A. Introduction

Since 2018, stablecoins initiatives have mushroomed. After the Covid-19 outbreak, trading volume in stablecoins peaked in 2020.[1] In September 2020, the European Commission broke new ground in devising a bespoke authorisation regime for crypto-asset service providers, subject to enhanced regulatory requirements.[2] It is widely perceived as a response to Facebook's Libra project to obtain a first-mover advantage driven by political fear.[3] Some central banks have initiated plans to issue their own digital currencies (i.e. Central Bank Digital Currency ("**CBDC**")).

The quote presents a contest between public and private issuance. But it is dangerous to assume a false dichotomy. Developing stable currencies is not a political tug-of-war. Rather, public-private collaboration is key. I argue that a private-public partnership model of synthetic CBDC ("**sCBDC**") is the way forward.

B. Arguments for privately-issued stablecoins

"Stable currencies" here can mean a general reference to currencies that are stable, or – of greater contemporary relevance – issuing "stablecoins". This essay focuses on the latter. What distinguishes stablecoins from other cryptocurrencies is that the former rely on a set of stabilisation tools to minimise fluctuations of their price,[4] often backed by a pool "stable" asset. For instance, Libra is backed by a portfolio of assets including government bonds and bank deposits.[5] This is critical to avoiding the volatility problems that afflict earlier cryptocurrencies (e.g. Bitcoins).

Private issuers, such as the Libra Association, profess to tackle financial inclusion and facilitate cross-border payments. Globally, 1.7 billion adults lack access to traditional banks and remain

[1] ECB, 'Stablecoins' (ECB Occasional Paper Series No 247) 11.
[2] European Commission, 'Proposal for a Regulation on Markets in Crypto-assets' COM/2020/593.
[3] Ringe, 'Building a European market for crypto-assets: Who's afraid of Libra?' (OBLB, 27 Oct 2020) < www.law.ox.ac.uk/business-law-blog/blog/2020/10/building-european-market-crypto-assets-whos-afraid-libra> assessed 11 December 2020.
[4] Bullmann et al, 'In search for stability in crypto-assets: are stablecoins the solution?' (ECB Occasional Paper Series No 230) 9.
[5] Libra Association, 'Libra White Paper' <https://libra.org/en-US/white-paper/> accessed 12 December 2020.

outside of the financial system.[6] This arises out of a lack of standardisation and interoperability of payment services, significant costs in AML/CFT compliance, and divergence in domestic laws.[7] Accordingly, where existing payment systems are expensive and the trust in the currency is low, stablecoins can quickly establish a stronghold.[8] For instance, Venezuela's El Petro (backed by Venezuelan oil reserves) was seen as an attempt to circumvent sanctions and overcome liquidity shortages.

A "private" approach professes to be free from the limits of CBDC, one of which is that it disintermediates public access to the central bank balance sheet.[9] Depositors have lower incentives to maintain balances with commercial banks when CBDC is the more attractive and safer option. When the public maintains less deposit, commercial banks' ability to lend out their excess reserve is weakened. This could send a shockwave to the traditional business model of commercial banking. In addition, it is inefficient for central banks to act as the exclusive provider. The Bank of England candidly recognises that central banks lack the comparative advantage of devising user-friendly customer-facing services. Excluding private actors is therefore detrimental to innovation and competition.[10]

C. Concerns about privately issues

Nevertheless, privately-issued stablecoins have provoked disquiet in many quarters.

First, regulatory gap. Traditionally, bank money is regarded as safe because they are subject to extensive banking regulations. Once the issuer falls outside its ambit, systematic risks abound. These private attempts were described as "bad money" because these emerging money institutions resemble money market funds, yet they are not subject to similarly vigorous regulation.[11] Further,

[6] ibid 4.
[7] G7 Working Group on Stablecoins, 'Investigating the impact of global stablecoins' (October 2019).
[8] Bullmann (n 4), 47.
[9] BoE, 'Central Bank Digital Currency' (Discussion Paper, March 2020), 35.
[10] ibid 24.
[11] Awrey, 'Bad Money' (2020) Cornell Legal Studies Research Paper No 20-38.

domestic law might not have the conceptual tools recognise stablecoins (and cryptocurrencies generally) as money or property. Virtual currency is not "money" under the EU Electronic Money Directive. English law, which traditionally prides itself on its flexibility, struggles to ascertain their legal nature and refuses to recognise cryptocurrencies as "money".[12]

Yet these concepts are not static. We have witnessed an increasing willingness to accommodate innovations. In *AA v Persons Unknown*,[13] proprietary injunction was granted over Bitcoins as Bryan J accepted the UK Jurisdiction Taskforce's argument that cryptocurrencies can constitute a *sui generis* category of intangible property. In any event, these challenges arise regardless of the identity of the issuer.

Second, opaqueness in governance. Private issuers inevitably pursue profit-maximisation. They are likely to enjoy natural monopolies due to strong network effects.[14] With Facebook's extensive customer-base, the Libra project has encountered significant regulatory pushbacks. Tackling big-tech has been a dominant theme in European regulation, most prominently in antitrust and data protection. Unsurprisingly, Libra's ecosystem is described by the ECB as "cartel-like" due to concerns that its governance is centralised in the hands of conglomerates.[15]

Third, eroding central banks' monetary policy autonomy. Displacing national currencies affects states' ability to obtain financing internationally and service sovereign debt. Crucially, central banks control nominal interest rates to influence borrowing in the real economy. Where the stablecoin is backed by a pool of different currencies, it weakens the linkage between domestic monetary policy and interest rates on stablecoin-denominated deposits. Domestic interest rates become more sensitive to foreign fluctuations.[16]

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[12] McKendrick, *Goode and McKendrick on Commercial Law* (6th edn, LexisNexis 2020) [17.27]-[17-28].
[13] [2020] 4 WLR 35.
[14] European Parliament, 'Public or Private? The Future of Money' (Monetary Dialogue Papers, December 2019).
[15] Mersch, 'Money and private currencies: reflections on Libra' <www.ecb.europa.eu/press/key/date/2019/html/ecb.sp190902~aedded9219.en.html> accessed 15 December 2020.
[16] Public or Private? (n 14) 15.

Finally, the ECB raised a more fundamentally challenge by invoking Knapp's state theory of money. It argued that Libra's supporters overlooked the nature of money as a public good and an expression of state sovereignty.[17] The ECB's hostility is understandable given the unique constitutional framework of the European Monetary Union. Yet, it is unclear why we cannot endorse instead the more realistic societary theory of money – what truly matters is whether the community where it circulates treats it as such.

The difficulties outlined above are not insurmountable. Much hinges on the design of the system, the nature of the underlying assets, and whether regulatory safeguards are palatable to regulators. That is why most discussion papers remain cautiously optimistic.[18]

D. A Partnership Model

A private-public model is not new. In 2018, the IMF floated the possibility for central banks to allow private providers to keep accounts at the central bank.[19] Libra Association similarly suggested that as central banks develop CBDCs, they could be directly integrated with the Libra network to reduce credit and custody risk.[20] An sCBDC framework entails that central banks would cooperate with private issuers. The central bank offers settlement services and access to central bank reserves. The end relationship with customers (e.g. data management, KYC/AML reporting) is maintained by private providers.[21] This captures the technological expertise of private providers and their customer base. In gist, the private providers are intermediaries, and the crucial element of *trust* remains furnished by the central bank.

Admittedly, customers may not have a direct claim against the central bank since the "coins" are held by intermediaries. Issuer and credit risks remain, leading some to characterise sCBDC as not a true CBDC. Nevertheless, sCBDC's competitive advantages are clear. First, initiation costs for

[17] Mersch (n 15).
[18] BoE (n 9) 6.
[19] Adrian, Mancini-Griffoli, 'The Rise of Digital Asset'(IMF Fintech Notes 2019).
[20] White Paper (n 5).
[21] Public or Private? (n 14) 11.

central banks are lowered. Exploiting private experience gives central banks an easier head-start to overcome their inertia, as various CBDC initiatives are still in their infancy. Second, by imposing privacy and data protection standards as pre-conditions to access central banks reserves, central banks can better manage systematic risks.[22] Third, it minimises disruption to existing financial infrastructure. Fourth, central banks can ensure interoperability and prevent customers from the dominance of major private providers who enjoy network effects.[23] Finally, it limits the central bank's exposure to reputational and operational risk.

Some projects have already taken off. The People's Bank of China requires major payment providers to hold client funds at the central bank in the form of reserves.[24] The Hong Kong Monetary Authority also implemented a licensing regime allowing fintech firms to hold reserve balances. Central banks should provide a regulatory sandbox for private providers to create synergy.

Finally, the solution must be tailored to individual jurisdictions depending on the sophistication and public confidence in the financial infrastructure. The synthetic approach may not thrive where the private sector is weak and financial inclusion is low. But it is suitable for the UK, which has a dynamic private payment sector.[25]

E. Conclusion

"Cooperation is key".[26] The ECB's vociferous rhetoric is ripe for reconsideration. sCBDC strikes a middle ground by allowing central banks to hold the reins in establishing a licensing regime and supervisory rules. The partnership approach would assuage regulators' concerns.

[22] ibid 19.
[23] Adrian and Mancini-Griffoli (n 19) 13.
[24] ibid 12.
[25] BoE (n 9) 24.
[26] Lagarde, 'Central banking and Fintech – A brave new world?' (29 September 2017).