

Cryptocurrency Regulation Pros & Cons 2022 PDF



Ilan Gildin of the Israel Securities Authority and Maya Zehavi have it out at the latest Israeli Crypto Conference May 22. “Should The Government Regulate Cryptocurrency?” This was the question that was hotly debated read more to learn about some of the as the many advantages and disadvantages of crypto regulation.

This past May, Israel’s premier team of investors came together to discuss the state of the crypto market in Israel and it’s future plans.

A report on the Israel Crypto Conference May 2022 Panel – Defi: The Financial Backbone of the New Economy



Sheldon Friedman, a Lawyer from Gibraltar, now living in Israel opened the forum. He welcomed the team of highly economically trained in the crypto field and looked forward to a discussion on the Financial economy on Defi and it's future prospects.

Members of the forum included, Ilan Gildin, chief economist and strategic adviser at the Israel Securities Authority. Jonathan Shek of Oz Finance, to share his thoughts on DeFi's future prospects. Maya Zehavi, was there as an investor and investor advisor, And Shauli Rewan had joined them too as an investor and entrepreneur.

Maya Zehavi began by saying that following the Luna crash the last five/ six months more fraudulent and unsustainable crypto protocols have been flushed out of the ecosystem. This is a good thing as the valuations that we have been seeing the past were not something that were reasonable even compared to Israeli cyber industry, and bear markets are an amazing opportunity to go back to building. She explains that the eco

system is going to need a lot more primitives. The Defi space is complicated and has a lot of risks associated with it. She thinks Israel is going to see much more of what they call CDefi to simplify things on one side, and then the other, more institutional and sophisticated investors get into Defi. Retail may go more into the NFT media /gaming side of crypto.

After covid, it was noted the investors wanted increased yield for their investment, because all the central banks in the developed world basically lowered their interest rate in order to retain liquidity in repo markets. Suddenly one saw Defi pools coming in, initially giving you 30-35 % and then came in the new protocols and this is like the web 3 bootstrapping strategy. In crypto and specifically in Defi, yield farming was the way to go. Especially when a protocol was just launched, they needed liquidity, so they would offer new tokens which offered really high yield, some times as much as 100%.

However, there was a high risk with this as sometimes these company would just take off with the money and there would be no returns at all. The stable coin ensured that the liquidity within the Defi have seen the yields come down. Post Terra Luna, about \$45 billion has left the ecosystem both from stable coins and from the liquidity locked on the Blockchain.

How interest rates ensure the stability of the markets

Shauli Rewan who is an investor and entrepreneur responded that interest rates will help to ensure the stability of the market. The interest rates are the main tool for central banks to set the liquidity and the amount of money that's streaming the ecosystem. Whereas once governments preferred providing some good deposit opportunities which came with the risk of losing money deposited, now people prefer investing is something with less risk.

Sheldon Friedman then called upon Ilan Gilden who is a Chief Economist at the Israeli Security Authority to discuss how the

demise of the stable coin has affected him and others. He responded saying that the fall of the stable coin has indeed caused a lack of sleep for some as stable coins we supposed to be the core of the crypto market. In a traditional financial system if one would want to buy an aperture, they would pay, for example \$140, and the pair for the share is basically the dollar. Most people who buy up the shares don't think about the dollar. One can't buy two thirds of a Microsoft chip and buy an aperture. It doesn't work like that. So, when one takes it to the crypto world one won't buy Ethereum with Bitcoin as one has to have some stable coins for each and every transaction. If one does not trust stable coin then the system can't work. Stable coins were supposed to create a ceiling. Following the Luna crash, which Gildon claims was a scam, there was a debugging of the USD, albeit a small one, one did notice a liquidity coming out of the market which may continue. The more stress in the market, the more liquidity comes out, that's the way it works. Gildon surmises that the entire crypto system needs to come to terms with building a more robust and regulated stable coin. Just as before the 19th century people knew flying aeroplanes could be done, they just had not reached there yet, the same is with stable coins. Its part of the evolution, it can be done but we are not there just yet.

Jonathan Shek was then asked if he thought stable coins should be regulated. He responded saying that one needs to have trust in the stable coin. In order to have trust the first thing one needs is transparency. One also needs to know what is being done to back up the coin and how the whole eco system works. So, whether stable coins should be regulated is a yes and no answer. Yes, because it needs to be regulated in order to form some level of trust. On the other hand, in a Defi space there needs to be a certain level of transaction which gives people the Defi freedom they want.

Maya responded by saying she thinks it's a bit misconceiving to be talking about regulating the stable coin. She thinks it is not something new. (Apart from the Israeli Security Authority which is always late) others have been talking about regulating the stable coin for a while now. Even the Trump administration already had the Mnuchin Working Group. She thinks the stable coin should be regulated the question is how and what, and how it would affect non-custodial wallets and liquidity pools. She explained that essentially there are 3 kinds of stable coins. One is Centralized Reserved Backed stable coins which is already regulated with a bank charter under the OCC. You also have a new and recent-backed asset-backed stable coin with Nouriel Roubini that's going to launch in the US. Reserve backed stable coins are money market funds that are not a novel concept, every time someone wants to redeem their stable coin they're going to have to go through AML, KYC.

She goes one to say that most of the Algo stable coins like Luna have broken apart because of the history of finance, this again this is nothing new that crypto has invented. This is what happened with the Hong Kong dollar and it happened in Argentina with the Pesto. It happens often. The question, she says, is what happens later? If one looks at the reserve backed stable coins, she thinks it's inherently important to have a serious conversation with regulators how to build that framework so that it doesn't kill Defi. The other side of the regulations not where the reserves are, people put a stable coin in a liquidity pool. Does every protocol need to be KYC? How do we decipher between the two novelties and keep crypto permissionless? The nuance is where the stable coins really play in to the health of crypto.

The protocol is what keeps the coin regulated

Shuali added that with Defi, when one is looking at the protocol, that's the governance, the authority. If one were writing a protocol, one would add the specific rules of what

one can do with it or not. He thinks that this makes it regulated, because one cannot do anything that is against the protocol. However, we still need to refer to the authorities because you also have the free markets. To take this a step further the concept of Defi and the whole system crypto is to have code. The code is the rule. It is important to trust the code and believe in distributed systems. We trust that the code will act and will give the same conditions to any type of player that's obtaining the rules.

On the other hand, sometimes the markets are open to manipulations. Today we know there are three types of stable coins, some of them are more regulated by the authorities and have specific agreements and got specific license to issue them like the USDC which is a terrific example. On the other hand, when some want to take innovation forward, they will have things like Luna crash happening because people are manipulating the algorithms. Where as some will say Luna may have been a scam, however it is more likely it was manipulation of how the eco system works.



Sheldon Friedman agreed with what he said. He described how he was at a conference in NY when the Luna crash had just happened and the billionaires are just agreeing that these crashes tend to happen. However, it was there that he heard the real answer, and that is, that the markets are manipulated!

Ilan Gildin liked to compare it to a buffet. If the food would not be regulated and two people would die, one would not say, well, it happens, regulations are not needed. On the contrary, one relies on the food regulation and one eats without worrying too much because its regulated. The same needs to be in the crypto world. There needs to be a 'glass ceiling'. The crypto industry can't evolve until it becomes statistically insignificant. The market needs to be regulated in order to protect the investor.

Maya disagreed strongly. She raised 3 points, the first is that she believed that Luna was completely transparent and everyone knew ever thing there was to know, it was not hacked nor manipulated she claims. The second thing is that wall street and the billionaires had a lot of money invested in Luna so they too have a stake in the way it shapes out so. So, if one would want investor protection one should rather go to the investors who fund that particular coin and not the retail. Her third point is that none of the toxic spiral that occurred after the Luna crash, spilled over to any other market. The crypto space was able to sustain itself.

Mr Friedman then called upon Jonathen Shek to give his view on how important Defi is as an economic backbone to the entire ecosystem. Jonathan responded saying they are working on defi free zones around the world. This has been done in the Philippines. It has been legislated there and been approved by the president's office and the congress too. They are looking the create similar projects around the world. This is essentially a tax free or near zero tax living. One can either live in their free zone or you can live outside you get the same

benefits. It has regulatory cover which is t's very important as regulatory cover makes Defi legal in their free zones. It enables growing one's own wealth in their free zone's wealth creation economic activity, as well as investing. And finally, a very important factor in free zones is actually financial privacy banking. Secrecy, so no government has the ability to check up on any one's crypto bank accounts.

Mr Shek believes this to be important from an economical point of view and also philosophical one. This is because there are people who would like economic activity to be in the Defi free zone. He stresses that it is important for a person to have their freedom, to buy what they want, send their money where they want, and since now it is getting a little bit more difficult sending money across borders with the swift system, this would make it easier from a practical point to view too.

He adds that other countries in Central America, Latin America, South America and the South Pacific are doing this too. It is however from the country's government level.

What Israel is planning to do regarding regulating the Crypto space

Illan Gilden was called upon to share with the audience what was in the pipeline in terms of liberalising crypto. Making it more digestible, active and acceptable in Israel. Were there any policies that may be imminent? He answered that in Defi and in Cefi they have features that have economic beneficiaries that traditional markets don't have. They have the engagement of users in the financial operation or company. The same is with Defi, there are some benefits but there are some problems too. In order to invest in something, there has to be a level of trust. In Cefi one would trust the platform. In Defi one would trust the code. The trouble is, he says is that most people don't understand the code. That is

where the regulation comes in. It's the advisors that understand the code that can explain it to the others.

He continues that the Ministry of Finance have been working on putting together a report of their holistic regulation viewpoint, and the Israeli regulations have added their views regarding taxes and securities. It has been looked at in a very methodical way and he hoped that with the political situation as it is in Israel it will not be too long before this report is released. Mr Friedman wanted Ilan to share what its driving sentiment and dynamic are. If it's personal, industry pressure, or public opinion. After discussing the issue with community members, other regulators and searching the field they feel that since there are a significant number of Israelis who are invested in cryptos that is why they would like to see the industry develop in Israel.

Maya wanted to know if it was another report or a legislation. He confirmed that it was a legislation. She added that as an Israeli in the crypto market she feels the market is global. One would not be affected by Israeli regulations. The crypto industry is not waiting for the Israeli government or the Knesset to say we need code auditors, as there already are code auditors, most people do not put money in any protocol without a code auditor. if one were looking to investing in a stable coin one would not necessarily need the Israeli government to say there is a need for a stable coin legislation. She feels that even though the Israelis have been working hard the regulations are in fact going to come from the US and the international zones.

Shauli Rewan added that he thinks there should be different regulations between entrepreneurs who know what they're doing, and taking the risks, and professional investors to the average joe that doesn't exactly know to read code. He feels there needs to be a separation between the two. Defi is a whole new world right now. One takes a liquid asset, locks it

and for that one is creating a new asset and it provides interest. One just makes a simple action but one needs to have a full system to calculate interest rates, how one will be affected by the number of participants in the particle, and the amount of liquidity that's available.

Ilan reiterated that those who invest in crypto that has been regulated may get less of a return but they know that it has the 'okay stamp'. Each person is entitled to choose where they invest their money. The Israeli government would like to offer a regulated path. They want to give some access to entities that are willing to be regulated, and willing to take the cost of being regulated be able to give the investors that sit at home the security that if any time they wake up in the morning the money is still there.

How regulating the Crypto market affected Singapore and other counties too



Since Jonathen Shek is from Singapore, he wanted to share what happened in Singapore. Last year, in 2021, the government wanted to regulate the crypto market. What happened was, that those who wanted to be regulated, stayed

like FTX and Coin Hub, and those who did not want to be regulated, like Binance, just got up and left. So, he is saying that one has to look at the effect that regulating the markets could cause.

One last question for Ilan was, what was his financial economic view of the whole Defi as an economic asset and as an economic paradigm for the economy? He answered saying, he thinks there are economic features that will sustain, that aren't available in the current financial system. Even though there may be some hot air in the sector right now, if the liquidity continues there will be some level for stress testing. Some of the protocol will survive, others may not. From this we will see which of the fundamentals have value.

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