

LCQ15: Policy on digital assets

Following is a question by Dr the Hon Johnny Ng and a written reply by the Acting Secretary for Financial Services and the Treasury, Mr Joseph Chan, in the Legislative Council today (December 11):

Question:

It has been reported that financial enterprises around the world have increased their investment in digital assets one after another, with the price of bitcoins, hailed as "digital gold", rocketing in tandem since this year, and the development of the global currencies will move toward digitalisation. Moreover, some overseas regions plan to position bitcoins as strategic reserve assets of the government, and even propose to set up a dedicated commissioner in charge of formulating and implementing the relevant policies, as well as promoting the development of the cryptocurrency industry. In this connection, will the Government inform this Council:

(1) as there are views pointing out that while the cryptocurrency industry is fast flourishing, the current regulatory regime related to cryptocurrencies has yet to be improved in Hong Kong, whether the Government will further expedite improvement to the relevant regulatory regime;

(2) whether the Government will consider setting up a new dedicated department or commissioner to study and formulate policies relating to digital assets and cryptocurrencies;

(3) as there are views that bitcoins have been gaining recognition worldwide, and as a digital asset, bitcoins are characterised by decentralisation despite having inherent risks, whether the Government will consider including digital assets and cryptocurrencies in its fiscal reserves and acquiring the same continuously through the Exchange Fund for long-term holding; and

(4) whether the Government has assessed and studied the impact of positioning bitcoins as strategic reserve assets by foreign countries on the financial security of China and Hong Kong (e.g. whether this will in the long run put pressure on the Hong Kong dollar system and its economic situation); if the Government has, of the relevant impact, together with the Government's corresponding measures in place, including whether it will leverage Hong Kong's first-mover advantages and unique resources in the field of cryptocurrencies to formulate sound strategic deployment, with a view to contributing to safeguarding national financial security?

Reply:

President,

On Dr the Hon Johnny Ng's question, upon consulting the Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC), my

reply is as follows:

(1) and (2) The rapidly evolving virtual asset (VA) sector is bringing new opportunities for financial innovation and inclusion while adding complexities to the financial system. In respect of regulation, the interconnectedness between the traditional financial system and the VA markets appear to be more apparent and rising, with international organisations and standard-setting bodies (SSBs) having accorded considerable attention to the potential risks posed by the prevalence of VAs on monetary and financial stability. Among others, in July 2023, the Financial Stability Board, in consultation with relevant SSBs, published a finalised global regulatory framework for crypto-asset activities. The framework provides recommendations relating to the regulation, supervision and oversight of crypto-asset activities and markets as well as global stablecoin arrangements. As a leading international financial centre in Asia, Hong Kong has key influence in the regulation and development of VA. In this connection, to facilitate the long-term sustainable development of industries related to VA, the Financial Secretary established the Task Force on Promoting Web3 Development in 2023 to make suggestions to the Government in respect of the sustainable and responsible development of the industries. Besides, in October 2022, the Government also issued the Policy Statement on Virtual Assets Development in Hong Kong, setting out that the Government and regulators would adhere to the principle of "same activities, same risks, same regulations" in enhancing VA-related regulatory frameworks.

In respect of VA-specific regulatory policies and measures, the Financial Services and the Treasury Bureau (FSTB) is responsible for formulating relevant policies and co-ordinating various departments and financial regulators. Among others, the Government has amended the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) to introduce a licensing regime for VA service providers, ensuring that VA trading platforms comply with relevant international requirements on anti-money laundering and counter-terrorist financing while protecting investors. Further to the commencement of the licensing regime last year, FSTB has consulted the Panel on Financial Affairs of the Legislative Council (LegCo) this year on the regulatory regime for fiat-referenced stablecoin issuers, and will introduce the relevant legislative Bill to the LegCo within this month. Besides, regarding the over-the-counter trading services of VA, we are adjusting the proposal taking into account outcomes of the public consultation conducted early this year, and will conduct the second public consultation next year. We will also introduce a proposed licensing regime to regulate VA custodian services next year.

(3) The Exchange Fund invests in globally diversified asset classes and markets to diversify risks and enhance long-term returns. While crypto-assets are not the target assets of the Exchange Fund, the external managers appointed by the HKMA also invest in diversified asset classes and markets around the world. It cannot be ruled out that there may be investments involving crypto-assets during the investment operations of the external managers at different points of time, but the relevant proportion is minimal.

(4) The Linked Exchange Rate System (LERS) has been operating for more than four decades since its establishment in 1983, weathering many economic and interest rate cycles, as well as multiple global and regional economic and financial crises. It is the cornerstone of financial and monetary stability in Hong Kong and has continued to work well. Operating under the robust regime of the currency board arrangement, the LERS enjoys strong credibility in the global financial and monetary markets. International organisations such as the International Monetary Fund have continuously endorsed the suitability of the LERS as the monetary system for Hong Kong.

As mentioned above, the VA sector is having increasing interconnectedness with traditional financial activities. On one hand, the development of VA and related technologies can bring potential benefits to the financial market as a whole. For example, the efficiency and transparency of economic and financial activities could be enhanced by utilising blockchain technology. On the other hand, VA is associated with risks in different aspects including financial stability, money laundering and investor protection. The Government and regulators will continue to formulate regulatory regimes to address such risks under the principle of "same activities, same risks, same regulations". This approach can create a facilitative environment to foster innovation in a sustainable and responsible manner, while ensuring financial safety at the same time, so as to strengthen Hong Kong's key role as an international financial centre.

Other than enhancing the regulatory regime, the Government and regulators have also launched measures to facilitate market development. On tokenisation, to enhance market clarity, the SFC issued two circulars in November last year, respectively on intermediaries engaging in tokenised securities-related activities and on tokenisation of SFC-authorized investment products to shed light on the regulatory expectations from an investor protection perspective. The SFC also announced in October this year a number of measures to facilitate the VA development in Hong Kong, including a swift licensing process for VA trading platforms, and establishing a consultative panel for licensed trading platforms which is expected to operate from early next year.