

Herding cats: English law and Decentralised Autonomous Organisations

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Background

On 11 July 2024, the Law Commission published a [scoping paper](#) (the Scoping Paper) on Decentralised Autonomous Organisations (DAOs) setting out preliminary considerations about how these arrangements may be viewed by and treated under English law and identifying main options for legal reforms or innovations to facilitate their uptake.

As identified by the Law Commission in the Scoping Paper, one of the primary difficulties with the analysis of the legal nature and status of a DAO is that, beyond a very high-level description as ‘a new type of online organisation using rules set out in computer code’, DAOs cannot be easily described. The term ‘DAO’ does not refer to a single type of arrangement, but rather to features that may manifest in an infinite universe of arrangements. To further complicate matters, there is no industry or academic-wide consensus on what characteristics an arrangement must have to constitute a DAO.

It is often said that, like nature, law abhors a vacuum. Even these shapeshifting and often elusive arrangements will attract some kind of legal treatment. This is precisely what the Scoping Paper intends to address, by identifying (in a technologically neutral manner) the issues under English law arising from the use of DAOs, focusing on their nature rather than their activities.

What are DAOs?

Organisations

The Scoping Paper provides a useful overview of DAOs as arrangements facilitating the coming together of individuals to realise certain shared goals (commercial or otherwise) and, in many cases, be rewarded for their efforts.

Decentralised and Autonomous

DAOs are conceptually different from traditionally recognised legal entities to the extent that they may try to achieve this goal in a decentralised and autonomous manner. Decentralisation (that is, the dispersal of control and decision-making power) and ‘autonomy’ are key (yet aspirational) traits of a DAO even if certain concepts (like ‘autonomy’) are not themselves entirely clear.

The decentralised and autonomous nature of DAOs is in reality dependent on the nature of the arrangements and may be present in different degrees. The Scoping Paper recognises that these traits may be more aspirational than practically achievable and that different DAOs may exhibit some traits but

not others. More importantly, the Law Commission concludes that adherence to these goals does not make it possible to 'opt out' of national and international laws merely by setting up a novel form of organisation and makes clear that DAOs will necessarily attract some form of legal treatment.

The legal status of a DAO

The Scoping Paper recognises that DAO participants may have not given any thought to their collective legal status or legal liability, or may, in some cases, have deliberately chosen to avoid adopting existing legal forms. However, English law will still seek to retrospectively identify the nature of the arrangement from a legal perspective and determine which laws (and in which jurisdictions) would be relevant in relation to a particular fact-pattern.

Why does it matter?

Given the growing relevance of on-chain activities in the financial system, the pervasiveness of DAOs, the recent recognition in English law of [digital assets as objects of personal property](#) in both case law and through legislative means, characterising a DAO legally is becoming a pressing need.

In particular, the Scoping Report has identified a few specific areas of focus in this regard which raise practical questions that need to be addressed:

- **Liability:** how does liability (criminal, contractual or in tort, etc) apply to a DAO and/or to all or certain participants within it (eg as if they were part of a general partnership, unincorporated association, or within a network of contractual and/or agency relationships)? Will participants in a DAO retain personal liability and if that is the case how can such liability be quantified and allocated among them (eg are certain criteria such as the holding of a majority of tokens or the power to amend the code determinant)?
- **Capacity matters:** who in a DAO can be party to contracts, hold property and be a subject of rights and obligations?
- **Roles and responsibilities:** how should the various participants of the DAO relate towards each other, third parties and the world? Are there any fiduciary duties or tortious duties of care arising under certain circumstances and in certain relationships?
- **Regulation:** if a DAO undertakes an activity that is regulated under the relevant financial services law, would it require authorisation (eg by the Financial Conduct Authority) to carry out such an activity? In that case, the relevant person that should be authorised depends on the legislation, as well as the approach of the relevant regulator. In the UK, it may be the DAO itself that must be authorised to carry on the relevant activity – but how would all the requirements apply in the event of a pure DAO (broadly, a type of DAO most closely aligned with the original philosophical aims of decentralisation and autonomy, which does not make use of traditional legal forms and arrangements) for example? Would approving a DAO be within the regulators' risk appetite even if it were technically possible? How would the relevant authority determine the appropriate jurisdictional nexus in the context of a decentralised DAO?
- **Tax:** given the borderless nature of a DAO, where should tax be payable and by whom?

The Law Commission has concluded that the answers to these questions, and the ease of finding them, will depend on the fact pattern and type of DAO and that 'there are no answers of universal application.'

Jurisdiction and extra-territoriality

A further overarching aspect to consider (which the Law Commission is considering in relation to digital assets [generally](#)) is the international or borderless nature of some DAOs, which may mean that it is challenging to identify to which laws it is subject. DAOs are not traditionally structured or established in a given jurisdiction and may even fail to be tied to, or associated with, any particular place. As with DLT, a DAO could be said to exist 'everywhere and nowhere' - a corollary of its decentralisation - and, equally, it may be difficult to identify or locate its participants.

The Law Commission recognised that although in the realm of private law individuals and entities are generally free to choose which law should govern their relationships with other private parties – eg under a valid contractual choice of law provision within a contract – this is not the case under public law (eg for taxation, regulatory or criminal law purposes), where the choice of law will not affect the regulatory regime that applies to the parties, as parties cannot contract out of mandatory rules.

What are the next steps?

The Law Commission was not asked to make formal recommendations for law reform at this stage and considers that DAO-specific reforms (including a DAO-specific legal entity) would be premature at this stage.

However, the Scoping Paper outlines areas for further work to explore how some of these new types of arrangements could be accommodated under English law, including:

- proceeding with the Law Commission's planned review of trust law and fiduciary duties;
- considering the case for the introduction of a limited liability, not-for-profit association with separate legal personality (similar to the unincorporated non-profit association structure sometimes used by DAOs and other organisations in the United States);
- reviewing company law to enable organisations to leverage DLT and other technology at the governance level of a legal structure;
- reviewing of the anti-money laundering regime to consider whether the same policy objectives can be achieved in a manner more compatible with the use of DLT and other technology;
- considering of the regulatory position of DAOs in the context of collective investment schemes and the regulated activities framework; and
- considering the development of an international tax framework for DAOs.

What should DeFi market participants be doing?

Rather than proposing DAO specific legislation at this stage, it is expected that English law will look through to the substance of DAO arrangements in a technologically neutral manner and apply the relevant legal concepts to regulate the rights and obligations of a DAO and/or its participants.

While market practice and case law develop, some inconsistency and uncertainty are to be expected. Depending on the role of the DAO in a particular project and the ultimate goals that the DAO seeks to pursue, participants in the DeFi ecosystem may wish to consider their position carefully, by seeking advice on potential issues and risks arising out of the use of DAOs.

The Scoping Paper recognises that DAOs that have proactively adopted traditional structures may be able to transact in the 'real world' more easily and to better anticipate and manage their liability and their participants' potential personal exposure to legal liabilities. Although this approach will not be appropriate in every instance, there may be benefits for participants seeking to engage in DAOs in adopting more traditional structures for the time being.