

Bankrupt Me If You Can

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ABSTRACT

This Article explores the growing tension between the blockchain and cryptocurrency industries and U.S. bankruptcy law, specifically addressing the challenges faced by entities that, by their nature, do not fit neatly into the existing framework of the U.S. Bankruptcy Code, with Decentralized Finance (DeFi) entities serving as a prime example. This gap in the Code conflicts with fundamental principles of American legal policy. The Article proposes a novel framework for addressing these challenges and the complexities involved in restructuring such entities.

The discussion underscores the importance of allowing decentralized entities, which inherently do not conform to traditional legal structures, to undergo bankruptcy proceedings when necessary, while highlighting the complications this presents. It emphasizes the historical U.S. legal stance that contract terms waiving the right to file for bankruptcy or excluding certain debts from discharge are unenforceable and against public policy. This perspective is illustrated through examples like bankruptcy-remote special purpose entities and industries such as cannabis, where legal ambiguities arise from differences between state and federal law, providing historical context for Chapter 11.

The Article explores the intricacies of U.S. bankruptcy law as it applies to entities that, by their nature, resist classification under traditional legal frameworks, with a particular focus on Chapter 11, but also considering broader challenges across the entire Bankruptcy Code. It addresses the difficulties these entities face, whether in voluntary or involuntary filings, and the complexities involved in restructuring decentralized entities without a traditional legal structure or "wrapper." The analysis extends to global perspectives on the bankruptcy of "wrapper-less" DeFi entities, examining the varied approaches adopted by different jurisdictions.

Additionally, the Article examines judicial dealings with these unique entities, including a recent class action challenge against a DeFi entity. It also analyzes the landmark case of Hector DAO, a Decentralized Autonomous Organization (DAO), which, on July 15, 2024, was granted recognition under Chapter 15 of the U.S. Bankruptcy Code. This case sets a significant precedent, demonstrating that even entities that do not conform to traditional legal structures can be recognized as debtors in cross-border insolvency cases.

Ultimately, the Article questions whether a uniform approach to all entities that inherently defy traditional legal classification, like those in DeFi, is prudent in bankruptcy cases, or if their distinct characteristics warrant different legal considerations in U.S. bankruptcy courts. The discourse concludes by emphasizing the need for more comprehensive research to enhance the understanding and management of such decentralized entities within the bankruptcy framework, paving the way for more informed policy-making.