Stabilizing stablecoins: A deep dive into regulations surrounding cryptocurrency

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Singapore's excellent standing as a financial hub is predicated on the rule of law and built upon transparency and regulatory diligence. However, pressing issues have emerged in the crypto arena that demand deeper study for solutions.

This is the topic Singapore Management University Assistant Professor of Law Rachel Phang has recently devoted herself to, since she realized while in private practice that disruptive technological innovation is making financial regulation that much harder.

Moving to academia to tackle such research, Professor Phang authored in 2023 two well-regarded research papers on regulatory developments surrounding stablecoins, the second of which won an award at a prestigious industry event. Stablecoins are cryptoassets with the potential to serve as a practical medium of exchange, since they are designed to maintain a stable value.

The first paper "Singapore's Emerging Regulatory Approach to Stablecoins" critically analyzed the Monetary Authority of Singapore (MAS)'s stablecoin regulatory framework that was finalized in August 2023. Singapore, the paper sets out, "presents an especially interesting case study because of the vibrancy of its digital asset landscape, its position as a global financial center and the regulator's relatively dynamic approach."

Un-stablecoins?

As the paper notes, the first stablecoins appear to have emerged in 2014 as the world sought a more reliable means of payment compared to the extreme price swings of other cryptocurrencies. However, the term "stablecoins," as many have pointed out, can be a misnomer as they may be neither "stable" nor "coins," even though they are largely defined as cryptoassets "designed to maintain a stable value relative to another asset… or a basket of assets."

Depending on how a stablecoin is designed, it may be backed by collateral such as currencies, commodities or other cryptoassets. Other stablecoins may not be backed by any collateral, but may rely on algorithms to adjust their supply, and thereby stabilize their price.

Hence, the label "stablecoins," Assistant Professor Phang tells the Office of Research, can be apt to mislead. Many of them, particularly algorithmic stablecoins, may not involve robust stabilization mechanisms. The shock collapse of the algorithmic stablecoin TerraUSD, for example, contributed to the "crypto winter" of 2022 that saw prices of leading cryptocurrencies like Bitcoin and Ethereum fall by more than 55 percent each.

How, then, can regulation enable stablecoins to realize their promise of value stability, as well as address other pressing regulatory concerns? The key concerns of money laundering and terrorism financing remain, since stablecoins, like many cryptoassets, are often pseudonymous. Other concerns abound as well, such as user protection, market integrity risks, issuer solvency and value stability.

To address some of these concerns, MAS has since confirmed that it intends to introduce a new category of MAS-regulated stablecoins under its latest framework, Professor Phang says, and is working on required legislative amendments that it will consult on in the future.

The Singapore authority, she says, has generally "been a very progressive regulator" that is conscious about running alongside innovation, not ahead of it.

As Professor Phang notes in her paper, Singapore's case study highlights the merits and issues of an approach that "(a) places the majority of stablecoins (i.e., algorithmic stablecoins and most asset-linked stablecoins) in the same category as other cryptoassets, not designed to maintain a stable value; and (b) introduces a new regulatory category and bespoke regulatory treatment only for single-currency stablecoins that fulfill specific criteria."

The approach of MAS, she adds, also shows how certain policy tools may be used in regulating stablecoins. These include entry regulation, as well as anti-money laundering/countering the financing of terrorism, reserve asset, timely redemption, disclosure and solvency requirements.

Tale of three cities

In the other award-winning research paper—a natural follow-up to the first one—Professor Phang analyses and compares incipient stablecoin regulatory frameworks between Singapore, New York and London that she describes as "trailblazing."

"Stablecoin Regulatory Frameworks in Global Fintech Hubs: Perspectives from New York, London, and Singapore" was one of four winning papers at the leading industry event DC FinTech Week, which was held in Washington DC, U.S., in November 2023.

Notable regulatory developments, the paper states, include New York's June 2022 guidance on the issuance of US dollar-backed stablecoins; the United Kingdom's legislative amendments that established a new concept of digital settlement assets; and Singapore's August 2023 finalization of its stablecoin regulatory framework. In doing so, the paper notes, each of the jurisdictions has "carved out a new sui generis regulatory category for a specific subset" of single-currency stablecoins.

There are commonalities and differences in the various approaches by regulators around the world, including in other jurisdictions like Hong Kong and Dubai, but crypto regulation, Professor Phang reminds the Office of Research, is very much a work in progress. Regulators in various fintech hubs need to constantly keep pace with technological innovation and market developments. This ties in with the observation in her paper that the perspectives presented are "but a portion of the ongoing discourse and developments" in stablecoin regulation.

The discussion "takes place in the shadows of larger and longer-running debates: on the history and functions of money, and the competition between private money and state money," among many other things, the paper notes.

But given the instability that so-called stablecoins have triggered, such as the estimated US$60 billion crash caused by the collapse of TerraUSD and its sister token Luna, do regulators need to be even more proactive?

"In crafting the present regulatory approach, lessons indeed already have been and should be drawn from past crises and failures, both in traditional and crypto markets."

However, crypto regulation is very much still evolving, she adds. Hopefully, she tells the Office of Research, it will be "an expeditious and smooth process" that builds on lessons learnt over the years from traditional financial services regulation."

"At the end of the day, as the different regulatory approaches develop, the hope is that this will eventually forge a critical mass of best practices for stablecoin regulation."

Provided by Singapore Management University

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