Pratt's Journal of Bankruptcy Law

LEXISNEXIS® A.S. PRATT® SEPTEMBER 2025

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Pratt's Journal of Bankruptcy Law

VOLUME 21 NUMBER 6 September 2025

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Library of Congress Card Number: 80-68780

ISBN: 978-0-7698-7846-1 (print)

ISBN: 978-0-7698-7988-8 (eBook)

ISSN: 1931-6992

Cite this publication as:

[author name], [*article title*], [vol. no.] PRATT'S JOURNAL OF BANKRUPTCY LAW [page number] ([year])

Example: Patrick E. Mears, *The Winds of Change Intensify over Europe: Recent European Union Actions Firmly Embrace the "Rescue and Recovery" Culture for Business Recovery*, 10 PRATT'S JOURNAL OF BANKRUPTCY LAW 47 (2025)

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(2025–Pub.4789)

Editor-in-Chief, Editor & Board of Editors

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POSTMASTER: Send address changes to *Pratt's Journal of Bankruptcy Law*, LexisNexis Matthew Bender, 230 Park Ave. 7th Floor, New York NY 10169.

Decentralized Reorganizations: How Thorchain Reimagines Bankruptcy Without Law

By Francisco Javier Garibay Guemez*

In this article, the author examines the first large-scale attempt to conduct a decentralized debt restructuring entirely through decentralized code: Thorchain's issuance of fixed-supply $TCY tokens to resolve more than $200 million in unpaid obligations. The author notes that, by implementing a novel, market-driven adaptation of a core bankruptcy tool – the debt-for-equity swap – entirely through decentralized code, without court supervision, fiduciary duties, or disclosure requirements, Thorchain's restructuring presents a provocative fusion of bankruptcy principles with DeFi architecture. He adds that while the approach offers speed, alignment, and market-based recovery mechanisms, it abandons essential procedural safeguards, raising serious questions about fairness, enforceability, and regulatory compliance. Drawing on U.S. bankruptcy law, securities regulation, and recent developments as of May 2025, the author argues that tokenized reorganizations like Thorchain's demand a new legal framework – one that can reconcile code-based execution with core insolvency values such as transparency, legitimacy, and creditor protection.

Between 2022 and 2024, Thorchain – a decentralized cross-chain liquidity protocol – launched a suite of savings and lending products under the brand "ThorFi." These offerings attracted significant user deposits but collapsed in 2024 due to undercollateralization, poor risk controls, and adverse market conditions. As a result, users were left with approximately $200 million in unpaid obligations.

Unlike traditional financial institutions, Thorchain is not a corporation and cannot file for bankruptcy. It has no board, no legal domicile, and no ability to initiate formal insolvency proceedings. In response to this crisis, the protocol implemented a novel, fully automated restructuring: it created a fixed supply of new tokens ($TCY) and distributed them to affected users, granting them rights to a portion of future transaction fees. The entire process was carried out via decentralized code – without courts, contracts, or negotiations.

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This article introduces Thorchain's restructuring as a case study in decentralized insolvency, situating it within U.S. bankruptcy law and regulatory frameworks to assess its legal and functional implications.

INTRODUCTION

The rise of decentralized finance (DeFi) has brought powerful technological disruption to traditional financial markets, but it has also exposed a widening gap between economic activity and legal accountability. Built on public blockchains and governed by code rather than corporate entities, DeFi protocols typically lack legal personality, fiduciaries, or access to courts. Yet as these systems mature, they encounter the same financial risks that burden traditional firms: excessive leverage, user defaults, and cascading liquidations. Unlike centralized companies, however, DeFi protocols cannot seek Chapter 11 protection, initiate formal workouts, or designate representatives to negotiate with creditors.

Following the collapse of its ThorFi product line, which had exposed users to undercollateralized lending risks, Thorchain implemented a novel token-based recovery mechanism that substituted court-supervised restructuring with automated decentralized code distributions.

This article contends that Thorchain's restructuring, while innovative, challenges the fundamental principles of insolvency jurisprudence. It achieves debt extinguishment and incentive alignment, but at the cost of due process, transparency, and enforceability. By replicating the economic structure of a Chapter 11 debt-for-equity swap in a DeFi environment, the plan reveals both the promise and peril of tokenized reorganization.

This article continues in five parts. Part I outlines Thorchain's restructuring, incorporating updates as of May 2025. Part II compares the plan to Chapter 11 mechanisms, emphasizing the absence of procedural protections. Part III explores securities law and enforceability risks, including the applicability of the Howey test and the limits of pseudonymous governance. Part IV evaluates the merits and vulnerabilities of Thorchain's model, including recent liquidity challenges and market volatility. Part V proposes a policy framework to regulate DeFi restructurings – suggesting legal reforms that could bring DeFi-based insolvency resolution into closer alignment with the values of fairness, legitimacy, and systemic stability.

I. THORCHAIN'S PREDICAMENT: DECENTRALIZED DISTRESS

Thorchain is a decentralized cross-chain liquidity protocol that enables trustless swaps of native assets across disparate blockchains, such as Bitcoin and Ethereum. Unlike many DeFi systems built atop Ethereum, Thorchain operates as an independent layer-one blockchain constructed with the Cosmos SDK,

and it maintains its own consensus mechanism and validator set. Its architecture relies on a decentralized network of node operators, each of whom must post collateral in Thorchain's native token, RUNE, as a bonding requirement to secure the network and process transactions.[1]

Between 2022 and 2024, Thorchain expanded beyond its core swapping function by launching a suite of DeFi products known collectively as "ThorFi." These included lending and yield-bearing savings programs, underpinned by collateral from the protocol's liquidity pools. However, the ThorFi experiment proved short-lived. Amid deteriorating market conditions and protocol-level mismanagement, ThorFi's lending operations became significantly undercollateralized. In early 2024, the program was suspended indefinitely, leaving an estimated $200 million in unpaid liabilities to depositors and lenders.

Under the restructuring proposal, Thorchain minted a fixed supply of 210 million $TCY tokens and distributed them in Q1 2025 on a 1:1 basis to affected ThorFi users – effectively converting $1 of unpaid debt into one $TCY token. These tokens entitle holders to 10% of the protocol's daily swap fees, denominated in RUNE and distributed pro rata via decentralized code.[2] The airdrop was implemented unilaterally, without individualized consent or opt-in, and was structured as a smart contract execution rather than a negotiated reorganization. At launch, $TCY traded near $0.10, implying an initial recovery of ten cents on the dollar; however, prices fell as low as $0.04 in early trading amid liquidity constraints and indiscriminate selling by distressed holders. To mitigate volatility and support secondary-market stability, Thorchain seeded a $600,000 RUNE/TCY liquidity pool and later committed an additional $5 million in treasury funds for buybacks and yield incentives. Despite these interventions, market depth remained shallow, and $TCY's fully diluted market capitalization hovered near $15 million – well below the $200 million in extinguished obligations. As of July 28, 2025, $TCY trades at approximately $0.22, reflecting a modest recovery from post-airdrop lows but still implying a steep impairment relative to original claim values. RUNE, the protocol's native asset, currently trades at $1.43, reinforcing the dollar-denominated discount embedded in TCY distributions. Governance reforms were similarly constrained: Thorchain introduced a "TCY Advisory Council" in February 2025, but its mandate remains purely consultative, with no formal authority to amend token mechanics, initiate binding proposals, or impose

[1] Thorchain, Protocol Overview, https://thorchain.net/dashboard (last visited May 13, 2025).

[2] Thorchain, ThorFi $TCY Restructuring Plan, https://thorchain.net/dashboard (last visited May 13, 2025).

protocol-level changes. The absence of robust participatory mechanisms underscores the informal and non-legal character of the restructuring process, even as it mimics certain attributes of traditional bankruptcy reorganizations.

Importantly, the restructuring was implemented unilaterally, without creditor voting, opt-out provisions, or individualized disclosures. This approach was dictated by the protocol's decentralized architecture, which lacks a legal debtor, centralized decision-making body, or administrative apparatus capable of organizing a collective process. Claimants were automatically included in the airdrop without the opportunity to negotiate or consent ex ante – although, as with any blockchain-based distribution, they retained the practical ability to disclaim the tokens or pursue litigation independently. The plan also did not segment claimants into classes based on claim size, seniority, or nature of exposure, as would be required under traditional reorganization law to ensure fairness across similarly situated creditors.[3] In a Chapter 11 proceeding, for example, class-based treatment allows for differential recoveries, voting rights, and priority enforcement under the absolute priority rule – safeguards that are absent in Thorchain's single-tier distribution. The restructuring terms were disseminated primarily through blog posts and social media announcements, with the operative mechanics embedded in immutable decentralized code.[4]

While the restructuring's economic design mirrors that of a prepackaged Chapter 11 plan – converting fixed liabilities into contingent equity-like interests and distributing them through a single, predefined mechanism – it operates entirely outside the ambit of legal process. There is no solicitation of creditor votes, no court oversight, and no disclosure statement approved under § 1125. Instead, the plan is implemented through autonomously deployed distributions, without procedural safeguards or legal adjudication. This article begins by situating Thorchain's approach within the framework of Chapter 11 to examine how structural similarities mask deeper procedural and normative departures.

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[3] See 11 U.S.C. § 1122(a) (2024) (requiring that a Chapter 11 plan "place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class"); see also In re Tribune Co., 476 B.R. 843, 855-56 (Bankr. D. Del. 2012) (discussing the rationale for separate classification of creditors to reflect differing legal rights, priority, or contractual relationships); Melissa B. Jacoby, Corporate Bankruptcy Hybridity, 166 U. Pa. L. Rev. 1715, 1743-44 (2018) (explaining that classification ensures procedural fairness and guards against domination by majority creditor blocs in plan voting).

[4] Thorchain, Community Update: $TCY Airdrop (Jan. 15, 2025), https://thorchain.net/dashboard.

II. BANKRUPTCY LAW PARALLELS AND DEPARTURES

Thorchain's restructuring reproduces the economic function of a debt-for-equity swap, a common feature of Chapter 11 reorganizations, but it departs radically from the legal and procedural safeguards embedded in the U.S. Bankruptcy Code. The divergence is not merely formal – it raises fundamental questions about fairness, enforceability, and creditor participation in decentralized systems.

Functional Parallels: The Debt-for-Equity Swap

At its core, the $TCY plan resembles a traditional Chapter 11 recapitalization. In bankruptcy, debt-for-equity conversions allow insolvent debtors to extinguish liabilities by issuing new ownership interests to creditors, preserving the going-concern value of the enterprise. This approach was famously used in the Chrysler reorganization, where secured lenders received equity in "New Chrysler," preserving both operational continuity and tens of thousands of jobs.[5]

Thorchain's plan mirrors this structure. Creditors – here, ThorFi users – surrender fixed-dollar claims in exchange for contingent upside linked to protocol revenues. Rather than receive repayment in cash or digital assets, claimants obtain $TCY tokens entitling them to 10% of future swap fees, distributed pro rata, in RUNE. The economic substance is clear: former lenders become residual claimants, their recoveries tied to the success of a restructured business model.

Yet while the structure replicates the economic objectives of a Chapter 11 plan – such as discharging liabilities, preserving going-concern value, and aligning incentives – it bypasses the legal architecture that confers procedural integrity, creditor voice, and institutional accountability.

Procedural Departures From Chapter 11

Chapter 11 does not merely authorize debt-for-equity swaps; it regulates them through an elaborate framework of disclosure, voting, oversight, and judicial review. Thorchain's restructuring bypasses each of these requirements.

Disclosure and Transparency

Section 1125 of the Bankruptcy Code mandates that creditors receive a court-approved disclosure statement containing "adequate information" to make an informed judgment about the plan.[6] This includes financial projec-

[5] In re Chrysler LLC, 405 B.R. 84, 92-94 (Bankr. S.D.N.Y. 2009).

[6] 11 U.S.C. § 1125 (2024).

tions, liquidation analyses, risk factors, and details about post-confirmation governance. Thorchain, by contrast, disseminated its plan through a series of blog posts and community updates. These materials did not include any financial models, stress tests, or sensitivity analyses, nor did they address the feasibility of diverting 10% of protocol revenue indefinitely to token holders.[7]

Voting and Creditor Assent

Section 1126 requires that impaired classes of creditors vote to accept the plan by at least two-thirds in amount and a majority in number.[8] Thorchain's plan includes no voting mechanism. The $TCY airdrop was executed unilaterally, with no opt-out, no right to reject, and no alternative remedy. Unlike cramdowns under § 1129(b), where dissenters can be overruled only if the plan is "fair and equitable," Thorchain's structure bypasses class-based treatment altogether.

Judicial Review and Feasibility

Section 1129(a)(11) requires courts to find that a plan is "feasible," meaning not likely to be followed by liquidation or further financial distress.[9] No such feasibility test was applied to Thorchain's plan. The protocol diverts 10% of all swap fees to $TCY holders without examining long-term effects on node incentives, network participation, or protocol growth. Recent reports of liquidity shortfalls and early token dumping suggest that this omission may have material consequences.

Thorchain has informally cited the $MAYA token – a prior protocol with a similar fee-sharing model – as a proof of concept. $MAYA reached a $25 million market capitalization without centralized governance or formal legal process. Yet unlike a confirmed bankruptcy plan, the $TCY proposal includes no feasibility determination, liquidation analysis, or creditor oversight. Recovery is premised entirely on protocol sustainability and market acceptance – factors that may be volatile or short-lived.

Moreover, Section 1129(a)(3) requires that a plan be "proposed in good faith and not by any means forbidden by law."[10] In a traditional case, the United States Trustee and interested creditors may challenge a plan on this basis. In Thorchain's case, there is no legal "proposer," no identifiable debtor, and no

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[7] Thorchain, Community Update: $TCY Airdrop (Jan. 15, 2025), https://thorchain.net/dashboard.

[8] 11 U.S.C. § 1126 (2024).

[9] 11 U.S.C. § 1129(a)(11) (2024).

[10] 11 U.S.C. § 1129(a)(3) (2024).

fiduciary subject to judicial scrutiny. The restructuring was implemented by pseudonymous developers, without formal accountability or review.

Absence of a Legal Debtor

A more structural departure lies in the absence of a legal debtor. Chapter 11 presupposes a juridical person – corporation, partnership, or individual – who may file a voluntary petition and become a debtor-in-possession. That entity assumes fiduciary duties, is subject to court supervision, and becomes the locus of creditor claims. Thorchain has no such entity. It is a decentralized software protocol composed of open-source decentralized code running on a permissionless blockchain, coordinated by pseudonymous developers and a distributed set of node operators. It operates without incorporation, registered domicile, or legal personality.[11] As such, it cannot file for bankruptcy, retain professionals, or enter into restructuring support agreements.

This absence undermines the entire creditor rights framework. In Chrysler and other cases, dissenting creditors could object, litigate valuation, or seek appellate review. ThorFi claimants, by contrast, have no forum for recourse, no contract to enforce, and no counterparty to sue. The restructuring is executed and enforced solely through decentralized code, insulated from challenge unless plaintiffs can pierce the veil of decentralization and establish liability against identifiable actors – a daunting task under current law.[12] These departures raise a critical question: Can the core economic objectives of bankruptcy law – maximizing estate value, ensuring equitable treatment, and promoting creditor participation – be achieved through decentralized, non-judicial processes?

III. REGULATORY IMPLICATIONS

Thorchain's $TCY restructuring circumvents traditional insolvency proceedings, but it raises significant legal questions across adjacent regulatory domains – particularly under U.S. securities and commodities law, where revenue-sharing tokens may be classified as investment contracts or derivatives.[13] As tokenized restructurings proliferate, the legal status of instruments like $TCY will likely become a focal point for regulators and courts adapting legacy doctrines to blockchain-based mechanisms.

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[11] Hilary J. Allen, DeFi: Shadow Banking 2.0?, 64 Wm. & Mary L. Rev. 1, 25-30 (2023).

[12] Chris Brummer & Nakita Cuttino, Decentralized Finance and the Law, 56 U.C. Davis L. Rev. 123, 150-55 (2023).

[13] Commodity Exchange Act, 7 U.S.C. §§ 1-27f.

Securities Classification Under the *Howey* Test

The Securities and Exchange Commission (SEC) continues to apply the four-prong test from *SEC v. W.J. Howey Co.*[14] to assess whether a digital asset constitutes an "investment contract": (1) an investment of money, (2) in a common enterprise, (3) with a reasonable expectation of profits, (4) derived from the efforts of others. While $TCY was issued in exchange for past claims rather than new capital, it arguably satisfies all four prongs:

- *Common Enterprise*: The token's value is directly tied to the performance of Thorchain's swap protocol and treasury decisions.
- *Expectation of Profits*: Holders receive pro rata distributions of future protocol revenue – 10% of daily swap fees in RUNE – creating an economic interest similar to dividend-bearing equity.
- *Managerial Efforts*: Treasury operations, buybacks, liquidity support, and code upgrades are conducted by identifiable developers and node operators.

Notably, recent SEC enforcement actions – including *SEC v. Ripple Labs,*[15] *SEC v. Terraform Labs*,[16] and *SEC v. Coinbase*[17] (2023) – have expanded the agency's interpretation of managerial control, holding that even decentralized or pseudonymous governance structures may meet the "efforts of others" threshold if protocol maintenance and token value depend on identifiable actors.

If $TCY is classified as a security, its unregistered issuance to U.S. persons could violate Sections 5 and 12(a)(1) of the Securities Act of 1933, which prohibit the offer or sale of securities unless a registration statement is in effect or an exemption applies. While no formal action has targeted Thorchain to date, the SEC's post-2023 enforcement agenda – emphasized in its Fiscal Year 2024 Enforcement Results – signals a willingness to treat such distributions as securities offerings when tied to passive profit schemes.

CFTC Jurisdiction and Derivative Risk

The Commodity Futures Trading Commission (CFTC) has also moved aggressively into the DeFi arena. In its 2023 settlement with Uniswap Labs, the CFTC alleged that decentralized platforms facilitating token swaps could

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[14] SEC v. W.J. Howey Co., 328 U.S. 293, 298-99 (1946).

[15] SEC v. Ripple Labs, Inc., No. 20 Civ. 10832 (AT), 2023 U.S. Dist. LEXIS 120486 (S.D.N.Y. July 13, 2023).

[16] SEC v. Terraform Labs Pte. Ltd., No. 23 Civ. 1346 (JSR), 2023 U.S. Dist. LEXIS 236123 (S.D.N.Y. Dec. 28, 2023).

[17] SEC v. Coinbase, Inc., No. 1:23-cv-04738 (S.D.N.Y. filed June 6, 2023).

constitute unregistered derivative marketplaces under the Commodity Exchange Act.[18] The settlement extended the agency's jurisdiction beyond intermediaries to include protocol developers, even when operating without a formal business entity.

Given $TCY's function as a revenue-sharing instrument that may fluctuate in value based on protocol performance, it could be viewed as a synthetic derivative or commodity-based income instrument – triggering additional registration or compliance obligations under CFTC rules.

While Thorchain lacks a formal U.S. presence, both agencies may assert jurisdiction under long-standing doctrines such as the conduct test and effects test,[19] which allow U.S. law to apply to foreign transactions if there is substantial domestic impact or involvement of U.S. persons. If $TCY tokens were offered through interfaces accessible to U.S. users, distributed via platforms with U.S. footprint, or marketed by developers located in the United States, the SEC and CFTC may claim enforcement authority.

Enforceability and Liability Risks

Traditional bankruptcy regimes provide a legal forum for creditors to assert rights, challenge distributions, and hold fiduciaries accountable. In the Thorchain model, none of these protections exist.

There is no debtor-in-possession, trustee, or statutory fiduciary. The restructuring's enforcement depends entirely on preprogrammed execution logic, without oversight or recourse. Users who disagree with the plan or allege procedural unfairness have no contractual or judicial remedy unless they can:

1. Identify specific contributors responsible for plan design;
2. Establish a duty owed by those contributors to claimants; and
3. Prove jurisdiction and overcome procedural hurdles to serve process across borders and anonymity shields.

Even where developer identities are known – for example, via GitHub contributions or public statements – courts would face novel questions of whether protocol contributors bear duties analogous to directors, fiduciaries, or plan proponents. As U.S. courts have yet to adopt a clear standard of liability

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[18] CFTC Press Release, "CFTC Orders Uniswap Labs to Cease Offering Illegal Derivatives" (Sept. 4, 2023), https://www.cftc.gov/PressRoom/PressReleases/8700-23.

[19] Morrison v. Nat'l Australia Bank Ltd., 561 U.S. 247, 266-67 (2010).

for pseudonymous actors in decentralized systems, enforcement risk remains highly contingent on future litigation and regulatory action. [20]

The Limits of Code-Based Rights

The $TCY revenue-sharing mechanism is hardcoded into on-chain contracts, whose enforceability is contingent on uninterrupted protocol function. If the contract fails – due to a bug, exploit, or governance fork – holders have no legal fallback. There is no post-confirmation jurisdiction akin to that under 11 U.S.C. § 1142, no plan administrator, and no contractual dispute resolution forum.

This reliance on code over courts creates what scholars have described as an "accountability vacuum."[21] While code can execute payouts deterministically, it cannot adjust to unforeseen events, ensure procedural fairness, or resolve conflicts. Unlike traditional reorganization plans – subject to judicial confirmation, amendment, and enforcement – Thorchain's plan is immutable once deployed. This immutability, while efficient, exposes users to risk without remedy.

International Considerations and Cross-Border Insolvency

Thorchain's user base spans dozens of jurisdictions, yet the restructuring plan lacks any legal anchor in corporate or insolvency law. There is no legal entity initiating proceedings, no forum to recognize or enforce rights, and no administrator empowered to act transnationally. This precludes application of frameworks like the UNCITRAL Model Law on Cross-Border Insolvency, which presuppose a "foreign main proceeding" initiated by a debtor or insolvency representative in the debtor's "center of main interest."[22]

Consequently, users cannot seek recognition of Thorchain's restructuring under Chapter 15 in the U.S., nor could foreign courts coordinate enforcement. The lack of a legally cognizable debtor frustrates creditor remedies and undermines procedural protections offered by multilateral insolvency instruments.

Regulatory Trends and Impending Enforcement Risks

As of July 2025, no public enforcement action has been initiated against Thorchain's $TCY plan. However, recent pronouncements by U.S. regulators suggest that similar restructurings may soon attract scrutiny.

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[20] Chris Brummer & Nakita Cuttino, Decentralized Finance and the Law, 56 U.C. Davis L. Rev. 123, 150-55 (2023).

[21] Hilary J. Allen, DeFi: Shadow Banking 2.0?, 64 Wm. & Mary L. Rev. 1, 40-45 (2023).

[22] UNCITRAL Model Law on Cross-Border Insolvency (1997), arts. 1, 17.

In its Fiscal Year 2024 Enforcement Results, the SEC emphasized that the decentralized nature of a protocol does not preclude regulatory liability if tokens are distributed in a manner consistent with securities offerings.[23]

Likewise, the CFTC's enforcement stance following its 2023 actions against Ooki DAO and Uniswap Labs shows an expanded willingness to hold pseudonymous developers and DAO participants liable for violations of commodities law. In both cases, the CFTC argued that the absence of formal legal wrappers did not eliminate accountability if developers acted as de facto organizers or promoters.[24]

Together, these trends suggest that token-based DeFi restructurings like $TCY are not immune from legal risk, even if executed autonomously and without centralized control. Thorchain's use of decentralized code in lieu of formal agreements or court proceedings may insulate its contributors from immediate legal exposure – but only temporarily. As regulatory frameworks evolve to address DeFi-specific enforcement challenges, the protocol's restructuring may become a litmus test for applying traditional investor protection principles to decentralized insolvency events.[25]

In parallel with enforcement activity, legislative efforts are underway to bring regulatory clarity to decentralized financial systems. The Lummis-Gillibrand Responsible Financial Innovation Act, reintroduced in 2023, proposes a comprehensive framework for digital assets, including a mechanism to distinguish between commodities and securities, expanded oversight for the CFTC, and tailored disclosure exemptions for certain decentralized protocols. [26]A related legislative effort, the Digital Asset Market Clarity Act (CLARITY), introduced in May 2025 and passed by the U.S. House of Representatives in July 2025, establishes registration pathways for digital asset exchanges, including decentralized platforms, and mandates disclosure requirements to enhance transparency in DeFi governance. CLARITY, which garnered bipartisan

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[23] Securities and Exchange Commission. (2024, November 22). SEC Announces Enforcement Results for Fiscal Year 2024. https://www.sec.gov/newsroom/press-releases/2024-186.

[24] Hilary J. Allen, DeFi: Shadow Banking 2.0?, 64 Wm. & Mary L. Rev. 1, 25-30, 40-45 (2023). See also, CFTC v. Ooki DAO, No. 3:22-cv-05416 (N.D. Cal. June 8, 2023). Commodity Futures Trading Commission. (2024, September 4). CFTC Announces Settlement with Uniswap Labs for Offering Illegal Leveraged Retail Commodity Transactions, https://www.cftc.gov/PressRoom/PressReleases/8789-24.

[25] Chris Brummer & Nakita Cuttino, Decentralized Finance and the Law, 56 U.C. Davis L. Rev. 123, 150-55 (2023).

[26] See Lummis-Gillibrand Responsible Financial Innovation Act, S.2281, 118th Cong. (2023), https://www.congress.gov/bill/118th-congress/senate-bill/2281.

support with a 294–134 vote, reflects a growing consensus that DeFi activities, such as Thorchain's $TCY token restructuring, must align with U.S. financial regulation while accommodating blockchain's technological nuances. For tokenized reorganizations, CLARITY could provide legal recognition for creditor recoveries through registered exchanges or certified digital commodities, imposing baseline standards for disclosure, governance, and compliance. If enacted, such legislation may legitimize DeFi restructurings as regulated financial instruments, bridging the gap between code-based execution and investor protections. Additionally, the Guiding and Establishing National Innovation for U.S. Stablecoins Act (GENIUS), signed into law in July 2025, establishes a federal regulatory framework for payment stablecoins.[27]

The election of President Trump to a second term in 2024 has ushered in a pro-crypto regulatory environment. The administration has issued executive orders supporting the responsible growth of digital assets, established a Strategic Bitcoin Reserve, and signed the GENIUS Act into law. On one hand, personnel changes at the SEC and CFTC have resulted in a more restrained enforcement posture, particularly if agency leadership adopts a narrower view of jurisdictional reach or prioritizes centralized actors over protocol-level innovation. On the other hand, continued market volatility may compel regulators to maintain an aggressive stance in the absence of further Congressional clarity. The regulatory treatment of smart contract-based token distributions – like Thorchain's $TCY issuance – thus remains contingent on evolving institutional priorities alongside recent statutory reforms.

IV. EVALUATING AND POLICY IMPLICATIONS

Thorchain's restructuring represents a landmark experiment in decentralized debt resolution, offering a glimpse into how financial distress may be addressed in non-corporate, trustless systems. While the $TCY token plan succeeds in certain economic and functional respects, it also exposes foundational weaknesses in DeFi's ability to ensure fairness, accountability, and systemic stability. This section evaluates both the strengths and weaknesses of Thorchain's approach and proposes initial policy responses.

Merits: Efficiency, Incentive Alignment, and Continuity

From a functional perspective, the $TCY plan achieves a key goal of reorganization law: the conversion of unsustainable liabilities into contingent upside, enabling the debtor (here, the protocol) to continue operations. As in Chapter 11, the restructuring extinguishes legacy obligations and substitutes a new class of claimants aligned with future performance.

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[27] Guiding and Establishing National Innovation for U.S. Stablecoins Act, S.1582, 119th Cong. (2025), https://www.congress.gov/bill/119th-congress/senate-bill/1582.

The 10% revenue share embedded in $TCY creates an incentive-compatible recovery mechanism. Token holders are not entitled to fixed payments but instead benefit proportionally from increases in protocol usage. This aligns with the logic of equity participation in post-confirmation Chapter 11 reorganizations and mimics the structure of recovery notes or contingent value rights in distressed debt workouts.

Additionally, Thorchain seeded liquidity for $TCY through a $600,000 RUNE/TCY pool and committed $5 million in treasury assets for buybacks and incentives.[28] These actions mirror "plan sponsor" contributions in formal restructurings, designed to foster market stability and exit options. Claimants unwilling to hold speculative tokens could theoretically liquidate their positions, even if at a discount.

Operationally, the replacement of ThorFi with a more capital-efficient system – Liquidity Nodes – represents a strategic pivot akin to post-confirmation business restructuring. Unlike the passive deposit-based model used in ThorFi, Liquidity Nodes require operators to actively bond capital and provide liquidity in exchange for protocol rewards, thereby aligning incentives and mitigating undercollateralization risk. According to protocol updates, Liquidity Nodes double capital throughput and offer improved fee distribution mechanisms, addressing structural flaws that led to ThorFi's collapse.[29] From a systems design perspective, the restructuring is not merely financial – it incorporates governance and technical adaptation.

Vulnerabilities: Speculation, Procedural Deficits, and Structural Risk

Despite these functional gains, the plan suffers from several significant shortcomings when assessed under both normative and operational criteria. From the standpoint of insolvency law, fairness, procedural transparency, and legal enforceability remain absent. Functionally, the plan's long-term sustainability is uncertain and its incentive alignment potentially unstable.

First, valuation uncertainty undermines recovery expectations. $TCY's implied price at launch was approximately $0.10 per token, suggesting a recovery rate of 10 cents on the dollar. That valuation depends on sustained

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[28] Shaurya Malwa, THORChain to Issue Equity Tokens to Battle $200M Debt After Pausing Bitcoin, Ether Lending, CoinDesk (Feb. 3, 2025), https://www.coindesk.com/markets/2025/02/03/thorchain-to-issue-equity-tokens-to-battle-usd200m-debt-after-pausing-bitcoin-ether-lending. See also @AaluxxMyth, X (Apr. 1, 2025), https://x.com/AaluxxMyth/status/1922029139365650930.

[29] Thorchain, ThorFi $TCY Restructuring Plan, https://thorchain.net/dashboard (last visited May 13, 2025).

swap volume and user adoption – factors that remain volatile in DeFi markets. Token price data from March-April 2025 shows persistent discounting and signs of early token dumping by claimants seeking immediate liquidity.[30] This introduces the risk of negative feedback loops: price instability deters holding, which further depresses prices.

This dynamic was observable in early trading behavior: on-chain analytics and third-party reports showed that trading volume in the RUNE/TCY pool peaked in late March 2025, but dropped significantly by mid-April as incentives tapered off and early claimants sought to exit their positions. The lack of lockups, time-based vesting, or staggered distributions contributed to rapid sell-offs, with $TCY frequently trading below $0.09 initially but recovering to $0.21 by late July. Many users voiced frustration on community forums, with one wallet holder noting that the airdrop felt "forced and opaque," while another described the plan as "dumpable debt wrapped in optimism." These reactions underscore not only valuation instability but also the procedural legitimacy concerns that arise when participation is automatic and not accompanied by formal notice or choice.

Second, the absence of procedural protections erodes the fairness and transparency of the restructuring. Unlike Chapter 11, Thorchain's plan lacks voting mechanisms, classification of claims, disclosure statements, opt-out options, or judicial oversight. There is no feasibility requirement akin to § 1129(a)(11), [31] which mandates that a reorganization plan be likely to succeed and not lead to further liquidation or financial distress, no enforcement authority like a U.S. Trustee, and no judicial forum to challenge unfair or discriminatory treatment. All affected users were automatically enrolled, regardless of consent or individualized circumstances.

Third, the plan's sustainability is questionable. Diverting 10% of future revenue may undermine node incentives or reduce protocol reinvestment capacity, particularly with the current node count at 118. Unlike fixed-term recovery instruments, $TCY's perpetual entitlement to protocol income could distort governance, particularly if token holders' interests diverge from those of active network participants. There is no mechanism to sunset the fee diversion, revise the distribution ratio, or rebalance stakeholder priorities through a deliberative process.

These weaknesses reflect broader structural limits: in the absence of a legal debtor, there is no fiduciary actor to mediate between stakeholder classes,

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[30] CoinDesk, Thorchain's $TCY Token Faces Liquidity Woes (Apr. 10, 2025), https://coindesk.com/thorchain-tcy-liquidity.

[31] See 11 U.S.C. § 1129(a)(11) (2024) (feasibility requirement).

implement plan modifications, or defend the reorganization's integrity.[32] Thorchain's reliance on algorithmic execution, rather than negotiated compromise, sacrifices responsiveness and adaptability in favor of automation.

Policy Recommendations: Bridging DeFi Innovation and Legal Process

Thorchain's restructuring illustrates both the promise and peril of tokenized reorganizations. While judicial insolvency may not be feasible in DeFi ecosystems lacking legal personality or centralized control, policymakers and legal scholars should explore hybrid frameworks that preserve innovation while introducing minimal procedural safeguards.

Potential interventions include:

- *Statutory Safe Harbors*: Create exemptions from securities registration for DeFi restructurings that meet minimum governance and transparency standards. Criteria might include disclosures, voting thresholds, and public auditability of decentralized code.
- *DeFi Insolvency Protocols*: Develop template decentralized code or "protocol-level" procedures for decentralized restructuring events, incorporating features like class-based voting, opt-outs, and time-based vesting.
- *Arbitration and Governance Forums*: Encourage DeFi protocols to adopt dispute resolution forums or arbitration layers to resolve tokenholder disputes, interpret restructuring mechanics, and enforce fiduciary-style duties in code-based systems.[33]
- *International Coordination*: Amend or supplement the UNCITRAL Model Law on Cross-Border Insolvency to recognize decentralized restructurings, enabling users to invoke limited rights in their jurisdictions even in the absence of a legal debtor.[34]

In addition to procedural and regulatory innovations, DeFi protocols could also adopt adapted versions of traditional insolvency planning tools designed to anticipate and mitigate financial distress. For example, Contingent Convertible tokens (DeFi CoCos) could be embedded in protocol treasuries, automatically converting governance or liquidity rights into equity-like tokens in response to predefined triggers such as treasury shortfalls, oracle failures, or liquidity

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[32] Hilary J. Allen, DeFi: Shadow Banking 2.0?, 64 Wm. & Mary L. Rev. 1, 40-45 (2023).

[33] Chris Brummer & Nakita Cuttino, Decentralized Finance and the Law, 56 U.C. Davis L. Rev. 123, 150-55 (2023).

[34] UNCITRAL Model Law on Cross-Border Insolvency (1997), arts. 1, 17.

collapse.[35] Similarly, protocols could publish "living wills" or recovery and resolution plans (RRPs) – predefined restructuring playbooks encoded into decentralized code or governance documents – outlining steps for liquidity recovery, fee reprioritization, or capital reallocation in the event of systemic stress.[36] The development of best-practices frameworks – through Decentralized Autonomous Organization (DAO) governance, technical consortia, or DeFi standards bodies – could further standardize these tools and support regulatory engagement. These approaches offer a bridge between formal insolvency regimes and automated governance, equipping decentralized systems with modular, ex ante mechanisms for preserving continuity and managing collapse.

These measures need not replicate full judicial insolvency but should aim to restore essential features: creditor participation, procedural fairness, and redress mechanisms. As DeFi protocols grow in complexity and systemic relevance, their failure modes – and recovery tools – must be designed with both economic functionality and legal legitimacy in mind.

V. RETHINKING REORGANIZATION IN THE AGE OF CODE

Thorchain's $TCY restructuring presents a compelling case study in how decentralized finance attempts to replicate the economic effects of bankruptcy without the machinery of legal process. Through its tokenized debt-to-equity conversion, implemented entirely via decentralized code, Thorchain extinguished over $200 million in unpaid obligations while preserving operational continuity and aligning claimants with future protocol performance.[37]

From a structural standpoint, the plan achieves several objectives traditionally associated with Chapter 11: discharge, capital restructuring, and creditor alignment. Yet it accomplishes these goals in a legal vacuum – without debtor-in-possession duties, court supervision, voting rights, disclosure obligations, or enforceable remedies. Claimants are converted into token holders not

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[35] On CoCos as a convertible distress tool in traditional finance, see Basel Committee on Banking Supervision, The Regulatory Treatment of Contingent Convertible Instruments (2011); see also Hilary J. Allen, DeFi: Shadow Banking 2.0?, 64 Wm. & Mary L. Rev. 1, 47-52 (2023) (noting DeFi's failure to adopt layered defenses typical of traditional finance).

[36] On living wills and RRPs, see Financial Stability Board, Key Attributes of Effective Resolution Regimes for Financial Institutions (2014).

[37] This estimate is based on community disclosures and protocol-level analyses following the collapse of ThorFi. See Thorchain, ThorFi $TCY Restructuring Plan (Jan. 2025), https://thorchain.net/dashboard (last visited May 13, 2025); see also DeFi Pulse, Thorchain's ThorFi Collapse: A $75M Lesson in DeFi Risk (Mar. 15, 2025), https://defipulse.com/thorchain-thorfi-collapse.

through deliberation, but through automated protocol execution. The governance mechanisms are informal and advisory, the contracts immutable, and the remedies nonexistent.

This raises fundamental questions for scholars, regulators, and market participants: Can fairness be ensured in the absence of due process? Can enforceability be achieved through code alone? Can a protocol without legal personality conduct a restructuring without invoking law? Can meaningful consent be obtained when participation is automated and opt-outs are unavailable? Can accountability exist without fiduciaries or adjudicative forums? Can equitable treatment be guaranteed when all claimants receive uniform recoveries, regardless of size, priority, or risk exposure? And can cross-border financial ecosystems function without legal standards for recognition, enforcement, or finality?

In Thorchain's model, disclosure is replaced by blog posts, and governance by GitHub pull requests – substituting community signaling for fiduciary accountability.

For all its innovation, Thorchain's model demonstrates the limits of purely algorithmic reorganization. Efficiency is gained, but at the expense of legitimacy and accountability. The reliance on market dynamics rather than legal safeguards places users at the mercy of price volatility and governance asymmetries. The lack of opt-outs or judicial review raises concerns about procedural justice and investor protection.

As DeFi expands and decentralized entities grow more complex and interconnected, the need for hybrid legal-technical frameworks becomes urgent. Rather than impose traditional insolvency law wholesale, policymakers should explore mechanisms that preserve the benefits of decentralization while restoring essential safeguards: transparency, creditor voice, and dispute resolution.

Thorchain does not mark the end of law in insolvency – it marks its transformation. The challenge now is to craft a legal architecture that can govern entities without chief executive officers, courts, or borders. Tokenized reorganizations are not simply technical innovations; they are a provocation to reimagine the foundations of creditor-debtor relations in the digital age. It invites us to ask: what does it mean to reorganize in a system with no court, no debtor, and no law?