An interesting and thoughtful whitepaper called “A Legal Framework for Decentralized Autonomous Organizations” was co-authored by a general counsel of one of the major venture investors in the blockchain space suggesting a framework for DAOs under the legal system in the United States. A decentralized autonomous organization, or a “DAO,” is an “organization” encoded as a transparent computer program, controlled by the organization members, and not by a central corporate entity. Currently, many DAOs are not established as legal entities, potentially exposing their members to a number of risks and liabilities.

The whitepaper highlights some of the major legal issues facing DAOs, including difficulty with tax reporting, difficulty in entering contracts, and potential general partner liability for DAO participants. The whitepaper suggests that an ideal
solution will involve new laws that recognize a type of non-entity that could at least have sufficient legal personality to provide some protections for these above-mentioned concerns.

However, there are several hurdles facing a new type of regulation both from the regulators themselves, as well as from many people involved with DAOs who believe that constituting these organizations as a legal entity is antithetical to the philosophy behind a DAO.

In the meantime, prior to the introduction of a new corporate structure, the whitepaper proposes the use of an unincorporated nonprofit association (UNA) as a ‘wrapper’ for a DAO to give which would give such organizations sufficient legal coherence including the ability to pay taxes, make filings, and the like. Unincorporated nonprofit associations are broadly defined and, in many jurisdictions, can consist of just a few people agreeing to work, either orally or with an agreement, on a charitable endeavor together. Many states provide for a simple mechanism for these groups to obtain a tax ID number, and, while it may not be feasible for many DAOs due to their activities or structure, they also are permitted to apply for tax-exempt status under Section 501(c)(3) of the tax code. Much of the question as to the applicability of UNA for a DAO will rest on whether the activity of that DAO is considered “not-for-profit” under something called the Uniform Unincorporated Nonprofit Association Act (UUNAA) that has been adopted by many states. While many DAO generate profits, in general, that is allowed under the UUNAA if the profits are not being distributed to members.

Another existing legal structure suggested by one of the members of Polsinelli’s nonprofit organizations group for use by DAOs is a public benefit limited liability company, which he believes may be a more effective structure for these organizations. While it would mean that the DAO would need to more formally adopt a corporate structure than a UNA requires, it would also create limited liability for its members as a matter of law.

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