

Influencing Protocols at Scale

Guest Speaker:



Park Feierbach Protocol Onboarding Lead Figment Hosts:



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Last time on DiffuseTap, Park Feierbach, Protocol Onboarding Lead at Figment, talked to us about the role of validators in a blockchain project, drawing the line between proof of stake and proof of work, and how protocols are influenced by token holders.

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DiffuseTap

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Meet the Speaker



About Diffuse®

Park Feierbach runs a research team at <u>Eigment.io</u>, a stakingas-a-service provider focused on growing Web3 implementations and ecosystems. As a leading provider of blockchain infrastructure, Figment enables protocol staking, which gives users a secure way to earn crypto rewards with their supported proof of stake protocols while simultaneously contributing to the network.

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KENNY ESTES: Park, over to you. Do you want to tell the good folks a little bit about you?

PARK FEIERBACH: Sure. My name is Park. I run a research team at figment IO. We're a validator provider. We provide staking-as-a-service to over 60 protocols. You actually got me right in the middle of our company "All Hands". We're down here in Fort Lauderdale right now getting to know each other, because we're a fully remote team of like almost 300 people.

What my team does in particular is we both allocate information on all the different protocols that we support across all of our internal infrastructure, and we interface with the teams that build protocols themselves. And then, we also act as stewards of the space on behalf of Figment. This team consists of 12 people. We have different kinds of specializations in the different protocols, and we work as a team to evaluate what might be good decisions, or what the trends are on all the protocols that we support. We either participate with them, or comment on it to see where we should go next as a validator.

AYLA KREMB: Beautiful. I usually like to kick off with a "setting the stage" type of question. What is a validator, and how do validators contribute to blockchain projects?

PARK: That's a great question. The idea behind <u>blockchain</u> technology is that you have a ledger that things are being put into. In order to trust the records that are going into that ledger, you need parties who are all agreeing upon what's put into that ledger. <u>Validators</u> are one of those parties.

You have multiple parties who all engage in the same act of signing the transactions that go into blocks. Different protocols have different ways of doing this, and we do it on all of the protocols we support. All of them do it in different ways based on all the different pieces of how it is they want to build their technology stack, the security model that they choose, and how they want to have signing happen based on different components and qualities that they want for their blockchains.

Some blockchains want really high transaction times, so they'll have smaller blocks. Our validators are signing blocks really quickly, and have to have really high uptime requirements. Sometimes, we may have other approaches that are more along the lines of a larger block, which have a lot more transactions in them. They have a slower transaction time, but larger inclusion. That takes a different <u>block signing</u> <u>model</u>.

Without getting too technical with it, the idea behind it is we secure the information that goes into the public ledgers that are supported by blockchains so that it can be used for whatever asset transfer needs that are the fundamental value proposition of the blockchain.

Kenny Estes: Okay, so how does that work from a logistical point of view? Let's say I have some digital assets sitting in Coinbase, or in cold storage. How would I actually interact with you? Do I send those assets to you and you manage them? Logistically, what does that look like?



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PARK: Yeah. One of the great things about <u>Web3</u> is you can either have, like you're saying, like custody, or you can custody your own assets. It's a lot more about the financial freedom that otherwise we haven't had space for in the banking system. You could keep money in your couch, but you can't do too much with money that's in your couch. But in crypto, you have the ability to take your own assets and make decisions about what you want to do with them with more flexibility. You fully own what it is that you represent as an asset of value in a particular chain.

Some assets are stackable, and some are not. That's because there are different security models. And sometimes, people have assets that are part of their blockchain project but are not used for staking. In order to secure the chain, you need to have trust in the validator. And in order to have trust in the validator, you need people who attest to the trustworthiness of a particular validator.

If you have your assets in Coinbase, Coinbase runs their own validators. By holding your assets with Coinbase, you're attesting to their credibility as a validator, and the chain that you are sticking with. However, if you were holding your own assets, or you were doing it through some other custody provider, you would potentially want to have a relationship with us. That would be the same attestation to our credibility. And so, what you'll do with your tokens at that point is you delegate them to a particular validator.

The key phrase there is that you delegate them. You don't send them. To your question about whether you send them to us, the answer is no. You fully custody your own assets. It's the same way with Coinbase cold storage. They custody your assets for you. But with Coinbase, in delegating their tokens to their own validator, they're using the tokens as a voting mechanism to say, I believe this validator will do the work that is necessary to sign blocks of transactions onto the ledger.

And so, you can do this from your own wallet, you can do it through a number of different custody providers. But the base effect is the same, which is that you're pointing to a validator and you're saying, I believe this validator will do a good job. And if you make a bad decision, there will be consequences. For example, a portion of it can be <u>slashed</u>. That can be on the validator side, or that can be on your side.

It's a collective decision. You put yourself in a position to take on the risk of attesting to a particular validator. The reason that your funds might get slashed is because you attested to someone who did not do what they were supposed to do. But fundamentally, the assets are separate. We don't custody assets. We don't plan to custody assets. We just manage them.

AYLA: Interesting. When it comes to spotting a validator that might be a bad actor, is there a specific system or practice?

PARK: I would say that there should be rather there is. A lot of this space right now is very young. And because of that, you have to go off reputation. You have to do your own research. You have to go in there and figure out which validators have the longest block history, which ones have the highest uptime, and so on.



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You can look for validators that have been around for a while and use that as a metric for them being dependable. You can also look at things like how many chains they support. There are a lot of different characteristics like that. But I wouldn't say that we're necessarily at a point where you can definitively say what you want to look for in a good validator. It's more to do with whether they have a good history with the protocol and the protocol's community, and whether they have a good reputation even outside of the protocol.

KENNY: I get that validators, as you explained, are doing ledger things. But what is this whole proof of stake, proof of work thing? Ethereum is obviously trying to move from one to the other. Do both of them have the concept of a validator? How does this all fit together?

PARK: In the <u>proof of work</u> model, what you're doing is you're calculating hashes at a <u>hashrate</u>. It's a little bit different. In a <u>proof of stake</u> model, what you have is a group of computers who are agreeing to the inclusion of transactions. Whereas with proof of work, it's all about calculations. Miners get blocks, and they calculate a consensus result. It's fundamentally more much more math based, which is why sometimes <u>people believe in that model more</u> than they would with the validator model.

It has an approach that is a lot more definitive. Whereas with the proof of stake model, a lot of times people have the sense that inclusion itself is not necessarily enough. Some people don't see it as cryptographically secure. But historically, especially as someone who is representing a proof of stake only validator, that assumption that a lot of people make is simply untrue. Proof of stake is a lot more secure. It's come a very long way.

All the different security models that have been developed over the last 10 plus years have proven to be really well-supported and quite secure, relative to other models. I would say that the main difference is, with proof of stake, it is a lot more ESG compliant, and a lot easier to iterate on. It requires less processing power because it's just about transaction inclusion and agreeing upon the inputs that you're including.

AYLA: One of the things that we should talk about is the fact that individuals are able to influence set protocols. How does that work? We've spoken a lot about DAOs in some of these sessions before, and people like talking about how they can influence things. And how does that work in your universe?

PARK: Generally speaking, I would be very careful using the term influence. That's because a big value proposition of blockchain specifically is that there is no one person who's in control of the system. We talk about influence, but I think we're using the term more to talk about collaboration and coordination, instead of making something do the thing you want it to do.



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Fundamentally, if you're making the system do the thing you want it to do and everyone else isn't agreeing with that, that means the system is broken. The great thing is, if it's a well-built protocol, influencing a protocol is pretty hard to do. It takes a lot of capital to do that. So, when it comes to influencing things or contributing, being a part of the community plays a big role.

The other thing is that most proof of stake networks really depend on their model around token governance. The amount of tokens that you have can be used to vote at a certain rate for different governance decisions about fundamental changes to the protocol. Something that comes up in conversations often is whether one party can have the voting power to completely determine the direction of a protocol. I can't say <u>that level of influence</u> doesn't exist.

There are some people who have a lot of capital and can get things to pass quite easily. You might have 3,000 people who vote, but they have small amounts of capital. If you have one person who has as much as all of the rest of the people, they can turn a vote towards whatever direction they want, either to cut something down or to bring it up. But honestly, I would say that the two components that play a role in influence are collaboration and contribution. And then, you also have token volume as a quality that is used for voting.

KENNY: That makes sense. Let's jump on another question here. You're taking assets, and you're generating returns from them. How do regulators look at what you're up to? Maybe you can also touch on the tax situation, whatever the case may be.

PARK: We do have a pretty well developed tax thesis. I'm not the person to talk about that because I'm not a CPA. I don't really have a head for that. I just dig really deep into the technicals. However, similar to a lot of how people talk about rewards, I think it's a bit of a misnomer. You're not really being necessarily rewarded for your contribution to securing a network. It's more like you're hedging against the inflation of the tokens on a particular chain.

You have a bunch of different dynamics that can play out. As a protocol's tokens inflate in terms of quantity, some protocols will <u>burn tokens</u> in order to keep it underneath a certain threshold to ensure that sense of scarcity. But fundamentally, inflation is more of a way to think about holding a set amount of what it is that you've contributed to blockchain.

When you are attesting to a particular validator, as the blockchain continues to increase in its value and utility, and as you get more and more tokens, you're maintaining your portion of ownership in some ways over what it is that you originally have put into the chain. If you just purchased assets and inflation continues to go up, that doesn't mean that the tokens won't go up in value. But you're not hedging against the inflation of the actual protocol itself.

Staking is the greatest way for you to make sure that you are hedging against the inflation of a protocol itself. You can still fundamentally articulate it as rewards because you're doing work, and you're getting paid for the work you're doing by attesting to a particular validator. Validators are also getting their return



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in the same way. I would say that it's less about rewards and more of a hedge against inflation of a particular protocol's token volume. You can also sell if you want to. That way, you can look at it as rewards.

AYLA: In terms of your customer base who are using your services at the moment, what percentage is trapped by standard funds who are looking for yield revenue? And more generally, what does the customer base look like?

PARK: Our customer base is primarily crypto-focused. Right now, we do have relationships with a number of more traditional finance representatives and people in that field. But we have mostly targeted people who are already pretty deep in the crypto space. We have a bunch of different customer types, and we're focused on anything from retail to custodians. We just recently launched a <u>liquid staking</u> protocol, and we will be contributing to that.

The idea behind that protocol is we will start catering to people who are looking to utilize their assets in more flexible ways beyond just staking. To describe what liquid staking is, in case no one's familiar with it, staking locks up your tokens. It makes them illiquid. Most protocols also have an unbounding period, where you attest your tokens to a particular validator, and you have to wait a certain period of time before you can take those tokens back and unattest or undelegate them.

What that does is it makes sure that if there are market fluctuations, like the ones that we've been seeing recently, you don't have the ability to just pull out arbitrarily. And as a result, all the validators in the set are protected from suddenly not having attestation, in terms of delegations from people. On the other hand, liquid staking allows you to delegate but still use your tokens, or <u>synthetic versions of your tokens</u>, more flexibly. Right now, our primary customers are people who are in the crypto space.

That includes people who have invested in a particular protocol. That includes people who hold a lot of assets themselves, which is rare, but some people do that. But we're mostly working with custodians directly. And then, we have a pretty substantial retail base that is mostly based on our relationships with protocol communities. That's more of a passive customer type. We don't engage directly all too much with retail. That is primarily based on our reputation in governance involvement.



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