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The Unbuilt Sandbox: Regulatory Pathways for Digital Asset Payments in Reform-Stage Economies

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Extended Abstract

In the past decade, the establishment of innovation units and the adoption of RegTech tools have become the most visible signals of a financial regulator's engagement with digital assets. They are useful instruments, and in jurisdictions with stable political environments and depth of human resources they have enabled meaningful piloting and scale-up of new payment infrastructures. This abstract does not contest that contribution. It rather observes, from field experience accumulated through the UNDP SDG Blockchain Accelerator Digital Payment Track in reform-stage economies between September 2025 and February 2026, that innovation units and RegTech are not the most realistic starting point for formalizing the relationship between stablecoin-based payments and supervisory authorities in countries where financial regulators are simultaneously rebuilding traditional financial infrastructure and attempting to restore correspondent banking and card-network access. In those contexts, blockchain-based payment rails are widely perceived as a luxury layer, and the bandwidth required to staff and politically sustain a dedicated innovation unit is rarely available. An innovation unit that has products in the pipeline under one leadership is often viewed as discretionary by the next, and quietly turned down. What emerges in its place is a regulatory gray area that functions, in practice, as an unacknowledged sandbox.

The contribution of this paper is twofold. First, it offers a working definition of the *Strategic Regulatory Gray Area* (SRGA) as it is observed in reform-stage economies, and distinguishes it from regulatory uncertainty, formal sandboxes, no-action letters, and unregulated markets. Second, it proposes a *Gray Area Exit Framework* (GAEF) that allows financial regulators to acknowledge the gray area as a transitional supervisory posture, bound it through a surveillance mechanism tied to public-purpose payment flows, and exit it not through a stand-alone digital-asset act but through targeted annexes to existing financial inclusion, anti-money-laundering, and consumer-protection frameworks — in a sequence designed to be incrementally compatible with FATF Recommendation 15 obligations on virtual assets and virtual asset service providers.

The *Strategic Regulatory Gray Area* is, in its current form, emergent rather than engineered. It is the supervisory posture in which financial regulators neither prohibit nor formally authorize digital-asset payment activity, advise pilot operators to grow and report on request, and preserve political optionality by avoiding a public regulatory commitment while higher-priority reform files occupy the institutional agenda. The SRGA is differentiated from regulatory uncertainty, which is passive and unintentional; from sandboxes, which are bounded and documented; from no-action letters, which are firm-specific and written; and from unregulated markets, which lack supervisory contact altogether. The distinction matters because the gray area, when left unacknowledged, quietly reduces oversight on financial-inclusion metrics, generates single-source data on transaction volumes, and creates conditions in which established operators with closer supervisory relationships are better positioned to navigate it than emerging local fintech actors, with consequences for competition and the development of domestic technical capacity.

The argument draws on field evidence from two reform-stage pilots that together illustrate both the operational reality of the SRGA and the cost of leaving it unaddressed. In Syria, a pilot was designed to pay contractors engaged in debris-removal work under a UNDP project. The previous practice involved a middle contractor distributing US-dollar cash envelopes, with documented risk of informal deductions and delayed disbursement. The pilot used a stablecoin backend with a user-facing application that allowed contractors to view their balance and cash out the same day through money transfer operators. The pilot ran after the comprehensive lifting of US sanctions on Syria in July 2025 and the Central Bank of Syria's reconnection to SWIFT, conditions that in principle opened the formal banking channels necessary for supervised engagement. The pilot still operated under verbal supervisory tolerance with no integrated reporting channel, because no domestic regulatory framework for digital-asset payment activity existed to receive one. Syria's case makes a point the broader literature on post-conflict finance has not yet addressed directly: the SRGA is not primarily a sanctions artefact. It persists after the external constraint lifts, because the domestic regulatory infrastructure has not been built alongside it. The gray area in Syria is now a post-sanctions gray area, and the question of how to exit it is more urgent than it was before.

In Haiti, the pilot was embedded within an existing UNDP multi-fund program and digitized cash disbursements to pregnant women at heightened malaria risk, enabling them to cover transportation and check-up costs to health facilities. The previous arrangement required physically transporting cash from the capital toward Cap-Haïtien through corridors exposed to gang violence. The redesigned scheme used a stablecoin payment rail with cash-out through mobile-money agents and POS operators settled in local currency. In both cases, the pilots represented a sound operational arrangement at small scale, but the absence of a defined exit pathway from the gray area became the binding constraint at the moment scale-up momentum appeared.

No jurisdiction reviewed has articulated an agreed roadmap for exiting the gray area when conditions allow. There is no shared view on what data to collect, which metrics matter, or how to convert verbal supervisory tolerance into structured reporting and into timely amendment of AML and consumer-protection rules to accommodate digital-asset activity. The risk of postponing this conversation is that once a stand-alone digital-asset act is eventually proposed, it requires the simultaneous amendment of multiple pre-existing regulations, which is operationally heavy and politically costly. In lower-capacity jurisdictions, it may also generate an adverse FATF mutual evaluation finding before the framework has had time to stabilize.

The *Gray Area Exit Framework* proposes three components: The first is a *financial innovation surveillance mechanism* operated by a small supervisory cell within the relevant regulatory authority, drawing on existing financial stability monitoring mandates rather than requiring new legislation, and designating specific bounded public-purpose payment flows as authorized pilot gateways for digital assets in coordination with the wider government. Both government-to-person social transfer schemes and multilateral development fund disbursements to identified beneficiary groups qualify, because they are bounded in scale, politically defensible, and carry existing monitoring infrastructure that can be extended to cover digital-asset reporting. In reform-stage economies where technical capacity is limited, international development partners can provide early-phase compliance support within the cell's operational scope. The second component is a *defined exit metric set*, agreed at the start of the pilot rather than at the moment of scale-up, comprising scale thresholds, reporting cadence, AML touchpoints, and consumer-protection triggers. To give this operational meaning: a pilot crosses the exit threshold when cumulative

disbursements exceed a pre-agreed transaction volume within a twelve-month period and at least one structured AML reporting channel to the supervisory authority has been activated, with a documented roadmap toward Travel Rule compliance consistent with FATF Recommendation 15. The third component is an *annex-based legislative pathway* that integrates digital-asset clauses into existing financial-inclusion strategies, AML frameworks, and consumer-protection acts. This pathway is most effective where the supervisory authority holds delegated authority to issue binding prudential guidance under existing financial law, a condition that most FATF member states can meet without parliamentary action and that should be confirmed through legal mapping as the first implementation step.

For financial regulators, the framework offers a way to treat the gray area as a recognized transitional posture rather than a regulatory failure. It is designed to be light on institutional bandwidth, compatible with the political economy of reform-stage economies, and consistent with the priority sequencing that supervisory authorities follow. It also addresses a structural tension the field evidence surfaces directly: stablecoin payment rails in reform-stage economies are often filling a gap created by correspondent banking de-risking, the same gap financial regulators are simultaneously trying to close through traditional reform. The GAEF converts that de facto substitution into a supervised, time-bounded entry point rather than an arrangement that advantages connected operators while remaining invisible to international assessments. The question is not whether reform-stage economies will develop regulatory frameworks for digital asset payments, but whether those frameworks will be built on the evidence that already exists or assembled after the gray area has already shaped the market.