins. This has the effect of creating a buffer between the stablecoin system and the Hong Kong banking system. If

there is a market disruption in stablecoins, as occurred during the collapse of FTX and the collapse of Silicon Valley Bank and Silvergate Bank, the OTC shops stop trading, and this creates a circuit breaker that insulates the Hong Kong financial system from instability in the stablecoin market. Furthermore, because the OTC shops do much of their reserves in paper fiat, it is very hard for them to engage in excessive leverage, and because the OTC market has low barriers to entry and low barriers to exit, we do not have too big to fail issues.

The current regulatory proposals do not show any evidence of understanding how stablecoins and virtual assets work in Hong Kong, and as a result of these misunderstandings, these regulatory proposals have harmed and will continue to harm Hong Kong's position as an international financial center. Specifically, by imposing licensing, the proposed regulations would tend to concentrate settlement risk into a few small entities which would have the effect of increasing both settlement risk and providing a small number of targets that could be targeted as "chokepoints" for a sanctions regime. Furthermore, by removing the role of OTC shops, they are removing buffers and circuit breakers which insulate the general financial system from contagion and systemic shock. By discouraging paper fiat transactions, they are encouraging leverage and risk-seeking behavior which have been long-standing problems with the financial system,

The use of frequent OTC transactions to limit risk is an example of how the capitalist system of Hong Kong can create new and creative solutions to issues, and why we believe that "light touch" regulatory is the best approach toward virtual asset regulation, and why we believe that the regulatory approach that the Hong Kong government has taken over the last few years has clearly harmed innovation and financial development in Hong Kong. Given our experiences in the informal stablecoin market, we do not believe that the proposed measures will create a good environment for Hong Kong.

Specifically, we believe that any stablecoin issuer that seeks licensing in Hong Kong will be blacklisted outside of Hong Kong, and conversely any stablecoin issuer with active markets outside of Hong Kong will be strongly discouraged from becoming regulated in Hong Kong. The result of this is that regulated stablecoin issuers will be restricted to the Hong Kong markets, where one already has an active payment infrastructure whose liquidity is limited, and will be useless for cross-border payments to areas of the world with no traditional banking infrastructure or for uses such as acquiring advanced technology, which unfriendly foreign powers find objectionable.

We note that many of these unfriendly foreign powers find Chinese efforts to promote trade and commerce between China and nations such as Libya and the Democratic Republic of Congo to be objectionable and have therefore made it impossible for persons in Hong Kong to transact with these areas through the traditional banking system.

We also note that all of these transactions with so-called high-risk jurisdictions are legal under Hong Kong law, and if a person tries to use stablecoin in ways that are illegal in Hong Kong such as trading with parties that are subject to the United Nations Sanctions Ordinance (Cap 537) or undertaking payments that violate the National Security Law, stablecoins provide a permanent unalterable record that makes it simple for law enforcement in Hong Kong to take legal action.

My prediction is that licensed stablecoin issuers will find extreme difficult in being able to create commercially viable business models, and will risk going out of business. Regulation will force licensed stablecoin issuers to simply duplicate existing systems and force them into unprofitable business models while restricting them from entering profitable ones. Although some would welcome a license as a market restriction which would increase profits and keep out competitors, we predict that licensed stablecoin issuers like most virtual asset service providers will find that they have a legal monopoly over a non-existent market.

Furthermore, we have grave concerns over the moral hazard presented by these proposals. The risk management of stablecoins has been successful because users of the stablecoins are aware of the risks and dangers, and attempt to mitigate those risks. The major disasters in financial regulation do not occur when people deal with unreliable and unstable systems but rather come from the moral hazard when people deal with systems that are more reliable than they are. In any stablecoin system that is usable for cross-border transactions much if not most of the coins will need to be situated outside of Hong Kong where the regulatory authorities have limited powers to control or monitor activity. We saw this perverse interaction with the Singaporean regulators who approved the FTX onshore activities while being unable to control FTX's offshore activities. We foresee the same regulatory difficulties with stablecoin, where either you have stablecoin which is useless because it circulates only in Hong Kong, or that is dangerous

in that it circulates heavily offshore beyond the control of local regulators.

Finally, because of the efforts of certain foreign powers to prevent technology from reaching China, many overseas companies have already found it difficult to do business with Hong Kong. Adding government restrictions and creating “chokepoints” by which unfriendly foreign powers will simply make Hong Kong more unattractive and prevent capital flows from funding technology innovations such as those my company is working on. Reducing regulation will not encourage bad actors to come to Hong Kong, because they can reach the city through the internet, but will prevent good actors from setting up businesses here.

**Q9. Do you support granting the authorities necessary powers to adjust the parameters of in-scope stablecoins and activities, similar to the VASP regime?**

**Q10. Do you consider the proposed criteria and factors relevant and appropriate for the authorities to take into account when exercising such powers?**

Because the VASP regime is based on a flawed and untenable policy of “same risk, same activity, same regulation” it has been a public policy failure, and we believe that the main focus of the VASP regime is to have a hard look at how it failed and what we can learn from its failure. We believe that the legislation has created severe damage to the Hong Kong virtual asset industry while not providing any positive benefits. The purpose of the VASP licensing was to attract good businesses while punishing bad ones but it has pushed out good businesses while doing nothing to deter bad ones.

One can argue that the VASP regime should not be so harshly judged because it has not been fully implemented. However, the slowness of policy is itself a problem. How can a company survive if it takes years to decide on a license, and the VASP licensing regime is designed to address problems that the markets have resolved years ago. Moreover, if it takes regulators years to react whereas fraudsters and scammers can adapt their tactics instantly, how can investors and consumers possibly be protected?

In an industry that changes day by day, a system in which it takes years to make decisions is simply unacceptable. While we are regulating horse carriages, the world has moved on to using airplanes, and forcing Hong Kong to use horse carriages in a world of airplanes places the People’s Republic of China at grave national security risk.

The high cost of compliance has made setting up a VASP situated purely in Hong Kong to be commercially unviable, and the only profitable model we can see is for an exchange to profit from overseas activities, which means that none of the overseas VASP licensees are interested in making Hong Kong their headquarters or put significant expansion in Hong Kong. What is more as long as Hong Kong is merely the tail and not the dog, Hong Kong regulators will find it impossible to effectively regulate offshore activities, leading to situations where Hong Kong investors are impacted by the actions that a VASP takes offshore.

As an example of this policy failure, we can see the impact of VASP policy on efforts to create a Bitcoin ETF. We believe that there is huge demand and interest in creating a Bitcoin ETF in Hong Kong that can be traded on the Hong Kong Exchange and therefore made available to retail traders in mainland China, and Bitcoin ETF based in Hong Kong would benefit national goals as we see it as very unlikely that large numbers of mainland Chinese stock traders would be allowed access to Western markets. However, we cannot see this effort as being successful. It appears that the SFC will require ETFs to trade through regulated VASPs in Hong Kong. However, because SFC regulations have made Hong Kong VASPs uncompetitive with overseas exchanges, and because the SFC seems intent on limiting retail access to virtual assets in the name of investor protection, we predict that Bitcoin ETFs will simply be unable to find the necessary liquidity in Bitcoin in Hong Kong.

In addition, the VASP licensing system has increased regulatory uncertainty and frightened away the virtual asset industry. The regulators are under the impression that a light touch system will attract bad actors while scaring away good actors. Because of the internet, bad actors can already access the Hong Kong market, and the introduction of licensing has forced good actors into other jurisdictions leaving a vacuum that has been filled by bad actors acting remotely.

Furthermore, we believe that the VASP approach has harmed the ability of Hong Kong to integrate regulated global institutions with informal virtual asset markets. Hong Kong has developed a vibrant informal market in virtual assets which are disconnected from the institutional markets. Instead of trying

to kill the informal markets, the SFC and HKMA could issue regulations that would create intermediaries between formal and informal markets. Instead, the regulatory approach has been to kill the little fish and then wonder why the whales are starving and going elsewhere.

We believe that the VATP licensing scheme has made frauds such as JPX easier rather than harder and that licensing stablecoins and OTC desks will end up hurting investor and consumer protection rather than helping it. Others may disagree, but this is an ongoing debate that we must have and continue to have. Perhaps we are wrong, and licensing is the right approach. But it seems absurd to pass these types of laws without coming back and reviewing if the laws have performed what they were intended to do.

We believe that given the failure of virtual asset trading platform licensing scheme for the Legislative Council to give regulators a “blank cheque” to conduct regulations is a recipe for continued disaster, and must in this and future legislation concerning virtual assets establish permanent legislative oversight, by which the administration should make mandatory periodic public reports to some permanent body of the Legislative Council such as the Panel on Commerce, Industry, Innovation, and Technology for debate and discussion by the legislature and by the general public.

A permanent mechanism for legislative oversight would address several issues such as the fragmented nature of financial regulation in Hong Kong, the lack of institutional representation of new businesses or for businesses and industries that do not yet exist, and the lack of forums by which valid but competing social interests may be reconciled. Moreover, a permanent legislative oversight mechanism would allow for different stakeholders with different interests within Hong Kong to participate in policy formulation.

## **Conclusion**

I do not doubt the sincerity and patriotism of those in the Hong Kong government, but I ask them to look at the outcomes, and it is my opinion is that the efforts at regulation in Hong Kong have not helped the development of a virtual asset ecosystem but considerably hindered it.

Rather than encouraging good companies and restricting bad companies, the result of virtual asset regulation has been to restrict good companies while doing nothing to limit bad actors. As such, I am hopeful that the Legislative Council and Financial Services Treasury Bureau will take this and upcoming consultations on virtual asset OTC licensing as an opportunity for a deep strategic review of Hong Kong’s virtual asset regulatory system rather than simply making minor changes and polishing proposed legislation and enhancing the role of the Legislative Council not only drafting legislation but in the development of legislative strategy and in overseeing its implementation.

One good aspect of the Hong Kong regulatory system is that things occur slowly and only after great deliberation. I am also pleased with how the Hong Kong government listens and responds to stakeholders, but only asks that these deliberations widen the scope of people who contribute their opinions. I am honored to be part of the public consultation process and hope that I have raised issues that will be considered in the upcoming legislation.

Many are perplexed as to why I am so optimistic about the future of Hong Kong and the future of China.

I am optimistic because we are engaged in conversations such as this. A senior regulator in the Hong Kong government was quoted as saying that the regulations on virtual assets will be tight and those that do not like them are ‘welcome to go elsewhere’. I believe that these new tight regulations are destroying Hong Kong as an international financial center and that tight regulations on virtual assets are not in the interests of Hong Kong or of the Chinese nation. I oppose the regulatory philosophy of “same activity, same risk, same regulation”. I oppose this legislation. I oppose the upcoming legislation on virtual OTC.

But I will not go elsewhere, because as a patriot I love this city too much to go elsewhere. I will not leave, so I will stay and fight. I believe that after rational, civil, frank, and reasoned discussion and debate, we will come up with the right policies for Hong Kong.

When people ask me why they should come to Hong Kong rather than saying “if you don’t like our policies, you are welcome to go elsewhere” my attitude is “if you don’t like our policies, then we desperately need your ideas on how to make things better.” As long as someone is willing to act within the legal framework of Hong Kong, their views and criticisms will be heard regardless of whether they are motivated by patriotism or by commercial interest, and the capitalist system of Hong Kong exists precisely so that the People’s Republic of China can make use of the wealth, talents, expertise, and energies of those whose love is not directed at either Hong Kong or China but whose love is focused elsewhere. Moreover, under



the principle of “patriots ruling Hong Kong,” the only criterion for full participation in public affairs is that you love Hong Kong and love China, and once you are a patriot, then your opinions as to what should be done can be and often is as important as those of the heads of HKMA and FSTB, the Chief Executive of Hong Kong, or the President of China.

The political leaders have their role, but what often matters in Hong Kong is not what happens in the board rooms and conference tables, but what happens on the streets, and, in the shops and the back alleys of this city, and I have seen amazing things.

We will debate, we will argue, we will succeed at some things and fail at others. We will make mistakes, and we will correct those mistakes. But in the end, I have confidence that given honest, civil, rational, and democratic discussion, we will find the right path and Hong Kong will fulfill its role as an international financial center and fulfill its responsibilities to the central government and the Chinese people in the glorious history of the great rejuvenation of the Chinese nation.

To paraphrase the great President of the United States, John F. Kennedy in an earlier era of technological competition that I have used as guidance for my efforts at developing science and technology for the good of the Chinese nation and the good of all of humanity.

We do these 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.

Some claim that “Hong Kong is over”.

I say nonsense.

We have only just begun.

Faithfully yours,



Joseph Chen-yu WANG  
Bitquant Digital Services