Smart Contracts

Tools for transactional lawyers.

BY **SUSAN GEORGE**

You have likely seen "smart contracts" in recent headlines almost as frequently as blockchain—perhaps even in headlines suggesting they may finally rid the world of lawyers. Your clients, of course, are seeing the same headlines and hearing the same buzz. While rumors of our demise may be greatly exaggerated, these technologies promise to dramatically impact our practices as they continue to develop.

A number of prominent national law firms already have well-established blockchain and smart contract practice groups. Short of needing to specialize, lawyers can expect questions from clients about how these technologies can work for their businesses and transactions. Familiarity with the concepts and a basic understanding of what the technologies can do is increasingly necessary. The focus of this discussion is smart contracts.[1]

Generally, lawyers use the term "contract" to describe an agreement covering an entire transaction. A traditional contract defines expected performance and also memorializes intent and how the parties agree to conduct themselves before, during, and after performance. For example, a typical real estate sales contract covers closing, where money and property are exchanged, and also governs pre-closing risk allocations, sets out the parties' warranties and representations, and defines post-closing recourse.

The term "smart contract" has varying definitions, but it generally refers to something different from a traditional, transaction-encompassing contract. Although smart contracts have recently increased in visibility, the concept is not new. The classic example is a vending machine. After money is deposited and a selection is made, delivery of the purchased item is irrevocably triggered.

Once the machine has been built, participants simply use it to conduct the transactions.[2] There is no middleman living in a vending machine. The machine verifies funds and dispenses snacks accordingly. Smart contracts exist in digital code written to execute performance in the same manner as the vending machine. The construct is suited for the "if, then" parts of a transaction—if encoded conditions are met, then the code triggers performance. They can efficiently complement traditional contracts in a transaction.

Smart contracts are more accessible today, in part, because of rapid developments with blockchain technology and the "Internet of Things." Blockchain technology—popularized by association with bitcoin—but highly adaptable for other applications, works by posting transactions in a successive ledger format. This naturally works well for the smart contract construct. Once posted, transactions are considered to be immutable. The actual immutability is a highly technical topic, but the widely accepted perception as such adds to the appeal of blockchain for smart contracts, both from a cybersecurity perspective and as protection against third-party intervention or buyer's remorse.

Ethereum, live since 2015, is perhaps the best-known blockchain platform for smart contracts. OpenLaw is a more recent development, offering a host where "Lawyers can create, deploy, and edit next-generation legal agreements relying on blockchain technology."[3]

The "Internet of Things" expands the universe of automated performance that can be triggered, furthering the appeal of smart contracts. Considering all of the household appliances that can already be controlled with "Hey, Google" or "Alexa," the possibilities for encoded performance seem endless. Smart contracts will not make lawyers obsolete, but we will increasingly need to help clients analyze whether and how a smart contract makes sense in a particular transaction. **TBJ**

Notes

1. An overview of blockchain technology can be found in the April 2017 issue: Ronald L. Chichester, *Wide Open Spaces*, 80 Tex. B. J. 228 (2017).
2. Of course, this assumes that the machine works and performs as intended. A body of law on who bears responsibility—and how much—for when a code malfunctions while executing a smart contract will undoubtedly develop and evolve over time.
3. OpenLaw, https://openlaw.io/ (2017).

SUSAN GEORGE is senior counsel to the real estate and corporate practice group of Andrews Myers in Houston. Her interest in blockchain technology stems from her day-to-day work with contracts as a commercial real estate lawyer.