

Press Release

LCQ4: Regulation of trading activities of bitcoins

Wednesday, March 25, 2015

Following is a question by the Hon Leung Yiu-chung and a reply by the Secretary for Financial Services and the Treasury, Professor K C Chan, in the Legislative Council today (March 25):

Question:

It has been reported that recently, a bitcoin trading portal suddenly ceased operation, and its office was also found not in operation. It is estimated that about 3 000 investors have suffered losses, involving a total amount as high as HK\$3 billion. In this connection, will the Government inform this Council:

(1) of the number of the investors concerned who have reported to the Police so far and the total amount of money involved; how the Police handle such cases and what progress they have made; whether the Police have completed the handling of some of such cases; if so, of the outcome; and

(2) given that the Government has repeatedly reminded the public of the risks involved in trading bitcoins and reiterated that bitcoins are no more than a kind of "commodities" created in the virtual world, whether the authorities have grasped the situations in respect of the trading of bitcoins, as well as their being used for making purchases in Hong Kong; whether the authorities will proactively investigate the operation of bitcoin exchange platforms, and whether they will consider enacting legislation to regulate or ban the relevant activities; if they will, of the details; if not, the reasons for that?

Reply:

President,

As repeatedly pointed out in our reminders to the public through the media, and in my reply to a question raised by the Hon Chan Kam-lam at the meeting of this Council held on January 8, 2014, bitcoins are not a legal tender, and their value is not backed by any physical items, issuers or the real economy.

Their pricing is highly volatile. We have also sounded relentless warnings of the high risks involved in exchanging, trading or holding such kind of virtual commodities for speculative purposes. The Investor Education Centre and the Consumer Council have reminded the public from time to time that trading bitcoins may result in monetary losses, and that holders may not be able to obtain a refund of their monies should a virtual commodity collapse or those who deal in it cease to operate. We have been discouraging people from engaging in such speculative activities or transactions without considering the risks involved. The Government's reply to the two parts of the question is as follows:

(1) According to the information provided by the Police, the Police received the relevant complaints since February 11, 2015. The complainants had been participating in the trading of bitcoins through a local company since early 2014. The complainants found that the accounts opened with the company could no longer be operated, and no withdrawal from and trading of bitcoins through the accounts were allowed since December 2014. The complainants suspected that it might be a fraud case. To date, over 100 persons have reported their cases to the Police, and the amount involved totalled \$180 million.

The Commercial Crime Bureau of the Police is investigating the case, and has searched various locations and seized a number of computers, tablets, mobile phones, account records, etc. Two men and four women, aged between 34 and 55, were arrested for conspiracy to defraud. All the arrested persons have been released on bail pending further investigation. The Police will continue with the investigation. Those who might have fallen prey to the fraud are urged to report the cases to the Police.

(2) Given that the circulation of bitcoins varies from place to place, we note that supervision over such virtual commodities also varies, depending on the market situations. According to our understanding, bitcoins have not yet been accepted widely as a medium of payment in Hong Kong as compared with other places, and their circulation as a medium of exchange in daily life or business transactions is insignificantly limited. There are only a very small number of vendors claiming that they would accept bitcoins as a medium of payment. We therefore consider that bitcoins and other kinds of virtual commodities do not qualify to be an e-currency, having regard to their nature and current circulation in Hong Kong. They are, in most cases, be regarded

generally as commodities or virtual commodities for individual speculative activities. It is also unlikely that bitcoins, given its circulation, will pose a significant threat on Hong Kong's financial system. As such, the Government does not consider it necessary to introduce at the moment new legislation to regulate trading in such virtual commodities or prohibit people from participating in such activities.

Like most jurisdictions, Hong Kong does not have any targeted regulatory measures on virtual commodities specifically in terms of their safety or soundness, and the trading platforms or operators of such commodities. That said, our existing laws provide for sanctions against unlawful acts, such as money laundering, terrorist financing, fraud, pyramid schemes and cyber-crimes, whether or not these virtual commodities are involved. For the purpose of crime prevention and detection, the Police conduct patrols, including search for relevant information via public platforms on the Internet where necessary. The Police will take enforcement action if they find information which involves criminal conduct.

Meanwhile, the financial regulators (including the Hong Kong Monetary Authority, the Securities and Futures Commission, the Office of the Commissioner of Insurance, and the Customs and Excise Department) have required financial institutions to assess stringently money laundering and terrorist financing risks associated with virtual commodities, according to the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (AMLO). Such institutions are required to comply continuously with customer due diligence and record keeping requirements when establishing or maintaining business relationships with customers or clients who are operators of any schemes or businesses relating to virtual commodities.

Under the Organized and Serious Crimes Ordinance, the Drug Trafficking (Recovery of Proceeds) Ordinance or the United Nations (Anti-Terrorism Measures) Ordinance, any individuals (including financial institutions, virtual commodity dealers or operators), shall, on any occasion, report any suspicious activities in relation to money laundering or terrorist financing to the Joint Financial Intelligence Unit (JFIU) set up by the Police and the Customs and Excise Department (C&ED). A failure to disclose such suspicious transactions to the JFIU may amount to an offence.

Also, any operators whose transactions involve money changing or remittance services are required to apply to the Commissioner of Customs and Excise for a "money service operator" licence under the AMLO. In relation to that Ordinance, the C&ED conducts regular patrols, including cyber patrols, to combat unlicensed operation of a money service. Among the patrols, it will check whether any bitcoin-related platforms are involved in unlicensed money service business.

The Government and financial regulators will keep a close watch on the development of bitcoins and other virtual commodities, and maintain contacts with their counterparts in other places through active participation in meetings of the relevant international organisations (such as the Financial Action Task Force).

Given the highly speculative nature of bitcoins, I would like to once again remind the public to exercise extra caution and be risk-conscious when considering participating in the trading of virtual commodities such as bitcoins to avoid losses.

Ends