Barefoot Innovation Podcast with Tara Rice,
Head of Secretariat of the Committee on Payments and Market Infrastructures, Bank for International Settlements

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Jo Ann Barefoot: We have a wonderful and timely guest today because she is Tara Rice, the head of the Secretariat of the Committee on Payments and Market Infrastructures at the Bank for International Settlements and the perfect person to be talking today with about stablecoin. Tara, welcome.

Tara Rice: Thanks so much, Jo Ann. It's a pleasure to be here.

Jo Ann Barefoot: It's wonderful to have you. We are going to be focusing in our conversation on the emerging regulatory environment and principles that are beginning to emerge for stablecoin regulation. We are recording this as the FTX crisis is really continuing to unfold and become more clear. And I think it's a great time to be talking about stablecoin in the context of the future of digital assets at crypto payments. So I want to start by asking you just to introduce yourself, talk a little bit about your background, and then tell us specifically about the Secretariat.

Tara Rice: Thanks very much, Jo Ann. So Tara Rice, head of the CPMI Secretariat. I worked for a number of years in the Federal Reserve and have been here in Basel, Switzerland for about five years. The CPMI is, it's at a very important point in it's history, I would say. The Committee on Payments and Market Infrastructures is the international standard setting body that's concerned with the safety and efficiency of payments, clearing and settlements.

We have a sister standard setting body, I can discuss that a little bit more later, called the International Organization of Securities Commissions, IOSCO. They're the Global Standard Center for Securities Markets. And together both of us, CPMI and IOSCO, we work to enhance the coordination of standards and policy development as well as implementation for financial market infrastructures. We both work intensively with the G20 and with the Financial Stability Board on global regulatory reform issues.

We've just recently published in July a guidance on our standards for financial market infrastructures. And we'll get into that a little bit more as we talk about stablecoins. But just to go back to the history about 10 years ago now, 11 years ago, we published Principles for Financial Market Infrastructures. It's really the core of our standard setting in this space, and they're designed to help ensure the safety and efficiency and resilience of financial market infrastructure supporting global financial markets. And so they're full and timely and consistent implementation is really fundamental to everything we do.

Jo Ann Barefoot: Great. So you are among the very key international organizations that are helping us figure out what this infrastructure should look like, what's necessary to make sure it will work smoothly, what could go wrong and so on. So again, I'm really thrilled to have you with us today. Maybe the place to start is to ask you to outline the primary recommendations that are coming out of the new report, the new guidance that you've issued.

Tara Rice: Sure. I think it's helpful to have just a little bit of context first. So we've seen really rapid changes in the payment's landscape over the past several years, including the introduction of stablecoins and crypto assets. The innovation can bring lots of benefits, but we know it can also bring some risks. And so about two years ago, CPMI and IOSCO started to comprehensively review these standards that I just mentioned in light of these new innovations to see whether they were still fit for purpose. And in July we published our guidance on the application of these joint standards to stablecoin arrangements.

So the way we think about this in the standard setting world is there's a number of different functions that a stablecoin can do, and we are kind of focused just on one of them, the payments function or we call it the transfer function. There's others and other standard setting bodies are concerned with those, but we're thinking about this as a payment system.

So the main message I think that comes out of the guidance is, if a stable point arrangement performs this transfer of payments function, it's then considered a financial market infrastructure for the purposes of applying our standards. And if it's determined also to be systemically important by relevant authorities, then it is expected to observe all of the relevant principles in the PFMI or the standards. It's a clear application in our view of the same risk, same regulation approach. That means the regulation doesn't have to be identical, but the regulatory outcomes should so that we have a safe and efficient and robust framework to support any payments that are conducted or transacted in that stablecoin arrangement.

We look at four main principles having to do with governance, with comprehensive risk management, and with money settlement and settlement finality. The other piece that is covered in our guidance is it highlights some notable and novel features of stablecoin arrangements as compared to just existing financial market infrastructures. And the first is that stablecoins could have potential use of settlement assets that are neither central bank money nor commercial bank money, both of which we think are very safe settlement assets. The second is there's a number of interdependencies between multiple stablecoin arrangement functions, which we don't see in other existing financial market infrastructures. There's also a degree of decentralization in the operations and governance. And last, there's a potentially large scale deployment of emerging technology such as distributed ledger technology.

Jo Ann Barefoot: So you've issued this guidance in July and have been working on it for a long time. We at the time were seeing I think the recent turmoil in the markets with the Terra Luna situation that developed. And now more recently we have the

FTX, whatever the right word for it is, meltdown or crisis. Talk about how you see the role of stablecoins emerging within this ecosystem and also what you think maybe the impacts of this turmoil will be on the emergence of a workable stablecoin system.

Tara Rice: Well, I think it's fair to say that these recent developments in the crypto asset market and stablecoin market have really brought to the fore the urgency for authorities to address potential risks posed, risks that we've been talking about for some time. The recent market disruptions have been costly, well, very costly for many, but to date they haven't been systemic events. But I think especially with the FTX exchange, they've certainly showed the speed at which confidence can be eroded and how volatile crypto assets and stablecoins could be. One of the biggest concerns I have is that those who are potentially trading or investing in stablecoins and other crypto assets may not fully realize that they are speculative assets and would not have the sort of education, let's say financial literacy education, to know that they could lose all of their money. And so these risks are really coming to the fore and they illustrate the importance of having really sound robust regulatory frameworks.

Jo Ann Barefoot: If you think about this issue of whether people have the financial sophistication to understand these instruments, what are the solutions to that?

Tara Rice: First of all, having I think some consumer protection or consumer education, financial literacy education that outlines the risks of these different assets is very important. But more important is the fact that these speculative assets are not designed to be used as a means of payment. They're currently being used, for example, to exchange as a bridge between fiat currency and crypto, but they're not designed to be safe retail payments instruments. I think that there's serious issues or concerns about the role of having these unregulated intermediaries in the system. We've seen that the recent incidences or developments have shown deep-seated shortcomings that are probably unlikely to be able to be fixed by regulation alone. This is because they reflect, I think, inherent limitations of a decentralized system with permissionless blockchain.

Jo Ann Barefoot: Well, when you look at this from the standpoint of the case for stablecoin, what technical features do they have that we don't find in the traditional infrastructure that can make them a useful addition to the ecosystem?

Tara Rice: So let me start by saying that our standards were designed to be technology neutral. That means regardless of the technology used, that payment system or transfer function should still be safe, reliable, robust, fully trustworthy. And money, if we're thinking about a payment system, well money has three functions, right? It should be a good unit of account, it should be a good store of value, and it's meant to be a means of payment. So these functions don't necessarily rely on technology. And in fact, it's not clear to me at least that stablecoin themselves could provide benefits over fast payment systems or CBDC based on technology.

But that said, I think the technology that is developed around the stablecoin and crypto ecosystem could be used in different ways. For example, distributed ledger technology could be used for security settlement. It would make it faster or perhaps near instant, and it could reduce the risks of settlement fails. In such a securities transaction, you could think also about a smart contract which could enable payment and delivery, payment versus delivery we would say, of the security at the same time, thus making risks, they're also lower, making the transaction quicker.

And we can think of a number of other potential use cases for DLT, in distributed ledger technology. One other example that's been cited is I'm trying to... Or on building a regime, a database around know-your-customer, KYC. So if you could get on an unmutable ledger, the information needed to do consumer due diligence and know-your-customer that was accessible, that was resistant to fraud and that was available, that could help us also with just reducing money laundering and helping to bring more people onto into the financial system.

Jo Ann Barefoot: Yeah, that's a great point. There's so much work going on with digital identity and more broadly than know-your-customer system, which is at best very inefficient today, and also excludes some people who really deserve to be inside the financial system but are hard to process properly with the system that we have today.

Tara Rice: Yeah, let me take that point just one step further, and that is the crypto world offers to be anonymous, but actually what we want is the opposite of that. Imagine if we could create a global digital ID. Even if people didn't have a bank account, they could still make transactions because they would have a legitimate ID with which to make a transaction and that could then help them to get them into the financial system more broadly.

Jo Ann Barefoot: Yeah, absolutely. I just recently was at the Singapore FinTech Festival, which is the result of the work of the Monetary Authority of Singapore and I was spending some time with the India delegation there. And as you know, India has accomplished an incredible feat in creating the Aadhaar system that has given everyone a digital identity, and it's a massive force for financial inclusion when people have that, although not easy to do with proper protections around privacy and security.

When we look at the work that you're trying to do, we're in the midst of a set of innovations that are sweeping the globe and are opening up potential for problems with differences in regulation in different countries, including regulatory arbitrage, people looking for countries that have weaker regulation and then using that as a platform from which to launch global and international activities. How should we think about this issue of fragmentation of regulation? I know you're working to diminish it, but what's the outlook there and what are the risks if we fail to raise a basic set of standards that are in nearly universal usage?

Tara Rice: This is a really important point, Jo Ann. There's good cause story about fragmentation in regulation. Lax rules lead to what we call a race to the bottom. So when you have lack of or weak financial regulation, well, it puts people's hard earned money at state. Businesses want to take on more risk. Well, if businesses want to take on more risk and avoid robust regulations, they can easily move jurisdictions. And this is even more possible or easier with today's technology. So stablecoin doesn't need to be located at any one particular jurisdiction. And we've seen the ability to be able to move around. So when that happens, I mean they can move to another jurisdiction, take on those lesser or no regulations and cause some stability risks there. This is why we say we need consistent application of standards across the globe.

Common standards lead, we would say to a common denominator or baseline for regulation. We call them minimum standards, right? We always want to try and be above the minimum, but it leads to uneven playing field for all jurisdictions. But one challenge I think that we'll always face with is keeping up with innovation. Innovation can lead to greater benefits of course, and we talked about that, but authorities must always keep up with novel technologies and developments. It's a challenge now, but it's always been a challenge. If you think about even today we've got super fast-paced age of digital transformation, I like to say it's kind of grounded in the Hegelian dialectic, which is thesis, antithesis, synthesis. But in our world, we start with a set of existing regulations or standards and then firms innovate and then authorities must consider whether and how there's a need to reregulate. And so regulate, innovate, reregulate is just a constant cycle to make sure that we're at the cutting edge of developments.

Jo Ann Barefoot: Yeah, that is such a great point. It seems to be one of the biggest challenges facing regulators, and our listeners know I'm a former regulator myself, is this question of how to create almost a continuous ability to adjust to what the market is doing because the technology in the marketplace is changing so fast. And I think we're kidding ourselves if we think that somehow there's going to be sort of a modernization of regulatory content and structure and technology and then we can sit back for 10 years or whatever. That's not going to happen. It's going to be continuous.

The crypto sector has always been rooted in an ethic or a culture of not being very regulated. It arose originally as a way of circumventing the Federal Reserve system for example. And then as it's matured, more and more players are welcoming regulation as a way to understand the rules of the road and make it easier to scale. But let me ask you how you would describe the advantages for the stablecoin community or the stablecoin evolution in getting a clarified and more universal regulatory framework in place?

Tara Rice: Well, we can see what's developed just recently in the crypto space. Lack of a regulatory framework leads to lack of trust. And we've seen contagion, right? Panic losses. We've done the heavy lifting of our guidance CPMI and IOSCO. Now jurisdictions are working very intensely to develop their regulatory frameworks for this. So work is ongoing.

I think in general, developments have shown that markets don't necessarily self-regulate, and then it's easy for fear and contagion, so to speak, to spread. Money is a social convention. A dollar is worth a dollar to you or to I because we know that it'll hold that value. And then it can be widely used. And that trust in money is ultimately what is provided by the central bank. And through history, we've seen that the central bank can provide that trust in money. And then in combination with that, bank regulation and supervision means that commercial bank money or deposits are also trusted for the most part. But without all of that, we don't have that trust in money. We don't know that stablecoin will hold their value. We know that they're volatile.

In many cases, the information about the backing of those reserves for the stablecoin is opaque. It may not even be available at all. And so by actually providing regulation and supervision, we're providing that minimum set of standards, which should lead to a minimum amount of trust to be able to know that would there be any kind of issue that arises, that the regulators, supervisors actually, would be there to try to minimize or mitigate any potential large losses that would come from those stablecoin arrangements.

Jo Ann Barefoot: That's a great segue into asking you how you see stablecoins interacting with, or fitting into a framework with Central Bank Digital Currency, CBDCs? Do we need both? And if their roles are going to be differentiated, how do you see the roles of stablecoin versus CBDCs?

Tara Rice: I think you've hit on the $100 million question. So actually, I see kind of choice between fast payment systems and CBDCs, not between stablecoins and CBDs for the reasons that I said about the shortcomings of stablecoin arrangements. That said, I'm not ruling them out in the ecosystem and I'm happy to talk about how I see the ecosystem in the future. But what we're seeing in CBDC development is so interesting right now and so exciting.

BIS has done a CBDC survey to central banks for the last five years. And in fact, we've just launched our survey this year, so we'll be publishing our 6th early next. And over the past two years, we've seen a real increase in both the development of and the motivations for CBDCs. Right now we see about nine out of 10 central banks exploring Central Bank Digital Currencies. And more than half of those are either in development or running experiments. For motivations, respondents had noted some limitations in the current payment system such as limited operating hours and the length of transaction change, and I'll talk about that a little bit with the G20 Cross-border Payments program. And so I think that there's a lot of interest and a lot of opportunity here with Central Bank Digital Currencies. The BIS Innovation Hub is also conducting a number of really interesting pilots and projects. So I don't want to make any recommendations for CBDC because each jurisdictions really, they're going to investigate it and decide on their own for their own best use case.

We like to say that every jurisdiction starts with its own institutional history, its own sort of starting conditions, its own motivations. We're also seeing differences in motivations between advanced economies and emerging market and developing economies, but still the same amount of interest in CBDCs. Finally, the BIS Innovation Hub, CPMI, IMF, and World Bank published a G20 report in July, which outlined some considerations for access to an interoperability of CBDCs across border. One of the main messages that I took out of that was it's important to think about interoperability of systems at a very early stage. So that means that jurisdictions that are thinking about Central Bank Digital Currency development should really be thinking also about how to make that potentially interoperable with other systems, be it fast payment system or another Central Bank Digital Currency.

Jo Ann Barefoot: Yeah, that makes much sense. Would you care to try to project into the future a little bit, say 10 years out and suggest to us what the payments system might look like then, how different or similar it may be to what we have today?

Tara Rice: Yeah, let me start with what I'd like to see. I'd like to see a diverse ecosystem where customers have a lot of choices and they have low cost in making payments both domestically and cross-border.

One objective I think we all want to see is greater financial inclusion, and that can be done through using technology as we said, but also through the G20 Cross-border Payments program, which I'll touch on. In 2020, the G20 launched this Cross-border Payments roadmap or program. So for two years we've been looking to improve or enhance cross-border payments in a number of ways. I think what's really exciting, we've hit sort of an inflection point in the program. We've spent two years writing a number of reports and now we've turned to thinking about how to implement those recommendations and best practices that we've written about.

So just last month, the G20 received a paper from the FSB with our input that outlines three priority themes that have to do with some of these challenges that we've just discussed today. The first one is payments interlinking and expansion. So really the technical side of things, how do we improve those structures, those infrastructures? The second one is improving data and information exchange, so back to KYC and issues that we talked about. And then the third one is harmonizing legal and regulatory frameworks, which is really important. It's another concept in interoperability. We can't just have technical interoperability if our legal and our regulatory frameworks don't talk to each other, which you would know well. So these three themes really get to the heart of the challenges.

So what I'd like to see is continued political support and really broad-based engagement and commitment from central banks and from the private sector to actually implement some of these improvements to payment systems. CBDCs are included in the program, that's part of it. And I think we'll see a choice of options, so a menu of options. I think where we will want to spend special attention over the coming years is especially in jurisdictions outside of the G20 and the CPMI that have potentially greater frictions in cross-border payments and more need to bring in an enhanced financial inclusion.

Jo Ann Barefoot: Are you optimistic that we can have all the things we want, inclusion, interoperability, good anti-crime, anti-money laundering, and good privacy and security? And did I say speed? We want a lot from our payment systems, don't we? Do you think we can make all of those things better over the next decade? Or do you think that there are likely to be some trade-offs among them?

Tara Rice: Well, there's one thing we can't trade off for sure, and that is safety and efficiency and making sure that those payments get through. So we talk about proportionality in a number of things, but one area where we don't want to see proportionality is in payments. So if you send $100 payment, Jo Ann, what percent of that do you want to arrive?

Jo Ann Barefoot: Well said.

Tara Rice: And that's our base. That's our basis. We don't want to give up on that. But I do think that a lot of these enhancements that are coming down the pike are really going to make a measurable change. We have now an operation more than 60 fast payment systems. It's amazing. If we can think about interlinking those fast payment systems, we're already reducing a lot of frictions. And we are doing that.

You mentioned India. I'm so excited for India to have the G20 presidency this year. They have done so much with their payment systems, and we're going to learn I think a lot from them. We've been discussing with them also various priorities that we can put forward for the G20 this year. And let me just note one challenge that we will have. We will regulate and supervise stablecoin arrangements even so it's not clear to me that regulation and supervision alone will be sufficient to remove the risks of stablecoin. And that is one of the reasons that we are so focused on improvements in the existing payment infrastructure and exploration or development of Central Bank Digital Currencies.

Jo Ann Barefoot: Great. Is there anything we haven't talked about that you'd like to add?

Tara Rice: I would just add one more point that the FSB had noted back in 2020, the G7 also with the introduction or the announcement of potentially new large stablecoin arrangements, they had said that no global stablecoin arrangement should be an operation before sufficiently robust regulatory and supervisory systems were in place. I think we need to stop and reflect on that. It was said two years ago, and we are still working on those. We are working on those regulatory frameworks. And back to the point about having a trusted payment system, we really need something in place. And it's coming before we consider stablecoin arrangements as a retail means a payment that's safe for everyone.

Jo Ann Barefoot: That's a great note to end on. It's very difficult work and we appreciate the fact that you're doing it. Where can people get more information about the guidance and work that you're doing?

Tara Rice: www.bis.org has all of our publications, the guidance, information on the Cross-border Payments program.

Jo Ann Barefoot: Wonderful. Tara Rice, thank you so much for being our guest today. I really appreciate it.

Tara Rice: Thanks so much, Jo Ann. It was a pleasure.