

Legal Service Delivery and Support for the DAO Ecosystem:

A Journey to Relevance

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Abstract

The Distributed Autonomous Organization (DAO) development community seeks to decentralize decision making and reduce the imposition of nonconsensual constraints and the corresponding waste on organizational operations to the greatest extent possible. Deploying blockchain, cryptocurrency, smart contracts and Artificial Intelligence applications, a virtual organization can be created through emerging technologies which functions autonomously in a decentralized manner. A DAO allows its members to democratize decision making through approved rules and policies which are executed automatically consistent with the group's decentralized decisions and amended by the group as necessary.

In contrast, the world's legal systems and the enforcement of their decisions represent a highly centralized approach to enforcing agreements and resolving disputes that arise from them. The supply chains which deliver legal services are antiquated, wasteful and inefficient which imposed excessive costs on clients and the legal professionals who serve them.

This article will make the case for and recommend the operational details of a complete legal ecosystem for the DAO community. Deploying the benefits of decentralized decision making and problem solving, LegalDAOs can be developed to augment distributed ledgers which serve DAOs in lieu of coercive, hierarchical and nonconsensual decision making.

The article will review the legitimate purposes to be served by a centralized legal system and how to achieve equivalent or improved outcomes through decentralized decision making and problem solving. Although some degree of essential centralized legal authority will remain, it can be reduced significantly through the functionality of a well designed and constructed DAO.

We will justify the need for and propose the creation of three LegalDAOs:

1. Legal System Reform DAO - (forming multidisciplinary membership groups representing many different sectors of professional expertise),
2. Resolution of Smart Contract Disputes DAO – (creating a services platform for the DAO community for training and onboarding mediators and arbitrators who understand the issues presented with smart contracts and how best to address them).
3. Jurisdictional Legal Wrapper DAO and legal support for the DAO Ecosystem – (creating a services platform for the DAO community including Crypto attorneys in different jurisdictions who can help set up legal wrappers for DAOs around the world).

Finally, we envision an environment of DAO operations which seeks to comply with the most favorable laws and regulations while serving the members of each DAO through decentralized autonomous decision making to the highest degree practically possible.

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1. Introduction

The impact of centralized systems of governance, products and services might be best illustrated by a recent account of an initiative by Mark Cuban, the billionaire entrepreneur, philanthropist and owner of the NBA Dallas Maverick's professional basketball team.¹ Cuban was approached by a friend and pharmacist who introduced him to the highly costly, yet profitable US system of retail prescription drug sales. Cuban cites the instance of a lifesaving drug to combat leukemia, which is sold under a perversely centralized supply chain model that insures the drug manufacturer will receive over \$9000US for the same prescription which he can sell to consumers for \$47US at Cost Plus Drugs, the company he founded.²

Of course, this example can be duplicated countless times by reference to legal services³, consumer products⁴, currency exchange⁵ and even the administration of justice⁶. Whenever a product or a service depends on multiple players to deliver a desired commodity, a supply chain is required. Supply chain management has become an essential discipline deployed to reduce the waste and delay occasioned when multiple providers are neither integrated nor even concerned about the cost to the consumer of getting the product or service to the purchaser.

¹ Mark Cuban launches affordable online pharmacy, CBS News, January 24, 2022. <https://www.cbsnews.com/video/mark-cuban-launches-affordable-online-pharmacy/> (last accessed July 4, 2022).

² <https://costplusdrugs.com/mission> (last accessed July 4, 2022)

³ Richard G. Stock, Managing the Legal Supply Chain, Legal Business World, January 20, 2020 <https://www.legalbusinessworld.com/post/2020/01/20/managing-the-legal-supply-chain> (last accessed July 4, 2022).

⁴ Knut Alické, Daniel Rexhausen, and Andreas Seyfert, Supply Chain 4.0 in consumer goods, McKinsey & Company, January <https://www.mckinsey.com/industries/consumer-packaged-goods/our-insights/supply-chain-4-0-in-consumer-goods> (last accessed July 4, 2022).

⁵ H. Neil Geisner, Chelliah Sriskandarajah, Yunxia Zhu, A Review of Operational Issues in Managing Physical Currency Supply Chains, Production and Operations Management, Vol. 26, No. 6, June 2017, pp. 976–996. <https://onlinelibrary.wiley.com/doi/10.1111/poms.12593> (last accessed July 4, 2022).

⁶ Aline Pietrix Seepma, Dirk Pieter Van Donk, On publicness theory and its implications for supply chain integration: The case of criminal justice supply chains, Journal of Supply Chain Management 2021, 57(3), 72–103. <https://onlinelibrary.wiley.com/doi/full/10.1111/jscm.12245> (last accessed July 4, 2022).

Centralized control of the supply chain was the only tool available for managing waste and insuring quality. However, with the growth of Blockchain (distributed ledger technology), decentralized control became a means of improving the quality and speed of supply chains while eliminating waste and reducing economic costs.⁷ Treiblmaier, makes the case that only Blockchain applications can satisfactorily address and improve the “triple bottom lines” of the supply chain’s goals for social, economic and environmental sustainability.⁸



Figure 1. Triple bottom line (TBL) goal system.

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The presenting question is, “Under whose control will these complex and multidisciplinary decisions be made?” Blockchain applications may be distributed, but they can also be controlled in a centralized manner (and most are). The terms and conditions of the use of a Blockchain application are generally determined by a small group of owners as applicable to all users in a take it or leave it manner. The “consensus protocol” is the core approval filter through which each blockchain validates and executes transactions. The foundation of

⁷ Treiblmaier, Horst. 2019. "Combining Blockchain Technology and the Physical Internet to Achieve Triple Bottom Line Sustainability: A Comprehensive Research Agenda for Modern Logistics and Supply Chain Management" *Logistics* 3, no. 1: 10. <https://doi.org/10.3390/logistics3010010> (last accessed July 4, 2022).

⁸ Id.

⁹ Id.

decentralized blockchain functionality is technologically driven by a centralized functionality determined by a few.¹⁰

This article proposes that a functional decentralization of blockchain technology can be more fully achieved through Decentralized Autonomous Organizations (DAOs). DAO's operating in legally enforceable and protected fashion are the tools by which the theory of democratized and decentralized operations of blockchain can be realized more completely. However, the ideal of fully democratized technological organizations will be as difficult to achieve as governmental experiments in democracy have proven to be.

2. Current State of (De)Centralized Legal Systems

Legal systems which attempt to eliminate disparities of outcomes (injustice) are highly centralized dispensers of legal rights and remedies.¹¹ The French Revolution and the rise of Civil Law are intrinsically related (code based law).¹² The less discretion at the local level, the greater the control a legal system exerts over the equality of the justice dispensed.

In contrast, the Common Law tradition values equity and individual justice at the expense of consistency of outcomes.¹³ For example, the UK and US common law systems provide great discretion at the local level (courts, legislation, regulation) to individualize outcomes based on

¹⁰ H. Cho, "ASIC-Resistance of Multi-Hash Proof-of-Work Mechanisms for Blockchain Consensus Protocols," in *IEEE Access*, vol. 6, pp. 66210-66222, 2018.

<https://ieeexplore.ieee.org/abstract/document/8516911> (last accessed July 4, 2022).

¹¹ Bertrand Crettez, Bruno Deffains, and Olivier Musy, Legal Centralization: A Tocquevillian View, *The Journal of Legal Studies* Volume 47, Number 2, p. 295 (2018).

<https://www.journals.uchicago.edu/doi/full/10.1086/698860> (last accessed July 4, 2022).

¹² Id.

¹³ Id.

regional, societal and circumstantial factors. What's good for the goose isn't always good for the gander in democratized justice systems.

Historically and politically, centralization vs. democratization of justice have been binary choices. The greater the centralized control of justice (civil, criminal and administrative) the less variability due to the individual circumstances of each situation is possible. The greater the democratization of justice individual circumstances, the less control exists to insure consistent outcomes. Republican forms of government (US) attempt to create hybrid justice systems. However, each form of justice suffers at the hands of the other. The tension is real and persists.

Enter Decentralized Autonomous Organizations (DAOs).

3 Growth of Decentralized Autonomous Organizations (DAOs)

A recent empirical analysis of the origins of DAOs states:

Decentralized autonomous organizations (DAOs) are blockchain-native, decentralized organizations that are collectively owned and managed by their members via smart contracts. DAOs represent a new organizational model that has the potential to fundamentally change how organizations operate. Organizational innovations associated with the rise of DAOs are enabled by a novel technological infrastructure. Blockchain technology serves as the platform on which DAOs are set up. Blockchain technology refers to a distributed and digital ledger that records transactions in a transparent and immutable way. The advent of blockchain technology had a major impact on the business world and is one of the major pillars of the movement towards a decentralized economy and a decentralized financial system, partly driven by new ventures' tokenizations through initial coin offerings (ICOs). [internal cites omitted for clarity]¹⁴

The authors further distinguish DAOs from traditional top-down organizational structures such as corporations:

¹⁴ Bellavitis, Cristiano and Fisch, Christian and Momtaz, Paul P., The Rise of Decentralized Autonomous Organizations (DAOs): A First Empirical Glimpse (April 4, 2022). <https://ssrn.com/abstract=4074833> or <http://dx.doi.org/10.2139/ssrn.4074833> (last accessed July 4, 2022).

DAOs operate through public and distributed decision-making, in which any DAO member can typically put forward proposals for any type of corporate decision and vote on them. This framework facilitates collaboration and community engagement among all members of the DAO that share common goals and ideals.¹⁵

Not all commentators view DAOs in such idyllic terms. Some criticize the reality of DAO's as mere exploitation by the haves of the have nots. Comparing DAO theory to cybernetics ("The Californian Ideology"), one author argues:

Some scholars warn against these unchecked visions of decentralized, autonomous futures arguing that the ideological promises of the uses of decentralized technologies, such as widening political participation, contradict the reality of these tools in practice which inevitably collapse into re-centralisation under the forces of commerce as a powerful driver of technological innovation.¹⁶

Regardless, the relative recency of the advent of DAO's holds promise that forms of self-governance may yet evolve to improve upon the state sponsored versions of democracy with their many unfulfilled promises.

An early exploration of the origin of DAOs attributes Bitcoin founder(s) as the creator of the first DAO.¹⁷ Bitcoin's blockchain application replicates the function of decentralized decision makers by virtue of the miners who manage the value and exchange of cryptocurrency. In contrast, the centralized features of banks maintain all transactional records on a single ledger requiring customers to trust the bank's accounting as accurate. Since Bitcoin's emergence,

¹⁵ Id.

¹⁶ Nabben, Kelsie, Imagining Human-Machine Futures: Blockchain-based 'Decentralized Autonomous Organizations' (October 30, 2021). <https://ssrn.com/abstract=3953623> or <http://dx.doi.org/10.2139/ssrn.3953623> (last accessed July 4, 2022).

¹⁷ Hsieh, YY., Vergne, JP., Anderson, P. *et al.* Bitcoin and the rise of decentralized autonomous organizations. *J Org Design* 7, 14 (2018). <https://doi.org/10.1186/s41469-018-0038-1> (last accessed July 4, 2022).

thousands of DAOs have been created with widely divergent purposes. DAOs have been created as:

- Investment DAOs in which individuals, friends, and colleagues form clubs to invest in web3 startups;
- Collector DAOs which acquire NFTs;
- Social DAOs that convene web3 communities;
- Collective/Cooperative DAOs in which groups of artists and engineers deliver services to other DAOs;
- Charitable DAOs that promote good causes and public interest;
- DAOs to own real property;
- DAOs to cap carbon emissions;
- DAOs to perform drone deliveries;
- DAOs to provide banking or other financial services;
- DAOs to run a business;
- DAOs which partner with other existing businesses;
- DAOs to launch satellites, and;
- DAOs to promote any number of real-world purposes.¹⁸

In other words, if an association/organization of humans exist for any agreed upon goal for profit or non-profit purposes, a DAO can be created to support those needs.

Thus, the tensions between democratic and republican forms of government persist in the self-governing technology functionalities of blockchain.

4. Need for New Legal Applications for the DAO Development Community

In terms of the passage of time, traditional wisdom holds that legal rules and policies follow technology developments by a significant order of magnitude. However, other analysis depicts a more strategic approach adopted by platform technologies to delay governmental

¹⁸ Miles Jennings, David Kerr, A Legal Framework for Decentralized Autonomous Organizations Part II: Entity Selection Framework, a16z Crypto, June 12, 2022 <https://a16zcrypto.com/wp-content/uploads/2022/06/dao-legal-framework-part-2.pdf> (last accessed July 4, 2022).

involvement in order to build influence and data mass.¹⁹ It is not coincidental that Facebook's theme has been "move fast and break things" and Uber's has been "it's better to beg forgiveness than ask permission"²⁰

Whether intention or neglect, legal developments rarely maintain pace with emerging technologies. It is for this reason DAO's currently have amazing opportunities to generate self-governance models which might positively influence the inevitable legal oversight to follow.

DAO evangelists are fond of promoting the independence of their organizations as unbound by legal constraints due to the democratized self-governing nature of this new business structure.

In their most canonical incarnations, DAOs operate without any formal legal recognition, eschewing dependence on governmental authority for their existence, and resisting the rigidity imposed on them by regulations. The result: pseudonymous, distributed, and ad hoc organizational structures.²¹ (footnotes omitted)

This purist view from the perspective of technological possibilities fails to consider an essential need of all organizations: the ability to deal with and enter into enforceable agreements with other entities than the DAO itself. The legal rights, responsibilities, and remedies of associations of individuals are only ignored at their peril. Should the members of a DAO wish to contract with a bank or service provider vendor or enter into a joint enterprise, what are the applicable legal rights applicable to each? Despite the code efficacy of a smart contract, can all legal eventualities be anticipated? Clearly not. Therefore, what rights does the

¹⁹ Mazur J, Serafin M. Stalling the State: How Digital Platforms Contribute to and Profit From Delays in the Enforcement and Adoption of Regulations. *Comparative Political Studies*. June 2022. <https://journals.sagepub.com/doi/full/10.1177/00104140221089651> (last accessed July 4, 2022).

²⁰ Id.

²¹ Brummer, Christopher J. and Seira, Rodrigo, Legal Wrappers and DAOs (May 30, 2022). Available at SSRN: <https://ssrn.com/abstract=4123737> (last accessed July 4, 2022).

DAO have to enforce its expectations and resolve disputes with its members and other entities if not correctly captured in the autonomously executed terms of a smart contract.?

For example, the options for legally recognized organizational models were not prepared for the unique nature of DAOs. Because there was no square hole in which to force this round peg, legal analysts opined that DAO's must be like legal partnerships.²² However, there are many additional organizational structures which could apply to DAO's, including:

US Models

- Unincorporated DAOs
- Corporation
- Limited Liability Company
- DAO LLC
- Nonprofit
- Private Foundations and Public Charities
- Political Nonprofit
- Social Clubs
- Unincorporated Nonprofit Association
- Limited Cooperative Associations

International Models

- Ownerless Foundations
- Guernsey Special Purpose Trust²³

Between the many purposes and the many structural forms, DAO founders would be ill advised to make a decision about the "legal wrapper" that best suits its purposes without experienced legal counsel's input and/or assistance.

The choices and their consequences have led two states in the US (at the time of this writing) to create a unique statutory form of organization for DAO's. These legislative enactments address some of the deficiencies of the current list of options. Specifically, the inferred partnership model that courts might be inclined to adopt would impose "joint and

²² Id.

²³ Id.

several liability” on all the members of the DAO. This is a Draconian result that would allow a successful legal claim (from a member, customer, vendor, lawyer or other entity) to be owed equally by all the members. This outcome would permit a successful claimant to collect the value of the recovery from any one or all of the members up to the total sum of the claim.

Wyoming²⁴ and Tennessee²⁵ enacted remedial statutes in 2021 and 2022 to address this concern. Both statutes require DOA formation documents, charters, articles of incorporation, operational agreements and name to clearly reflect the uniqueness of the DAO’s nature. They each provide limited liability protections similar to those afforded LLC’s under their state’s laws.

Whether DAO’s can create a completely self-governed set of enforceable policies and procedures akin to these statutes and continue to operate outside a jurisdictional governance model remains to be seen. The concept of enforcement implies resort to a dispute resolution system which is jurisdictionally binding on the entity, its members and others who might pursue legal claims. Unless every agreement made by the DAO with others can reduced to an automated smart contract with payment provisions in the event of breach, and dispute resolution mechanisms which automatically operate, this outcome seems impractical and unlikely.

Therefore, much remains to be done by the DAO community to achieve these additional legal protections. The following are suggested DAO organizations created to explore these potentials.

a. Legal System Reform DAO

²⁴ Wy. Stat. § 17-31-104 (a).

²⁵ TN Code Ann. § 48-250-10

The DAO ecosystem is comprised of many different legal, professional and economic interests.

The entities and individuals that could be impacted by the growth of DAO development include at least the following:

- Founders
- Voting Members
- Non-voting Associates
- Engineers
- Developers
- Vendors
- Customers
- Legal Advisors
- Legal Jurisdictions (federal, state and local)
 - Taxing authorities
 - Investment regulators
 - Policy makers
 - Courts
 - Enforcement authorities
- Shareholders
- Media outlets
- Academic Institutions
- Standard Setting Bodies (ISO, IEEE, etc.)
- Etc., etc., etc.

A more diverse and potentially conflicted set of interests cannot be imagined.

This writer's experience in implementing new technology with a large stakeholder group was ultimately successful after a botched initial effort.²⁶ A subsequent project proceeded far more effectively and efficiently because of the deliberate attention paid and the engagement of the many stakeholders impacted by the technology.²⁷ This process does not require active approval involvement by all stakeholders. However, obtaining input, adjusting the project plan and keeping stakeholders informed is critical to success bringing technology to fruition by users, owners and those impacted by it.

DAOs are an organizational tool by which these obstacles can be addressed. A DAO created to categorize, analyze and recommend legal reforms could govern the impact of DAO development in the most inclusive and democratized manner. A legal reform DAO could be established to provide voting membership to the key decisionmakers and informational/input to those impacted. Legal reform DAOs could be created for local, state, and national legal reform initiatives to involve and inform policymakers on the key attributes of DAO regulation and enforcement. DAOs can provide a pre-regulation platform by which issues can be addressed and interests protected to provide recommended language and content for adoption by legislative bodies. Facilitated legislative creation is most likely to achieve adoption and implementation.

²⁶ David Alan Larson, Designing and Implementing a State Court ODR System: From Disappointment to Celebration, 2019 J. Disp. Resol. 77 (2019)

²⁷ Tennessee Court Pilots New ODR Platform to Mediate Medical Debt Disputes, ABA Online Journal, June 1, 2022 <https://www.abajournal.com/magazine/article/tennessee-court-pilots-new-odr-platform-to-mediate-medical-debt-disputes> (last accessed July 4, 2022).

Brummer and Seira categorize similar organizations as Lobby DAOs.²⁸ However DAOs which engage more stakeholders than just the advocates for a position could have more influence through the processes of facilitated decision making.

b. Dispute Resolution DAOs

A major concern for the growth of the DAO ecosystem pertains to the mechanisms by which disputes are addressed arising from the functions of the DAO and the smart contracts which govern agreements reached by the DAO.²⁹ Although the self-governing nature of DAO's and the automated functions of smart contracts will lessen the occurrence of disputes, it is unreasonable to suggest all disputes will be eliminated exclusively through technology.³⁰ In view of the economic value of assets maintained and managed by many DAOs, unresolved disputes could be hugely consequential.

Even if the DAO's self-governance models maintain robust dispute resolution mechanisms for members and associates, the same cannot be said for those outside the DAO with whom the organization reaches agreements for services and products. Reliance on traditional models of dispute resolution may not fully meet the needs of the DAO community and those with whom it may work. The very thought of bringing the types of disputes which

²⁸ Brummer, Seira, p. 28

²⁹ Keung Tueck Minn, Towards Enhanced Oversight of "Self-Governing" Decentralized Autonomous Organizations: Case Study of the DAO and Its Shortcomings, 9 NYU J. Intell. Prop. & Ent. L. 139 (2019-2020) <https://heinonline.org/HOL/LandingPage?handle=hein.journals/nyuinpe9&div=10&id=&page=> (last accessed July 4, 2022).

³⁰ Sims, Alexandra, Decentralised Autonomous Organisations: Governance, Dispute Resolution and Regulation (May 31, 2021). Available at SSRN: <https://ssrn.com/abstract=3971228> (last accessed July 4, 2022).

involve the technologies of smart contracts, decentralized organizations, blockchain, NFTs and cryptocurrency to a state court judge and/or jury is soul shatteringly frightening.

The traditional dispute resolution options of courts, state sponsored specialty tribunals, self-regulating industry schemes, mediation, arbitration, and online dispute resolution processes all leave much to be desired when confronted with the complexity of DAO formation, operation and functionality.³¹ The knowledge and wisdom needed to meaningfully address the types of disputes DAOs encounter requires extraordinary expertise and experience possessed by an extraordinarily small group of processes and people.³²

Sims further reports on the growth of Decentralized Dispute Resolution Services (DDRS) platforms for DAOs. As with all great ideas, improvements over time lead to far better solutions than originally envisioned. As a result, DDRSs are coming online with sophisticated and variable options for disputants depending on the nature of the dispute. To date there are no autonomous dispute resolution systems available. They all involve some level of human engagement or judgment. Functioning like DAOs, some DDRSs provide voting and staking privileges for decision makers. Typically decentralized and blockchain based, the primary distinctives between the current processes available relates to the degree to which outcomes are determined by reference to the law of jurisdictional systems and enforceable in state sponsored adjudication entities (i.e. courts). Many DDRSs eschew government involvement.³³

³¹ Id.

³² Id. at pp. 157-170

³³ Id.

As these DDRS systems continue to mature, utilization and incorporation of their services will undoubtedly become more central to the smart contracts which govern DAOs and others doing business with them.

c. Legal Wrappers and Legal Support DAO for DAOs

The tension between total technological democratization and any degree of centralized decision making inherent in the DAO ecosystem also applies to the application of law and legal systems to their functionality. Purists would have their DAO exist independently of state oversight or involvement and rely on completely autonomous self-governing mechanisms. That day may come, but has yet to arrive. Like the promise of General Artificial Intelligence, until machines can replicate in all ways the capacities of the human brain, we will have to rely on Narrow Artificial Intelligence as the primary advanced technology tool to process data and recommend decisions. Humans are still needed to exercise judgment.

In the meantime, the practicalities of organizational rights, responsibilities and liabilities to others remains a reality to be managed for the benefit of the DAO's purposes. As a natural result, ignoring the impact of legal systems will only complicate and expose the DAO to greater risk and responsibility than the organizers, founders, members and associates ever envisioned.

Therefore, strategic thought and counsel need to go into choosing a legal framework within which the DAO will best thrive and be least encumbered.

In terms of organizational identity, many forms of legal entities exist.³⁴ In the US currently, the states of Wyoming and Tennessee have enacted enabling legislation to protect DAO's from the unintended consequences of joint and several liability imposed by inference on

³⁴ See above at p. 8

general partnerships.³⁵ Additionally, Delaware has recognized the legitimacy of any “records administered to be stored on one or more distributed electronic networks or databases”³⁶ In addition, in 2018 Malta created a framework for decentralized entities governed by AI.³⁷ However, it has no applicability to DAO’s governed by people.

The legislation in Wyoming and Tennessee are the best current examples of legal wrappers for DAOs to date that recognize and protect much of their unique nature while limiting liabilities.

In addition, DAOs could be formed to feature global resources available to organizers and founders of these unique forms of organizational entities to provide the best legal counsel for their specific needs. Using a reputational DAO format³⁸ these listed legal resources (lawyers, law firms, alternative legal service providers and consultants) could create a trusted marketplace for the availability of legal advice and counsel on the myriad of issues confronting DAOs.

5. Conclusion

Since their origin, DAOs have demonstrated potentially transformational impact on the interests of the economy, law, organizational governance and individual rights. Much remains to be developed in order to increase the acceptance and implementation of DAOs in order to realize the potential for positive change they can bring. This paper merely seeks to summarize

³⁵ See fn. 24 and 25 above.

³⁶ 8 DE Code § 224 (2017)

³⁷ Innovative Technology Arrangements and Services Act 2018 (Malta)

³⁸ Kaal, Wulf A., REPUTATION AS CAPITAL – How Decentralized Autonomous Organizations Address Shortcomings in the Venture Capital Market (November 13, 2021). Available at SSRN: <https://ssrn.com/abstract=3962614> (last accessed July 4, 2022)

how they have come to be and highlight the potential challenges and opportunities DAOs must confront to improve the legal frameworks within which they can optimally function.

This writer commits to be on the journey along with the development of DAOs to help improve their chances of success as law strives to catch up with technology.

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