



Are Smart Contracts Legally Binding In The U.S.?

For many years parties entering an agreement have relied on traditional contracts but with the development of blockchain technology, more people have embraced smart contracts. Smart contracts increase efficiency and reduce costs by eliminating middlemen.

Smart contracts run on public ledgers and can neither be changed nor deleted. This feature addresses trust issues between parties entering an agreement. With smart contracts, parties know the expected outcome. Further, the next terms are only satisfied if certain conditions are met.

More businesses across [various industries are embracing their use](#) in digital transactions their legal status raises concerns. Contract law in different jurisdictions guides traditional contracts. However, some of the differences between traditional and smart contracts pose a challenge to the enforceability of smart contracts.

Defining Smart Contracts

Simple and complex transactions use smart contracts. You have likely interacted with a smart contract when getting a drink or a bag of chips from a vending machine. A smart contract is an agreement that uses coded instructions for execution. It uses 'if/ when - then' commands to execute the agreement.

In the example of the vending machine, when someone inserts money and selects an item, the machine releases the item. The machine only releases the soda once it verifies the money is enough for the selected item. One event triggers the next.

Traditional contracts are agreements between parties with terms and conditions written down. Like traditional contracts, a smart contract is an agreement but it uses software on blockchain networks to store the details of the agreement in data blocks.

In a more complex transaction like NFTs, upon purchase, the artist automatically receives funds. Such transactions are more straightforward than having third parties send royalties. Smart contracts don't need middlemen. When a condition is met, it automatically activates the fulfillment of a defined term.

Are Smart Contracts Legally Enforceable?

In the U.S. smart contracts can be enforced legally but it depends on the nature of the agreement. The smart contract needs to meet the [legal requirements of a contractual agreement](#) to be legally binding.

A legally enforceable contract should contain the following basic elements:

- **Valid offer and acceptance expressing mutual assent:** Both parties must understand and agree to the terms of the agreement
- **Consideration:** The parties exchange something of value
- **Capacity:** Each party must have the legal capability to enter the agreement
- **Legality:** A contract must adhere to the laws of the jurisdiction in which it operates

In a legally enforceable contract, a party may take legal action if the other party is in breach of contract. Although enforceability in the traditional sense may not be an issue in smart contracts because of their automated nature. For example, if a buyer doesn't make the full payment, the system will not release the item. However, smart contracts raise some legal concerns.

Legal Issues Associated With Smart Contracts

The formation and execution of smart contracts present several legal challenges when there's a breach, unlawful enforcement or disagreement between parties. Some of the smart contract features that facilitate efficiency also present challenges within the existing legal frameworks governing contracts.

Here are some of the legal issues that you should consider before using a smart contract in your transactions.

E-signatures Eligibility

The law recognizes that some contracts aren't in written form and allows for electronic signatures under the [E-sign Act](#). Contracts can be legally binding if they meet the criteria for e-signature eligibility in their jurisdiction.

Some smart contracts may not be binding due to this factor. Some jurisdictions don't permit electronic signatures in contracts involving:

- Family law documents
- Wills
- Court orders
- Eviction notices
- Toxic substances transport documents
- Utility services cancellation documents

It's possible to have smart contracts for an array of issues, but confirm the law recognizes e-signatures on the matter.

Contract Modification

The execution of smart contracts is irreversible. Unlike traditional contracts where the parties can modify certain clauses in an agreement, you can't make changes to a smart contract if needed. You would need to cancel the contract and draw up a different one with the desired changes.

Code Interpretation

When issues arise in contracts written in human language due to ambiguous language, courts intervene in the interpretation. For example, words like 'best efforts' or 'market value', in a contract can have different interpretations. Judges can weigh the prevailing circumstances to determine such a disagreement.

Since smart contracts treat the code as the law, ambiguous language can complicate the enforcement. It can be harder to find legal remedies with smart contracts.

Enforcement Issues

Automatic enforcement of smart contracts is a major point of appeal when seeking efficiency but it also presents challenges. Automation complicates the use of legal remedies in unlawful enforcement.

Secondly, their automatic enforcement on a decentralized network makes it difficult to use legal channels to handle contract breaches. The decentralized network used by blockchain

technology introduces jurisdiction issues. It can also be difficult to track down anonymous parties involved in the agreement.

Legal Complexities And The Future of Smart Contracts

Despite their legal complexities, smart contracts have great potential to revolutionize agreements in various industries. States like [Arizona have passed laws](#) that recognize their validity in commerce. More states are discussing legislation around them.

Legalities are getting more attention as more people adopt the use of blockchain technology. The solutions need to address the difference between smart and traditional contracts. Years of handling arising disputes in written contracts have helped fine-tune contract law. Smart contracts will have a similar process.