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A Renewed Focus on Stablecoins

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Welcome to Bracewell Crypto Bits, a podcast that explores news and topics relevant to the cryptocurrency and blockchain communities.

The podcast is hosted by ***Anne Termine***, a partner in Bracewell's Washington, DC office and head of the firm's ***cryptocurrency and blockchain practice***. Prior to entering private practice, Anne spent approximately 13 years in the Division of Enforcement at the Commodity Futures Trading Commission, one of the key regulators with jurisdiction over digital assets.

In this episode, Anne discusses stablecoins and the impact that recent news may have on regulation and policy issues surrounding them.

Highlight

Today we're going to talk about stablecoins and how recent news may impact the regulation and policy issues surrounding them and what stablecoin issuers should think about and plan for in the coming months. So, let's jump into it.

What are stablecoins? They're digital assets designed to maintain a constant, or stable, value relative to other certain assets. One common example are stablecoins tied to the US dollar, where one US dollar stablecoin has an equivalent value to one US dollar.

For this discussion today, I'm not going to go in into the differences between asset-backed stablecoins versus algorithmic stablecoins. We're going to stay focused here about the policy issues facing stablecoins today.

Critics of stablecoins raise concerns about the assets used to back them, which are not necessarily actual dollars but instead can be a composition of assets. The assets may not all be readily convertible into cash, and also may not maintain their value to the dollar, so that the stablecoins can be redeemed on a one-to-one basis. This is something that we just saw play out in the past week with the stablecoins offered by Tether and Terra.

If you'd asked me last year, which area in cryptocurrency would Congress address first with new legislation, I would've absolutely said stablecoins, for a number of reasons.

First of all, the growth in the stablecoins in just one year was tremendous, moving from a market capitalization of around $5 billion in 2020 to $175 billion, just one year later in 2021.

At the same time, there were frequent news reports about stablecoins. Tether, one of the largest stablecoins in the world, with its USDT had just settled an enforcement case with the CFTC, my old agency, not long after settling one with the New York AG, in which both agencies alleged that Tether's stablecoin USDT was not backed one to one with US dollars as they claimed.

Then the president's working group led by the Treasury Department released its report on stablecoins and the concept of a central bank digital currency, or CBDC. The report laid out three concerns about stablecoins from the perspective of government agencies: (1) the risk of a run on a stablecoin, which contagiously spreads to other stablecoins and the funding markets behind them, which could result in instability; (2) a payment system risk in which the PWG argued that as stablecoins are more regularly adopted as a means of payment in financial services, or otherwise, any failure in that payment system could have cascading effects; (3) the risk of the concentration of economic power in the companies offering stablecoins, or those who scale up so quickly and become outsized to the market and are largely operating without supervision. Those are viewed as significant risks by the agencies involved in the PWG report. The suggestion was made that the issuers of stablecoins should come under regulation likely by prudential regulators. By that, I mean the banking regulators.

The PWG report was then followed rather quickly by the president's executive order, which was entitled "Executive Order on Ensuring the Responsible Development of Digital Assets." This was the administration's all-agency approach to cryptocurrency and specifically called on multiple agencies, including the prudential market regulators and even the DOJ, to develop reports on the risks and regulatory gaps facing digital assets like stablecoins.

With all these reports ringing in their heads, members of Congress face an additional concern that dollar-backed stablecoins could impact the US dollars dominance of the world's global currency. Based on all of these factors, the issue seemed absolutely right for legislative action. Then I listened to two hearings that happened in the first quarter of this year, one by the Senate Banking Committee and one by the House Financial Services Committee, both of which focus on the PWG report on the risk of stablecoins. What these hearings exposed was a deep divide among members of Congress on whether stablecoins should be regulated, how these should be regulated and who should regulate them. Without a clear direction in Congress and given that this is also an election year with the midterms occurring this fall, the momentum for stablecoin legislation had seemed to lose all steam.

Have questions about stablecoins or about the issues facing the cryptocurrency and blockchain communities? Email ***Anne Termine****.*