

# The COMPUTER & INTERNET *Lawyer*

Volume 37 ▲ Number 5 ▲ MAY 2020

Ronald L. Johnston, Arnold & Porter, LLP, Editor-in-Chief

## Legal Statement on Cryptoassets and Smart Contracts: A Step in the Right Direction

By **Yulia Makarova and Alistair Maughan**

An influential panel of experts in the United Kingdom has published a legal statement on the status of cryptoassets and smart contracts under English law. This development will help to move English law towards a clearer basis of recognition for cryptoassets and smart contracts as an asset class.

Although the recommended approach is not binding in law, this is an important landmark in the process of establishing the principles that cryptoassets, as an asset class, should be recognized as property, and that smart contracts as enforceable under English law.

The UK Jurisdiction Taskforce (“UKJT”) is one of the six taskforces of the LawTech Delivery Panel, an industry-led group that is supporting the digital transformation of the UK legal services sector. The Legal Statement on Cryptoassets and Smart Contracts (the

“Statement”) was published by UKJT after a wide consultation and based on input from some influential sources.

In the Statement, the UKJT found convincing reasons to conclude that cryptoassets are valid as property and that smart contracts could be valid under English law.

### **Cryptoassets: How Will English Law Treat Them?**

Cryptoassets exist in such variety that they are almost impossible to summarize in a single definition. The Statement therefore classifies them as generally having the following distinctive features:

- Intangibility;
- Cryptographic authentication;
- Use of a distributed transaction ledger;
- Decentralization; and
- Rule by consensus.

---

**Yulia Makarova**, of counsel in the London office of Morrison & Foerster LLP, is a member of the firm’s Global Corporate practice. **Alistair Maughan** is co-managing partner of the firm’s London office and a member of the firm’s Technology Transactions Group and the Global Sourcing Group. The authors may be contacted at [ymakarova@mofocom](mailto:ymakarova@mofocom) and [amaughan@mofocom](mailto:amaughan@mofocom), respectively.

# Cryptoassets and Smart Contracts

---

The Statement acknowledges that different cryptoassets may have different characteristics and so that there is no one-size-fits-all solution.

Another key feature is how cryptoassets are transferred. While traditional assets can be sold and passed to the buyer, “on-chain” transactions result in a cryptoasset being recognized as “spent” by the central ledger (and the corresponding key becoming useless) and a new cryptoasset (with a corresponding new key) being generated.

This can pose problems when fraudulent sellers “double spend” their cryptoassets, selling them twice before the blockchain has recognised the first transaction and rendered their private key invalid.

In this case, both new owners validly own the asset, but one asset will be rendered worthless once the blockchain updates.

## Are Cryptoassets Property?

UKJT takes the position that it is important to be able to define cryptoassets as property so that owners can assert their rights to them. The Statement notes that cryptoassets are sufficiently certain, can be controlled exclusively, and are as permanent as other conventional financial assets.

That said, the Statement also raises issues in relation to whether cryptoassets are assignable and stable, the two other qualifying criteria selected for analysis. For instance, because cryptoassets can be transferred “off-chain” external to the central ledger, there will be instances in which multiple parties have access to the private key.

A similar issue is raised as to whether they are sufficiently stable. As it takes time for a consensus on the state of the central ledger to develop, questions can be raised over the validity of some transactions during this period. Despite noting these issues, the Statement concludes that, based on English law principles, cryptoassets possess all the characteristics of property.

There is also the question of whether cryptoassets are simply information – which would disqualify them from being property. The Statement concludes that the answer to this question is clear: the essence of the cryptoasset is not the recorded data itself but the fact that the person in possession of the data can effect and authenticate dealings in the cryptoasset.

Finally, there is a question as to whether cryptoassets fall within the definition set out by the English courts approximately 130 years ago in *Colonial Bank v Whinney*.

In this case, it was held that there are only two types of personal property: things in possession, which is centred on the physical possession of tangible objects; and

things in action, which is generally taken to mean a right of property that can be enforced.

The Statement asserts that cryptoassets cannot be a thing in possession because they are intangible. Similarly, as in a fully decentralized system based on consensus rules, the participants do not undertake any legal obligations to each other, a cryptoasset could not be definitively considered a thing in action.

However, the Statement argues that the case should not be interpreted restrictively but instead, based on the facts of the case, it demonstrates that ability of the common law to stretch traditional definitions to adapt to new business practices. As such, it is argued that while a cryptoasset may not fall within the strict definition of property given, this does not mean it cannot be considered property.

The logical conclusion of cryptoassets being property is that they can be both owned and transferred – and capable of being offered as security.

## Application of English law

Certain attributes of cryptoassets, namely their decentralized nature, mean that an argument can be made that normal jurisdictional rules should not apply. The Statement instead asserts that, as the purpose of the rules is to identify the most appropriate law to govern an issue, each instance should be decided based on the individual facts. Having said this, the Statement admits that it is likely that legislative action will be required to provide much needed clarity on this issue, most likely following international cooperation.

## Smart Contracts: Will English Law Accept Them?

UKJT addressed the question of whether English law will recognize and enforce smart contracts. In short, it concluded: yes – although with the caveat (reflecting the practical reality under English law) that the actual legal treatment will depend upon the parties’ words and conduct.

Smart contracts incorporate agreement, an intention to be legally bound and the passing of consideration; so, as such, smart contracts are capable of being valid under English law. The Statement then focuses on the problem posed by the automaticity of smart contracts, the fact that they can at least partially be performed without the need for human intervention.

Some argue that, because the computer code in smart contracts operates without humans, there is no need for either party to resort to the law for enforcement. This view fails to take into account that while the scope for legal invention may be narrower, there is always a chance that performance can be affected by

external, unpredicted events. In these instances, it is then vital that the meaning of the agreed terms can be determined. To do this, English law's flexibility means that it is simply a case of analyzing the words and conduct of parties, as would be done with any other contract. Even where the code itself contains an ill-defined construction, by being able to look beyond the terms and at all the admissible evidence, a judge can ascertain and determine a meaning.

Another issue noted is whether English law can accommodate the issues raised by anonymous or pseudo-anonymous parties contracting with each other. It is highlighted that not only can English law accommodate, but it does already on a regular basis, for instance with sales at auctions.

Requirements in various statutes for documents to be signed or "in writing" are also noted as potentially

posing an issue. For both sets of requirements, it is argued that the wording and application of the individual body of law will determine the matter, and the law's widespread adoption and acceptance of electronic signatures, including for documents satisfying requirements first drafted several hundred years ago, is used as evidence for why this will be acceptable under English law.

The legal community, regulators worldwide and the business community more broadly continue to consider the legal nature, the possible ways of use and the potential for continued development of the new technology, including cryptoassets and smart contracts. The Statement is a welcome step forward in developing the legal thinking for the new advance technology that will hopefully continue in other professional, expert, and judicial fora.

Copyright © 2020 CCH Incorporated. All Rights Reserved.  
Reprinted from *The Computer & Internet Lawyer*, May 2020, Volume 37, Number 5,  
pages 17–18, with permission from Wolters Kluwer, New York, NY,  
1-800-638-8437, [www.WoltersKluwerLR.com](http://www.WoltersKluwerLR.com)

