2025

IFWG Crypto Assets Regulatory Working Group

# South African Stablecoin Landscape Diagnostic

competitioncommission south africa

FIC Financial Intelligence Centre

FSCA Financial Sector Conduct Authority

NCR National Credit Regulator

national treasury Department: National Treasury REPUBLIC OF SOUTH AFRICA

SARS South African Revenue Service

South African Reserve Bank Prudential Authority

South African Reserve Bank

# Contents

# 1. Purpose and introduction

The Intergovernmental Fintech Working Group's (IFWG) 2021 Position Paper on Crypto Assets[1] (Position Paper) puts forward a set of recommendations for a revised South African policy as well as a legal and regulatory position on crypto assets and related activities, and essentially provides a roadmap for putting in place a framework for regulating crypto asset service providers (CASPs) in South Africa. In those recommendations, the IFWG acknowledged that new use cases would emerge and that it would continue to monitor crypto asset-related developments, both globally and domestically. So-called 'stablecoins' − a type of crypto asset that derives its value from one or more external reference assets − have gained traction within the crypto asset ecosystem and attracted the attention of the international regulatory community.

While stablecoins are a type of crypto asset, they present new value propositions for users, create unique risks and have the potential to amplify existing risks, meriting closer scrutiny. As reflected in the *2024 Budget Review,*[2] the IFWG, through the Crypto Asset Regulatory Working Group (CAR WG), will conduct analytical work to understand the applicable use cases of stablecoins to inform an appropriate policy and regulatory response by the financial services regulators.

The CAR WG proposes to do this in two phases. Phase 1 entails a diagnostic of the South African landscape with a focus on stablecoin arrangements pegged to the South African rand (ZAR).[3] The diagnostic (this paper) provides an overview of existing ZAR-pegged stablecoin arrangements and examines the risks and issues that these stablecoins present, for the consideration of the regulators. Additionally, it reflects how the regulatory interventions aimed at bringing crypto assets into the regulatory perimeter impact stablecoin arrangements in South Africa and identifies current gaps for further consideration to develop a comprehensive regulatory approach to stablecoin arrangements. Phase 2 will look at balancing innovation and risk mitigation by unpacking the potential benefits and macroeconomic risks associated with stablecoin arrangements in greater detail; consider options to address the identified

1 IFWG, 2021. https://www.ifwg.co.za/Reports/Position%20Paper%20on%20Crypto%20Assets.pdf
2 National Treasury, *2024 Budget Review*. https://www.treasury.gov.za/documents/National%20Budget/2024/review/FullBR.pdf
3 A stablecoin arrangement refers to the combined range of functions and related activities that aims to maintain a stable value relative to a specified asset or pool of assets. (FSB, 2023).

gaps with due consideration of international recommendations, developments and prevailing best practice; and consider regulatory options for the comprehensive regulation of stablecoin arrangements.

## 1.1. What are stablecoins?

Stablecoins are a type of crypto asset that attempt to maintain price stability (value) through collateralisation, meaning they peg or tie their value to an external reference in the form of real-world assets such as fiat currencies (singular or a basket), to physical assets in the form of commodities such as gold, or to one or more crypto assets. Alternatively, price stability is sought through leveraging algorithmic formulas and smart contracts that control supply by buying and selling the reference asset or its derivatives. The Financial Stability Board (FSB) defines a stablecoin as "a crypto-asset that aims to maintain a stable value relative to a specified asset, or a pool or basket of assets".[4] There is no universally agreed legal or regulatory definition for stablecoins, and the use of the term is not intended to imply that its value is in fact stable. Instead, this paper, in line with international standard-setting bodies (SSB), employs the term because it is commonly used within the crypto ecosystem.[5]

Stablecoins can generally be categorised by their stabilisation mechanism and/or by their custodial arrangement type. The stabilisation mechanism relates to how the stablecoin retains its value relative to the underlying asset or assets to which the stablecoin purports to be equal. In turn, whether or not a custodial arrangement is required depends on the nature of the stabilisation mechanism. A custodial arrangement is required for stablecoins that utilise real-world assets such as currency/fiat or gold as these assets need to be 'physically held' or custodied. Such custody arrangements occur outside of the distributed ledgers that generally underpin stablecoin arrangements. Hence, these arrangements are also referred to as 'off-chain' (i.e. off-[the block]chain), while stablecoins that are backed by, or derive their stability from, unbacked crypto assets do not require this custodial arrangement as all the reserves are online or 'on' the distributed ledger (i.e. on-[the block]chain).

Algorithmic stablecoins are categorised as non-custodial as they are generally not backed by any assets. Instead, these coins use an on-chain computer algorithm or

4 FSB, 2023
5 BIS-FSI, 2024a.

protocol and smart contracts to adjust supply based on demand in an attempt to maintain price stability. The programmed algorithms enable a dynamic adjustment to the supply of tokens in reply to any demand changes. In cases where demand rises, the algorithm can mint or issue new tokens to maintain price stability. Conversely, when demand decreases, it can burn or destroy tokens to reduce supply. TerraUSD (UST), for example, adjusted supply relative to another digital asset − its sister token called Luna − within the same stablecoin arrangement. The pair of coins together formed an algorithmic stablecoin that aimed to maintain a value of USD1 for each UST by using a parallel floating rate cryptocurrency, Luna, to back up the target peg.

Table 1 summarises off-chain and on-chain custodial arrangements. The summary is non-exhaustive, and it is acknowledged that some stablecoin arrangements could feature a mix of stabilisation mechanisms.

**Table 1: Off-chain and on-chain custodial arrangements**

| Off-chain/custodial arrangements | On-chain/non-custodial arrangements |
|---|---|
| • Fiat-backed e.g. Tether (USDT) and ZARP | • Crypto asset-backed e.g. Wrapped Bitcoin (WBTC)[6] |
| • Commodity-backed e.g. Tether Gold (XAUT) and Paxos Gold (PAXG) | • Algorithmic e.g. TerraUSD (UST) and DAI, including the Seigniorage shares approach.[7] |

## 1.2. Stablecoin use cases

Crypto assets, in general, purport to have the potential to improve financial inclusion and democratise finance. One of the long-term objectives of stablecoins is to improve the efficiency of cross-border payments, which proponents argue could lower the costs associated with intermediaries and offer faster settlement than traditional payment methods.[8]

---

6 Wrapped crypto assets attempt to overcome interoperability issues by enabling crypto assets to be used on blockchains to which they are not native.

7 The seigniorage share model generally consists of two forms of cryptocurrencies: stablecoin (coins) and seigniorage ownership (shares). When the price of a currency exceeds the intended peg, shares are utilised to increase the supply of coins.

8 Coinbase Institute, Stablecoins: Coinbase White Paper, July 2022. https://assets.ctfassets.net/c5bd0wqjc7v0/79db1PxjBTv1JbL574fFvA/dc38c8c96dc97c3752fd81a61d0f134a/CBI-StablecoinWhitepaper-July-2022.pdf

Stablecoins are currently primarily utilised as the 'currency' of decentralised finance (DeFi) and as a trading pair on crypto asset exchanges, that is, stablecoins assist with (arbitrage) trading by acting as a substitute for fiat currency in the crypto ecosystem and as collateral in crypto asset transactions by allowing users to move in and out of more volatile (unbacked) crypto assets faster, thus eliminating the need to convert into and/or from fiat currency.

Central bank digital currencies (CBDCs) are not considered stablecoins by international SSBs and for the purposes of the work being undertaken by the CAR WG. CBDCs are issued by central banks and generally considered legal tender, while stablecoins are privately issued and, although considered a type of crypto asset, are generally not treated as legal tender.

## 1.3. The rationale for focusing on stablecoins

Stablecoins backed by traditional assets and pegged to a single currency mimic the three functions of money in that they constitute units of account, can be mediums of exchange, and act as stores of value. Therefore, they can rapidly become widely used as a form of payment and/or store of value.[9] Broad adoption could have far-reaching implications for financial stability, monetary sovereignty, financial integrity and other macroeconomic risks.[10] This particular stablecoin design, which involves collateralising with real-world assets, necessitates the use of financial sector incumbents, such as banks and investment firms. This can represent a significant source of contagion risk between the traditional financial sector and the crypto ecosystem. Although adoption by, and interconnectedness with, the traditional financial system is currently limited, this can change over time and do so rapidly.[11] This paper focuses primarily on stablecoins pegged to the ZAR and backed by deposits with banks and/or rand investments with financial institutions such as investment firms, given the above-mentioned implications and potential risks.

Given the ongoing issuance of stablecoins in South Africa, a comprehensive and effective regulatory framework is necessary to appropriately mitigate any risks these arrangements may introduce, particularly before stablecoins become more widely

[9] BIS-FSI, 2024b.
[10] FSB, 2023.
[11] IMF-FSB, 2023.

used in South Africa. Such a framework should address the risks associated with stablecoins and leverage their purported potential benefits, including cost reduction, convenience and functionality.

International SSBs and international organisations have developed several standards aimed at ensuring globally consistent and comprehensive regulation, supervision and oversight of stablecoin arrangements. This includes the FSB,[12] the Basel Committee for Banking Supervision (BCBS),[13] the Bank for International Settlements (BIS) Committee on Payments and Market Infrastructures (CPMI),[14] the International Organization of Securities Commissions (IOSCO)[15] and the Financial Action Task Force (FATF).[16] As a member of these SSBs and international organisations, South Africa is expected to 'lead by example' and implement these recommendations to the full extent possible and within the expected timelines.

# 2. South African stablecoin landscape

At the time of writing this paper, there were six rand-backed and rand-pegged stablecoin arrangements in South Africa (hereafter referred to as ZAR stablecoins), with several others being planned. These ZAR stablecoins are all issued by non-banks, while several regulated entities continue to investigate the feasibility of a range of use cases that utilise stablecoins.[17]

The CAR WG[18] conducted surveys and met with five[19] ZAR stablecoins to better understand their design configurations, use cases, functions and characteristics.

---

12 FSB, 2023.
13 BIS-BCBS, 2022.
14 See the *Application of the principles for financial market infrastructures to stablecoin arrangements*, July 2022, available at https://www.bis.org/cpmi/publ/d206.pdf
15 See the *Policy Recommendations for Crypto and Digital Asset Markets: Consultation Report*, May 2023, available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD734.pdf
16 See the *FATF Report to the G20 Finance Ministers and Central Bank Governors on so-called Stablecoins*, June 2020, available at www.fatf-gafi.org/publications/virtualassets/documents/report-g20-so-called-stablecoins-june-2020.html
17 See *Project Khokha 2*. The report is available at https://www.ifwg.co.za/Reports/Project%20Khokha%202_2022%20Full%20Report.pdf
18 The CAR WG is a working group under the auspices of the IFWG and aims to develop clear and appropriate recommendations on a variety of emerging crypto asset use cases in order to deepen regulatory certainty.
19 The sixth stablecoin arrangement was launched after the consultation period.

Table 2 presents an overview of the five ZAR stablecoins consulted as part of the analysis.

**Table 2: Overview of five rand-backed and rand-pegged stablecoins**

| | **A** | **B** | **C** | **D** | **E** |
|---|---|---|---|---|---|
| **Issuer** | Single | Single | Single | Multiple | Single |
| **Peg/ reference point** | ZAR | ZAR | ZAR | ZAR | ZAR |
| **Stabilisation mechanism** | Fiat-backed (ZAR) | Fiat-backed (ZAR) | Fiat-backed (ZAR) | Fiat-backed (ZAR) | Fiat-backed (ZAR) |
| **Reserve assets/ collateral*** | ZAR with an asset manager<br>Full reserve | Bank deposit (ZAR).<br><br>Full reserve | Bank deposit (ZAR).<br><br>Full reserve | ZAR with an Asset manager<br>Full reserve | Bank deposit (ZAR)<br><br>Full reserve |
| **Underlying DLT** | Ethereum and Solana | Ripple | Ripple | Proprietary | BNB Smart Chain |
| **Governance** | Centrally managed by private company issuer | Centrally managed by private company issuer | Centrally managed by private company issuer | Centrally managed by consortium with on-chain governance mechanism | Centrally managed by private company issuer |
| **Custodial wallet included in arrangement** | No | No | Yes | Yes | No |
| **Exchange controlled by arrangement** | No | No | Yes | No | Yes |
| **Liability*** (Who/what is the claim on and are there conditions?) | Claim on the issuer | Claim on the issuer | Claim on the issuer | Claim on the issuer | Claim on the issuer |
| **Redemption rights*** (Redeemable with issuer? In return for? Conditions?) | Redeemable at par in ZAR directly with the issuer | Redeemable at par in ZAR directly with the issuer | Redeemable at par in ZAR directly with the issuer | Varies per issuer | Redeemable at par in ZAR directly with the issuer |

* *Information supplied by the issuers and not verified by the CAR WG*

It is important to note that the information contained in this section has not been verified by the CAR WG. Instead, the section presents the information as provided by the ZAR stablecoins, and the reflections and insights shared are based solely on the information provided to the CAR WG.

**Use cases**

In general, all the ZAR stablecoins aim to facilitate domestic and international payments. However, the ZAR stablecoins are primarily used for arbitrage trading and rand access to DeFi applications. The underlying business model is based on interest earned on reserves.

**Adoption**

The uptake of ZAR stablecoins is generally limited as the number of users averages between 100 and 2 000 clients or wallets (wallets may not represent unique users), while the collective market cap totalled approximately R106 million at the time of drafting.[20]

**Reserves**

All the ZAR stablecoins claim to be fully backed by reserves, and they each cite that the reserves are either held in cash in a bank account or with an investment firm that invests the funds in predefined liquid assets. This serves to ensure customer withdrawals can be honoured, regardless of market conditions. These reserves are generally kept separate from operational balances, with each ZAR stablecoin indicating that client funds are not co-mingled with the entity's own funds and that their reserve assets are independently audited once a year, on average. These safeguards are currently applied on a voluntary basis, in the absence of regulatory requirements.

**Disclosures**

Generally, the specific structure, size and operations of these ZAR stablecoins remain somewhat opaque, and the arrangements are circumscriptive in their public disclosure of information necessary to understand their design and operations. They provide very limited, and in some cases inconsistent, details related to reserve assets, market capitalisation, coins in circulation as well as ownership and governance arrangements. Disclosures of coins in circulation and reserve assets tend not to be reflected on their websites. However, coin issuance and redemptions can be viewed on independent third-party on-chain crypto tracking websites.

[20] June 2024 and based solely on information provided by the stablecoin issuers.

**Multiple functions**

Stablecoin arrangements are different from traditional payments as the functions can, and tend to, be distributed across several entities, with each fulfilling a different role.[21] The fulfilment of multiple functions is not consistent across the stablecoin arrangements; however, some issuers operate trading platforms for purposes of issuing and obtaining the stablecoin and there are also instances where custodial wallet services are offered by the issuer/arrangement.

**Other aspects of the ZAR stablecoins**

The engagements with the stablecoin arrangements indicate adherence to emerging best practice on a voluntary basis in the absence of a regulatory obligation for prudential risks (e.g. reserves management and liquidity). Examples include the auditing and segregation of reserves and redemption at par on demand with the issuer. All the issuers also claim to be applying Know Your Customer (KYC) and anti-money laundering and countering the financing of terrorism (AML/CFT) onboarding requirements for cash-in and cash-out purposes.

# 3. Regulatory landscape

The IFWG's 2021 Position Paper[22] presents a functional analysis of the five crypto asset use cases most prevalent at the time, namely (i) the buying and selling of crypto assets by individual consumers and legal persons; (ii) payments using crypto assets; (iii) capital raising through initial coin offerings; (iv) crypto asset funds and derivatives; and (v) crypto asset market support. Based on the use case analysis, the Position Paper identifies three overarching risks related to crypto assets that are of immediate concern, namely (i) money laundering/terrorist financing; (ii) the circumvention of exchange controls; and (iii) consumer protection and market conduct. The Position Paper makes 25 recommendations for a revised South African policy as well as a legal and regulatory position on crypto assets and related activities, essentially suggesting a risk-based and phased roadmap towards implementing a comprehensive framework

[21] FSB, 2023.
[22] IFWG, 2021. https://www.ifwg.co.za/Reports/Position%20Paper%20on%20Crypto%20Assets.pdf

for regulating CASPs in South Africa. The identified risks and recommendations remain relevant and are being addressed by the relevant regulatory agencies.

The Position Paper defines a crypto asset as "…a digital representation of value that is not issued by a central bank, but is capable of being traded, transferred or stored electronically by natural and legal persons for the purpose of payment, investment and other forms of utility; applies cryptographic techniques and uses distributed ledger technology." The definition presupposes the inclusion of stablecoins. Aligned with the recommendations in the Position Paper and international sectoral guidance,[23] IFWG members have implemented regulatory measures aimed at CASPs that have implications for stablecoins as the latter is considered a type of crypto asset.

As part of its analysis, the CAR WG assessed the prevailing regulatory frameworks applicable to crypto assets and their applicability to stablecoin arrangements with the objective of identifying gaps that need to be addressed. The next section presents an overview of legislative changes applicable to crypto assets and, by extension, stablecoin arrangements.

**Financial Intelligence Centre**

The Financial Intelligence Centre (FIC) finalised the amendment of schedules 1, 2 and 3 to the Financial Intelligence Centre Act 38 of 2001 (FIC Act). Effective on 19 and 31 December 2022, the amendments brought CASPs into the FIC's regulatory purview as accountable institutions to address anti-money laundering, countering the financing of terrorism and combating proliferation financing (AML/CFT/CPF).

The FATF requires that jurisdictions with crypto asset businesses operating within said jurisdiction ensure that such businesses comply with AML/CFT/CPF standards − FATF (revised) Recommendation 15.

The FATF defines a 'virtual asset' as a digital representation of value that can be digitally traded or transferred and can be used for payment or investment purposes. Virtual assets do not include digital representations of fiat currencies, securities and other financial assets that are already covered elsewhere in the FATF Recommendations. The FATF further defines a 'virtual asset service provider' as any

[23] For example, the FATF's Updated Guidance for a Risk-Based Approach to Virtual Assets and Virtual Asset Service Providers (fatf-gafi.org)

natural or legal person who is not covered elsewhere under the FATF Recommendations and as a business that conducts one or more of the following activities or operations for or on behalf of another natural or legal person:

i. exchange between virtual assets and fiat currencies;
ii. exchange between one or more forms of virtual assets;
iii. transfer of virtual assets (transfer means to conduct a transaction on behalf of another natural or legal person that moves a virtual asset from one virtual asset address or account to another);
iv. safekeeping and/or administration of virtual assets or instruments enabling control over virtual assets; and/or
v. participation in, and provision of, financial services related to an issuer's offer and/or sale of a virtual asset.

Consequently, jurisdictions that have such crypto businesses operating in their jurisdictions must, at a minimum, regulate the five crypto activities listed above for AML/CFT/CPF purposes.[24]

The FATF has stated that a virtual asset, as defined above, includes stablecoins.[25] In brief, this means such businesses must comply with AML/CFT/CPF obligations as set out in the FIC Act. This includes, among other things, that the business must register with the FIC as an accountable institution, deal with customer onboarding, conduct enhanced customer due diligence, report suspicious transactions, report cash transactions of R50 000 and above, and have a risk management and compliance programme in place.[26]

Those crypto businesses that are licensed by the Financial Sector Conduct Authority (FSCA) under the Financial Advisory and Intermediary Services Act 37 of 2002 (FAIS Act) are accountable institutions under item 12 and also under item 22 (where such

[24] See the FATF's Updated Guidance for a Risk-Based Approach to Virtual Assets and Virtual Asset Service Providers (fatf-gafi.org)

[25] See the FATF Report on so-called stablecoins to the G20 Ministers of Finance and Central Bank Governors, June 2020, VIRTUAL ASSETS – DRAFT FATF REPORT TO G20 ON SO-CALLED STABLECOINS (fatf-gafi.org)

[26] For additional guidance published for accountable institutions regarding their obligations, refer to the FIC website: FIC – Making South Africa's financial system intolerant to abuse

activity is an intermediary service). These businesses need to comply with FIC Act obligations in respect of their customers.

**Financial Sector Conduct Authority**

The FSCA published the declaration of crypto assets as a financial product under the FAIS Act (declaration), which was gazetted on 19 October 2022. The declaration brought providers of financial services in relation to crypto assets within the FSCA's regulatory jurisdiction.

The following definition is used in the declaration contained in General Notice 1350 of 2022:

*"crypto asset" means a digital representation of value that –*

> *(a) is not issued by a central bank, but is capable of being traded, transferred or stored electronically by natural and legal persons for the purpose of payment, investment and other forms of utility;*
>
> *(b) applies cryptographic techniques; and*
>
> *(c) uses distributed ledger technology.*

This definition of a 'crypto asset' in the declaration includes stablecoins. Therefore, any person rendering financial services (advice or intermediary services) in respect of stablecoins (unless exempted) falls within the scope of the FAIS Act and, consequently, such person must be licensed to render such service. The FAIS Act regulates the provision of advice and the rendering of intermediary services to financial customers, but it does not regulate product providers. Therefore, stablecoin issuers (product providers) are not regulated by the FAIS Act as issuers. Stablecoin issuers are only captured under the FAIS Act if they also provide financial services in respect of that stablecoin in addition to the issuance or minting.

**Gaps in the current legislative framework**

An analysis of the salient or differentiating features of stablecoins and the provisions currently affected in law reveal that certain key functions in a typical stablecoin arrangement are not captured (as the Position Paper and regulatory interventions were not focused on stablecoin regulation). These features are discussed below.

## 1. Issuance

As mentioned, the FAIS Act regulates the provision of financial services consisting of advisory and intermediary services. Therefore, the issuance activity of a stablecoin (a product) is not captured as a regulated activity. The issuance of a stablecoin would need to be accompanied by the provision of financial advice and/or intermediary services to fall within the ambit of the FAIS Act. The issuance of a stablecoin is also not covered under the FIC Act.

## 2. Governance

The FAIS Act does not cover governance aspects regarding which entities may be involved in the arrangement (i.e. banks or non-banks). The only governance-related requirement in the FAIS Act is that if financial services, as defined, are rendered, then that entity must be a licensed financial services provider (FSP). Other governance elements in stablecoin arrangements such as the protocol for validating transactions and the mechanism for maintaining the peg are also not covered. In terms of financial soundness, the FAIS Act, through Chapter 6 of the fit and proper requirements in Board Notice 194 of 2017, provides general solvency, working capital and liquidity requirements in respect of the FSP. However, these requirements are not placed on the stablecoin issuer as an issuer, but rather as an FSP in the event that the stablecoin issuer provides financial services, as defined.

## 3. Reserve assets

In terms of managing the funds that back the value of the stablecoin, the FAIS Act does not impose any requirements regarding the composition or quality of the reserve assets. There are no financial soundness requirements that are based on the risk weights of the underlying exposures. As previously explained, the financial soundness requirements apply to the FSP, not to a stablecoin issuer, in terms of the issuance activity. Equally, custody of the reserve assets backing the stablecoin is not considered customer funds; therefore, the requirements of the FAIS Act are not applicable.

Requirements related to the management and custody arrangements of reserve assets do not fall within the FIC mandate and are therefore also not covered under the FIC Act.

### 4. Transfer of coins

There are no requirements from a FAIS Act perspective on the blockchain protocol that determines the roles and levels of access to the stablecoin arrangement.

Equally, the validation and authorisation processes done through the validator nodes are not captured in the FAIS Act, as these participants are currently exempted from the FAIS Act through the FSCA FAIS Notice 90 of 2022.

### 5. Storage and interactions with users

Under the FAIS Act, providing and managing cryptographic wallets and storing public and private keys in stablecoin arrangements as a regular feature of a business requires licensing as an FSP, or a person providing these services must be appointed as a representative of an authorised FSP. This activity is captured as keeping a financial product, which a client purchased, in safe custody.

In terms of the activity of purchasing/exchanging a stablecoin for/with fiat currency, or a stablecoin with other stablecoins or crypto assets, the facilitation of this process through an exchange will bring about a transaction in respect of a financial product, being a crypto asset (i.e. the acquisition of the crypto asset is therefore captured under the FAIS Act).

Market makers that are employed to ensure sufficient liquidity and efficient trading are not captured under the FAIS Act.

These legislative gaps are summarised in Table 3.

**Table 3: Gap analysis of crypto asset-specific regulations and their applicability to stablecoins**

| Function | Activities | Regulatory coverage |
|---|---|---|
| **Governance** | Establishing rules governing the stablecoin arrangement, including defining and ensuring compliance related to the purchasing, redeeming, holding and transferring of stablecoins | Limited and not directed at stablecoin issuers |
| **Issuance** | Coin issuance/creation (minting) and destruction (burning) by entities or software protocols | No requirement |
| **Reserves** | Management of reserve assets | No requirement |
| | Reserve custody/trust service | No requirement |
| **Transfer of coins** | Operating the infrastructure | No requirement |
| | Transaction validation or verification | Exempted, therefore no requirement |
| **Storage and interaction with users** | Private key storage | Licensing required. Captured as keeping a financial product in safe custody that a client purchased under the FAIS Act |
| | Exchange, trading and reselling | Requirements and licensing under the FAIS Act and accountable institutions under the FIC Act |
| | Market making | No requirement |

# 4. Risks and issues identified

The insights gained from engagements with the ZAR stablecoins and the regulatory gap analysis for stablecoin functions and activities highlight substantive gaps that need to be addressed for the comprehensive regulation, supervision and oversight of stablecoin arrangements. Given the limited adoption of ZAR stablecoins, the macroeconomic implications related to widespread stablecoin adoption will be addressed in Phase 2. This phase will also reflect on the risks related to privacy, cybersecurity and investor protection. This section provides an overview of prevailing practices by the stablecoin arrangements and the issues that surface in the absence of regulation, briefly highlights recommendations from SSBs for the identified gaps, and shares commonalities in regulatory responses by jurisdictions for each risk or issue identified.

## 4.1. Definition

There is currently no universal legal or regulatory definition for stablecoins.[27] The term is used by regulatory authorities and SSBs in line with the sector's usage and should not be read to imply that the value of these instruments is stable. There appears to be two approaches to defining stablecoins: (i) define the overall phenomenon; and (ii) define a desired stablecoin, or range of stablecoins, as 'properly designed and regulated' stablecoins. The definition of stablecoins matters because some definitions in law are akin to rules that, by default, disqualify particular design configurations. A narrow definition of the most 'stable and low-risk' stablecoin would automatically exclude algorithmic stablecoins.

There continues to be varying definitions applied to stablecoins globally. For example, some jurisdictions have defined 'in-scope' stablecoins and limited them to those primarily used to facilitate payments or reference reserve coverage (i.e. full or partial reserves). A shared feature of emerging stablecoin regulation is that it addresses stablecoin issuers who have pegged the stablecoin to a single fiat currency which can be used or intended to be used to facilitate payments. [28]

[27] BIS-FSI, 2024a.
[28] BIS-FSI, 2024b.

When defining stablecoins, other constructs such as ‘tokenised deposits’ and ‘deposit tokens’ also need to be considered. The United Kingdom, for example, does not allow stablecoins to attract interest to distinguish between them and bank deposits (BIS-FSI, 2024b).

Likewise, there is currently no definition for stablecoins in South African legislation. However, papers issued by regulators or government departments have provided definitions or descriptions of stablecoins. For example, the FSCA Crypto Assets Market Study [29] describes stablecoins as “[a] type of crypto asset [that] aims to have a stable price value. This objective is normally pursued by the crypto asset being linked to a single asset or a basket of assets, for example, fiat funds, commodities such as gold, or other crypto assets.”

## 4.2. Issuance

As things currently stand in South Africa, anyone can issue a stablecoin, as reflected in the regulatory analysis, without the need to consult with or advise any regulator of their intentions to do so. The absence of restrictions on who can issue stablecoins opens the market to potentially undercapitalised and high-risk issuers. Key issues related to issuance can be categorised as follows:

### a. Who can issue stablecoins in South Africa?

In the absence of legislation specifying which entities or persons may issue stablecoins, there are currently no formal regulatory restrictions regarding who may be a stablecoin issuer. The five ZAR stablecoins discussed in section 2 of this paper are all actioned by non-bank entities and are not regulated for the specific function of stablecoin issuance.

The FSB (2023) recommends that stablecoin issuance be governed and operated by identifiable legal entities and that stablecoin arrangements meet all applicable regulatory requirements prior to commencing operations, including informing the designated authority of its intention to issue a stablecoin before going to market.

Several regulatory regimes currently require a South African presence to be licensed to perform a financial activity or provide a financial product within the country’s

[29] Available at: https://www.fsca.co.za/Documents/Crypto%20Market%20Study.pdf

borders. The IFWG members have generally amended existing frameworks to widen regulatory nets to capture fintech business models. Due consideration should be given to whether international-based companies actively marketing to local consumers should be required to establish a presence in South Africa. The decentralised, cross-border and digital nature of stablecoin arrangements may necessitate a deviation in this baseline requirement and/or require the formulation of new regulatory tools and improved cross-border cooperation among relevant regulatory authorities.

### b. Governance arrangements

Governance and risk management principles from traditional financial services are not always appropriately applied by CASPs and the consequences thereof can be far reaching, as demonstrated in the FTX collapse[30] in 2022. Issues such as executive management's expertise and reputation, risk management practices related to operational risk including cybersecurity, illicit finance and consumer/investor protection, and the segregation of duties can be addressed through mandatory governance protocols and independent oversight. Specific to stablecoin arrangements are policies and procedures for reserve assets and coverage aspects, such as credit, liquidity and concentration risks.

Additionally, ethical guidelines for stablecoin issuers need to be addressed, particularly relating to how they interact with users. Issuers should adhere to an ethical code, ensuring transparency, accountability and user-centric policies.

As reflected in section 2 of this paper, the five ZAR stablecoin arrangements fulfil multiple roles, functions and/or activities, such as being or providing a trading platform, providing wallets, market making and/or arbitrage trading. The fulfilment of multiple roles by a single entity, or a group of closely affiliated entities that are ultimately part of one group structure, could make the stablecoin arrangement systemic as it can exacerbate and transmit risks. In such instances, and aligned to a risk-based approach, entities should be subject to greater prudential requirements (e.g. liquidity, market, group and operational risks) (Bains et al., 2022). Vertical integration may also result in conflicts of interest that cannot be mitigated through the segregation of certain

[30] See for example: https://bankruptcyroundtable.law.harvard.edu/2023/02/28/crypto-bankruptcy-series-ftx-bankruptcy-a-failure-of-centralized-governance-in-the-name-of-decentralized-cryptocurrencies/

activities or disclosures. Consequently, due consideration should be given to prohibiting the fulfilment of certain functions with each other or creating provisions related to independence requirements.[31]

Some jurisdictions have prohibited stablecoin issuers from performing functions other than their primary business as defined in their licence while allowing separate entities within the same group to perform related business activities on the provision that conflicts of interest are sufficiently mitigated or managed (BIS-FSI, 2024b). A mandatory governance structure for stablecoin issuers may include independent conflict resolution mechanisms. Such frameworks could help resolve disputes around redemption rights, reserve audits or governance breaches before resorting to legal action, reducing systemic risk.

## 4.3. Stabilisation mechanism, reserves management and custody

The 2022 turmoil in crypto asset markets revealed discrepancies in redemption rights for users, exposed the ineffectiveness of stabilisation mechanisms (particularly in times of stress), and demonstrated the opaque nature and inconsistency of reserve assets across stablecoin arrangements.[32]

The underlying reference asset and the reserve asset coverage (whether fully or partially backed) are significant determinants of a stablecoin's stability.[33]

### a. Reserve asset composition, denomination, valuation and attestation

The sample of stablecoin arrangements that the CAR WG engaged with are rand-backed and rand-pegged and claimed to hold 100% reserves in cash (ZAR) or other financial instruments with duly licensed and regulated financial institutions. They generally voluntarily engage in some form of independent attestation or the auditing of reserves at varying frequencies (one advised of daily attestation, while annually applied to three, and one had not conducted an audit due to a lack of uptake).

Interest income is generally the primary business case for stablecoin arrangements. Without appropriate guardrails in the form of regulations, supervision or appropriate governance arrangements, stablecoin issuers may be incentivised to invest in high-

[31] IOSCO, 2023.
[32] IMF-FSB, 2023.
[33] Steyn et al., 2023.

risk projects to maximise returns. This form of maturity transformation, typically undertaken by banks, can result in asset-liability mismatches if not appropriately managed or regulated and provide a fertile ground for runs (BIS-FSI, 2024b).

This equally illustrates the need for regulations that require, track and verify that issuers always maintain reserves at least equal to the stablecoins issued, while the market value of the reserves should be at least equal to the nominal value of all outstanding units of the stablecoin. Reserves should be held in cash, cash equivalents or conservative high-quality and highly-liquid assets that face minimal credit and market risk and are unencumbered and easily convertible to fiat (FSB, 2023).

Although requirements for various aspects of reserves vary across jurisdictions, all regulatory authorities are focused on mitigating liquidity risk and preventing runs. Equally, most jurisdictions require that reserve assets be subject to independent attestations and audits but at different frequencies (BIS-FSI, 2024b).

**b. Segregation and custody**

All the stablecoin issuers claim to segregate customer funds from operational funds and do not co-mingle funds, while reserves are custodied by duly licensed and regulated entities (banks and asset managers). Customer funds are not held in a trust account (i.e. there is legal separation where the account is opened by one person for the benefit of another) but in a normal separate bank account and are therefore not afforded continued protection in insolvency proceedings.

Regulatory requirements in the existing financial system are worth considering in addressing stablecoin arrangements. Such requirements include requiring that customer assets be segregated from proprietary assets, held in separate accounts and custodied by authorised banks and non-bank financial institutions, and that assets not be pledged, encumbered or rehypothecated, and when held by overseas-based custodians, they be subjected to certain restrictions.

## 4.4. Prudential risks

Effective stablisation mechanisms require appropriate prudential requirements, such as capital and liquidity requirements, to ensure sufficient liquidity for outflows and that losses can be absorbed (FSB, 2023). Both the creation of assets and the transfer

mechanism should be prudentially overseen to ensure safety, soundness and efficiency (Bains et al., 2022).

The reserve assets backing stablecoin arrangements are not considered customer funds and consequently fall outside of the prevailing regulatory framework(s). This means that stablecoin arrangements in South Africa are not subject to any prudential regulation.

The FSB (2023) recommends that prudential requirements should account for reserves and operational risks, and endeavour to ensure the availability of adequate capital buffers. Capital buffers should be based on the size of the stablecoin arrangement and be proportionate to the risk posed by the arrangement. Regulation should be risk-based and ensure that the entities carrying out multiple activities are subject to greater prudential requirements.

Stablecoin issuers in other jurisdictions are subject to minimum capital requirements commensurate to the stablecoin arrangement's size, exposure, scope of activities and risk profile (BIS-FSI, 2024b). Stablecoin issuers are also required to adhere to liquidity requirements to ensure that they can continue to fulfil ongoing business obligations.

## 4.5. Interconnectedness with the traditional financial sector

The custodian arrangements currently prevalent for asset-backed stablecoins are inextricably linked to the traditional financial sector. Cases where the reserve or backing assets are found to be insufficient, while holders and the wider market have been led to believe that sufficient reserving has been provided for, can lead to a 'run' on the stablecoin. This affects confidence in the wider crypto ecosystem, which can subsequently spill over into the traditional financial sector. A fiat-backed stablecoin, for example, is linked to the traditional financial sector as the stablecoin arrangement would use traditional entities such as banks for purchasing the stablecoin and to safeguard the reserve or backing assets, as is the case with the ZAR stablecoins consulted. The ramification of such interconnectedness was demonstrated with the de-pegging of USDC with the US dollar following the collapse of Silicon Valley Bank, clearly highlighting the interlinkages between stablecoins and the traditional financial sector (FCA, 2023).

## 4.6. Disclosure

Stablecoin arrangements tend to be opaque and circumscriptive in their disclosure of information. Information related to market capitalisation, the number of coins in circulation or even establishing who runs/owns the stablecoin arrangement is not easy to find. A lack of requirements or guidance on what information should be publicly available and easily accessible has, in some part, contributed to the inconsistencies in the types of information disclosed.

Self-publication of reserve assets (without ongoing and independent verification) is inadequate as stablecoin arrangements can make claims without consequence or mislead consumers.

SSBs recommend that stablecoin arrangements provide comprehensive, clear and transparent information related to conflicts of interest and the management thereof, redemption rights, stabilisation mechanisms, operations, governance, risk management frameworks and financial conditions, and that these must be disclosed to users and relevant stakeholders (FSB, 2023 and IOSCO, 2023). The clear disclosure of rights is important to ensure customer protection. For example, with stablecoins that are pegged or tied to commodities, it should be clear to the holder whether they have ownership rights on the underlying commodities or a contractual claim.

Most jurisdictions, in their regulatory responses to stablecoin arrangements, subject stablecoin issuers to disclosure obligations, including risk statements, enabling clients to make informed decisions. Ongoing disclosures to users related to the number of stablecoins in circulation and the value and composition of reserves backing them are also commonplace, with jurisdictions like the United Kingdom and Hong Kong requiring daily updates. The requirement for independent audits of reserve assets and the publication of audit statements are also becoming standard best practice (BIS-FSI, 2024b).

## 4.7. Redemption rights

There is currently no guarantee that stablecoin issuers can redeem users' stablecoins in full and on demand. Depending on the structure and the contractual arrangements, the customers holding stablecoins may or may not have a redemption right against the

issuer or direct claim on the reserve assets. The ZAR stablecoins assert that their stablecoins are redeemable at par with the issuer (except the multi-issuer stablecoin arrangement where redemption rights are independently determined by each issuer). This claim has not been tested or verified for extreme circumstances or stress scenarios. The CAR WG was not able to obtain definitive clarification on whether claims extend to the reserve asset. Issuers who hold reserves in cash in bank accounts believe their stablecoin to be largely insulated from liquidity risk.

Common to most jurisdictions is the requirement to have clear policies related to redemption rights. Authorities that regulate stablecoin issuers generally require that redemption be at par (1:1) for the referenced asset, on demand, and that these requirements be guaranteed by stablecoin issuers. There is divergence across jurisdictions related to redemption fees and whether the claim is against the issuer or the reserve assets. These decisions tend to be a consequence of the jurisdiction's general regulatory posture to crypto assets and the regulatory framework and licensing regime applicable in each jurisdiction (BIS-FSI, 2024b).

The FSB (2023) recommends that there be alignment between a stablecoin's redemption, legal claim and redemption times to those of other (traditional) payment and settlement assets.

## 4.8. Currency substitution

In addition to ZAR stablecoins, South Africans have access to foreign currency-pegged stablecoins. Globally, the most popular fiat-backed stablecoins are pegged to the US dollar, increasing currency substitution risk for emerging markets and developing economies.[34] Currency substitution refers to an instance where residents choose to hold stablecoins instead of the domestic currency. The macro-financial risks presented by the use of foreign currency-pegged stablecoins can increase financial stability risks by destabilising financial flows and straining fiscal resources. This risk is present, particularly for economies with high inflation, an unstable currency, and a lack of access to investment and cost-effective payment options (IMF-FSB, 2023).

Although designed as a payment mechanism in the 'home' jurisdiction, a stablecoin arrangement could perform a different economic function within South Africa (e.g. as

[34] Bains et al., 2022.

an investment, through participation in staking or liquidity pools, or acting as a bridge between the ZAR and the crypto asset ecosystem for arbitrage trading). Equally, a foreign currency-pegged stablecoin could become systemic in South Africa without reaching the systemic thresholds as defined in its 'home' jurisdiction.[35] Due consideration needs to be given to such instances in the development and implementation of regulatory and licensing frameworks that provide regulatory authorities adequate tools and/or enforcement powers to comprehensively regulate a foreign currency-issued/pegged stablecoin.

In addition to monitoring the use of foreign-pegged stablecoins, regulatory authorities would need to strengthen regulatory collaboration and coordination with neighbouring economies and other financial regulators to harmonise regulation and extend information-sharing arrangements to stablecoin arrangements.

# 5. Conclusion

The diagnostic highlights a number of gaps in the current regulatory framework. These gaps include definitions; clarity on who can be a stablecoin issuer; concerns related to currency substitution risks; the regulation and oversight of the stabilisation mechanism; reserve management and custody arrangements; and the absence of prudential requirements, disclosure requirements and redemption rights.

To address these gaps, issues and shortfalls, the CAR WG will undertake further analytical work in Phase 2. Phase 2 intends to unpack the policy and regulatory implications of stablecoin arrangements with a view to developing a comprehensive response to stablecoin arrangements. This will include assessing whether existing frameworks can be extended to stablecoin arrangements and making recommendations for further consideration

Due consideration will be given to the possible trade-off between comprehensive coverage and the time needed for implementation to meet the timelines set for compliance by international SSBs.

[35] FSB, 2024.

# References


Bains, P, Ismail, A, Melo, F, and Sugimoto, N. 2022. 'Regulating the crypto ecosystem: The case of stablecoins and arrangements'. *International Monetary Fund (IMF) Fintech Notes No. 2022/008,* 26 September. https://www.imf.org/en/Publications/fintech-notes/Issues/2022/09/26/Regulating-the-Crypto-Ecosystem-The-Case-of-Stablecoins-and-Arrangements-523724

Bank for International Settlements-Basel Committee on Banking Supervision (BIS-BCBS). 2022. 'Prudential treatment of cryptoasset exposures'. .https://www.bis.org/bcbs/publ/d545.pdf

Bank for International Settlements-Financial Stability Institute (BIS-FSI). 2024a. 'Recommendations for the regulation, supervision and oversight of global stablecoin arrangements – executive summary'. https://www.bis.org/fsi/fsisummaries/global_stablecoins.pdf

Bank for International Settlements-Financial Stability Institute (BIS-FSI). 2024b. 'Stablecoins: regulatory responses to their promise of stability'. *FSI Insights on policy implementation No. 57*, April. https://www.bis.org/fsi/publ/insights57.htm

Coinbase Institute. 2022. 'Stablecoins White Paper'. https://assets.ctfassets.net/c5bd0wqjc7v0/79db1PxjBTv1JbL574fFvA/dc38c8c96dc97c3752fd81a61d0f134a/CBI-StablecoinWhitepaper-July-2022.pdf

Financial Conduct Authority (FCA). 2023. 'Regulating cryptoassets, Phase 1: Stablecoins'. *Discussion Paper DP23/4.* https://www.fca.org.uk/publication/discussion/dp23-4.pdf

Financial Stability Board (FSB). 2022. 'Review of the FSB high-level recommendations of the regulation, supervision and oversight of "global stablecoin" arrangements: Consultative report', 11 October. https://www.fsb.org/2022/10/review-of-the-fsb-high-level-recommendations-of-the-regulation-supervision-and-oversight-of-global-stablecoin-arrangements-consultative-report/

Financial Stability Board (FSB). 2023. 'Final report and high-level recommendations: Regulation, supervision and oversight of "global stablecoin" arrangements', 13 October. https://www.fsb.org/wp-content/uploads/P131020-3.pdf

Financial Stability Board (FSB). 2024. 'Cross-border regulatory and supervisory issues of global stablecoin arrangements in EMDEs', 23 July. https://www.fsb.org/2024/07/cross-border-regulatory-and-supervisory-issues-of-global-stablecoin-arrangements-in-emdes/

Intergovernmental Fintech Working Group (IFWG). 2021. ‘Position paper on crypto assets’.
https://www.ifwg.co.za/Reports/Position%20Paper%20on%20Crypto%20Assets.pdf

International Monetary Fund-Financial Stability Board (IMF-FSB). 2023. ‘IMF-FSB Synthesis Paper: Policies for Crypto-Assets’, 7 September.
https://www.fsb.org/2023/09/imf-fsb-synthesis-paper-policies-for-crypto-assets/

International Organization of Securities Commission (IOSCO). 2023. ‘Policy recommendations for crypto and digital asset markets: Final report’, 16 November.
https://www.iosco.org/library/pubdocs/pdf/IOSCOPD747.pdf

Steyn, H, Campbell, H, Van Deventer, G and Chibi, B. 2023. ‘A primer on stablecoins’. *South African Reserve Bank Topical Briefing Note,* February.
https://www.resbank.co.za/content/dam/sarb/what-we-do/financial-stability/A%20Primer%20on%20Stablecoins.pdf

# Abbreviations

| | |
|---|---|
| AML | anti-money laundering |
| BCBS | Basel Committee for Banking Supervision |
| BIS | Bank for International Settlements |
| CAR WG | Crypto Asset Regulatory Working Group |
| CASP | crypto asset service provider |
| CBDC | central bank digital currency |
| CFT | countering the financing of terrorism |
| CPF | combating proliferation financing |
| CPMI | Committee on Payments and Market Infrastructures |
| DeFi | decentralised finance |
| FAIS Act | Financial Advisory and Intermediary Services Act 37 of 2002 |
| FATF | Financial Action Task Force |
| FCA | Financial Conduct Authority |
| FIC Act | Financial Intelligence Centre Act 38 of 2001 |
| FIC | Financial Intelligence Centre |
| FSB | Financial Stability Board |
| FSCA | Financial Sector Conduct Authority |
| FSI | Financial Stability Institute. |
| FSP | financial services provider |
| IFWG | Intergovernmental Fintech Working Group |
| IOSCO | International Organization of Securities Commission |
| SSB | standard-setting body |
| USD | United States dollar |
| UST | TerraUSD |
| ZAR | South African rand |