

15 December 2022

Financial Stability Board (FSB)
Via email to fsb@fsb.org

Subject: Response to the FSB's Public Consultation on International Regulation and Supervision of Crypto-asset Activities

To whom it may concern,

The Cardano Foundation appreciates the FSB's engagement with the digital asset and distributed ledger technology community, and welcomes the opportunity to comment on the proposed framework and recommendations for stablecoins, and on crypto-asset activities and markets.

The Cardano Foundation is the independent, Swiss-based, and non-profit organization responsible for stewarding the advancement of the public, permissionless blockchain platform Cardano. Our mission is to anchor the Cardano blockchain as a base layer for current and future financial and social systems, thus empowering the architects of the future. We aim to de-risk decentralization for regulators and organizations, while also giving the Cardano community the necessary tools and support to leverage the Cardano protocol to solve real world problems.

Kindly find our comments and responses, according to the respective questionnaire, in the following. We remain gladly available to address any follow-up questions or to participate in further discussions with the FSB and any of its associated institutions.

Yours sincerely,

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1 Preliminary Remarks

The Cardano Foundation is convinced that an adequate, risk-based legal and regulatory framework, built on sensible and suitable principles, is beneficial to realizing the digital assets' and distributed ledger/blockchain technology's potential as well as its positive adoption, both now and in the future. We thereby appreciate the high-level approach and the quality of the FSB's proposed recommendations. Furthermore, we welcome the prudent and well-informed context provided in the consultative documentation underlying the FSB's rationale concerning the proposed recommendations.

We believe that good regulatory policy, which is innovation-friendly while also accurately mitigating potential risks, should consider the broad range of potential applications of blockchain technology and recognize the need for relevant differentiations, if indicated. It is our conviction that the principle of "same activity, same risk, same regulation" provides an important guideline for policy makers and regulators in evaluating and applying existing regulatory frameworks to blockchain technology and crypto-assets. In fact, we are of the opinion that some of the currently perceived regulatory shortfalls could be addressed by existing instruments and frameworks, if applied and enforced sensibly. This, however, also highlights the necessity to assess all use cases and their potential risks with due care in order to avoid creating a basis for overreaching or inadequate regulation, ultimately hampering growth and innovation.

Given the FSB's mandate and overall focus on financial regulation, we understand the FSB's approach reflects a perception of blockchain technology and crypto-assets filtered through the lens of finance and financial markets. However—and even though the current predominant use cases of blockchain technology revolve around financial or finance-like activities—, we firmly believe it should not be reduced to that. This also carries the implication that the assumption that blockchain technology and crypto-assets are *a priori* financial in nature (and that financial regulation provides appropriate remedies for assumed risks), should be more nuanced. As one of the key global standard setters for financial regulation, we comprehend the FSB to be in a great position to make a valuable contribution to facilitate a broad and sufficiently differentiated understanding of blockchain technology and crypto-assets, both on an international level as well as through the national competent authorities as addressees of the present recommendations.

2 Answers to the Questionnaire

- The below responses follow the FSB's questionnaire as published on <https://www.fsb.org/wp-content/uploads/P111022-2.pdf>, dated 11 October 2022; all questions have been copied without changes from said document.
- To avoid repetitions, cross-references between different responses might have been made, as indicated accordingly.
- Certain questions might have been omitted; such instances are indicated accordingly.

2.1 General

1. ***Are the FSB's proposals sufficiently comprehensive and do they cover all crypto-asset activities that pose or potentially pose risks to financial stability?***

We generally believe the proposed recommendations capture relevant activities and risks, provided they are within a financial context and concern crypto-assets which might realistically pose a risk to financial stability, hence, have a sufficient similarity to traditional financial activities. As indicated in our preliminary remarks above, as well as in the answers to the following questions, we are of the opinion that a more nuanced approach towards the notion of crypto-assets should be adopted.

2. ***Do you agree that the requirements set out in the CA Recommendations should apply to any type of crypto-asset activities, including stablecoins, whereas certain activities, in particular those undertaken by GSC, need to be subject to additional requirements?***

We generally believe that the requirements set out in the recommendations address relevant risk dimensions for crypto-assets and respective activities with a sufficient similarity to traditional financial activities. However, as indicated in our preliminary remarks above, as well as in the answers to the following questions, we are of the opinion that a more nuanced approach towards the notion of crypto-assets should be adopted. Therefore, we believe that not all activities should be similarly subject to the proposed

requirements and that a differentiating terminology should be implemented, based on the characteristics of the crypto-asset(s) concerned by a respective activity.

3. *Is the distinction between GSC and other types of crypto-assets sufficiently clear or should the FSB adopt a more granular categorisation of crypto-assets (if so, please explain)?*

As indicated in our preliminary remarks above, we are of the opinion that a more nuanced approach towards the notion of crypto-assets should be adopted to accurately capture and distinguish the relevant aspects of blockchain and crypto-assets, and its assumed respective risk dimensions. In particular, we see the need to establish an appropriate distinction between crypto-assets which have indeed financial purposes, and which might realistically pose a risk to financial stability, versus crypto-assets which are outside the scope of a direct financial purpose. Thus, in our view, the definition of crypto-assets as proposed by the FSB's recommendations is too comprehensive and does not take into account the technology's potential use cases outside a financial scope and the resulting need for differentiation. We would like to highlight that there are various promising use cases for the blockchain technology—some emerging, some already deployed, and many still to be explored—, for instance in the area of supply chain, Environmental, Social and Governance (ESG), identity and privacy, the Internet of Things (IoT), or the management of specific data records, to only name a few. Depending on the use case, a crypto-asset can have vastly different functions, many of which might prove to be quite far away from what is presently deemed a financial application or a financial asset. In our opinion, it should be made clearer that, even though all crypto-assets and/or related activities might be subject to laws and regulations, not all crypto-assets are *a priori* financial in nature and necessarily subject to financial regulation. Additionally, we also deem it crucial to differentiate between activities that concern the blockchain technology as an infrastructure technology versus activities that build and implement use cases and business models on top of the technology layer. Consequently, in light of the principle of “same activity, same risk, same regulation”, it should be closely assessed if seemingly alike activities actually render the same risks and if current remedies are suitable to address them effectively.

We are concerned that a non-differentiating and overly broad terminology might expand to use cases which are not (necessarily) suitably addressed by the proposed

recommendations and, potentially, lead to inefficient and/or ineffective approaches towards implementing the FSB's recommendations.

Finally, it seems important to mention that blockchain technology and crypto-assets are, in many areas, still an emerging technology, subject to ongoing development and fast-paced innovation. As such, we believe it to be crucial to not unnecessarily hinder those innovations.

4. *Do the CA Recommendations and the GSC Recommendations each address the relevant regulatory gaps and challenges that warrant multinational responses?*

We generally share the FSB's view concerning regulatory gaps and challenges. Particularly, we concur on the challenges around the availability of reliable data around crypto-assets for regulatory purposes and the challenges posed by the global and inherently cross-border nature of blockchain technology and crypto-assets.

In the first case, from an ecosystem perspective, we see great effort and progress in both availability as well as the quality of data and services around it. We also see tremendous potential stemming from the concept of so-called embedded supervision. Based on this, regulators would have access to more immediate data feeds and the possibility to verify certain data coming directly from a blockchain ledger¹. This could potentially significantly contribute to the efficiency and effectiveness of regulatory supervision, specifically around monitoring risk factors relating to financial stability.

In regards to the second main challenge, we generally believe that, in many cases, there exist valid regulatory remedies (or, more broadly, legal instruments stemming e.g. from corporate or criminal law) already in place which, when properly applied and enforced, would be able to address certain risks from crypto-assets and respective activities without the need for new regulation. However, as alluded above, in our understanding a coherent and appropriate conception of blockchain technology and crypto-assets, an international alignment on how existing rules can be applied in a suitable way, as well as efficient, cross-jurisdictional administrative cooperation, play an important role to facilitate adequate and effective regulatory enforcement.

¹ See for instance: BIS Working Paper No. 811 from September 2019 by Raphael Auer on "Embedded supervision: how to build regulation into decentralised finance", available at <https://www.bis.org/publ/work811.htm> , lastly visited on 11 December 2022.

5. ***Are there any financial stability issues that remain unaddressed that should be covered in the recommendations?***

- n/a -

2.2 Crypto-assets and markets (CA Recommendations)

6. ***Does the report accurately characterise the functions and activities within the crypto-ecosystem that pose or may pose financial stability risk? What, if any, functions, or activities are missing or should be assessed differently?***

Referring to our general elaborations as per the responses to the questions above, in particular to question 3, we would like to specifically highlight the need to apply an adequate understanding and, where indicated, appropriate distinction between blockchain technology as an infrastructure technology, on one hand, and, on the other, the use cases which implement it as a base layer and back-end technology, building utilities and business models on top of the technology.

7. ***Do you agree with the analysis of activity patterns and the associated potential risks?***

As this, directly or indirectly, relates to the scope of the underlying terminology regarding the understanding of blockchain technology and crypto-assets, we kindly refer to our preliminary remarks above as well as to the answers to the questions above.

8. ***Have the regulatory, supervisory and oversight issues and challenges as relate to financial stability been identified accurately? Are there other issues that warrant consideration at the international level?***

We kindly refer to our answer to question 4 above.

9. ***Do you agree with the differentiated requirements on crypto-asset issuers and service providers in the proposed recommendations on risk management, data management and disclosure?***

As this, directly or indirectly, relates to the scope of the underlying terminology regarding the understanding of blockchain technology and crypto-assets, we kindly refer to our preliminary remarks above as well as to the answers to the questions above.

10. ***Should there be a more granular differentiation within the recommendations between different types of intermediaries or service providers in light of the risks they pose? If so, please explain.***

As this, directly or indirectly, relates to the scope of the underlying terminology regarding the understanding of blockchain technology and crypto-assets, we kindly refer to our preliminary remarks above as well as to the answers to the questions above.

2.3 Global stablecoins (GSC Recommendations)

11. ***Does the report provide an accurate analysis of recent market developments and existing stablecoins? What, if anything, is missing in the analysis or should be assessed differently?***

We believe stablecoins to play an important role in bridging the gap between the blockchain ecosystem and the traditional financial system, and, ultimately, contributing to building a more transparent, fair, and inclusive financial system of the future. To fulfil their promises, stablecoins have to be implemented on principles of good governance, professional conduct, prudent risk management, and appropriate solvency. We are of the view that the FSB's recommendations duly reflect those notions.

12. ***Are there other changes or additions to the recommendations that should be considered?***

- n/a -

13. ***Do you have comments on the key design considerations for cross-border cooperation and information sharing arrangements presented in Annex 2? Should Annex 2 be specific to GSCs, or could it be also applicable to crypto-asset activities other than GSCs?***

- n/a -

14. ***Does the proposed template for common disclosure of reserve assets in Annex 3 identify the relevant information that needs to be disclosed to users and stakeholders?***

- n/a -

15. ***Do you have comments on the elements that could be used to determine whether a stablecoin qualifies as a GSC presented in Annex 4?***

- n/a -