GBBC Global Blockchain Business Council

Global Blockchain Business Council: Response to The Bank of England's approach to innovation in money and payments

About us:

GBBC is the largest leading industry association for the blockchain technology and digital assets community. Launched in Davos in 2017, GBBC is a Swiss-based non-profit, with more than 500 institutional members, and 301 Ambassadors across 117 jurisdictions and disciplines. The organisation is dedicated to furthering the adoption of blockchain technology by convening regulators, business leaders, and global changemakers to foster collaboration and advance dialogue to create more secure, equitable, and functional societies.

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Introduction

GBBC welcomes the opportunity to engage with the Bank of England (Bank) on considerations for innovation in money and payments. GBBC members, given their active involvement and engagement in the development of new forms of digital money are well qualified to contribute to the discussion around these topics and stand ready to assist the Bank as it moves forward.

Before moving to the Bank's questions, we set out below some high-level observations and recommendations:

- **Encouraging Collaboration and Flexibility**
    - GBBC believes that the Discussion Paper presents an opportunity to assess the UK's standing relative to global peers, address areas of stagnation, and ensure that the Bank of England's agenda is harmonised with broader government priorities. Emphasising both central bank and private sector innovations, revisiting regulatory frameworks for flexibility, and leveraging international insights are crucial steps to support a robust and innovative payments ecosystem. GBBC members would like to see a great focus on the interplay between stablecoins and CBDCs.
- **Integration with Government Initiatives**
    - Whilst we appreciate the comments that the Banks' approach will align with the delayed National Payments Vision (NPV) we are of the view that there is a lack of cohesiveness amongst UK regulators across the financial services sector that has the net effect of leaving the UK behind the curve when it comes to innovation and the forward-looking agenda for the future of money and payments. We sincerely hope that the NPV provides the necessary 'North Star' for the UK financial services industry so that it can maintain its reputation as a leader in financial services.
- **Benchmarking Against Global Peers**
    - The UK should benchmark its progress against both the EU and other global leaders to ensure competitiveness. This includes leveraging lessons learned from international initiatives without duplicating efforts, thereby enhancing efficiency and impact.

- **Balancing the "Singleness of Money"**
    - While we understand the Bank's emphasis on the "singleness of money", we question whether enforcing this concept across all platforms and instruments is necessary for monetary and financial stability. It may be more beneficial to allow for flexibility and the coexistence of multiple forms of digital money across various platforms and instruments. While we acknowledge the importance of the Bank's focus primarily on central bank money, we are of the view that it might be potentially overlooking valuable private sector innovations.
    - We suggest that the Bank should not obstruct alternative methods to achieve similar goals but rather foster an environment where both central bank and private sector solutions can thrive. For example, electronic money regulations have been in place for a long time and have been legally utilised without issue; revisiting and leveraging these existing frameworks could be advantageous.
- **Learning from Global Sandboxes**
    - There are many regulatory sandboxes and initiatives in hand across the various global standard-setting bodies and other regulators. The Bank should not seek to duplicate work already undertaken and should align its initiatives to add to the ever-growing knowledge base.
- **Coordination with other Regulators**
    - Whilst we appreciate the collaborative approach of the Bank in publishing this paper, we are concerned by the number of **consultations from regulators that run at the same time** on related topics, such as digital wallets, authorised push payment fraud, digital assets, and payment systems.
    - Improved **coordination among regulators** on consultation publication would be beneficial for the industry. We suggest:
        - **Streamlining consultations:** Regulators could better coordinate the timing and content of consultations to minimise overlap and reduce the burden on industry participants.
        - **Focusing consultations:** Limiting consultations to specific, non-overlapping topics can enhance efficiency and enable deeper, more meaningful industry engagement.

These recommendations were developed as part of GBBC's Working Group's discussions about the UK and global regulatory landscape. We hope that they can help provide a contextual perspective of industry actors, helping to facilitate the Bank's initiatives and regulatory efforts.

As the regulatory processes and projects in the digital finance space mature, GBBC believes that the continued dialogue between industry participants, regulators and financial institutions stands to gain from feedback channels focused on the improvement of the efficiency, safety and quality of regulatory processes. The above recommendations highlight the potential to harmonise existing and future regulatory frameworks and consultations of UK regulators by leveraging the expertise of the UK's financial industry, incorporating insights from other jurisdictions, and capitalising on the UK's leadership position in financial services.

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Paper Questions

1. Are there areas in which programmable platforms, including those enabled by DLT, might bring significant benefits and risks in payments and settlement?

GBBC members are of the view that programmable platforms can bring benefits to payments and settlement, leveraging DLT for Delivery versus Payment (DvP) as a core function, and the ability to automate processes can reduce time and cost. The end outcome and benefit will however depend upon whether the platform itself supports the settlement, or it has to link to another system or ledger to do so.

However, the ownership and governance of such platforms raise questions on risk and liability and consideration on how to manage on and off-chain disputes is an important consideration going forward. GBBC members believe that these are issues that can be addressed through governance frameworks that promote responsible innovation.

2. How likely are programmable platforms, including those enabled by DLT, to be taken up at scale by wholesale financial markets?

Programmable platforms are already live within the market (Fnality is an example) and hold significant potential for enhancing efficiency and automation within wholesale financial markets. However, their widespread adoption will depend on the Bank's ability to encourage these technologies through appropriate frameworks that are tailored to the risk.

3. What are respondents' views on the pace of innovation in private money – in particular, commercial bank money – used in retail payments?

The UK has a long history of financial services innovation, and private sector participants are already implementing innovative retail use cases for stablecoins that meet the needs of consumers and businesses, give consumers choices, and provide competition in the marketplace. Private sector innovation has been vital to spurring faster, cheaper, more efficient use and access to financial services. In addition, the Regulated Liability Network has showcased the art of the possible with commercial bank money.

Innovation continues at pace but the delays in progressing the regulatory framework for new forms of digital money cause uncertainty and result in challenges for go-to-market strategies for firms that risk losing investment and viable commercial business models.

4. What are respondents' views on the wholesale infrastructure that might support retail payment innovations, including ensuring that singleness of money can be maintained across stablecoins and tokenised deposits?

One of the main challenges that non-bank firms face is access to central bank money. Whilst the Bank was the first to allow such access, it is important for innovation and competition that the principles for such access are carried across to infrastructure that supports innovation in payments and financial services.

Question 5: What are the risks and benefits of the use of (a) tokenised deposits, and (b) stablecoins, for wholesale transactions?

- **Tokenised Deposits**

We see the following as the benefits of tokenised deposits:

Benefits

1. **Efficiency and Speed - Near-Instantaneous Settlement**
    - Tokenised deposits could enable almost immediate settlement of transactions, significantly improving upon traditional systems where settlements, especially in foreign exchange (FX), can take up to two business days (T+2). This rapid settlement reduces counterparty risk and enhances liquidity management.
2. **Programmability and Innovation - Smart Contracts**
    - The use of smart contracts allows for the automated execution of financial agreements with bespoke conditionality. This programmability fosters flexibility and enables the development of innovative financial products and services.
3. **Cost Reduction Reduced - Less Need for Intermediaries**
    - Utilising DLT and smart contacts can minimise reliance on intermediaries involved in clearing and settlement processes. By streamlining these processes, tokenised deposits lower transaction costs and increase operational efficiency.
4. **Stability and Trust - Issued by Regulated Banks**

- Tokenised deposits backed by regulated financial institutions and customer deposits offer enhanced stability. This backing mitigates insolvency risk and reduces price volatility, instilling greater confidence among users.

5. **Alignment with Regulatory Frameworks - Mainstream Adoption**

    - Tokenised deposits are more closely aligned with existing regulatory structures, easing compliance concerns and encouraging adoption by traditional financial institutions.

Risks

1. **Technological Vulnerabilities - Cybersecurity Risks**

    - Reliance on digital platforms exposes tokenised deposits to cyber-attacks, hacking, and software bugs. These vulnerabilities could compromise asset integrity and lead to financial losses.

2. **Bank Concentration Risk - Reliance on Specific Institutions**

    - If only a limited number of banks issue tokenised deposits this could result in concentration risk.

3. **Cross-Border Integration Challenges - Jurisdictional Differences**

    - Varying regulations across countries can complicate the integration of tokenised deposits in cross-border transactions, hindering seamless international operations and scalability.

Stablecoins for Wholesale Transactions

Our comments below are framed on the basis of the Banks' view that wholesale transactions are high-value, low-volume.

Benefits

1. **Near-Instant Settlement Faster for Cross-Border Transactions**

    - Stablecoins facilitate rapid settlement without the need for traditional clearing houses or correspondent banks. This efficiency improves liquidity management and reduces settlement risk in wholesale transactions.

2. **Cost Efficiency with Reduced Transaction Costs**
    - By reducing the number of intermediaries and streamlining processes, stablecoins lower fees associated with cross-border payments, currency conversions, and payment remittances.
3. **Simplified Cross-Border Payments as An Alternative to Traditional Systems**
    - Stablecoins offer a more straightforward method for international transfers compared to conventional systems like SWIFT, enhancing accessibility and speed.
4. **Programmability With Smart Contract Functionality**
    - The integration of smart contracts enables automated payments, escrow services, and conditional transfers, adding flexibility and efficiency to wholesale financial operations.
5. **Access to Decentralised Finance for Broader Financial Opportunities**
    - Stablecoins act as a bridge to DeFi platforms, opening new avenues for investment, lending, and other financial services.
6. **Market Diversification for Expansion into New Asset Classes**
    - Tokenisation through stablecoins is extending into various sectors, such as real estate and carbon credits, offering investors exposure to diverse markets.

Risks

1. **Collateral Quality and Transparency for Trust in Reserves**
    - The stability of stablecoins hinges on the quality and transparency of their collateral reserves. Insufficient or opaque backing can undermine confidence and pose systemic risks.
2. **Regulatory Ambiguity**
    - The lack of clear regulatory guidelines creates uncertainty. Navigating different legal frameworks across jurisdictions complicates compliance and may deter institutional adoption.

3. **Issuer Credit Risk from Dependence on Private Entities**

    - Stablecoins are often issued by private companies, introducing counterparty risk. The financial health and governance of these issuers may impact the stablecoin's reliability.

4. **Market Liquidity Risk in Stress Conditions**

    - In times of market volatility, liquidity for stablecoins may diminish, affecting the ability to execute large transactions without significant price impact.

5. **Interoperability Challenges Because Of Fragmented Standards and Networks**

    - Different technological standards and networks can create interoperability issues, leading to fragmented liquidity and inefficiencies in transaction processing.

6. **Technological Risks from Cybersecurity Threats**

    - As with all financial services, vulnerabilities to hacking, fraud, and technical failures pose risks, potentially resulting in financial losses and undermining trust in the financial system.

7. **Volatility in Algorithmic Stablecoins Based on Historical Failures**

Algorithmic stablecoins have experienced notable failures, leading to loss of value and market disruption. This history raises concerns about their reliability for wholesale transactions.

We note the Bank's definitions of wholesale and retail payments, in Box B of the Discussion Paper. The current distinctions between wholesale and retail payments are based on factors such as access, participant eligibility, and the protections afforded to each category. We believe that a distinction is important and are of the view that defining the difference based on the parties to the transaction, payments between individuals and businesses are retail; and payments between financial institutions are wholesale, therefore providing a more pragmatic way forward.

6. Are there innovations that could support central bank money being equipped with the requisite functionality to ensure safe settlement in light of technological advances in financial markets?

We understand that this question is in reference to electronically issued central bank money (that exists today) and not CBDCs.

ECB's "Exploratory work on new technologies for wholesale central bank money settlement" trials are a pertinent example in this context. In ECB's experiments, the Eurosystem's T2 and T2S platforms enabled central banks to develop three distinct blockchain-based mechanisms for submitting payment instructions into the TARGET2 system, with two operating on different networks. The trial demonstrates that payment instructions can be integrated into a central bank system without the payment mechanisms being CBDCs themselves. This approach could inform discussions on innovations in the integration of payment instructions into central bank systems without exclusive reliance on CBDCs.

7. What are respondents' views on potential functionalities of a wCBDC and how might these inform wCBDC design?

While ongoing initiatives under regulatory liability and regulated settlement network experiments have led to advanced projects, the interoperability of multiple wholesale CBDCs for cross-border payments remains an unresolved challenge. This issue merits further exploration and development, as there is currently no universally adopted template—various approaches are being taken, and region-specific solutions are still valuable. Prioritising interoperability on a multi-currency basis could demonstrate thought leadership, rather than simply replicating existing pilot initiatives. We encourage the Bank of England to focus on this area, leveraging its position and resources, such as the innovation hub in London, to advance this critical aspect of wCBDC functionality.

The issuance of wCBDC that is compatible with existing blockchain protocols, for instance, through the use of the ERC-20 token standard is likely to have beneficial outcomes for functionality and interoperability.

8. Will the proposed programme of experiments help to assess these potential functionalities for central bank money?

We reiterate the point named earlier about duplication and suggest the Bank focus more on the interoperability of multiple wholesale CBDCs for cross-border payments Project Agora to be forward-looking. It could consider a Payments Sandbox that builds on the work of the Regulated Liability Network to a wider range of participants.

9. What are respondents' views on the outcomes that the Bank seeks in retail payments and how can they be reflected in practical questions currently facing policymakers and industry?

We are fully supportive of the outcomes the Bank has detailed in the Discussion Paper for Outcomes 2, 3 and 4. With regard to the singleness of money and settlement, we refer the Bank to the caveat we raised earlier in this paper.

Examples of implementations from the industry:

- **Financial Institutions - leading adoption:**
  - Major banks like JPMorgan Chase have developed platforms (e.g., Quorum) to explore tokenisation, indicating strong industry interest and investment.
- **Blockchain Platforms - advancing tokenisation:**
  - Technologies like Hyperledger Besu and Tezos are accelerating the adoption of tokenised real-world assets, providing the structures for innovation and practical applications.
- **Stablecoin - use cases:**
  - Tether (USDT), a widely used stablecoin, facilitates liquidity and trading on exchanges. Expansion into other asset classes, such as real estate and green finance (e.g., tokenized carbon credits), highlights the versatility of stablecoins.

While tokenization presents clear benefits—such as reducing the need for intermediaries—it raises questions about how this aligns with the central bank's insistence on settling transactions in central bank money. This creates a natural friction between the decentralised efficiencies offered by DLT and the central bank's role in ensuring monetary control and financial stability.

Leveraging the cost reductions and efficiencies of tokenization and stablecoins may not be fully realised without the central bank's acceptance and integration of these technologies into their settlement processes. The central bank's cautious approach is understandable, given their fiduciary duties and the need to maintain oversight of the currency's availability and utilisation within the economy.

We recommend that the Bank of England considers being more accommodating of alternative settlement methods enabled by tokenization. By being open to integrating these new technologies, the central bank can help facilitate innovation while still upholding its essential functions.

GBBC members offer assistance to the Bank of England in this endeavour. By collaborating, we can jointly explore solutions that balance the benefits of reduced intermediaries with the central bank's requirements. This partnership would aim to advance the financial ecosystem in a way that promotes efficiency, innovation, and stability.