

REGULATORY INTELLIGENCE

Navigating Singapore's crypto landscape

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Singapore has been a popular destination for new and existing funds to set up their crypto investment products in recent years following wider growth in the asset class throughout Asia. This has also given rise to new problems which have come under scrutiny due to the perceived oncoming "crypto winter". This article takes a look at some important areas for consideration when setting up a crypto fund or business, or using digital assets from regulatory considerations, fund structures, exchanges, and tax treatments.

Regulatory compliance

In Singapore, the type of regulations which apply to crypto businesses (if they apply at all) and whether it needs to be licensed, depend on the business activities contemplated and the type of crypto assets involved. Crypto products and services come in many forms and are evolving continuously. There is no one "crypto licence" that applies universally. The specific regulatory authority that regulates the activities of the crypto product or service will vary depending on the scope of the product or service.

For example, businesses that deal in, or offer digital exchange or custodian services for, digital tokens that are deemed to be securities are required to be licensed (or exempt from licensing) under the Securities and Futures Act 2001 of Singapore and may be subject to the prospectus requirements of such act if offering/selling such securities. Also businesses that operate in Singapore are also required to comply with Singapore's laws and regulations in relation to anti money laundering and countering the financing of terrorism regulations.

Even where an act is done entirely outside Singapore, Singapore's licensing requirements would still apply if the conduct has a "substantial and reasonably foreseeable" effect in Singapore.

A coveted licence in Singapore is the major payment institution licence under the Payment Services Act 2019 of Singapore. This licence allows holders to provide various larger scale crypto services in Singapore. The Monetary Authority of Singapore has been thorough in reviewing the hundreds of applications for such licences and, as at June 22, 2022, a total of only 14 licences and in-principle approvals have been granted to digital payment token service providers.

Popular Structures

VCC

The Variable Capital Company (VCC) is a recent and popular corporate structure for investment funds in Singapore. They may operate as a standalone fund or as an umbrella fund with multiple sub-funds, each with different investment strategies and a portfolio of segregated assets and liabilities.^[1]

Limited Partnership

Another popular fund vehicle, the limited partnership, is constituted by a limited partnership agreement between at least one general partner (GP) and at least one limited partner (LP) ^[2]. GPs are the entities running the fund, and the LPs are the investors. The Limited Partnerships Act 2008 of Singapore (LPA) governs the establishment of limited partnerships.

Funds which are structured as limited liability companies in Singapore are incorporated under the Companies Act 1967 of Singapore (Companies Act), where investors would subscribe for shares in the fund company and become shareholders. If a fund is structured as a company in Singapore, it would typically be in the form of a private company limited by shares. However, the limited liability company is a less commonly used structure for funds domiciled in Singapore today.

Exchanges

The estimated overall market capitalisation of crypto assets has dropped from \$3 trillion to under \$1 trillion in the last seven months. The wipe out of more than \$2 trillion in value has placed strain on cryptocurrency exchanges and trade platforms. These exchanges serve as both borrowers and lenders to individuals or other exchanges in what was a decentralized finance (DeFi) industry. The interconnectivity of cryptocurrency exchanges due to their DeFi role has made some exchanges susceptible to counter party risk and margin calls by other exchanges.

Managing risk



The abilities of exchanges to manage these risks, including the ability to (i) mitigate counter party risks; (ii) manage the trading and withdrawals from customers; (iii) coordinate the same across different regulatory environments; and (iv) raise fresh capital in a rising interest rate environment, will determine the success of such business in weathering the "crypto winter".

T&Cs

The spotlight has turned to the various terms and conditions which govern the relationship between the exchanges and their customers/counterparties. If an exchange's terms and conditions allow for the exchange to treat custodized assets as its own assets to deal with as such, the customers would merely be general unsecured creditors of the exchange, entitled only to a proportional distribution of the exchange's residual assets after any secured or priority creditors have been repaid in an insolvency situation.

Related to this is whether the terms and conditions provide for the ability of the exchange/custodian to lend or provide security over crypto assets to or in favour of third parties, and the precise terms for it. Another issue in the spotlight is the inter-operation of these contractual terms when users switch between accounts or sub-wallets within an exchanges' digital user interface, particularly if the exchange/custodian may commingle the customer's holdings with other customers' holdings, or even its own, in a single crypto wallet controlled solely by the exchange.

Income tax treatment

There are potential tax liabilities that may arise from the sale of digital tokens. While Singapore does not have a capital gains tax, it is a common misperception that such gains are tax-free. The charge of income tax in Singapore is underpinned by the income/capital distinction, where only gains of an income nature are taxable in Singapore.

A gain in capital value however does not per se mean that it will be regarded as a gain of a capital nature (and hence non-taxable). Factors such as intention or purpose, length of holding and frequency of transactions are typically considered, and it is not only those who trade in digital tokens that will be taxed on the profits. Ultimately, it depends on the facts and circumstances of each case.

Employer consideration

Employers are also considering the use of digital tokens as employment remuneration. A practical consideration at the outset is whether the remuneration should be delineated by a fixed amount that is payable by digital tokens, or a fixed number of digital tokens which fluctuates in value over time. Generally, payments using digital tokens with a moratorium period will only be taxed when it is lifted. income tax treatment of a digital token may differ from another depending on its nature and use.

Closing remarks

Due to the dip in the crypto marketing, resulting in prominent crypto player becoming insolvent, more safeguards are being considered by Singapore to protect consumers including limiting retail participation and imposing rules on the use of leverage, or borrowed capital when transacting in cryptocurrencies.

[Complaints Procedure](#)

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