FINANCIAL INSTITUTIONS AND DECENTRALISED FINANCE: HOW TO REGULATE AN EVOLVING PHENOMENON?

*Luca Lamanna\**

abstract

The vulnerability and inefficiency of decentralised financial infrastructure (DeFi), and therefore the need for intervention by sound financial institutions, has been highlighted by a series of failures in the crypto market. Although there is no peacefully accepted definition of DeFi today, it would consist of an ecosystem of decentralised applications (DApps ) aimed at providing financial services on distributed ledger technologies (DLT), of which blockchain is a *species*. This paper therefore conducts a conceptual and empirical analysis around the ecosystem of decentralised finance that typically does not answer to any intermediary or institution, but is based on public protocols and DApps. This article examines the rise of centralised and decentralised exchanges (CEX and DEX) and the potential risks to investors and the financial system as a whole. Crypto investors who approach DeFi, do so without being able to rely, as in 'TradFi', on a clear representation of the risks involved in certain products, as they lack traditional intermediaries and authoritative financial institutions. The fact that 'play to earn' gaming apps offer rewards in tokens that can be used on their platforms encourages the onboarding of people who are often not fully aware of the dangers they may face. Therefore, this article analyses the regulatory approach of various countries and advocates global regulatory coordination, which would have the merit, among others, of reducing the risk of fraud*.* This paper suggests, therefore, some approaches to regulate decentralised finance without altering its entire architecture, encouraging accountability, compliance and enabling the various players to collaborate with regulators.

\*Phd candidate in Corporate and Financial Law at 'La Sapienza' University of Rome.