

10 points ...

on Decentralised Autonomous Organisations

This KWM BriefSheet sets out 10 points on the what, how and why of Decentralised Autonomous Organisations (“DAOs”)

- **DAOs are business vehicles ...** DAOs are a re-imagined form of business vehicle, somewhere between a collective investment structure, a partnership, a venture capital fund, and a crowdsourcing platform. They facilitate economic cooperation on a global scale, allowing anyone with an internet connection to become an owner and manager of a business, and share in its risks and rewards.
- **... that operate through the combination of smart contracts ...** Instead of articles of association and shareholders agreements, DAOs operate according to bylaws expressed in a web of interlocking software code. The components of this code are commonly called “smart contracts”. A [smart contract](#) is an agreement that can digitally self-execute some of its terms. Through self-execution, smart contracts can reduce the amount of human intervention that is required for the performance of an agreement.
- **... and blockchain technologies.** A “blockchain” is a transaction record that is held on a distributed ledger. [Blockchain](#) is the technology behind Bitcoin, but blockchain technologies can also be used to hold and execute smart contracts. For example, Ethereum is a decentralised, blockchain-based computing network on which services are paid for using Ether, a cryptocurrency. Like Bitcoin, Ether can be converted into “real” (mundane) currencies.
- **DAOs are not traditional legal entities ...** DAOs are not companies: they have no registered offices, directors or employees, and they are not recognised as their own legal “person”. A DAO is created by smart contracts, deployed on a blockchain that is capable of executing them. From that point on, human involvement is limited, as a DAO’s operation, management and control is automated under the smart contracts, and decisions are made by collective votes.
- **... but they might be partnerships ...** In some jurisdictions, a DAO is effectively a partnership. In others, it is a collective investment. In either case a court may not treat a DAO as having its own, separate, legal identity. That means, despite the smart contracts, courts may impose liability directly on the DAO’s participants or developers. “Companies” originally evolved to provide investors with limited liability. “Autonomy” from central management may come at a high price.
- **... with votes attached to tokens ...** Tokens are acquired by injecting funds into a DAO. These tokens can then be used to vote on proposals for how that DAO should allocate its resources. These proposals are submitted to the DAO by token holders, accompanied by a smart contract that will self-execute if the proposal is accepted by the required number of token holders.
- **... that are financial products.** A DAO token represents an investment in a DAO, and also entitles the token holder to share in the DAO’s profits. In this respect, DAO tokens look a bit like shares or units. However, token holders can control the minutiae of how the DAO operates, with each decision requiring token holder approval, more like a partnership. Securities laws are designed to adapt to innovative investment structures, and in most developed jurisdictions, DAO tokens will trigger securities regulations and laws governing misleading conduct — perhaps with surprising consequences for those involved.
- **Combined with emerging technologies, they have transformative potential.** DAOs purely manage funds, and cannot by themselves create goods or deliver services. To generate revenue, DAOs rely on engaging various service providers to perform tasks. However, the combination and integration of DAOs with artificial intelligence and the Internet of Things may change this. For example, when combined with internet-connected smart locks, a DAO could replace AirBnB by both accepting payment and remotely unlocking an apartment.
- **The first DAO has already died ...** The first DAO, simply called “The DAO”, launched on 30 April 2016. Throughout May over 11,000 investors contributed US\$150 million worth of Ether to The DAO. However, on 17 June 2016 it was announced that a loophole in The DAO’s smart contracts had been fatally exploited, with a hacker (or perhaps hackers) gaining control over one third of The DAO’s total Ether.
- **... but more are on the way.** Despite the failure of The DAO, many more DAOs are on the way. The lure of a transparent, flexible, and totally shareholder-controlled business vehicle with zero overheads is strong. How the law reacts to DAOs, however, remains an open question.

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to help you



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