THE EXISTENCE AND ENFORCEABILITY OF SMART CONTRACTS UNDER SERBIAN LAW

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Smart Contracts

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Defined by the Serbian Law on Digital Assets, Article 2 Paragraph 39, a smart agreement or contract is a computer program or protocol, based on technology of distributed database or similar technologies, which in whole or in part, automatically executes, controls or documents legally relevant events or actions in accordance with an already signed agreement, whereas the specified agreement can be concluded by electronic means via that program or protocol.

Defined more simply, they are "self-executing electronic instructions drafted in computer code" operating on the basis of the principle "If A, then B" and stored on a blockchain platform.

A typical and well-known example are vending machines, where the machine releases the chosen good so the buyer can pick it up when he or she enters a form of payment into the machine. Other examples include the Kickstarter app, or the functioning of insurances, or banks.

Given that smart agreements are self-enforceable, it is hard to imagine situations where a dispute could be raised from the non-execution of the agreement, and therefore situations where the intervention of a judicial authorities would be needed.

However, the automaticity of the execution of smart contracts doesn't mean they can't be challenged and disputed. For example, most blockchain platforms don't verify the capacity of the user engaging in the transaction. This means that theoretically, a child could create an account and be a user. This, however, is a defect of consent in light of the Serbian law (Article 56 of the Law of Contract and Torts) and is a ground on the basis of which the transaction could be attacked a posteriori.

But who would be legitimate to decide in such a situation? The logical and natural answer would probably be a court - or a judge, but do smart agreements have a legal nature and do they produce legal consequences for judicial bodies to have legitimacy to decide in such situations?

In order to answer that question, we must first determine the answer to another - whether the smart contracts fulfill requirements of the Serbian law in respect of the existence of contracts... There is no unanimity among law professors and law experts when it comes to the answer to the latter. Some academics observe smart contracts are means of performing obligations deriving from other agreements , rather than real legal agreements. Some, however, recognize that despite their untypical form, mandatory characteristics and elements of agreements are flexible enough to encompass new forms of agreements like the smart contract, which could replace typical written agreements in the near future as some academics observe . The self-enforceability of smart agreements is undoubtedly an attractive benefit.

We, here, share the standpoint that smart agreements are indeed contracts from the point of Serbian law, with certain minor reservations, because the basic agreement elements are met, and that they are consequently enforceable in Serbia in the majority of cases.

Firstly, acceptance of both parties is manifested respectively in the act of creation of the smart agreement which includes the creation of the terms of the agreement in the form of a digital code and its storage in a distributed database, and in the act of accepting the offered terms of agreement. It could be disputed however that this condition is met regarding the party which will automatically execute the contract via blockchain, because her or his will is not explicitly manifested during the execution phase.


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"At its core, law is information based and we are in the middle of an information revolution."
(Richard Susskind)

The previously mentioned consent refers to two mandatory elements which are also met in the smart contract: the price (counterpart) and the object of the contract. This results from the fact that in every smart contract, there is reciprocity of giving, so that each party is conditioned by giving or doing by entering into a smart contract. Second, the smart contract like any other contract creates obligations, even in the case where for some reason the execution wouldn`t be possible (notably if a technical problem happens). For example, if a cash machine stops dispensing money, the bank would still be obligated to give the cash to the client who made the demand.

Besides the above-mentioned elements, there are no other specifical requirements for contracts which could create an obstacle for the smart agreement to be recognized as one. Indeed, in contract law the principle is freedom of form (Article 67). However, for a limited number of contracts, there are specifical form requirements, notably the notarization before a notary public, like it is the case for real estate sales. In addition, the smart contract seems inadequate for some types of legal relations, for example in security law, when the intervention of a third party could be needed.

Now that we concluded that the smart contract represents a contract in accordance with the Serbian Law, the next question is how to prove its existence to courts or other legal bodies in case of dispute situation. We can here distinguish two situations. First, the one where a traditional agreement coexists with the smart agreement, notably for legal certainty reasons, or situations where we are in presence of a hybrid agreement. In these situations, the Court intervention would be simplified because the Court will look at the traditional written agreement for reference. Making a traditional agreement to go along with the smart agreement is also a solution we recommend to our client in order to facilitate the resolution of an eventual dispute. This is because, in the second situation where a smart agreement would stand alone (in the situation of a pure smart contract), judges would need help from an expert who could "translate" the solidity language to them to the human language. Considering that court practice isn't habituated to these unconventional agreements, some difficulties in handling them could happen. As an author correctly observed, "classic law falls short to the virtual environment."

But the question remains whether Serbian courts will have jurisdiction if the legal relation bears an international element. This question could easily rise as the practice of smart contract is mostly developed in foreign countries. To know which law is applicable and which country's court has jurisdiction, we must refer to the smart agreement itself, because the rule is party autonomy, embodying the principle of contractual freedom. However, if the applicable law and jurisdiction are not determined, private international law rules will intervene to regulate the situation. This should often be the case in the matter of smart contracts, given that it is difficult to incorporate a choice of law and court into the very simple equation of "If A, then B".

Every country has its own private international law rules, however, international conventions provide us with universal solutions to conflicts of laws and conflicts of jurisdictions. One of them is the Rome I Regulation of the EU which resolves conflicts of laws and covers obligations in civil and commercial matters. It, too, provides the freedom of choice principle in contractual matters (Article 3), but it apprehends the issue largely as no express choice of law has to be made: it can be clearly demonstrated by the terms of the contract or by the circumstances of the case.

Rome I also regulates situations where no choice of law has been made in its article 4 introducing a list of criteria for different types of contracts and dedicates articles to specific contracts like insurance contracts. It also regulates topics like incapacity or formal validity.

The precondition to the application of all these rules would be of course the standpoint that the smart agreement in question is in fact legally binding and as such enters into the material scope of the Regulation, as well as into the territorial one. The Brussel I bis Regulation, its counterpart for jurisdiction, provides similar solutions.

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Just as each country has its own laws under international law, so the Serbian law, relying on international conventions and agreements, has its own rules. However, a smart agreement is not a type of contract, determined by the subject, but a form of concluding a contract. In this regard, the determination of the applicable law when one party is Serbian and the other is a foreign non-EU citizen (as for EU citizens the previously mentioned Regulations will apply) will depend on the subject of the agreement, i.e., whether, for example, it is a contract of carriage, insurance, sale, etc. For example, in the case of an insurance contract, the seat of the insurer at the time of receipt of the bid will be relevant for determining the applicable law.

While open questions and ambiguities remain, smart contracts certainly represent the future of contract law. At the moment, they are limited to simple, mostly financial relations, but a better legislative regulation as well as the increase of court practice when it comes to handling these contracts, will certainly increase their application. It is the principle of self-enforceability of smart contracts which indisputably is its main feature that makes us believe that smart contracts will become in the future one of the main ways of contracting.

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