

Singapore: Tighter requirements for Digital Payment Token service providers

In brief

On 3 July 2023, the Monetary Authority of Singapore (MAS) announced new investor protection measures for Digital Payment Token (DPT) service providers (DPTSPs). These measures have been introduced following the [MAS' October 2022 public consultation on proposed regulatory measures to enhance investor protection and market integrity in DPT services](#). In this regard, the MAS has issued the following:

- (a) Part 1 of the MAS' response to the public consultation, where MAS introduces the requirements for segregation and custody of customers' assets by DPTSPs
- (b) Consultation Paper P007 — July 2023, under which the MAS invites feedback on the draft legislative amendments to the Payment Services Regulations to put these requirements into effect
- (c) Consultation Paper P008 — July 2023, under which the MAS invites feedback on its proposed regulatory measures to address market integrity risks in DPT services

An overview of key proposed measures is as follows:

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Response to public consultation on proposed regulatory measures for DPT services

<p>Segregation of customers' assets</p>	<ul style="list-style-type: none"> • Customers' assets must be segregated from the DPTSP's own assets and held on trust, meaning: <ol style="list-style-type: none"> (a) DPTSPs must keep customers' assets on a separate set of blockchain addresses from those containing the DPTSP's own assets. (b) DPTSPs are allowed to deposit a customer's assets in a trust account together with the assets of other customers.
<p>Custody of customers' assets</p>	<p>Safeguarding customers' moneys</p> <ul style="list-style-type: none"> • The existing requirements under the Payment Services Act 2019 (PSA) in relation to the safeguarding of customers' moneys will be extended to DPTSPs. <p>Daily reconciliation</p> <ul style="list-style-type: none"> • DPTSPs must conduct daily reconciliation of customers' assets, including moneys, at the entity level. <p>Recordkeeping</p> <ul style="list-style-type: none"> • DPTSPs must keep transaction records and always maintain separate books and records for each customer with details of the customer's assets. <p>Statement of account</p> <ul style="list-style-type: none"> • DPTSPs must provide monthly statements of account to customers or provide account information on a real-time basis in lieu of such monthly statements.

Risk management controls

- DPTSPs must maintain adequate systems, processes, controls, human resources and governance arrangements to ensure the integrity and security of customers' assets and mitigate the risk of any loss of customers' assets, in a manner that is commensurate with the nature, scale and complexity of their business. This would include the following:
 - (a) Putting measures in place to ensure that the movement of customers' assets is controlled by senior managers and personnel who reside in Singapore. These senior managers and personnel should be authorised to facilitate the return of customers' assets where required by MAS or in court proceedings.
 - (b) Implementing operational controls to prevent the loss of cryptographic keys of DPTs that are held or managed by DPTSPs.
 - (c) Assessing and clearly disclosing to customers the custody arrangements as to the location of devices storing means of access (private keys, seed keys or backup recovery packages) to customers' assets, and whether such arrangements affect the ability of the DPTSP and its customers to recover customers' assets.
 - (d) Adopting good risk management practices, including best practices stipulated under the MAS' Technology Risk Management Guidelines. The MAS expects DPTSPs to have stringent processes and controls with strong governance and oversight by senior managers who have good knowledge and capability to safeguard against technology risk and be responsible for the safety and operation of the business.
- DPTSPs must store suitable proportions of customers' assets in cold wallets. In particular the following:
 - (a) DPTSPs must keep at least 90% of customers' assets in cold wallets, while allowing up to 10% to be kept in other wallets.
 - (b) DPTSPs are expected to conduct periodic reviews and consider keeping a higher than 90% proportion of customers' assets in cold wallets, while considering their business and operational needs and other security controls that can mitigate the risk of loss of customers' assets.
 - (c) DPTSPs should also disclose to customers their policies on storage arrangements for customers' assets, including the following:
 - (i) Information on the circumstances in which the DPTSP keeps the customers' assets on storage media that are connected to the internet (e.g., hot wallets)
 - (ii) The DPTSP's considerations in doing so
 - (iii) The measures that the DPTSP has in place to mitigate the risk of loss
 - (iv) Processes for handling any losses of customers' assets, such as compensation arrangement or insurance

Custody function

- DPTSPs must maintain a separate custody function that is operationally independent from other business units.
- This function can be outsourced to an external service provider subject to additional requirements, including disclosing the terms and conditions and attendant risks to its customers and appropriate controls to, among others, reduce the risk of loss of assets due to fraud or negligence on the part of the service provider.

Disclosures to customers

- DPTSPs must disclose the following in writing to their customers:
 - (a) The terms and conditions, including the arrangements for receiving instructions from the customers and providing information to the customers, and applicable fees and costs
 - (b) That the customers' assets are segregated from the DPTSP's own assets, and held for the benefit of the customers
 - (c) Whether the customers' assets will be commingled with the assets of other customers and, if so, the risks of such commingling
 - (d) The consequences for the customers' assets if the DPTSP becomes insolvent, and the arrangements by the DPTSP to protect customers' assets

Annual audit

- Annual audits to include an assessment on DPTSPs' compliance with the above segregation and custody requirements.

Lending and staking	<ul style="list-style-type: none"> DPTSPs are restricted from facilitating the lending and staking of retail customers' assets. Retail customers will refer to customers that are not an accredited investor, expert investor or institutional investor. For non-retail customers, there must be explicit customer consent after having been provided a clear risk disclosure document.
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Consultation paper on proposed amendments to the payment services regulations

This consultation paper generally sets out the MAS' proposed amendments to the Payment Services Regulations 2019 to implement the above segregation and custody requirements, notably the following:

- (a) The segregation and custody requirements will be extended to not just licensed DPTSPs but also exempt DPTSPs including those that have submitted a licence application and are awaiting the MAS' determination on their application.
- (b) A DPTSP can safeguard customers' assets itself instead of having to use a third-party safeguarding institution. However, the DPTSP must disclose in writing to its customers the terms and conditions that would apply to the DPTSP's safeguarding of the customers' assets. The DPTSP must also ensure effective controls and segregation of duties to mitigate potential conflicts of interest that may arise from the safeguarding of customers' assets.

The paper indicates that these segregation and custody requirements will come into effect by October 2023, and, as such, licensed and exempt DPTSPs should prepare to comply with the requirements by then. Licensed and exempt DPTSPs should note the three- to four-month timeframe to make the necessary changes.

Consultation paper on proposed measures on market integrity in DPT services

In this consultation paper, the MAS proposes to amend the PSA or other acts administered by the MAS to give effect to measures that preserve market integrity in DPT services. These measures would generally require DPTSPs to ensure that the execution of customers' orders is handled in a fair, orderly and timely manner, and that unfair trading practices are prevented and detected. For instance:

- (a) DPTSPs should handle and execute comparable orders received from different customers in accordance with the time of receipt, and DPTSPs should not receive any commission or other form of payment from other persons for routing customers' orders to them.
- (b) DPTSPs should monitor orders and transactions for signs of unusual or suspicious activity on a real-time basis, and they should maintain proper records with adequate details of all on-chain and off-chain orders and transactions for a period of five years.
- (c) DPTSPs should maintain a controlled list of persons with access to material non-public information on a need-to-know basis and information barriers to restrict access by this list of persons to such information.

The MAS also proposes the following statutory amendments to prohibit unfair trading practices:

Prohibited conduct	<ul style="list-style-type: none"> The MAS proposes to introduce provisions for DPTs that are similar to the following Securities and Futures Act 2001 (SFA) provisions on prohibited market conduct, with the necessary modifications for the provisions to apply in relation to DPTs (instead of securities, securities-based derivatives contracts or capital markets products, as the case may be): <ol style="list-style-type: none"> (a) False trading and market rigging (b) Market manipulation (c) False or misleading statements (d) Fraudulently inducing persons to deal (e) Employment of manipulative and deceptive devices (f) Bucketing (g) Cornering (h) Dissemination of information about illegal transactions
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Insider trading	<ul style="list-style-type: none">The MAS proposes to introduce provisions for DPTs that are similar to the SFA provisions on insider trading, as follows:<ul style="list-style-type: none">(a) With the necessary modifications for the provisions to apply in relation to DPTs.(b) Excluding the exceptions for redemption of units in collective investment schemes, underwriters and unsolicited transactions by holders of a capital markets services licence or their representatives
Other provisions	<ul style="list-style-type: none">The MAS proposes to introduce provisions for DPTs that are similar to the SFA provisions on civil penalty actions, civil remedies, attribution of liability and other related areas.

The MAS indicates that it will issue guidelines setting out its expectations in relation to preserving market integrity in DPT services. The MAS will also consult further on the details of the amendments to subsidiary legislation and regulatory requirements, including amendments to the PSA to prohibit unfair trading practices.

Feedback

The MAS invites feedback on both consultation papers by 3 August 2023. If you have any feedback or questions, please let us know.

The above is not intended to be exhaustive or to constitute legal advice.

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