The Hong Kong Chartered Governance Institute

Submission to

Financial Services and the Treasury Bureau (FSTB)
and
Securities and Futures Commission (SFC)

Public Consultation on

Legislative Proposal to Regulate Virtual Asset Custodian Services

The Hong Kong Chartered Governance Institute 香港公司治理公會
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By Email: vacustody-consult@fstb.gov.hk

Division 5, Financial Services Branch
Financial Services and the Treasury Bureau
24/F, Central Government Offices
Tim Mei Avenue, Tamar Central, Hong Kong

Dear Sirs,

Submission on the Public Consultation on Legislative Proposal to Regulate Virtual Asset Custodian Services
[Words and expressions used herein shall have the meanings set out under the Consultation Paper.]

About HKCGI

The Hong Kong Chartered Governance Institute (HKCGI) is the sole accrediting body in Hong Kong and the Chinese mainland for the globally recognised Chartered Secretary and Chartered Governance Professional qualifications. Formerly known as The Hong Kong Institute of Chartered Secretaries (HKICS), HKCGI is the Hong Kong/China Division of The Chartered Governance Institute (CGI).

With a legacy of over 75 years, HKCGI has established itself as a trusted and reputable professional body in the region. Its influence extends to CGI's global network of around 40,000 members and students, making it one of its fastest-growing divisions. HKCGI's community comprises about 10,000 members, graduates, and students, with significant representation in listed companies and diverse governance roles across various industries.

Guided by the belief that governance leads to better decision-making and a better world, HKCGI is committed to advancing governance in commerce, industry, and public affairs. It achieves this through education, thought leadership, advocacy, and active engagement with its members and the broader community. As a recognised thought leader, HKCGI promotes the highest standards of governance while advocating for an inclusive approach that considers the interests of all stakeholders and ensures that every voice is heard and valued.

Overall Support

HKCGI welcomes and supports the proposal by the Financial Services and the Treasury Bureau (FSTB) and the Securities and Futures Commission (SFC) to introduce a licensing regime for over-the-counter (OTC) virtual asset (VA) trading service providers.

The proposed regime fills a significant regulatory gap. While VATPs and VA dealing services are now subject to regulation under the AMLO, OTC VA trading remains unregulated, leaving investors exposed to fraud, scams, and money laundering risks. By extending oversight to OTC providers—including those offering physical storefront services and online platforms—the regime enhances investor protection and strengthens Hong Kong's anti-money laundering and counter-terrorist financing (AML/CFT) framework.

Response to Consultation Questions

Question 1. Do you have any comments on the proposed definition and scope (e.g. too narrow or too wide) of VA custodian services to be regulated?

We support the proposed definition and scope of VA custodian services. It appropriately captures the safekeeping of VAs and instruments, enabling the transfer of VAs (such as private keys) on behalf of clients, which is central to investor protection and maintaining market integrity. By focusing on activities "by way of business," the definition distinguishes between professional custodians and self-custody, aligning with international best practices and ensuring regulatory clarity.

Question 2. For entities which do not safekeep private keys but arrange a third party to custody the client VAs or otherwise safekeep the private keys (such as a private fund trustee of a VA fund that delegates the safekeeping of private keys to a sub-custodian), should they be required to obtain a VA custodian service provider licence? Please explain your comments.

We support requiring entities that delegate safekeeping to third parties to obtain a VA custodian service provider licence. Delegation does not remove the ultimate responsibility for safeguarding client VAs, and licensing ensures that the principal entity remains accountable for AML/CFT compliance, risk management, and investor protection standards.

Question 3. Are there any entities which should be licensed or registered for providing VA custodian services but are not caught by the proposed definition? Please explain your comments.

We consider the proposed definition to be largely comprehensive. However, entities providing VA custody within complex corporate structures or acting as fund managers providing self-custody may need explicit inclusion to ensure there are no regulatory gaps.

Question 4. For an entity ("Entity A") within a corporate group that safekeeps private keys whereby personnel from different group entities ("Group Entities") may also be involved in safekeeping the private key and/or signing a VA transaction:

(i) Should the Group Entities be required or not be required to obtain VA custodian service provider licences? Please explain your comments.

In principle, we support requiring all Group Entities materially involved in safekeeping or signing VA transactions to obtain a VA custodian service provider licence. Any personnel

actively controlling client assets should fall under the regulatory framework to ensure accountability, compliance, and risk management oversight. There needs to be more consideration given to where the balance lies on the materiality issue.

(ii) If the answer to (i) is yes, please provide your comments on the types of personnel within the Group Entities which should obtain an individual licence ("Relevant Personnel"). What steps of the transactions should trigger this licensing requirement?

Relevant Personnel should include employees or officers with direct operational control over private keys or transaction authorisation. Licensing should be triggered by the steps of accessing, storing, transferring, or approving client VAs to ensure that all critical points of asset management are supervised.

(iii) If the answer to (i) is no, please provide your comments on whether the Relevant Personnel of the Group Entities should be required to be accredited to Entity A (assuming Entity A will obtain a VA custodian service provider licence) and also obtain an individual licence. Please explain your comments.

Where a Group Entity does not obtain a separate licence, it is still appropriate for Relevant Personnel to be licensed. This ensures that responsibility is properly traced, internal controls are maintained, and governance principles of accountability and segregation of duties are upheld.

Question 5. What are your comments on the proposed exemptions? Would there be other exemptions that are necessary?

We support the proposed exemptions for incidental activities, such as regulated entities holding client VAs in connection with other regulated services, or stablecoin issuers regulated by the HKMA. These exemptions are consistent with proportional regulation, focusing licensing on entities whose primary business is VA custody, avoiding unnecessary duplication.

Question 6. Do you have any comments on the proposed scope of allowed activities?

We support the proposed scope of allowed activities for licensed or registered VA custodian service providers. Allowing for the safekeeping of client VAs, instruments enabling the transfer of VAs, and settlement instructions ensures that core custodian functions are covered. The framework also provides flexibility for ancillary services, such as staking, subject to regulatory approval, which balances market development with risk mitigation.

Question 7. Do you have any comments on the types of VAs that a VA custodian service provider should not provide custodian services for?

We support a flexible approach without broad restrictions on VA types, provided that robust due diligence is conducted to assess ML/TF risks and operational capability for custody. This ensures that providers are responsible for evaluating the risks associated with each token and maintaining appropriate safeguards.

Question 8. Do you have any comments on the scope of individual licence and engagement as relevant individuals for providing VA custodian service?

We support the proposed scope for licensing or accrediting individuals who perform substantive VA custodian functions. This includes staff who directly supervise, approve, or execute custody-related activities. Clerical staff and internal support functions are appropriately excluded, ensuring proportional regulation and reducing unnecessary licensing burdens.

Question 9. Should individuals with authority to approve or sign VA transactions be required to obtain a licence or be engaged as relevant individuals? If yes, what steps of the transactions should trigger this requirement?

Individuals authorising, signing, or executing client VA transfers should be licensed or engaged as relevant individuals. This should include any step involving the movement, transfer, or approval of client assets, including signing transaction instructions and approving settlements. This will reduce operational and fraud risk, and support regulatory oversight, as individuals will be subject to fit-and-proper assessments, supervision, and compliance obligations.

Question 10. Do you think that licensed VA custodian service providers should be subject to similar financial requirements as licensed corporations carrying on Type 13 regulated activity of providing depositary services for a relevant CIS? Do you think additional resources calibrated with scale of business or operations are required?

We support applying financial requirements similar to those for Type 13 depositary service licensees. A baseline of paid-up capital and liquid resources ensures that VA custodian service providers have the financial capacity to operate safely, maintain robust infrastructure, and absorb operational or custodial losses. We also support additional requirements calibrated to the scale and complexity of the business to reinforce resilience, prudent risk management, and governance oversight.

Question 11. Should other regulatory requirements be added to mitigate the risks of VA custodian services?

In addition to financial requirements, we recommend robust governance, internal controls, and operational risk management. This includes cybersecurity measures, private key management standards, business continuity planning, segregation of client assets, and stringent AML/CFT controls. These measures are essential to safeguard client assets and mitigate risks of fraud, cyberattacks, or operational failures. Governance best practices also support the requirement of clear reporting, record-keeping, disclosure, and compliance oversight.

Question 12. What are your comments on the proposed transitional arrangement for the licensing regime for VA custodian service providers?

We support the proposed transitional arrangement. Requiring all VA custodian service providers to seek licensing or registration from the commencement date ensures a level playing field. It maintains investor protection while encouraging legitimate providers to engage early with the SFC or HKMA to avoid operational disruption. Overall, the transitional arrangement appropriately incentivises compliance, supports orderly market development, and aligns with international best practices for licensing fiduciary and custodial services.

Question 13. Based on the "user-pays" principle, do you have any comments on requiring higher licensing application fees and annual fees for a VA custodian service provider licensed by or registered with the SFC (such as requiring fees in the same amounts as those for Type 3 regulated activity under the SFO or other higher amounts)?

We support aligning the licensing application and annual fees for VA dealing service providers with those applicable to Type 3 regulated activity under the SFO, in line with the "user-pays" principle.

Question 14. 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 custodian services to the public of Hong Kong?

We agree with the proposed restriction. Prohibiting unlicensed entities from marketing VA custodian services is crucial to safeguard investors against the risks of fraud, cyberattacks, and the mismanagement of client assets. It ensures that only entities subject to regulatory oversight, fit-and-proper requirements, and AML/CFT obligations can offer such services to the public.

Question 15. Do you agree that the SFC and the HKMA should be provided with the proposed powers?

We agree that empowering the SFC and the HKMA with supervisory, inspection, and enforcement powers is essential for effective oversight of VA custodian service providers. These regulatory powers allow regulators to ensure compliance with statutory and regulatory requirements, investigate suspected breaches, and impose appropriate sanctions, which is crucial for investor protection and market integrity.

Question 16. Do you agree with the proposed sanctions, which are comparable to those under the existing regulatory regimes for VATPs?

We agree with the proposed sanctions, which are appropriately aligned with those under the existing regulatory regime for VATPs. By including fines, imprisonment, and disciplinary measures such as suspension, revocation, reprimands, remedial orders, and pecuniary penalties, the proposed regime ensures regulatory parity, reinforces market integrity, and protects investors.

Question 17. 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?

We agree that a review tribunal mechanism should be established to handle appeals against decisions made by the SFC or the HKMA under the VA dealing services licensing regime. Such a mechanism provides an important layer of procedural fairness and accountability, ensuring that affected parties have a formal avenue to challenge regulatory decisions.

If you have any questions, please do not hesitate to contact Ellie Pang FCG HKFCG(PE), Chief Executive, HKCGI, or Mohan Datwani FCG HKFCG(PE), Deputy Chief Executive, HKCGI, at 2881 6177 or research@hkcgi.org.hk.

Yours sincerely,

For and on behalf of
The Hong Kong Chartered Governance Institute

David J Simmonds FCG HKFCG
President