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Stablecoins – refining the regulatory landscape of crypto-assets

Blockchain and crypto-assets have changed the way people think about money, and this technology is a focus area for policymakers globally. To date there exist over 2000 different types of crypto-assets, with no precise definition of what these are, rather there are a variety of terms that describe more or less overlapping phenomena. The understanding in regulatory terms of what we are dealing with is varied, with some current classifications, commonly used by EU policymakers ie exchange/payment, security and utility tokens, being too broad and requiring further clarification based on a token's characteristics.

Today, the United Nations recognises 180 currencies worldwide from the US dollar to the British Pound to the European Euro, and more, with these currencies being used to buy goods and services. The value of most of these currencies is subject to minor changes on a daily basis, for instance a pint of milk will standardly cost £1 in the supermarket and one does not have to worry that it will be £2 on any day that same month. However, one of the criticisms of a number of cryptocurrencies (a sub-type of crypto-assets) as a means of payment, is the volatility in price fluctuations – the same pint of milk could cost anywhere between 20p - £10 in a given week.

'Stablecoins', another subset of crypto-assets, have characteristics that distinguish them from the categories mentioned above, most notably their stabilisation functionality with underlying or reference asset - what that underlying or reference asset may be varies from coin to coin. To date, the key distinctions among stablecoins have been the governance and the mechanisms for maintaining stability. However, it is important to flag that there are many different types of so-called stablecoins with some being neither stable nor a coin. That aside, the main benefit generally associated with stablecoins, is that depending on how and what they are pegged to, they may not be subject to the extreme price volatility that other crypto-assets are affected by.

In addition, they could potentially offer decentralisation, and in some cases global reach, with the ability to help the unbanked. These reasons are why this class of crypto-assets are seen by some as an attractive means of payment. Whilst there are a lot of discussions about the use of stablecoins, particularly from a policy perspective, the majority of industry participants are not yet launching anything in this space, primarily because of the lack of regulatory clarity on how such assets should be treated. Whilst there are benefits which warrant further discussion, this does not mean they are free from risks.

These include (i) risks to consumer protection, data privacy and financial stability, (ii) they could promote illicit activities, (iii) threats to weaker currencies and (iv) banks may lose their place as intermediaries if they lose deposits to stablecoin providers. The current financial markets uncertainty (brought upon by the COVID-19 crisis) has the potential for changing habits across all society in looking for technological 'safe havens'. While this may hasten some of the debate and support for certain crypto-assets, this still needs to be a measured and strategic response.

It is important that given the cross-border nature of many types of crypto-assets, that the industry and policymakers work together across jurisdictions to have agreed definitions and regulations to minimise the risks and maximise the benefits. Further, it is essential that the approach policymakers take is a uniform one that applies the principle of 'same activity, same risk, same regulation' in order to avoid fragmentation and allow market participants to benefit from scaling effects. ●