



Consultation Paper on Legislative Proposal to Regulate Dealing in Virtual Assets

The Law Society's Submissions

The Financial Services and the Treasury Bureau (FSTB) and the Securities and Futures Commission (SFC) released a consultation paper on “Legislative Proposal to Regulate Dealing in Virtual Assets” (“Consultation Paper”) on 27 June 2025.

In response, the Law Society provides the following submissions. Unless otherwise defined, the same abbreviations and definitions appearing in the Consultation Paper are used in this paper.

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

Law Society's response:

Yes. Subject to there being relevant exemptions similar to other regulated activities under the Securities and Futures Ordinance (Cap 571) (“SFO”) including, but not limited, to intragroup transactions and persons whose dealing in VAs is incidental to their other business(es). See, for example, paragraphs (i) – (vii) of the definition of “dealing in futures contracts” in Schedule 5 of the SFO. Paragraph 2.10 of the Consultation Paper only mentions excluding peer-to-peer trading between individuals where no intermediary is involved. However, in our view, there is no basis for not applying the long-standing exemptions from the scope of existing regulated activities reflected in the SFO to the regulation of VA dealing services. In our view, equivalencies of all of these exemptions should apply to the definition and scope of VA dealing services.

Separately, it should be made expressly clear (perhaps by way of guidance issued by the SFC in connection with the Consultation Conclusions) that dealing in securities or futures contracts whose underlying investments include VAs, should fall outside the scope of VA dealing services as they will be already regulated as “dealing in

securities” or “dealing in futures contracts”. In our view, double regulating such products would be detrimental to the Hong Kong market.

We note that there is a separate public consultation exercise on the regulation of VA custodian services which, we assume, will also be exempted from the definition and scope of VA dealing services.

Lastly, we also suggest that market participants would benefit from clarity on the treatment of algorithmic execution, smart contract protocols, and automated market-making activities that may not involve human intermediation but are sometimes core to VA trading environments.

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

Law Society’s response:

We support the proposal discussed in paragraph 2.22 of the Consultation Paper to permit SFC-licensed VATPs to acquire or dispose of VAs for their own clients via non-SFC-licensed VATPs regulated in jurisdictions which offer “sufficient investor protection safeguards”. We note the intention to conduct a separate consultation on these investor safeguards and add that it would be helpful (if not essential) to the market and industry participants if the SFC would issue a list of such jurisdictions sufficiently prior to the commencement of the new regulations.

Otherwise, we have no comments on the proposed scope of the allowed activities.

Q3. *If licensees or registrants providing VA dealing services are allowed to acquire or dispose of VAs for clients via non-SFC licensed VATPs or liquidity providers, what are your comments on the safeguards that should be put in place?*

Law Society’s response:

Under the “same risk same regulation” principle, the obligations on registrants providing VA dealing services who acquire or dispose of VAs for clients via non-SFC licensed VATPs should, in principle, be no different from those applying to intermediaries holding other licenses.

Q4. *If licensees or registrants providing VA dealing services are required to hold client VAs via regulated VA custodians, what are your comments on a commercially*

viable and AML-compliant operational flow to conduct VA dealing activities?

Law Society's response:

Consistent with the “same risk, same regulation” principle, to conduct VA dealing activities in Hong Kong under the proposed regulatory framework, licensees should adopt an operational flow that is both commercially viable and AML-compliant. Operational flows should cover:

1. Client Onboarding & Due Diligence

- (a) Perform Customer Due Diligence (CDD) in accordance with the AMLO
- (b) Verify identity, source of funds, and risk profile
- (c) Conduct VA knowledge assessment and suitability checks on clients (where applicable)

2. Wallet Setup & Custody Integration

- (a) For clients whose VAs will not be held in a designated omnibus account, assign each client a segregated wallet managed by an SFC-licensed VA custodian, dealer or licenced bank
- (b) Establish proof of ownership/control of client wallets
- (c) Maintain real-time reconciliation between client records and custodian holdings

3. Transaction Execution

- (a) Execute trades via SFC-licensed VATPs (or regulated offshore platforms with enhanced due diligence) and back-to-back settlement
- (b) Use either omnibus accounts or direct client wallets depending on platform capabilities

4. Settlement & Transfer

- (a) Post-trade, transfer VAs to a custodian wallet (or direct to a client wallet)
- (b) Ensure no temporary custody by the dealer unless indispensable to the transaction or otherwise unavoidable or impracticable
- (c) Fiat proceeds should be remitted via licensed banks, licensed money service operators or other suitably regulated intermediaries if applicable

5. Ongoing Monitoring & Reporting

- (a) Implement AML transaction and client monitoring systems
- (b) Flag and report suspicious activity to the Joint Financial Intelligence Unit (JFIU)
- (c) Maintain audit trails and transaction logs for at least seven years

6. Client Communication & Disclosure

- (a) Provide clients with clear disclosures on custody arrangements, trading, platform and counterparty risks and fees
- (b) Offer real-time access to portfolio and transaction history

7. Additional compliance considerations

- (a) No staking, lending or margin trading unless separately licensed
- (b) Ensure cybersecurity and private key management protocols are robust and auditable

Q5. Do you think the regulatory requirements proposed suffice in addressing potential ML/TF risks and offering adequate investor protection?

Law Society's response:

In our view the proposed regulatory requirements should suffice.

Q6. Do you agree with the proposed transitional arrangement?

Law Society's response:

In view of the inherent risks, we agree are aligned with the approach in Para 2.29 of the Consultation Paper that it would be inappropriate for a deeming arrangement to be provided for pre-existing VA dealing service providers.

However, in line with proportionality, we recommend consideration of a “light-touch” licensing pathway for smaller firms or start-ups that deal only with Professional Investors and operate with limited balance sheet exposure. This could (i) mirror the approach taken by the Hong Kong Monetary Authority with the “sandbox” used for trialling AI applications and/or (ii) involve issuing such market participants with licenses which have appropriate conditions attached and (iii) facilitate innovation and market development.

We note that the current definition of professional investor under the SFO still does not allow virtual assets to count towards an investor's portfolio. As a result, we suggest that the FSTB and SFC should take this opportunity to update the definition of professional investor under the SFO for virtual assets to become a contributing asset.

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

Law Society's response:

Given the rapid pace of development, we support the expedited licensing or registration arrangements proposed.

Q8. *Based on the “user-pays” principle, do you have any comments on aligning the licensing application fee and annual fee for a licensee or registrant providing VA dealing services with those for Type 1 regulated activity under the SFO?*

Law Society's response:

We have no views on the proposed licensing fees.

Generally, given that: (i) VAs remains a developing industry; (ii) the competitive landscape (regionally and globally) for VAs and providers of VA dealing services; and (iii) the Hong Kong Government’s commitment to developing Hong Kong as an industry-leading digital asset hub, consideration should be given to ensuring that the level of licensing fees remain competitive and not a hindrance to selecting Hong Kong (versus competitor locations) as a base for operations.

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

Law Society's response:

Agreed. We support the extension of the regulatory perimeter to cover persons who actively market VA dealing services to the public of Hong Kong in line with principles already enshrined in the SFO for other regulated activities. As well as protecting the Hong Kong public, this also incentivises business to operate in Hong Kong within the licensed ecosystem.

However, we caution against inadvertently capturing offshore firms whose only connection to Hong Kong is the passive accessibility of their website, trading app or other platform.

Q10. *Do you agree that the SFC and the HKMA should be provided with the proposed powers?*

Law Society's response:

We agree that both the SFC and the HKMA should have the proposed powers.

Q11. *Do you agree with the proposed sanctions, which are comparable to those under the existing regulatory regimes for VATPs?*

Law Society's response:

We agree that the proposed sanctions for VATPS should be consistent with those under the AMLO.

Q12. *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?*

Law Society's response:

We agree that a review tribunal mechanism should be put in place to handle appeals.

**The Law Society of Hong Kong
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