

28 January 2022

Our Ref: INS/TEC/10/48  
By Email

To: Chief Executives of all authorized insurers

**Regulatory Approaches of the Insurance Authority**  
**in Relation to Virtual Assets and Virtual Asset Service Providers**

Dear Sirs,

The Insurance Authority (“IA”) has recently received some enquiries from the industry on possible involvement or interaction with activities related to virtual assets (“VAs”) and Virtual Asset Service Providers (“VASPs”). This circular provides guidance on the pertinent issues that authorized insurers should take into account on this topic.

**Regulatory Developments**

In light of the risks associated with VAs and VASPs, international forums and standard-setting bodies have been closely monitoring developments and published reports as well as guidance focusing on mitigating and managing the risks associated with these innovations. For example, the Financial Action Task Force published an updated “Guidance for a Risk-Based Approach to Virtual Assets and Virtual Asset Service Providers”<sup>1</sup> in October 2021.

---

<sup>1</sup> The Guidance describes application of FATF Recommendations to member jurisdictions and competent authorities, as well as to VASPs and other obliged entities (including banks) that seek to engage in VA activities, so that they could better understand their anti-money laundering and counter-financing of terrorism obligations. It can be found at: <https://www.fatf-gafi.org/publications/fatfrecommendations/documents/guidance-rba-virtual-assets-2021.html>.

Similarly in Hong Kong, the Securities and Futures Commission (“SFC”) granted the first licence under a voluntary opt-in regime for platforms offering trading of securities-type VAs or tokens in December 2020, while the Government will introduce a bill on licensing of VASPs into the Legislative Council in 2022 after completed a public consultation<sup>2</sup> in May 2021.

Authorized insurers intending to engage in VA-related activities or with VASPs should keep abreast of regulatory changes and determine how the projects to which they are exposed are likely to be affected. In addition, authorized insurers should comply with all regulatory requirements in so far as they apply to VA-related activities, as outlined in the ensuing paragraphs.

### **Prudential Supervision**

Authorized insurers should ensure that they fully discharge their obligations under the Guideline on Enterprise Risk Management (“GL21”) in evaluating and addressing risks associated with VA-related activities. In general, GL21 requires an authorized insurer to have in place robust governance and processes to proactively identify and assess its risk exposures and to develop techniques to monitor, manage and mitigate its risks, taking into account all applicable legal and regulatory requirements. Section 6 thereof sets out an overriding obligation to regularly review risk exposures against risk appetite statement and risk limits. In respect of VA-related activities and engagement with VASPs, an authorized insurer should:

- a) consider whether involvement with such activities are within the limits of its risk appetite statement (section 5 of GL21);
- b) identify and evaluate all relevant material risks to which it would be exposed in engaging in such activities (sections 6.2 and 6.3 of GL21);
- c) establish monitoring and reporting processes to ensure that the relevant material risks are monitored and reported to its board, risk committee and senior management (section 6.3 of GL21); and

---

<sup>2</sup> Consultation Conclusions on Legislative Proposals to Enhance Anti-Money Laundering and Counter-Terrorist Financing Regulation in Hong Kong which is accessible at

[https://www.fstb.gov.hk/fsb/en/publication/consult/doc/consult\\_conclu\\_amlo\\_e.pdf](https://www.fstb.gov.hk/fsb/en/publication/consult/doc/consult_conclu_amlo_e.pdf)

- d) factor a risk management review into its decision making process governing such activities and install controls to mitigate or transfer the relevant material risks (section 6.4 of GL21).

Given that development of VAs is still at a nascent stage, authorized insurers are expected to adopt a conservative approach and should deduct the value of VAs in full when deriving their solvency positions. Moreover, authorized insurers carrying on general business should not include VAs as local assets in seeking compliance with section 25A of the Insurance Ordinance (Cap. 41) (“IO”).

### **Investment Risks**

Investment risks embrace market, credit, liquidity, and default risks. Authorized insurers should take account of the factors outlined in section 7.6 of GL21 to control and mitigate investment risks associated with VA-related activities, which typically include a lesser degree of transparency, governance and regulation, inadequate safe-keeping and recording mechanisms, potential of counterparty defaults, and the need to identify and make provision for any significant investment losses in a timely manner.

### **Cyber Risks**

VA-related activities or interaction with VASPs may expose authorized insurers to cyber risk and, as such, they should comply with applicable requirements under GL21 (section 7.11 thereof) and requirements under the Guideline on Cybersecurity (“GL20”). Authorized insurers should also satisfy themselves that the VASPs have put in place adequate and effective cybersecurity measures before commencing any business relationship.

### **Conduct Risks**

Where VA-related activities form part of the process in arranging contracts of insurance (through premium payment) or carrying out obligations under contracts of insurance (coverage provided in relation to VAs or benefits linked to VAs), it is imperative for authorized insurers to install processes, controls and training to ensure that customers are treated fairly and are placed in a position to make informed decisions. Due regard should be paid on obligations spelt out under section 10 of the Guideline on Corporate Governance of Authorized Insurers (“GL10”) and the factors contained in section 7.10.3 of GL21. Specifically, authorized insurers should:

- a) capture the circumstances and sophistication of customers in the product design phase<sup>3</sup>;
- b) make disclosure on risks associated with VA-related activities so that customers are positioned to make informed decisions;
- c) provide suitable training so that its licensed insurance intermediaries would only target customers for whom a product is designed and are positioned to assess a customer's individual circumstances and advise on the product's suitability; and
- d) exercise control and monitoring to ascertain the extent to which customers are being treated fairly.

### **Anti-money Laundering and Counter-financing of Terrorism (“AML/CFT”) Risks**

Authorized insurers carrying on long-term business should evaluate the VA-related activities or interactions with VASPs in the context of their obligations under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance as well as the Guideline on AML/CFT (“GL3”). In particular, they should identify and assess the risks that may arise in relation to new or developing technologies and take appropriate measures to manage and mitigate such risks. Long term insurers establishing and maintaining business relationships with VASPs should undertake due diligence measures, such as (without limitation) collecting sufficient information to understand the business nature of the VASPs and conducting appropriate assessment of AML/CFT risks which factors in the different risks associated with individual VASPs.

### **Risk of Offshore Clients and Compliance with Laws Outside Hong Kong**

Authorized insurers should be aware that approaches to regulation, supervision and enforcement governing VA activities and VASPs vary across different jurisdictions and may be different from that in Hong Kong. It is therefore imperative that when authorized insurers seek to provide service to policyholders located outside Hong Kong, attention should be placed on all applicable laws (locally and abroad). If VA-related activities are likely to be involved, the authorized insurers, their controllers, directors and key persons in control functions should exercise due diligence to ensure strict compliance with the applicable laws.

---

<sup>3</sup> For example, if an authorized insurer is designing a product with savings element linked to the value of VAs, it should bear in mind that the proposed new licensing regime in Hong Kong will limit the ability of VASPs to serving only Professional Investors.

## **Proposals on VA-related Activities**

Since the nature of VA-relative activities is evolving rapidly, authorized insurers contemplating to get involved are strongly advised to inform and obtain advice from the IA on the adequacy of their risk-management controls before launching any new products or services (including forming any type of relationship with VASPs). Meanwhile, we will keep in view the global regulatory landscape and provide further updates when appropriate.

Yours faithfully,

Tony Chan  
Associate Director  
Policy and Development Division  
Insurance Authority

c.c. The Hong Kong Federation of Insurers