

Hong Kong Licensing Regime for Virtual Asset Service Providers Passed with Three-Month Delay to Implementation Timelines

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On December 7, 2022, the Legislative Council (“**LegCo**”) of the Hong Kong Special Administrative Region (“**HKSAR**”) passed the Anti-Money Laundering and Counter-Terrorist Financing (Amendment) Bill 2022 (“**Amended AMLO**”) into law. On the same day, the LegCo’s Bills Committee also published a report (“**Report**”), providing clarification on certain concepts under the Amended AMLO, and explained the postponed timeline for the commencement of the licensing regime for virtual asset service providers (“**VASPs**”).^[1]

In our previous client alert^[2], we explained the proposal by the Government of the HKSAR (“**Government**”) to introduce a licensing regime for VASPs by amending the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) (“**AMLO**”). In this client alert, we explain and provide our views on the additional clarification provided on the licensing regime for VASPs, the updated timeline for the commencement of the licensing regime, and next steps.

I. Recap on the Key Proposals Under the Amended AMLO

The Amended AMLO introduces a licensing regime for VASPs, and imposes statutory anti-money laundering and counter-terrorist financing (“**AML/CTF**”) obligations on VASPs in Hong Kong. Some of the key takeaways are as follows:

- The operation of a virtual asset (“**VA**”) service will become a “regulated function”, such that VASPs will, in the future, be required to apply for a licence from the Securities and Futures Commission (“**SFC**”), before they can operate in Hong Kong.
- The licensing regime for VASPs is primarily intended to capture the operation of a VA exchange. However, the Government could expand the scope of “VA service” to cover other forms of VA activities, when the Government considers it necessary to do so in the future.
- The licensing requirements to be imposed on VASPs is likely to be modelled on existing requirements for the SFC’s licensing of regulated activities under the Securities and Futures Ordinance. This includes the fitness and properness requirements, and the requirement for a licensed VASP to have at least two responsible officers.
- The SFC has discretion to impose a range of licensing conditions on a VASP licensee, including conditions relating to financial resources, risk management policies and procedures, management of client assets, virtual asset listing and trading policies, prevention of market manipulation and abusive activities,

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[William R. Hallatt](#)

[Arnold Pun](#)

avoidance of conflicts of interest, among other requirements that can be imposed by the SFC as a licence condition.

- Licensed VASPs will be required to comply with existing requirements under the AMLO on customer due diligence and record-keeping requirements, which will be comparable to traditional financial institutions.
- A new enforcement regime applicable to VASPs will be introduced. Under the Amended AMLO it will be a criminal offence to carry on a business of providing VA service without a VASP licence and to issue advertisements relating to an unlicensed person's provision of VA service. It will also become a criminal offence to make fraudulent or reckless misrepresentations with the intention to induce others to invest in VAs and an offence to employ deceptive or fraudulent device, scheme or act, directly or indirectly, in a transaction involving VAs (which is likely to capture market manipulation activities).
- Relevantly, the offences of making fraudulent or reckless misrepresentations or employing deceptive or fraudulent devices, schemes or acts, are not limited to transactions on licensed VASPs and as such will capture all individuals and/or firms engaging in this type of conduct with a substantial nexus to Hong Kong.
- The SFC will be granted a significant range of supervisory powers over licensed VASPs. This includes the power to enter the business premise of a licensed VASP to conduct routine inspections of business records, request production of documents and other records, and to investigate non-compliance and impose disciplinary sanctions against licensed VASPs in contravention.

II. The Applicability of the VASP Regime to Non-Fungible Tokens

Under the Amended AMLO, “VA” generally captures a cryptographically secured digital representation value that:

- is expressed as a unit of account or a store of economic value;
- either:
 - functions (or is intended to function) as a medium of exchange accepted by the public as payment for goods or services, or for the discharge of debt, or for investment purposes; or
 - provides rights, eligibility or access to vote on the management, administration or governance of the affairs in connection with any cryptographically secured digital representation of value;
- can be transferred, stored or traded electronically; and
- satisfies other characteristics prescribed by the SFC.

In our previous alert, we noted that the proposed definition of “VA” did not capture non-fungible tokens (“**NFTs**”). This point was picked up during the LegCo meetings. The SFC has clarified that the assessment of whether an NFT is a VA needs to take into account its terms and features. In most cases, NFTs which merely represent a “genuine digital representation of a collectable” is unlikely to be captured by the definition of “VA” under the Amended AMLO; however where the NFT go beyond the scope of a collectable, for example where it contains fungible elements or allows holders to vote on its arrangement, then this may cause the NFT to be “a medium of exchange accepted by the public” or “a digital representation of value that provides holders with rights, eligibility or access to vote”, and therefore it will fall under the ambit of a VA.^[3]

The Government further explains that if a specific NFT is seen to be a VA, persons trading that specific NFT will require a licence if those dealings amount to a “VA service”, i.e., if the specific NFT is traded through the operation of an exchange. In other words, if the

trading occurs on a peer-to-peer basis, the persons would not be deemed as operating an exchange and their activities would not fall within the scope of a “VA service”, and therefore a VASP licence is not required.[\[4\]](#)

III. The Requirement of Providing VA Services to Professional Investors Only

In our previous client alert, we noted the proposal that, in order to promote investor protection, the licensing regime for VASPs will, at the initial stage, stipulate that VASPs can only provide services to professional investors (“**PI Restriction**”), and that this restriction will be imposed by the SFC as a licence condition. At that time, we observed that the use of the phrase “initial stage” and the proposal to impose the PI Restriction by way of a licensing condition, rather than in the legislation itself, suggested that the SFC may possibly allow expansion of VASP services to retail investors down the track when VA markets become more mature and regulated.

It appears that the Government recognises that VA markets have become more mature since the licensing regime for VASPs was first proposed. On October 31, 2022, the Government issued its policy statement on the development of VAs in Hong Kong[\[5\]](#) (“**Policy Statement**”), where the Government stated that it recognised the increasing acceptance of VA as a vehicle for investment allocation by global investors, be they institutional or individual. It was noted in the Policy Statement that the SFC would be conducting a public consultation on how retail investors may be given a suitable degree of access to VA under the new licensing regime for VASPs, while being careful and cautious about the risks to retail investors, including by enhancing investor education and ensuring that suitable regulatory arrangements are in place.

The Report provides further clarification on the Government’s position on the PI Restriction requirement, and notes that the PI Requirement will be imposed on licensed VASPs as a licensing condition at the initial stage. However it further states that the SFC will conduct a consultation on the detailed regulatory requirements on the new VASP regime; and during the consultation the SFC will consider whether to allow non-professional investors (i.e. retail investors) to partake in VA transactions with licensed VASPs, provided that additional investor protection measures are in place.[\[6\]](#)

The SFC’s thinking on the investor protection measures to allow retail investors to trade VAs with licensed VASPs will likely become clearer after the SFC publishes its consultation paper on the regulatory requirements under the new VASP regime.

IV. Postponement to the Commencement of the Amended AMLO and the Licensing Regime for VASPs

In the Report, the Government proposed to postpone the commencement of the Amended AMLO and the licensing regime for VASPs. Set out below is a summary of the original timeline and the new timeline for the commencement of the Amended AMLO and the licensing regime for VASPs, as well as the timing implications for the transitional period and the deadline to submit an application to the SFC under the licensing regime for VASPs.

Event	Original timeline	New timeline
Commencement date of the Amended AMLO.	January 1, 2023	April 1, 2023

Note that the criminal offences for fraudulent or reckless misrepresentations, or employing deceptive or fraudulent devices, schemes or acts, in relation to VA transactions, commences

from this date.

Commencement date of the March 1, 2023

June 1, 2023

licensing regime for VASPs

("VASP Regime

Commencement Date").

Start date for the 12 months Starting from March 1, 2023 Starting from June 1, 2023
transitional period

("Transitional Period Start

Date") for any corporation

that has been carrying on the
business of providing a VA
service in Hong Kong

immediately before the VASP

Regime Commencement

Date ("Existing VASPs"),

during which time the Existing
VASP can carry on VA
service in Hong Kong without
a VASP licence.

Deadline of the 9 months By no later than December 1, By no later than March 1,
period for Existing VASPs to 2023 2024

file an application to the SFC

for a licence under the
licensing regime for VASPs,
in order to be deemed to be
licensed from the day after
the expiry of the 12 months'
transitional period

("Application Deadline").

Existing VASPs that file an application to the SFC by the Application Deadline will be
deemed to be a licensed VASP from the day after the expiry of 12 months from the
Transitional Period Start Date (i.e. June 2, 2024) until the SFC has made a decision to
either approve or reject their licence application, or the licence applicant withdraws their
application.

The Report notes that the postponement is intended to provide the Government and the
SFC more time to work out the implementation details of the new regulatory regime,
including public consultation work by the SFC on the regulatory requirements for licensed
VASPs. The postponement is also intended to allow more time for the VASPs sector to
prepare for the introduction of the licensing regime.

We will continue to closely monitor developments in this area, and will provide a more
detailed update when the SFC publishes its public consultations on the regulatory regimes
for licensed VASPs.

[1] "Report of the Bills Committee on Anti-Money Laundering and Counter-Terrorist
Financing (Amendment) Bill 2022", LC Paper No. CB(1)855/2022 (December 7, 2022),
published by the Legislative Council, available at
<https://www.legco.gov.hk/yr2022/english/bc/bc05/reports/bc0520221207cb1-855-e.pdf>

[2] Hong Kong Introduces Licensing Regime for Virtual Asset Services Providers (June 30,
2022), published by Gibson, Dunn & Crutcher LLP, available at
<https://www.gibsondunn.com/hong-kong-introduces-licensing-regime-for-virtual-asset-services-providers/>

[3] Paragraph 13 of the Report

[\[4\]](#) Paragraph 14 of the Report.

[\[5\]](#) “Policy Statement on Development of Virtual Assets in Hong Kong”, published by the Financial Services and the Treasury Bureau on October 31, 2022, available at https://gia.info.gov.hk/general/202210/31/P2022103000454_404805_1_1667173469522.pdf

[\[6\]](#) Paragraph 27 of the Report.

The following Gibson Dunn lawyers prepared this client alert: William Hallatt, Arnold Pun, and Jane Lu.

Gibson Dunn’s lawyers are available to assist in addressing any questions you may have regarding these developments. If you wish to discuss any of the matters set out above, please contact any member of Gibson Dunn’s [Digital Asset Taskforce](#) or the Global Financial Regulatory team, including the following authors in Hong Kong:

William R. Hallatt (+852 2214 3836, whallatt@gibsondunn.com)

Grace Chong (+65 6507 3608, gchong@gibsondunn.com)

Emily Rumble (+852 2214 3839, erumble@gibsondunn.com)

Arnold Pun (+852 2214 3838, apun@gibsondunn.com)

Becky Chung (+852 2214 3837, bchung@gibsondunn.com)

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