The Regulation of Digital Currencies and Stablecoins

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Session 5: IOSCO-PIFS-Harvard Law School
Global Certificate Program for Regulators of Securities Markets
December 14, 2021
Outline

What is Money?

The Rise of Digital Assets
  • Bitcoin & First Generation Cryptocurrencies
  • The ICO Phenomenon

Stablecoins
  • Basic Structure & Variants
  • Use Cases & Policy Concerns
  • Legal Classification
    • Securities
    • Private Banking
    • Systemically Important Entity
    • Specialized Legal Regime
Definition of Money

A store of value,

A means of exchange, and

A unit of accounting.
Traditional Cash & Banking Payment System

Federal Reserve (Master Account)

Bank A (with deposits)

Depositor

Bank B (with deposits)

Depositor
Alternative Payment Arrangements

Federal Reserve (Master Account) → Bank A (with deposits) → Venmo → Venmo Client I

Federal Reserve (Master Account) → Bank B (with deposits) → Venmo → Venmo Client II

FedNow Reforms

Weaknesses
- Costs
- Cross-Border
- Access
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Bitcoin & Distributed Ledger Technologies

“Satoshi Nakamoto” (2008)

Miners
The market value of the ecosystem increased dramatically beyond Bitcoin

Market capitalization for crypto assets (billions of US dollars)

Sources: Bloomberg Finance L.P.; CoinGecko; and Deutsche Bank calculations.
It’s not uncommon for bitcoin to trade within 4-hour periods.

Prices fluctuate significantly and in the same direction.

2017: Bitcoins surged to an all-time high.

2018: Bitcoin’s value dropped by 2/3.

2021: New high. Tesla announced USD1.5bn investment in Bitcoin in Feb 2021. PayPal announced in October 2020 to support BTC, ETH, BCH and LTC.

Libra was formally announced on June 18, 2019.

Sources: Deutsche Bank, Haver Analytics. Note: as of November 3 2021.
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The DAO ICO

Distributed Autonomous Organization (Code)

Slock.it UG (with Curators)

DAO Tokens

“Investors”

Ether V.C. ($150m)

DOA Token Trading Facility

DAO = automated malleable corporate governance system

Projects (from Contractors)

Profits or Prods./Serv.

Ether V.C.
The “Howey” Test

An investment contract . . . means a contract, transaction or scheme whereby --

a person invests his money
in a common enterprise, and
is led to expect profits
solely from the efforts of others
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Libra: Facebook launches cryptocurrency in bid to shake up global finance

Digital currency will let billions of users make transactions, but is already facing opposition from US lawmakers amid privacy concerns

- Facebook's Libra launch will extend its global domination
- All you need to know about Facebook's new cryptocurrency

Mark Zuckerberg, Facebook CEO, is launching Libra, a new digital currency system. Photograph: Charles Platiau/Reuters

Kari Paul in San Francisco

Tue 18 Jun 2019 05.00 EDT

Facebook has announced a digital currency called Libra that will allow its billions of users to make financial transactions across the globe, in a move that could potentially shake up the world's banking system.
President’s Working Group on Financial Markets, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency

Report on STABLECOINS

Chart 1: Top Stablecoins by Market Capitalization (in billions)

Source: Daily reports, The Block
Updated: October 21, 2021

November 2021
Stablecoin Structure

Use Cases:
- Now: On-Ramp to Cryptocurrencies
- Future: Payment Vehicle

Tether
(with assets + redemption Commitment or algorithm)

Blockchain Platform for Trading for USDT

Federal Reserve
(Master Account)

Bank A
(with deposits)

Bank B
(with deposits)

Holder I (me)

Holder II (my son)

Policy Concerns
- Holder/Investor Protections
  - Responsibilities of “Issuer”
  - Responsibilities of Intermediaries
- Commercial Law Concerns
- Systemic Risk Concerns
- AML/National Security Issues
Blockchain Analysis of the Bitcoin Market
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Section 21(a)(2) of the Glass Steagall Act

[I]t shall be illegal . . . [f]or any person, firm, corporation, association, business trust, or other similar organization to engage, to any extent whatever with others than his or its officers, agents or employees, in the business of receiving deposits subject to check or to repayment upon presentation of a pass book, certificate of deposit, or other evidence of debt, or upon request of the depositor . . .

“Glass-Steagall Deposits”
Three Exemptions from Section 21(a)(2)

unless such person, firm, corporation, association, business trust, or other similar organization

• (A) shall be incorporated under, and authorized to engage in such business by, the laws of the United States or of any State, Territory, or District and subjected, by the laws of the United States, or of the State, Territory, or District wherein located, to examination and regulation, or

• (B) shall be permitted by the United States, any State, territory, or district to engage in such business and shall be subjected by the laws of the United States, or such State, territory, or district to examination and regulations or,

• (C) shall submit to periodic examination by the banking authority of the State, Territory, or district where such business is carried on and shall make and publish periodic reports of its condition, exhibiting in detail its resources and liabilities, such examination and reports to be made and published at the same times and in the same manner and under the same conditions as required by the law of such State, Territory, or District in the case of incorporated banking institutions engaged in such business in the same locality.
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What is Money?
The Payments Revolution (at HLS)
The Old Rails
  • Cash & Checks
  • Credit & Debit Cards
  • Automatic Bank Transfers/FedNow-RTP Initiative
FinTech Products on Old Rails: PayPal, Venmo & AliPay
The New Rails
  • Bitcoin & First Generation Digital Currencies
  • Diem (aka Libra), Tether & Stablecoins
  • Central Bank Digital Currencies
What’s Next?
The Regulation of Digital Currencies and Stablecoins

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