

Legislative Council Panel on Financial Affairs

Response to Hon Dennis Kwok's suggestion to discuss regulation and development of initial coin offerings and "cryptocurrencies"

In promoting financial technologies ("Fintech"), the Government strives to facilitate financial innovation on the one hand and to protect the investing public on the other.

2. We have repeatedly pointed out that "cryptocurrencies" are not currencies but a type of virtual commodities. They do not have any backing, whether in physical form or from the issuers. Such virtual commodities are highly volatile in valuation and do not qualify as a medium of payment or electronic currencies. This notwithstanding, the distributed ledger technology ("DLT") that supports "cryptocurrencies" has much wider applications. The Government supports the financial services industry to develop and apply such technology. The Hong Kong Monetary Authority ("HKMA") published its second whitepaper on DLT last year. The whitepaper confirmed the promising nature of DLT (e.g. proof-of-concept projects on mortgage loan application, trade finance and digital identity management). Seven banks in Hong Kong are now commercialising the DLT-based, trade finance proof-of-concept into a Hong Kong Trade Finance Platform ("HKTFP"). HKTFP allows banks to digitise and share trade documents, automate processes, and reduce risks and frauds. HKMA is also building a cross-border DLT infrastructure, "Global Trade Connectivity Network ("GTCN")", with the Monetary Authority of Singapore to connect HKTFP to the National Trade Platform in Singapore. GTCN would help promote the digitalisation of cross-border trade and trade finance processes between the two places and beyond.

3. At the same time, financial regulators are closely monitoring the development of initial coin offerings ("ICOs") and "cryptocurrencies" in Hong Kong. They are also taking appropriate measures to safeguard the interest of the investing public. In September 2017, the Securities and Futures Commission ("SFC") published a statement which pointed out that if digital tokens offered in an ICO were "shares", "debentures", or interests in a "collective investment scheme ("CIS")", they would fall under the definition of "securities". In such cases, dealing in or advising on the digital tokens, or managing or marketing a fund investing in such digital tokens, might constitute a "regulated activity" and would require registration or a licence from SFC.

4. SFC also noted that futures and commodities exchanges in the United States had launched Bitcoin futures contracts. SFC issued a reminder in December 2017 that dealing in such contracts for investors in Hong Kong and engaging in related services, including relaying or routing orders, constituted regulated activities and required a licence from SFC regardless of whether the business was located in Hong Kong.

5. In February 2018, SFC issued an announcement that it had taken regulatory actions against a number of “cryptocurrency” exchanges and issuers of ICOs. SFC had sent letters to “cryptocurrency” exchanges and issuers of ICOs in Hong Kong or with connections to Hong Kong, warning them that they should not trade “cryptocurrencies” which were “securities” without a licence. Most of these “cryptocurrency” exchanges either confirmed that they did not provide trading services for such “cryptocurrencies” or took immediate rectification measures, including removing such “cryptocurrencies” from their platforms. ICO issuers also confirmed compliance with SFC's regulatory regime or immediately ceased to offer tokens to investors in Hong Kong.

6. We note that the regulatory approaches towards ICOs and “cryptocurrencies” vary across jurisdictions. Some regulators impose a ban, while other regulators leverage on existing regimes to regulate. The G20 meeting held in end March 2018 discussed the risks and related issues brought about by “cryptocurrencies”. The meeting agreed that there was a need to closely monitor the situation. We will continue to monitor the development of ICOs and “cryptocurrencies” in Hong Kong, and maintain close contacts with regulators in other jurisdictions through active participation in meetings of relevant international organisations, such as the International Organisation of Securities Commissions.

7. Fintech can enhance efficiency, lower operating cost, and allow the public a new experience in financial services. Yet at the same time, Fintech can also bring about risks. The Financial Services and the Treasury Bureau and the Investor Education Centre jointly launched a public education campaign earlier on the risks associated with ICOs and “cryptocurrencies”. The campaign aimed to provide the public with a better understanding of the potential risks of participating in ICOs and “cryptocurrency” transactions.