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THE FUTURE OF FINANCE

Pathways for Aligning Innovation and Regulation in a DeFi World

OCTOBER 2022



Introduction

Ecosystem and Bitstamp, conducted an invitation-only Executive ThinkTank at the Point Zero Forum in Zurich. A select group of regulators and senior leaders from financial institutions from across the globe came together to share their insights and experiences on Decentralised Finance (DeFi), innovations in the industry, and the outlook for the future.

Here are the 5 key takeaways from the ThinkTank.



#1 Regulators: Perception vs. Reality

Regulators are generally perceived as having a bias against innovations in the Financial Services industry.

The truth is that they want to encourage innovation, and the industry players that want to impact the industry and change the status quo welcome these regulations as guardrails against unscrupulous practices.

If products make the risks known to consumers, regulators are not focused on stifling innovation in the industry. Today's regulators are aware that individuals have widely disparate risk appetites and different product offerings make the market competitive. Forward-looking regulators are also evaluating ways to make the crypto economy a part of a better real economy by introducing relevant frameworks to enable distinguishing high-quality projects from low quality ones.



#2 Institutional Players' Interest in DeFi

A lot of institutional players are interested in DeFi to enable processes and products that run smoothly and to reduce costs, including overheads. DeFi is being evaluated in areas such as lending, borrowing, and insurance. From a data perspective, projects are spanning the ownership, privacy, and transparent sharing of personal information to sharing and storing relevant information for KYC and AML purposes.

For the success of DeFi, a balance between static and rigid rules for industry flexibility is required.

The increase in the number of projects has also resulted in an increase in bad actors – having a structure and an agreement between regulators and industry players can address some of these issues.



#3 Key to Success of DeFi – Evolving Traditional Regulations

Regulations, legal certainty, and consumer protection will play a significant role in making DeFi an integral part of the real economy. Ultimately in a DeFi world, participants and actors are connected by technology. Hence, setting the framework and imposing good practices when building projects will be critical – albeit more difficult.

Regulations need to find the right balance between flexibility and rigidity. This is an ongoing effort of several regulatory bodies and standards setting organisations.

There is a need for a global understanding of an acceptable standard. Civil law is still very country-specific with jurisdiction specific interpretations making cross-border applications and real-life use cases difficult to implement.



#4 The Importance of a Digital Asset Listing Framework



There has been a long debate on who should be the gatekeeper of digital asset listings. The Exchanges are well positioned to do so. They are open to discuss further and agree on potential implementation efforts.

From a regulator's point of view, the liability of projects needs to shift from the consumer to the project and the gatekeeper.

The projects listed on exchanges should be subject to common standards, eliminating low quality projects that can negatively impact investments of non-sophisticated retail users.



#5 The Need for a Simplified Disclosure Document

A disclosure of key project information is widely seen as a positive step in developing further consumer protection. Regulators and key stakeholders within the industry are eager to support broader adoption and find appropriate ways to enable innovation and protect consumers at the same time. A proactive approach to regulation and implementation of relevant frameworks is key for driving mainstream adoption and demonstrating the broader value add of the industry – and more specifically DeFi applications.

Major players are willing to work with regulators to develop a simple disclosure document that describes the project for end-users or investors.

The disclosure would be a legal document unlocking better consumer protection to non-sophisticated retail users aiming to participate in digital asset projects.

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