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Unicorns and Dragons: Risk and Opportunity in Singapore's Digital Assets Space

Introduction

In August 2021, the Monetary Authority of Singapore (MAS) granted its first 'in-principle' approval for a cryptocurrency firm – the Australian cryptocurrency exchange Independent Reserve – to offer digital payment token services.[1] Independent Reserve would subsequently obtain a formal license to offer digital payment token services two months later, alongside DBS Vickers and following Singaporean FinTech FOMO Pay.

These license approvals reflect Singapore's strong interest in becoming a leading digital assets hub, part of the city-state's ambition of becoming a top FinTech hub, a strategic intent that was first articulated in 2017[2] and which by some measures has already been achieved. In 2022, FinTech investments in Singapore reached a three-year high of USD4.1 billion.[3] These efforts also rode on a global wave of interest in digital assets that began with the popularization of cryptocurrencies such as BitCoin in the 2010s.

In order to achieve its ambition of becoming a top FinTech and digital assets hub, Singapore had to establish new mechanisms through which it could govern and regulate these emerging sectors. On 7 July 2015, the MAS set up its FinTech and Innovation Group (FTIG) to guide regulatory policies and developmental strategies for the use of technology and innovation in the financial sector. Led by MAS's Chief FinTech Officer Sopnendu Mohanty, the FTIG comprises a Payments and Technology Solutions Office, Technology Infrastructure Office and Technology Innovation Lab.

While Singapore has yet to formulate a comprehensive regulatory framework for cryptocurrencies and other digital assets, there are several pieces of legislation that regulate the use of digital assets for payments and other financial transactions. These regulations have also been adapted over time in response to changes in the digital assets space.

Payment Services Act

Passed in 2019 and having taken effect in January 2020, the Payment Services Act replaced the Money-Changing and Remittance Businesses Act and Payment Systems (Oversight) Act to provide the MAS with wider ranging oversight of payment services in Singapore. The Act includes a Designation Framework that allows the MAS to designate significant payment systems and regulate payment systems providers accordingly as well as a Licensing Framework that requires providers to obtain a license for the type of payment services that they intend to provide.

Under the Payment Services Act, there are seven regulated payment services. These include:

- Account Issuance Service
- Domestic Money Transfer Service
- Cross-Border Money Transfer Service
- Merchant Acquisition Service
- E-Money Issuance Service
- Digital Payment Token Service
- Money Changing Service

In order to address the risks associated with the emerging digital payment tokens space, the Payment Services Amendment Act was passed on 4 January 2021, imposing additional measures on Digital Payments Token (DPT) service providers to mitigate money laundering and terrorism financing risks. This act requires providers to conduct regular account reviews as well as to monitor and report any suspicious transactions.[4]

More significantly, the new act broadened the scope of cross-border money transaction services to include transfers of money between persons in different jurisdictions, even when money is not accepted or received by the service provider in Singapore. This brought service providers outside Singapore under the regulatory ambit of MAS. Given that digital token transactions tend to take place across international borders, this new provision provides the MAS with greater regulatory powers over digital asset transactions, regardless of where the recipients of digital assets and payments are located.

Financial Services and Markets Bill

Passed in April 2022, the Financial Services and Markets Bill provides the MAS with greater regulatory powers and supervisory oversight of virtual asset service providers (VASPs) for anti-money laundering and countering of financing of terrorism (AML/CFT) activities. This bill was passed in response to the increasingly digitalised nature of financial services by consolidating the MAS's regulatory powers into a single bill. This includes consolidating the MAS's various technology risk management requirements, enhancing the MAS's ability to mandate adequate technology risk control measures in a financial institution.

Amendments to the Financial Services and Markets bill would subsequently be introduced in April 2023, providing the groundwork for Singapore's first centralised digital platform for financial institutions to request and share targeted information on individuals and companies confidentially. Known as COSMIC, or Collaborative Sharing of Money Laundering/Terrorism Financing Information and Cases, this platform aims to help flag, detect and prevent money laundering, terrorism financing and proliferation financing.[5]

Taken together, the Financial Services and Markets Bill aims to address the AML/CFT risks that tend to pervade the cryptocurrency and digital assets space by providing the MAS with greater regulatory powers as well as establishing the necessary platforms and infrastructure for better information sharing and reporting.

'Digital Assets. Not Cryptocurrency'

However, such efforts to clarify and standardize Singapore's cryptocurrency regulations overlapped with the occurrence of market failure both in the Singaporean and global cryptocurrency markets. Globally, a rapid decline in cryptocurrency value and the failure of major stablecoins such as TerraUSD and Luna as well as the cryptocurrency platform FTX would give rise to what has come to be known as the 'crypto winter'. In Singapore, the collapse of Singapore-based crypto hedge fund Three Arrows Capital further highlighted the risks involved in cryptocurrency trade. This was exacerbated by revelations that Singapore's sovereign wealth fund Temasek Holdings had invested SGD372 million (USD275 million) in FTX, all of which were written off with the collapse of FTX.[6]

As a consequence of these events, there was a shift in both public sentiment and regulatory approach towards cryptocurrency. On 29 August 2022, MAS managing director Ravi Menon described cryptocurrencies as "highly hazardous" for retail investors during a speech that was entitled "Yes to Digital Asset Innovation, No to Cryptocurrency Speculation".[7] At the same time, Menon emphasized Singapore's ambitions to develop a strong digital asset ecosystem as well as explore the use of distributed ledger technology in financial services.

These sentiments had already been made tangible in guidelines that were published by the MAS in January 2022, prohibiting cryptocurrency trading service providers from taking up public advertisements, engaging third parties like social media influencers and operating physical automated teller machines (ATMs) in public areas.[8] While these moves were seen by some observers as a setback to Singapore's crypto ambitions,[9] in reality they reflected a shift in Singapore's approach to the digital assets space towards more stable forms of digital assets and tokens.[10]

Purpose Bound Money

On 21 June 2023, the MAS launched a White Paper that proposed standards for the use of digital assets that include central bank digital currencies (CBDCs), tokenized bank deposits and some stablecoins.[11] The White Paper defines these assets as 'purpose bound money' (PBM), digital currencies that are limited in how they can be used and which are pegged to a real-world currency, commodity or financial institution. Unlike cryptocurrencies, PBMs are considered more stable and hence suitable as a medium of exchange. Importantly, the White Paper specifies the processes that users and institutions must follow, as well as the lifecycle of PBMs.

According to the MAS, the standardisation of processes and regulations pertaining to the use of PBMs can help unlock economic value and facilitate efficient and inclusive digital transactions while at the same time ensure protection for consumers.[12] This suggests that certain digital assets such as PMBs will play a growing role in both the financial sector and the real economy by serving as a medium of exchange and creating new sources of economic value.

Cautious Optimism

Despite the MAS's efforts to clarify its regulatory framework as well as its public messaging on retail cryptocurrency investments, the future trajectory of Singapore's cryptocurrency and digital assets space remains far from clear. On the one hand, the tightening of regulations has no doubt caused some level of shrinkage in Singapore's cryptocurrency market. On the other hand, both the Singapore government and general public maintain strong interest in the digital assets space.

A good indication of this is a 2023 poll by Independent Reserve Cryptocurrency Index, which found that while public confidence in cryptocurrencies had fallen from 61% in 2022 to 55% in 2023, more than 4 in 10 respondents who were polled continued to invest in cryptocurrencies.[13] This suggests that public interest in cryptocurrencies has not declined, reflecting strong investor interest in cryptocurrencies and digital assets. This corresponds with a KPMG survey, which found that more than 90% of family offices and high net worth individuals in Hong Kong and Singapore are interested in digital assets, with 58% already investing in digital assets.[14]

An additional indication of Singapore's cautious optimism towards cryptocurrency is the MAS's issuance of licenses to specific DPT providers. For instance, Crypto.com was recently granted a major payment institution license, allowing it to provide DPT services such as e-money issuance and account issuance as well as cross-border and domestic money transfers to customers in Singapore.[15] This brings the total number of cryptocurrency-related firms that have been issued either a major payment institution license or standard payment institution license to 13.

Conclusion

Hence, while Singapore has sought to curb, or at least minimize, retail trade of cryptocurrencies, it nonetheless retains its ambition to be a leading hub for digital assets. Digital assets of interest include PBMs and other stable digital assets with use cases that could potentially benefit Singapore's real economy and financial services sector. It is therefore likely for PMBs, in particular CBDCs and stablecoins, to grow in the short- and medium-term future.

It is also important to note that Singapore has not ruled out all crypto activity. As MAS Managing Director Ravi Menon articulated during his speech at the Singapore FinTech Festival 2022, "(i)f it is about tokenising real and financial assets to increase efficiency and reduce risks in financial transactions, yes we want to be a crypto hub. But if it is about trading and speculating in cryptocurrencies, that is not the kind of crypto hub we want to be".[16]

In short, Singapore will become a digital assets hub but only on its own terms. These terms include a robust, adaptive and transparent regulatory approach that facilitates financial innovation but minimizes risk to the public.

Notes

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