

## Announcement Clarifies Regulatory Position on Initial Coin Offerings in Hong Kong

### IN SHORT

**The Situation:** The Hong Kong Securities and Futures Commission has issued a statement explaining that, depending on the facts and circumstances of an initial coin offering ("ICO"), the ICO and any digital tokens that are offered or sold under it may be subject to the securities laws of Hong Kong.

**The Results:** The SFC has made clear that where the digital tokens involved in an ICO fall under the definition of "securities," any party dealing in or advising on such digital tokens, or managing or marketing a fund investing in them and targeting the Hong Kong public, is required to be licensed by or registered with the SFC, irrespective of where the party is located.

**Looking Ahead:** The SFC reminds parties engaging in ICO activities to seek legal or other professional advice to ensure compliance with the applicable legal and regulatory requirements in Hong Kong.

In light of the increased use of initial coin offerings ("ICOs") to raise funds in Hong Kong and elsewhere (see our recent *Commentaries*: "[SEC's Investigative Report Raises Difficult Questions for ICO Issuers](#)"; "[Announcement Clarifies Regulatory Position on Digital Token Offerings in Singapore](#)" and "[UK Regulator Examines Scope of Securities Laws, Warns of Initial Coin Offering Risks](#)"), the Hong Kong Securities and Futures Commission ("SFC") has issued a statement to explain that certain ICOs may be subject to Hong Kong securities laws. This is even if the ICO purports to offer a digital token described or otherwise labeled as a "virtual commodity."

The term "virtual commodity" has sometimes been used by certain Hong Kong regulatory and law enforcement agencies to describe Bitcoin and other speculative investments that are not legal tender in Hong Kong. The SFC has indicated that it will consider the substance, not the form, of an ICO to determine if a digital token offered or sold under it is a "security" that might be subject to regulation, or a "virtual commodity" that might not.



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The SFC has listed some examples of digital tokens from ICOs that may be regulated under Hong Kong law as "securities":

- Digital tokens that represent equity or ownership interests in a company (e.g., shareholders' rights, the right to receive dividends, and the right to participate in the distribution of the company's surplus assets upon winding up) may be regarded as "shares" (a type of "security");
- Digital tokens that are used to create or to acknowledge a debt or liability owed by an ICO issuer (e.g., the ICO issuer promises to repay the token holders the principal of their investment on a fixed date or upon redemption and pay interest to the token holders) may be regarded as "debentures" (another type of "security"); and
- If the proceeds of the ICO issuance are managed collectively by the ICO scheme operator to invest in projects with the aim of enabling token holders to participate in a share of the returns from the investments, a digital token in respect of such an ICO may be regarded as an interest in a "collective investment scheme" (yet another type of "security").

If any digital token offered or sold under an ICO is determined to be a "security," any party engaging in the secondary trading of such digital tokens (e.g., crypto currency exchanges) may also be subject to Hong Kong securities laws.

### THREE KEY TAKEAWAYS

1. It should be noted that in the People's Republic of China, the relevant authorities appear to have taken

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the approach of *prohibition* rather than *regulation* when it comes to ICOs.

2. Although Hong Kong is a part of the People's Republic of China, by virtue of its status as a Special Administrative Region, PRC laws and regulations relating to ICOs will not apply in Hong Kong unless they are listed in Annex III of the Basic Law and implemented by the Hong Kong legislature.
3. For the near future, therefore, there is likely to be a divergence between Hong Kong and the People's Republic of China in respect of the legal status of ICOs.



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