

31 March 2022

Submission by email (stablecoin_feedback@hkma.gov.hk)

Hong Kong Monetary Authority
Two International Finance Centre
8 Finance Street, Central
Hong Kong

Re: ASIFMA response to the HKMA's Discussion Paper on Crypto-assets and Stablecoins

Dear Sir/Madam

The Asia Securities and Financial Markets Association (“**ASIFMA**”)¹ appreciates the opportunity to respond to the discussion questions set out in the Hong Kong Monetary Authority’s (the “**HKMA**”) Discussion Paper on Crypto-assets and Stablecoins published on 12 January 2022 (the “**Discussion Paper**”). Feedback set out in this response has been collected from ASIFMA’s Fintech Working Group and Crypto Sub-Working Group, which has been closely following global, regional and local developments relating to virtual assets in recent years. We are grateful to ASIFMA law firm member Latham & Watkins LLP for their support in drafting this response based on input from ASIFMA’s Fintech Working Group and Crypto Sub-Working Group.

General comments

¹ ASIFMA is an independent, regional trade association with over 160 member firms comprising a diverse range of leading financial institutions from both the buy and sell side, including banks, asset managers, law firms and market infrastructure service providers. Together, we harness the shared interests of the financial industry to promote the development of liquid, deep and broad capital markets in Asia. ASIFMA advocates stable, innovative, and competitive Asian capital markets that are necessary to support the region’s economic growth. We drive consensus, advocate solutions and effect change around key issues through the collective strength and clarity of one industry voice. Our many initiatives include consultations with regulators and exchanges, development of uniform industry standards, advocacy for enhanced markets through policy papers, and lowering the cost of doing business in the region. Through the GFMA alliance with SIFMA in the United States and AFME in Europe, ASIFMA also provides insights on global best practices and standards to benefit the region. More information about ASIFMA can be found at: www.asifma.org.

ASIFMA members (“**Members**”) support the HKMA’s proposal to establish a regulatory framework for stablecoin activities that is consistent with international standards as they evolve and mature.

In light of Hong Kong’s institutional model of financial regulation, Members agree that the HKMA should work closely with other Hong Kong financial regulators (particularly the Securities and Futures Commission (“**SFC**”)) to align the proposed regulatory approach for stablecoin activities with existing and proposed regulatory regimes to avoid regulatory overlap.

Members also encourage the HKMA to continue its engagement with global standard-setting bodies and regulators to develop a consistent approach to the definition, categorisation and regulatory treatment of stablecoins in order to minimise regulatory arbitrage across jurisdictions and to create a predictable, effective regulatory framework that will be fit for purpose in the long term. This should help to instill consumer confidence and promote investor protection, as well as support innovation in this sector.

Members believe that stablecoin-related activities should be regulated on a risk-based approach. The regulatory regime should aim to tackle the key risks posed by stablecoins in a proportionate manner, in particular giving priority to areas that pose higher degrees of risk. Taking this into account, Members agree that the HKMA’s initial focus should be targeted at payment-related stablecoins that are systemically important but that the regulatory framework should have flexibility to adapt as needed as the market further matures. There should further be an emphasis on implementing effective prudential regulation of issuers of stablecoins but Members generally believe that it is not necessary to impose a mandatory requirement for issuers to be incorporated in Hong Kong as the HKMA can exercise effective supervision over branches, similar to its existing practices for banks. Given Hong Kong’s institutional model of financial services regulation, Members expect that the HKMA will need to carefully consider potential areas of regulatory overlap or regulatory gaps and ensure that they are adequately addressed, particularly with respect to secondary/ancillary stablecoin-related activities. Given the fast-paced nature of technology development in this area, there is a need to continuously assess ongoing risks of stablecoin-related activities, such as operational and cybersecurity risks, and embed that analysis in the regulatory approach.

ASIFMA wishes to thank the HKMA for the opportunity to share this feedback on the Discussion Paper. Members are supportive of continued dialogue between the HKMA and the industry as the regulatory regime is being developed to ensure the appropriate calibration of the twin objectives of effectively managing risk while also supporting innovation. We welcome the opportunity to contribute to further consultations on stablecoin regulation in the future.

Unless otherwise defined herein, the terms used in this response have the meanings assigned to them in the Discussion Paper. If you have any further questions or would like to discuss our response in further detail, please contact me.

Sincerely,

Laurence Van der Loo
Executive Director, Technology & Operations
Asia Securities Industry & Financial Markets Association

Responses to discussion questions

Question 1	Should we regulate activities relating to all types of stablecoins or give priority to those payment-related stablecoins that pose higher risks to the monetary and financial systems while providing flexibility in the regime to make adjustments to the scope of stablecoins that may be subject to regulation as needed in the future?
<p>Priority for payment-related stablecoins with flexibility in mind</p> <p>Members agree that the proposed regulatory approach should be sufficiently broad and flexible so that it can take into account any changes in systemic risks and international standards of stablecoins in the longer term. There is a need to implement a regulatory regime that ensures a level playing field, follows the principle of “same risk, same regulation” and which is future proofed and capable of pivoting to address other types of stablecoins based on need and international consensus. In particular, given the fast pace of innovation in this industry, Members believe that it is important for the regulatory regime to be sufficiently adaptable to address stablecoins that become systemically important regardless of the method of collateralization (single currency, multi-currency/asset basket or algorithmic) used by the relevant stablecoin.</p> <p>While the regime should be flexible to make adjustments as needed, Members generally consider that the regulatory focus should lie with systemically important stablecoins. At this point in time, this would mostly concern payment-related stablecoins – and especially payment-related stablecoins that are backed by a single fiat currency – since these stablecoins currently have the largest market share and are likely to pose higher risks to monetary and financial systems.²</p> <p>Prioritising systemically important stablecoins</p> <p>The FSB has focused on “global stablecoin” arrangements, meaning a widely adopted stablecoin with a potential reach and use across multiple jurisdictions. Members generally agree that, on a risk-based approach, the HKMA should prioritize payment-related</p>	

² Notwithstanding that Members agree that payment-related stablecoins should be an area of regulatory focus, we note that the FSB’s “Assessment of Risks to Financial Stability from Crypto-Assets” (February 2022) observes that stablecoins are at present primarily used to facilitate trading, lending, or borrowing of other crypto-assets on or through crypto-asset trading platforms and that the current generation of stablecoins are not yet used as a widespread means of payment. From a functional perspective, stablecoins currently are less aligned with SVF facilities, which are stores of value used by consumers to facilitate payments for goods and services. The FSB notes that should stablecoins be used more extensively for payments, they would face many of the same risks as current payment systems, including credit risk, liquidity risk, operational risks arising from improper or ineffective governance, and settlement risk.

stablecoins that are systemically important, and which have the capacity to impact financial markets, financial stability or incur mass scale adoption in multiple countries. Members encourage the HKMA to work together with international standard-setting bodies, including the FSB, CPMI, IOSCO and other regulators, to adopt a clear definition and consistent approach in reviewing the systemic importance of stablecoins to avoid the risk of uneven regulation or regulatory arbitrage. There should be alignment on thresholds to determine systemic importance and adoption of risk-based measures to ensure regulatory oversight over critical payment activities and functions.

Clear definitions are needed

Members strongly believe that any regulations on stablecoins should be underpinned by clearly defining what tokens are captured by the regulatory regime and such definitions should be aligned with international standards to prevent regulatory arbitrage and to reduce complexities that could be caused by inconsistencies in regulation for entities that conduct stablecoin activities across multiple markets. There are various initiatives seeking feedback on crypto-asset taxonomies³ in other contexts and we are of the view that the Hong Kong regulatory regime should be consistent with definitions that are adopted in a broader international context.

In respect of the HKMA's taxonomy used, Members would appreciate clarification on the following points:

- whether the HKMA contemplates asset-linked stablecoins encompassing stablecoins backed by a non-currency type of asset (*e.g.*, commodities, other financial assets such as securities);
- whether asset-linked stablecoins include those that reference a basket (*i.e.*, more than one) currency, commodity or asset;
- whether the HKMA has any proposed standards around the type of collateral which is expected to provide backing for the stablecoin; and
- whether there is any particular focus on stablecoins linked to the Hong Kong dollar.

Exclusions and potential overlapping regimes

³ For example, in relation to the FSB's consultation on 'Addressing the Regulatory, Supervisory and Oversight Challenges Raised by "Global Stablecoin" Arrangements', the response from the Global Financial Markets Association ("GFMA") included suggestions about how best to define crypto-assets, including stablecoins (see <https://www.gfma.org/wp-content/uploads/2020/07/gfma-response-fsb-cp-global-stablecoins.pdf> (Appendix A)).

Members are of the view that certain digital tokens (particularly “closed loop” tokens and tokens that are not used by consumers/clients) should be excluded from the definition of “stablecoin”, in particular:

- Central Bank Digital Currency (“**CBDC**”): A digital form of money that represents a liability of a central bank in a single fiat sovereign currency that may or may not pay interest. Members note the exclusion of CBDCs in the HKMA’s discussion paper and support such exclusion, which is consistent with the SFC’s approach to virtual asset regulation.
- Financial Market Infrastructure (“**FMI**”) Tokens: A digital unit of account issued by a FMI to its participants reflecting deposits held at a central or commercial bank in a single fiat currency that may or may not pay interest.
- Settlement tokens: Representations on distributed ledger technology (DLT) of underlying traditional securities/financial instruments issued on a different platform (*e.g.*, a traditional Central Securities Depository, registrar, etc.) where such representation itself does not satisfy the definition of a security or financial instrument under local law and is used solely to transfer or record ownership or perform other mid/back-office functions (*e.g.*, collateral transfer, recording of ownership).
- Tokenized commercial bank money/deposit tokens: Digital units of account representing deposits of cash to a bank by its customers that can be used to account for transactions internally within the bank or to net obligations between bank customers. These tokens have no value or utility outside the bank in which the corresponding cash has been deposited and they are not issued to or used by external counterparties.

With the exception of CBDCs, which are still being developed, these types of digital tokens are already in use within the financial services industry and members are of the view that they do not give rise to the same financial stability or investor protection concerns that the proposed regulation of stablecoins is seeking to address, and they are already subject to existing regulations.

In addition, Members are of the view that if the HKMA’s regulatory framework extends beyond single fiat currency-backed stablecoins, a clear distinction should be drawn between: (i) single fiat currency-backed stablecoins; (ii) stablecoins that are pegged to a basket of

assets; and (iii) algorithm-based stablecoins. Members note that stablecoins that are pegged to a basket of assets and algorithm-based stablecoins may share similar characteristics and functions comparable to that of money market funds, investment funds or structured products and such stablecoins could already be subject to regulation (or be exempt from regulation) under existing securities laws. Issuers and dealers in such products may already be subject to existing licensing, authorisation and other requirements, and to impose another layer of regulation could result in these entities becoming subject to overlapping regimes.

Question 2	What types of stablecoin-related activities should fall under the regulatory ambit, e.g. issuance and redemption, custody and administration, reserves management?
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Members generally agree with the list of activities proposed by the HKMA which should fall under the regulatory ambit, while recognizing that, on a risk-based approach, the primary focus should be on stablecoin issuers (*e.g.*, entities responsible for issuing the stablecoins and redeeming the stablecoin for the asset).

Practical concerns have been noted in relation to regulating secondary or ancillary activities associated with stablecoins, such as storing private keys providing access to stablecoins (as this appears to cover arrangements where a self-custody model is adopted) and executing transactions in stablecoins (as this might be overly broad and cover secondary trading between users or on virtual asset exchanges).

In addition, Members consider that the following stablecoin-related activities should also be included, insofar as they are not already covered by the existing proposed activities:

- investment activities in relation to reserve assets;
- provision of services to facilitate participants' access to the network or underlying infrastructure (such as any software or services necessary to participate in the use of the stablecoins); and
- the activity of purchasing/exchanging a stablecoin with fiat money.

As noted below, Members believe that existing financial institutions and intermediaries which are regulated to conduct analogous activities should be given exemptions or deemed licenses to prevent regulatory overlap and promote consistency.

Aligning with the existing regulatory framework

Members note that in introducing the licensing requirements to stablecoin-related activities, the HKMA proposes to either expand the scope of the PSSVFO or introduce a new legislation.

Depending on the regulatory framework which the HKMA proposes to adopt (including the regulatory perimeter and minimum authorization requirements), there may be efficiencies with expanding the scope of the PSSVFO and the Banking Ordinance – or adopting new legislation. Members believe that the manner of implementation can be addressed by way of further consultation when the overarching regulatory regime has been finalised.

Multiple entities in one stablecoin arrangement

The HKMA notes that multiple entities involved in one stablecoin arrangement may be required to seek authorisation from the HKMA. Members believe that this is an important area to be aligned with international standards as licensing multiple entities as part of a single stablecoin arrangement could create a significant compliance and cost burden.

Consistent with existing outsourcing rules and principles, a service provider who only provides services to an entity conducting stablecoin-related activities should not be brought within the scope of the licensing requirement if its activities are not licensable or not conducted in or from Hong Kong or not actively marketed to the Hong Kong public. The HKMA could rely in part or in whole on its existing Supervisory Policy Manual Module on Outsourcing (SA-2) when providing guidance for its expectations around outsourcing.

Question 3

What kind of authorisation and regulatory requirements would be envisaged for those entities subject to the new licensing regime?

Members generally agree with the list of high-level regulatory requirements proposed by the HKMA as applied on a risk-based approach (rather than a one-size-fits-all manner) following the principle of “same risk, same regulation”. Members expect that the HKMA will issuance guidelines and explanatory notes on licensing and supervision similar to its existing practices for the banking and stored value regimes.

Members stress the importance of ensuring that the regime for stablecoins is designed to avoid overlapping or creating regulatory arbitrage opportunities with respect to the regimes administered by the SFC or other Hong Kong regulators.

Members have the following specific comments⁴ on the regulatory requirements proposed by the HKMA: **(iv) Maintenance and management of reserves of backing assets**

Having regard to the existing requirements for SVFs and banks:

- Sufficient amounts of reserve assets should be held for each stablecoin issued/minted. The backing assets should be held by an authorized institution (“AI”) or a bank regulated/supervised by regulators in overseas jurisdictions. Reserve assets should be held either in the name of the stablecoin holders or for their benefit. Notwithstanding Members support for this requirement, we have observed that some stablecoin issuers (like many other companies operating in the virtual assets industry) currently find it difficult to obtain bank accounts as banks may be hesitant to deal with crypto-native companies. Members expect that the establishment of a robust regulatory framework would make banks more willing to provide services to stablecoin issuers but, to the extent there is hesitancy within the banking industry, this may be an area in which the HKMA could provide appropriate guidance in order to ensure that stablecoin issuers are able to comply with the requirement to keep reserve assets with a bank and to ensure that there is a level playing field.
- For stablecoins which are not issued by banks, the reserve asset requirements should be consistent with SVF issuers (*i.e.*, the stablecoins should be backed by cash or bank deposits and in adequately segregated accounts).
- Stablecoin issuers should be prohibited from pledging the reserve assets or otherwise using the reserve assets to secure the obligations of the issuer.
- Reasonable mechanisms for withdrawal/redemption of reserve assets by stablecoin holders should be in place.
- Consumers should be protected from the insolvency of the stablecoin and the holder of the reserve assets backing the stablecoin. Proper safeguards should be in place to ensure that the collateral does not form part of the estate of the issuer, any exchange, or the bank holding such reserve assets. In connection with this, the HKMA may also wish to consider customer compensation

⁴ We note that Members did not raise any additional specific comments with respect to items (i) (Authorisation requirements), (ii) (Prudential requirements) or (iii) (Fit and proper requirements on management and ownership).

arrangements in the event of insolvency of the stablecoin issuer.

(v) Systems, controls, governance and risk management requirements

Largely similar to the existing requirements for SVFs and banks:

- Conduct requirements as part of the corporate governance framework should be established.
- Standalone requirements for banks to assess their technology risk when conducting/being involved in stablecoin activities should be put in place.
- There should be requirements for issuers and service providers in relation to resolution, exit planning and business continuity planning (and persons are already subject to these obligations by virtue of being banks etc. should update their planning).
- Requirements relating to firms' internal record keeping processes should be established.
- Privacy protection standards should be set out. The appropriate minimum level of privacy protection should continue to apply, including (i) the ability for consumers to understand and permit specific data sharing arrangements at a granular level while ensuring the legal enforceability of those permissions; and (ii) the proper anonymisation of personal data that is pooled for aggregated analysis. Public trust in privacy designs could be enhanced through third party reviews of architecture and operations.

(vi) AML/CFT requirements

- The HKMA should provide guidance on its regulatory expectations on stablecoin-specific AML/CFT requirements, leveraging existing AML/CFT rules for banks/SVF issuers and reflecting any specific standards recommended by the FATF.

(viii) Financial reporting and disclosure

- There should be a requirement to make clear disclosures to potential holders and stakeholders about the reserves and risks involved.
- Reserve assets should be subject to periodic disclosures and audits. Stablecoin issuers should be required to disclose their ability and process to freeze

stablecoins.

- Working with bodies such as the Hong Kong Institute of Certified Public Accountants, HKMA can consider establishing standards and appointing licensed auditors specialized in payments to conduct an independent assurance assessment aside from financial reporting and disclosure. There is a need also for code auditing and reserve auditing/attestation.
- Requirements on disclosure/communication to stablecoin holders should include:
 - a clear articulation of the nature of the holder's claim and their redemption rights;
 - any limitations or conditions on the redeemability of the stablecoin;
 - the relevant risks, including market risks and those relating to the position of the reserve;
 - network rules and the responsibilities of participants in the stablecoin arrangement/network;
 - the identification of legal rights and recourse; and
 - applicable fees and conditions, including transaction taxes and other associated tax costs.
- Requirements relating to safe outsourcing of key services, if employed, should be implemented to ensure continuous and adequate functioning.
- There should be appropriate reporting and audit standards with respect to reserves.

(ix) Safety, efficiency and security requirements

- Safeguards should be place on wallets and exchanges to ensure users' stablecoins are properly protected, where applicable.
- Requirements should be imposed relating to privacy and security of private keys providing access to stablecoins.
- Open API standards should be adopted to foster innovation and improved customer experience.

(x) Settlement finality:

- Given the possibility of "forks" or stablecoins with governance features

(which allow holders to determine some or all of the aspects of management of the stablecoin), there should be requirements on how such matters are handled.

Deemed licences or exemptions for banks

Given that banks are already subject to stringent prudential and other requirements, the HKMA should consider granting deemed licences or other exemptions to banks to conduct stablecoin-related activities. For example, under the PSSVFO, licensed banks in Hong Kong are eligible to be SVF issuers and benefit from exemptions to certain statutory requirements.

Question 4

What is the intended coverage as to who needs a licence under the intended regulatory regime?

Members strongly believe that the HKMA’s proposal to limit the grant of licences for the activities listed in Question 2 to Hong Kong-incorporated companies is unduly restrictive. Given the global nature of stablecoin arrangements, the HKMA should permit companies incorporated overseas but registered as a branch in Hong Kong under the Companies Ordinance (Cap. 622) to be eligible to apply for a licence.

Members are concerned that limiting the grant of licences to Hong Kong incorporated companies would create a structural barrier to entry and would represent a departure from the typical structure of many companies that currently provide stablecoin-related activities on an international and cross-border basis. Members note that many large international financial institutions are authorized in Hong Kong as a branch and would therefore not be eligible to participate in stablecoin-related activities if such activities are limited to locally incorporated companies (and might also potentially concentrate risk within a limited number of institutions). Adopting a “same risk, same regulation” approach, the HKMA should allow branches to be licensed as long as they meet the same requirements expected of locally incorporated licensees. Having international alignment on capital, liquidity and other requirements identified in Question 3 will minimize potential regulatory arbitrage and ensure that Hong Kong’s locally incorporated stablecoin issuers are not disadvantaged. In connection with this, when the HKMA is considering a foreign-incorporated entity, the HKMA can have regard to the home supervisor and the home regulatory framework to assess whether it is equivalent to that of Hong Kong (similar to the existing assessment the HKMA conducts when considering authorization for foreign-incorporated banks).

Granting licenses to the Hong Kong branches of overseas incorporated companies would also benefit financial innovation and consumer choice in Hong Kong, and allow multinational companies which may have better financial and technological resources to provide services to Hong Kong consumers.

We also note that permitting Hong Kong branches of overseas-incorporated entities to be licensed would be consistent with the proposed regulatory requirements for virtual asset exchanges under the expected amendments to the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615).⁵

In addition, Members encourage the HKMA to consider potential cross-border recognition arrangements for stablecoins that are issued by companies or banks domiciled and supervised by an equivalent jurisdiction. This is especially relevant given the global nature of stablecoins and the fact that global systemically important stablecoins may not be actively marketed by a particular entity to a jurisdiction but may be sought out and used by people in that jurisdiction.

To ensure effective regulation over the relevant overseas entities that conduct stablecoin-related activities in Hong Kong, Members also believe that the HKMA should consider alternative supervisory or regulatory arrangements with overseas jurisdictions, such as information-sharing and other supervisory access arrangements, consistent with the HKMA's existing practice of engagement and cooperation with overseas banking regulators.

Question 5

When will this new, risk-based regime on stablecoins be established, and would there be regulatory overlap with other financial regulatory regimes in Hong Kong, including but not limited to the SFC's VASP regime, and the SVF licensing regime of the PSSVFO?

Members appreciate the HKMA's effort to coordinate with other stakeholders, financial regulators and relevant parties to avoid regulatory overlap or arbitrage.

Members agree that there may be overlap with existing financial regulatory regimes, including the VASP and PSSVFO regimes. For example, in addition to those mentioned above:

⁵ We note that the original proposal by the Financial Services and the Treasury Bureau was that virtual asset exchanges must be operated from Hong Kong-incorporated companies but in response to consultation feedback, this proposal was amended to allow Hong Kong branches of overseas companies to be eligible for licensing.

- trading or referral of stablecoins (*e.g.*, those issued overseas) to clients by intermediaries (whether on a recommendation/solicitation or reverse enquiry basis) may be caught by the HKMA and the SFC’s recent joint circular on intermediaries’ virtual asset-related activities (“**Joint Circular**”). On this basis, consumers may only be able to hold stablecoins through intermediaries on a SFC-licensed virtual asset trading platform and only if they are “professional investors”. There should be further clarification that stablecoins are not meant to be captured by the Joint Circular since they are not typically regarded as investment or similar products.
- activities related to management of reserve assets may constitute Type 9 (asset management) regulated activity.
- executing transactions in stablecoins may fall under the VASP regime.
- for transactions in respect of foreign currency stablecoins, money changing requirements may be relevant.

As mentioned above, Members encourage the HKMA to align the proposed regulatory approach for stablecoins with existing regimes and consider how stablecoin activities can be regulated or exempted under existing regimes to avoid regulatory overlap (*e.g.*, a bank holding reserve assets should not be required to obtain a separate licence under the proposed regime). For these purposes, deemed licences or exemptions for existing licensed entities could be adopted to promote consistency.

Members also believe that the proposed regulatory approach should consider elements beyond financial services regulations which will be important to the operation of the stablecoin arrangements. These include data protection, competition and cyber security issues. A holistic approach should be adopted so that, for example, data privacy and protection requirements are aligned with cross-sectoral rules for the use, processing, and management of data.

The HKMA should also incorporate key pieces of global stablecoin guidelines into the proposed regulatory approach, such as the BCBS proposal on the prudential treatment of crypto-asset exposures.

Question 6

Stablecoins could be subject to run and become potential substitutes of bank deposits. Should the HKMA require stablecoin issuers to be AIs under the Banking Ordinance, similar to the recommendations in the

	<p>Report on Stablecoins issued by the US President’s Working Group on Financial Markets?</p>
<p>Members agree strongly that the HKMA should work together with international regulators and standard-setting bodies to adopt a consistent approach to minimum requirements for stablecoin issuers, including whether stablecoin issuers are required to be banks. As mentioned in the response to Question 4, there should be consideration for jurisdictional equivalence so that overseas stablecoin arrangements can be recognized in Hong Kong with home regulators exercising consolidated supervision. This will require minimum requirements to be consistent internationally.</p> <p>Members believe that it is vitally important to ensure that stablecoin issuers meet high prudential standards like SVFs and banks in order to adequately protect stablecoin holders. They agree that the HKMA should adopt a risk-based approach and where appropriate apply higher prudential requirements (<i>e.g.</i>, capital and liquidity requirements) to systemic stablecoin arrangements similar to the current approach for banks. At minimum, the reserve assets should be held by AIs or banks regulated by an overseas jurisdiction. Members stressed that stablecoins should be adequately regulated to safeguard against risks to economic stability resulting from evolutions in the delivery of financial services, noting in particular that it will be important to ensure that banking risks do not build up in non-bank or less regulated sectors and that no unregulated forms of shadow banking will be created.</p> <p>All stablecoin issuers (whether or not they are banks) should be subject to the proposed requirements discussed in Question 3 above (including AML/CFT and sanctions screening requirements). Any non-bank stablecoin issuer (and any other entity assisting with the stablecoin operations) should be regulated in a manner similar to banks and/or entities issuing a non-digital asset analogous offering. In this instance, the sole responsibility of a bank involved in this arrangement would be to safeguard the collateral only. It should not be subject to additional requirements as this would disincentivise it from offering custody services for the collateral.</p>	
<p>Question 7</p>	<p>Would the HKMA also have plan to regulate unbacked crypto-assets given their growing linkage with the mainstream financial system and risk to financial stability?</p>

Members are supportive of the HKMA’s plan to monitor the development of crypto-assets more widely, as well as the HKMA’s proposal to apply the “same risk, same regulation” principle in steering its overall regulatory approach. It is important that the HKMA provide clarity on the prudential and regulatory framework which applies to crypto-assets, including the prudential and accounting treatment of such assets. As mentioned in the response to Question 6 above, the HKMA should coordinate with international regulators to ensure that its approach to crypto-assets is consistent with international regulatory developments.

Members also take note of the HKMA’s recent circulars⁶ providing additional guidance to banks and intermediaries on interface with virtual assets and conduct of virtual asset-related activities.

Question 8

For current or prospective parties and entities in the stablecoins ecosystem, what should they do before the HKMA’s regulatory regime is introduced?

Members believe that these parties should consider developing frameworks and standards focusing on the key functions of typical stablecoin arrangements, such as issuance and redemption of tokens and execution of transactions. These standards should include plans to manage risks related to money laundering and terrorist financing, know-your-customer and know-your-transaction.

In connection with this, Members seek additional clarity from regulators and supervisors on prudential, tax and accounting treatment. In particular, tax certainty is needed on how virtual currencies and other digital assets/crypto-assets fit within the existing tax framework and how are they classified and treated for tax purposes.

⁶ <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2022/20220128e3.pdf> and <https://apps.sfc.hk/edistributionWeb/api/circular/openFile?lang=EN&refNo=22EC10>