DE GAULLE
FLEURANCE
& ASSOCIÉS

SOCIÉTÉ D'AVOCATS

Memorandum

Subject : BlockChain Governance – Notes on May 3rd session

DATE: May 6th, 2016

First session : workshops and Q&A

1. **Distinction between governance of private BlockChain and public BlockChain**

Concerning the private BlockChain, the need is to define a set of binding rules in the aim to ensure the continuity of the legal frame, from an existing contract to future ones ("social contracts").
Therefore, since its creation (intern/extern), the private BlockChain has an evolving nature.

Concerning the public BlockChain, the question is about the algorithm governance which is based on reliability and sanctity conditions. It is conditioned by technologic free choices of the first BlockChain developer.
Two series of questions are raised:

- Who can decide of the irreversible nature of the transactions?
- Who can decide of the governance methods?

For the public BlockChain, we cannot talk about an evolving nature: choices are made at the beginning and retroactivity is not conceivable.

The evolution of the private BlockChain is possible because of the small amount of participants (whose votes can be surveyed). For instance, this voting system allows to modify the algorithm (retroactivity and e-voting).

2. **The global function of BlockChain**

The BlockChain can be perceived as a catalogue or a directory helping to gather every relevant data for the worldwide community (nominative data, individuals' professional status…). This data would be indexed in an open and accessible way even covering public domain at the end. Data would be transmitted to a private company and saved on the BlockChain through a rewarding system consisting in monetizing the data exchange.

The complexity would be to respect the legal frame, especially the protection of personal data principle imposed by the CNIL (it would require foreseeing a period of data audit and dissent to control its veracity and to avoid duplication and namesake).

3. **Smart-Contracts: evolution limits and what about their governance?**

They raise the question about the future of legal professions.

Why do we need to regulate them? This question especially concerns over-the-counter transactions (see for instance Ethereum and contracts which do not necessarily concern transactions).

Smart-contract basic model: **adjustable (flexibility)**

Counselling body: need to rationalize the number of smart-contracts due to the overloading risk (standardization, mutualisation, optimization).
The stake of governance is also related with the diminishing financial costs of transactions.

4. **States' reaction in front of digital cash**

3 scenarii in front of this deadly threat for States and their monopolies on currencies:

- A complete banning : this is unlikely because it would constitute a brake on innovation
- A swift adaptation : this is complex due to States' inertia
- A destabilization and a reaction: paradoxical situation where digital cash would be developed within the most indebted States. Plausible explanation: influent groups and lobbies.

Silicon Valley Effect (Business Model) 3 steps (bug phase, disappointment, exponential growth)

Conclusions:

- Due to a legal vacuum, everything needs to be created;
- Certitude that there is a risk of appropriation of BlockChain by some groups of interests;
- Diverse applications : data management, contracts management, governance;
- Private regulation: hierarchy within private BlockChain governance
- The contract as the frame of the private BlockChain: limitations of BlockChain's scope through contracts, organization of votes within a closed community.
- The absence of contract in the public BlockChain? The algorithm at the origin of the BlockChain is based on the notion of contract (Open Source MIT license); it would require to define the conditions of its reutilization because it is the only link with the users. The private BlockChain allows to go further in terms of governance organization.

Second session: workshops and Q&A

1. **A specific organism of BlockChain certification for each sector**

Fundamental distinction between BlockChain's applications: data management and services management

This is a matter of anticipation facing services revitalization: adaptation of the offer to the demand and means easing services and their accessibility.

Public Blockchain: the certification by a specific organism (to be defined) should be organized; this is a matter of regulation, transparency, and last but not least, of trust within the society.

Intermediaries' certification: it concerns the organization, the algorithm's protocol; it consists in providing a mechanism of commitment. With such mechanism, in case of change of algorithm, interested parties would be alerted and could decide to get out of the BlockChain.

Example: concerning financial products, an explanation of its organization must be provided in the contract; in case of uses, they can refer to the contract as well as to ACPR and AMF's control.

Protocol change must be done according with related files.

Third isolated party and playing rules by sector:
- Intermediaries' qualification
- Insurance of their independence

It could be helpful to organize an equal distribution of seats between interested parties and actors within these sectorial entities of surveillance.

2. BlockChain Governance

The BlockChain seems to be an "*Esperanto of transactions*."

Its success will depend on the answers that will be provided in face of the Internet's failure (detachment from the rules) concerning the verification and transaction and data surveillance.

The stake of certification comes from the removal of intermediaries (States, groups, banks).

A new independent authority of surveillance is required to enhance the credibility of public BlockChain governance.

This will require ensuring that data and transactions are impossible to forge.

Bitcoin success:
- Depends on the end of its ties with hard money
- Depends on its acceptation by companies and individuals; which could be the result of a participating or a performance incentive system functioning with Bitcoin, within companies.

"*The BlockChain would be the Internet which would have succeeded*."

3. The question of governance, a forgotten subject because of the current buzz targeting the BlockChain

- Bitcoin foundation: opacity of the organization and information asymmetry.
- Voluntary character: "influencers" try to avoid the major question about governance
- Traceability of the algorithm: who is writing it? Conflict of interests' risks (judge and parties)
- In front of this abnormal opacity: internal control

a) Bitcoin governance: an oligopoly without transparency
b) Governance costs: centralized (intervention of a limited number of people and Bitcoin foundation's autoregulation risk)
c) IT lobby to adapt the outdated systems: need to reform transaction systems;
Possible parallel with the CRM which has a similar organization than the BlockChain concerning asset management;
Lack of traceability of house sales: need of reforms to ensure transparency through the BlockChain, which is not able by current IT systems;
d) Financial stakes withhold risks
e) Going back to fundamental and traditional questions of governance

4. <u>Governance vs/and/or Trust</u>

a) Nature of the trust relationship : face to face or dematerialized
b) To create and to sustain this trust monitoring (such as local banks' offices: to entertain the face to face trust allows to sustain a certain level of trust comparing to intermediaries)
c) The leadership race
Experimenting period points out pitfalls, then consolidation
Necessity to adapt to localities for big players: "glocal" arrangement
"*The BlockChain has a glocal function of regulation*"

- Authorisation
- Certification
- Actors' legitimization
- Collaboration

A parallel has to be established between the World Trade Organization and the crypto-currencies framed by a digital currency (States' membership or not – regulation in small communities) and a currency governance by State.

This has some links with international commerce's bases but on digital principles with a regulatory element (monetary power and crypto-currency).

Conclusions:

Governance and regulation are held hostages by those in favour of the BlockChain model who do not want it to be discussed, or risking to be considered as reactionaries. However, governance raises some questions on playing rules and living together matters.
Therefore, the question of BlockChain governance cannot be avoided: it is indeed a person who is, on himself/herself, at the origin of the writing of the algorithm.