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Neo Banks: Future of Banking Sector and Corporate Law Challenges in the Era of Decentralised Finance

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ABSTRACT

The rapid confluence of financial technology and corporate law has engendered a considerable transformation within the global banking and financial ecosystem. This article seeks to critically examine the evolving interface between corporate legal frameworks and the scaling of fintech entities and digital banks. It delves into the domain of digitalisation of financial services that redefined corporate norms, governance mechanisms and fiduciary obligations, hence contending the adaptability of traditional corporate law. Drawing on contemporary regulatory developments and empirical data from jurisdictions including the United Kingdom, European Union, United Arab Emirates, United States of America and Singapore, the study analyses the legal implications of licensing, capital adequacy, data governance, anti-money laundering compliance and decentralised finance (DeFi). Upon thorough analysis of the domain, the study identifies significant gaps within extant legal frameworks, specifically regarding decentralised autonomous organisations (DAOs) and blockchain-based corporate bodies that function without conventional hierarchal setup. It cautions that lack of well-defined legal personhood and accountability structures poses substantial threats to market viability and investor protection. In response, the paper supports the establishment of adaptive, technology-driven corporate legislation incorporating fintech-specific governance codes, improved transparency mandates and

ethical data oversight. Finally, the study argues that a synchronised, globally coordinated legal architecture, anchored in accountability, inclusivity and innovation, will be imperative for ensuring that corporate law serves not as an impediment but as a catalyst for sustainable and responsible digital transformation in the financial segment.

1. Introduction

In 2024, global fintech revenues surged by 21%, eclipsing the 6% growth rate of incumbent financial entities, whilst EBITDA margins scaled from 12% to 16% as profitability became more widespread.[1] These figures do not only denote expansion, rather signify a tectonic shift in the evolving domain of finance, whereby digital-first banking and decentralised finance (DeFi) are incrementally eroding established paradigms. In such a milieu, corporate law must either evolve or risk obsolescence. Fintech and digital banking no longer occupy the periphery of finance; they now constitute its pulsating core. The global fintech market, currently valued at USD 340.10 billion in 2024, is postulated to reach nearly USD 394.88 billion by 2025 and over USD 1,126.64 billion by 2032 at a compound annual growth rate (CAGR) of 16.2%.[2] Meanwhile, fintech firms continue to deepen inclusion, as observed in a recent survey of 240 fintechs, consumer growth stabilised at 37%, down from 55%, with revenue and profit growth recording a 40% and 39% upsurge respectively.[3] Such dynamisms carry profound implications for the governance, regulation and corporate accountability of digital financial players.

Corporate law frameworks, conceived for industrial-era corporations, are grounded in hierarchies, fiduciary duties and established personhood concepts, which do not work in tandem with contemporary algorithmic protocols or decentralised autonomous organisations. The question therefore arises: how should corporate law adapt to govern enterprises that blur the line between software and corporate actors? Thisintend article addresses three interconnected research questions: 1) How must corporate governance doctrines evolve to remain relevant in fintech entities? 2) What regulatory and compliance tussles ensue at the interface of corporate law and financial regulation? 3) How should consumer and investor protection mechanisms be recalibrated in light of blockchain, smart contracts and non-hierarchical governance? In order to answer these questions, a doctrinal and comparative methodology is employed, drawing on recent regulatory regimes (UK, EU, Singapore, UAE) and evolving jurisprudence. The argument contends that a recalibrated and restructured corporate law, anchored in enhanced transparency,

hybrid liability regimes, adaptive governance and integrated contractualism can steer fintech innovation along accountable and sustainable trajectories. The article proposes policy reforms intended to reconcile legal certainty with technological agility.

2. Evolution of Fintech and Corporate Legal Frameworks

2.1 Fintech Expansion, Innovation and Market Structuring

A chain of structural inflexions emerged with the emergence of fintech, which cannot be depicted as a mere technological disruption. This phenomenon is marked by swell in venture financing and shifts in incumbents' business models. The year 2021 saw a whopping USD 132 billion global venture financing for fintech, creating a watershed moment for sectoral growth and investor confidence.[4] Concurrently, payment and integrated finance accelerated as a strategic arena for competition, prompting banks to offer services through application programming interfaces (APIs) and platform design to preserve relevance. The McKinsey Global Payments Report, 2023 reiterates the importance of open banking, API adoption, cloud infrastructure and flexible architecture to drive product innovation and hasten go-to-market cycles.[5] Technological advancement was tailed by regulatory experiments; for instance, jurisdictions adopted sandbox regimes and layered licensing to align innovation with supervisory objectives, exemplified by Singapore's Payment Services Act of 2019 that constituted a tiered approach to oversight in 2020.[6] Subsequently, Big Tech's penetration into financial services presented systemic and competition concerns, necessitating reassessment of market boundaries and data governance frameworks. The International Monetary Fund's policy analysis highlights this limitation as a potential source of regulatory arbitrage and monopolisation.[7]

2.2 Legal Lag, Fragmentation and Standard-Setting Responses

Empirical investigations have laid down the implications of fintech for financial stability and indicate complex interactions between non-bank finance growth and bank resilience that ensure prudential attention. One study shows how fintech governance characteristics such as board age, size and specialisation are statistically linked to risk and profitability, ultimately affecting systemic stability.[8] The McKinsey Global Payments Report, 2023 discusses technological evolution through cloud computing, open APIs and integrated architecture has enabled rapid innovation and product offerings but has simultaneously segregated governanceresponsibilities across digital platform providers, third-party developers and traditional deposit takers.[5] In response, global standard-setters, such as the Financial Stability Board (FSB) and Committee on Payments and Market Infrastructures (CPMI) have progressive

roadmaps for cross-border payments and called for alignment in regulatory treatment of non-bank providers.[9] In recent times, acceleration in adoption of digital currencies and tokenisation has intensified amongst central banks across the globe, with majority exploring the premise of central bank digital currencies (CBDCs), whilst standard-setters demanding more vigilance over tokenisation.[10] Post-2021, the funding has moderated and the industry has shifted its focus from growth to operational discipline and consolidation.[11] Uniformity in global regulatory frameworks diminishes compliance costs and legal uncertainties across different jurisdictions.[12]

3. Corporate Structure and Governance in Fintech Entities

3.1 Hybrid Governance Models and Legal Personhood

Fintechs operate within unique governance structures, where a cohesion is built between traditional corporate frameworks, and innovative and tech-driven models. This blend allows the fintechs to retain their dynamic and decentralised attribute while upholding the necessary legal and regulatory compliance. For example, blockchain technology and decentralised autonomous organisations (DAOs) are incrementally becoming popular amongst fintech; these solutions facilitate transparent and efficient decision-making processes. Nevertheless, in terms of legal personhood, these processes face challenges, as extant corporate laws lack provisions that can readily be applied to decentralised systems. The flowchart below is developed by the Fintech Global Incorporated (FGI) Group (Figure 3.1), presents the decentralised structure of fintech governance.

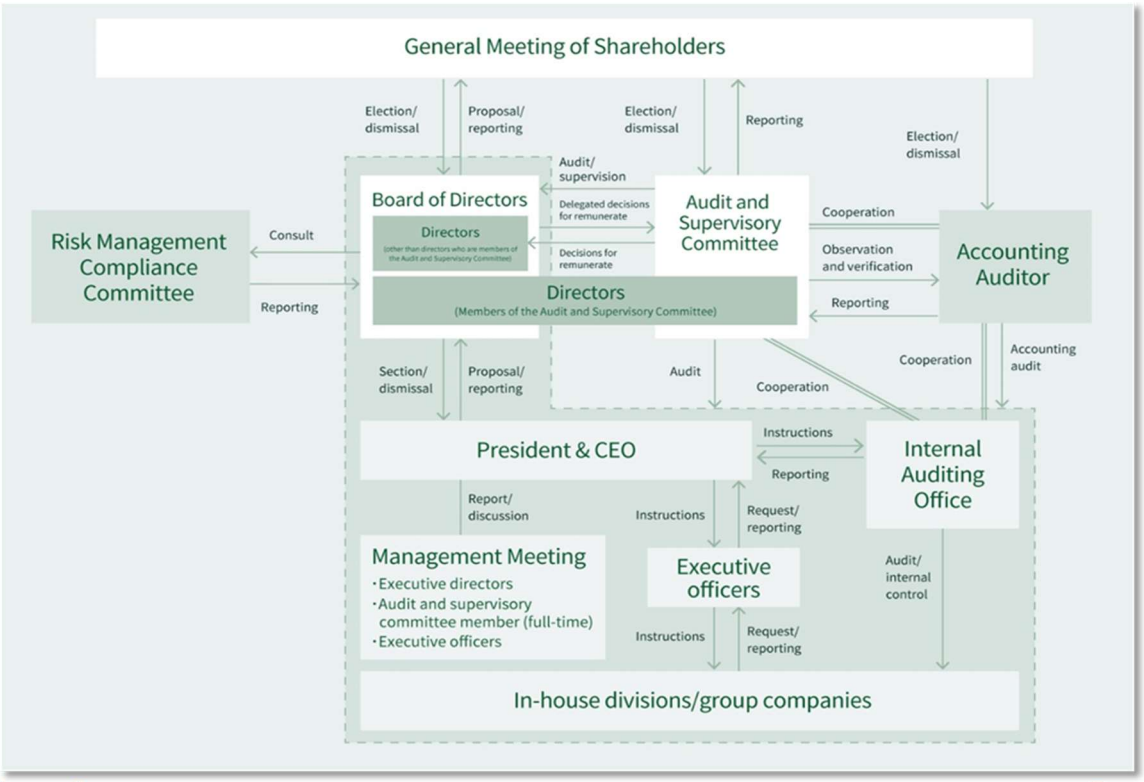

Figure 3.1: Hybrid governance model of fintechs[13]

Within the legal system, the concept of legal personhood determines the rights and responsibilities of an enterprise. In the context of fintech, the application of legal personhood to non-traditional structures such as DAOs raises concerns about liability, accountability and governance. Scholars have discoursed about the extent of legal personhood that these entities must be granted alongside debating the implications of such recognition.[14] Scholars caution against extending such recognition without proper guidelines and safeguards, whilst others cite that granting legal personhood to AI systems or decentralised entities could provide a actionable framework for responsibility and accountability.[15]3.2 Governance Challenges and Regulatory Responses

The innovative framework of fintech governance often lack comprehensive regulatory oversight and compliance. Traditional regulatory frameworks are not well-equipped to address challenges unique to fintech operations such as the use of smart contracts, blockchain technology and decentralised decision-making processes, urging the development of adaptive regulatory approaches that can effectively supervise fintech activities without soiling innovation. Various jurisdictions have started to explore and chalk out regulatory frameworks tailored to the fintech sector; the Reserve Bank of India has issued guidelines for the creation of self-regulatory organisations (SROs) within the fintech industry.[16] These SROs are expected to enforce regulatory standards and harbour transparency that will address the concerns pertaining to customer protection, data privacy, cybersecurity and internal governance. Studies recommend the integration of legal technology and blockchain into corporate governance practices to enhance transparency and operational efficiency. Incorporation of blockchain technology for shareholder voting and decision-making processes could mitigate agency costs and spearhead shareholder involvement, although the efficacy of such incorporation remains to be researched and investigated further.[17]

4. Regulatory and Compliance Challenges

4.1 Licensing, Capital Norms and Perimeter Definition

Regulators encounter substantial challenges regarding setting legal perimeters. The European Crowdfunding Service Providers Regulation (ECSP) mandates platforms to routinely conduct prudential measures such as own funds, insurance policy, or comparable guarantee amounting to EUR 25,000 or more, or an equal amount of the previous year's fixed indirect expenses in certain models.[18] This benchmark confirms fundamental financial robustness, even for non-banking institutions, expediting

investment. Moreover, the definition of "crowdfunding services" is restricted by project owner limits, which not only simplifies and augments scope but also aids in avoiding regulatory ambiguity.[19]4.2 Anti-Money Laundering (AML)/CFT Weaknesses in Virtual Assets Regulation

The Financial Actions Task Force (FATF)'s recent survey reveals that 75% of jurisdictions assessed under mutual and follow-up reports are only partly compliant or non-compliant with the FATF Recommendation 15 (R.15) regarding virtual assets (VAs) and virtual asset service providers (VASPs) as of mid-2023.[20] The survey also mentions that 52 of 151 respondents disclosed they had not conducted any ML/TF risk assessment concerning Vas/VASPs.[20] This portrays a dire situation, where deficits in foundational AML/CFT procedures aggravate exposure to illicit finance risks and dent regulatory integrity. The oversight is further exacerbated by jurisprudential and regulatory fragmentation. Several jurisdictions have either drafted or enacted legal frameworks, yet discrepancy in enforcement and supervision persists. Despite the existence of licensing and registration mandates, implementation remains unbalanced, and risk mitigation tools such as beneficial ownership tracing or the Travel Rule are enforced disproportionately.[20]

4.3 Balance between Innovation and Stability

Regulatory frameworks, such as ECSP, impose fixed cost and licensing burdens, which may deter smaller or nascent firms to align innovation with legislative protocols, resulting in violation of rules and risking consumer safety. Contrariwise, less stringent requirements could lead to financial instability. The lack of widespread and uniform risk assessment coupled with prevailing partial or non-compliance, indicates instability could ensue not from failure but from gradual corrosion of conduct, transparency and accountability.[20] Thus, governing frameworks must maintain a balance between spearheading innovation and safeguarding financial viability, particularly in lax jurisdictions with limited supervisory infrastructure.

5. Decentralised Finance (DeFi) and Legal Personhood

5.1 DeFi Protocols and the Blurring of Legal Boundaries

DeFi protocols function as algorithmic sequences on blockchains that enable lending, trading, staking, liquidity provision and derivatives without traditional intermediaries. Smart contracts are central to execution of these protocols, which operate autonomously without any parent entity playing the central part in decision-making process or bearing liability. Consequently, third parties engaging with DeFi

operate in the absence of a clearly defined contracting counterparty. A study on operational DAOs demonstrates that over 4,000 DAOs have been launched, yet many exhibit weak decentralisation in their governance mechanisms.[21] The foundational corporate laws – the concept of a legal person, a distinct body with capacity to sue, be sued and bear liabilities, differ from DeFi protocols. The conventional concept of corporate personhood rests on a centralised body that enforces rights and obligations, whereas DeFi protocols do not function as subsidiaries but as autonomous systems. An academic analysis illustrates that algorithmic governance in DAOs "fundamentally challenges the traditional concepts of personhood used for corporations and limited liability partnerships (LLPs)."[22] Therefore, the question arises whether to DeFi protocols should be recognised as legal persons/subjects, and if so, then under what circumstances. Scholars recommend an adapted liability regime that imposes default liability to upgrade contracts, protocol maintainers or governance token holders, rather than on the protocol itself.

5.2 Legal Personhood Models and Liability Attribution

COALA's Model Law for DAOs is one of the prominent models that grants legal personality to DAOs that meet specified criteria, such as an open-source code, a unique public address, certain governance transparency and a graphical user interface (GUI).[23,24] This model identifies DAO as a distinct entity, separate from its members; its assets and liabilities are discrete and legal personality allows it to sue and be sued.[24] Another paper suggests an innovative approach "embedded supervision" that integrates supervisory measures within DAO operations, and "polycentric co-regulation " which enables collaborative regulatory feedback from shareholders, fostering both trust and innovative growth.[25] Academic scholars support hybrid structures such as DAOLLPs "Decentralised Autonomous Organisation Limited Liability Partnerships," wherein code-based governance is combined with a legal envelop, offering limited liability and regulatory alignment.[22] When it comes to digital tools, the attribution of liability remains disputed; for instance, if a protocol causes harm such as hacking or flawed logic, on whom should the liability fall, token holders, or maintainers, or on a legal practitioner? Proposals span from full insulation of token holders to "responsibility by design," where compulsions are collated in governance procedures or smart contracts and deviation from protocol rules may result in culpability.

6. Consumer and Investor Protection under Corporate Law

6.1 Emerging Vulnerabilities in the Blockchain Landscape

The rapid scaling of blockchain firms has exposed structural flaw in the system; it failed to provide protection to both consumers and investors. Unlike traditional corporate norms that presume discernible management and transparent disclosure, blockchain organisations, particularly DAOs and DeFi protocols often lack both. As a result, investors participating in such investments encounter unregulated financial exposure, tampered information and a scantiness of compensation mechanisms. A report by OECD presents the poor digital finance literacy even amongst developed nations, with only 34% of OECD populace surpassing the passing target of digital financial literacy score and only 55% having the knowledge of crypto assets not being a legal tender in 2023.[26] In 2022, USA, 46% of crypto asset holders faced unexpected loss due to manipulative promotions, while only 15% reported unexpected profit.[27] These statistics paint the repentant state the fintech industry is undergoing currently in regulatory contexts – attributed to obsolete and stringent policies. Blockchain organisations avert majority of the obligations due to "code-based interactions," which lead to exploitative conducts, where consumers give consent, unaware of the inherent risks. Nonetheless, certain emerging economies such as India (public-private UPI model) and Brazil (regulator-based Pix) are experimenting on a fertile ground with massive digital permeability and are demonstrating how coordinated efforts can drive ingenuities, inclusivity and confidence in financial system.[28]

6.2 Towards a Reformed Regulatory Framework

Scholars suggest embedding corporate law principles into blockchain frameworks. One such proposition is the "Code as Prospectus" model, whereby publicly deployed smart contracts will be subjected to prior audit and disclosure standards that are equivalent to initial offering documents.[22] Algorithmic fiduciaries are also suggested, where directors are obligated to carrysome enforceable accountabilities.[22] the European Commission's 2024 FinTech working paper supports combining algorithmic supervision with regulatory inaccuracy, as per which automated compliance in smart contracts allow regulators to intervene directly when pre-articulated thresholds are violated.[29] Nevertheless, dispute resolution mechanisms using on-chain arbitration panels, smart escrow system or prominent decentralised networks are at nascent stage and once incorporated across networks, would prove essential tools to restore investor confidence.

7. Comparative Legal Insights

7.1 United Kingdom: Expanding Regulatory Mandate

The UK has enacted the Financial Services and Markets Act, 2023 (FSMA 2023) that revokes EU law and grants the Financial Conduct Authority (FCA) extended powers to regulate and authorise activities that previously lay outside its purview.[31] The new regime puts certain fintech businesses performing securities, crypto or payment-aggregator functions under Designated Activities Regime (DAR) even without full authorisation.[31] The FCA has also proposed new rules on third-party resilience, intended to strengthening supervision of critical technology providers within the fintech industry.[32] Simultaneously, the policymakers brought innovative initiatives such as open finance, payment system regulation, algorithmic sector rules to ensure timely intervention in uncertainties.[33] This approach reveals a calculated step, wherein the nation seeks to both widen regulatory intricacies and to foist structural safeguards on embryonic businesses that easily evade through legal loopholes.

7.2 Singapore and UAE: Tailoring Innovation-Friendly Frameworks

Singapore exemplifies a seamless blend of innovation and prudential guardrails. The Monetary Authority of Singapore (MAS) implements a two-tier licensing regime under its Payment Services Act to standardise oversight aligned with scale.[34] MAS also allows experimentation and temporary exemptions through its "regulatory sandbox."[35] Conversely, the United Arab Emirates is still at an emergent stage; the UAE Central Bank has drafted rules for loan-based crowdfunding platforms and digital payments to strike a balance between market advancement and risk alleviation.[36] UAE's emerging landscape signifies scope for regulatory innovation and potential legal uncertainties for fintech businesses operating in the region.

8. Conclusion and Policy Recommendations

The convergence of technology and finance have profoundly altered the corporate legal landscape. Lawmakers are now forced to navigate a delicate balance between innovation and regulation. This analysis elaborates that the revolution led by fintech entities and digital banks has not only promoted rapid financial proliferation but also outpaced the adaptability of traditional corporate governance and legal frameworks. Tussles encompassing licensing, data security, fiduciary obligations, capital adequacy and decentralised finance highlight the urgency for a more synchronised, technology-conscious legal paradigm.

Policy recommendations must hence entail regulatory coherence, accountability and inclusivity at its core. Policymakers must formulate adaptive corporate laws that corroborate fintech-specific governance codes, mandate transparent auditing and reporting mechanisms, ensure data ethics oversight and holistic consumer protection provisions. Additionally, the institution of regulatory sandboxes under corporate law supervision, equivalent to the FCA's and MAS's models, can simulate innovation while maintaining compliance. To address the complexities surrounding decentralised entities such as DAOs, corporate law must introduce conditional personhood to define liability without impeding decentralisation. Finally, as exemplified by jurisdictions such as India and Brazil, collaborative regulation can strengthen sustainable fintech governance by fusing national and international legal efforts reinforced through institutions such as the FSB and IOSCO. Such integration will solidify investor confidence, preserve market integrity and ensure that corporate law act as an enabler rather than a constraint to responsible digital transformation.

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