What are smart contracts?

The term 'smart contract' is commonly used in the tech world, especially when talking about cryptocurrencies. The term is mainly used to describe computer code that automatically executes all or parts of an agreement stored on the blockchain.

However, smart contracts can be much more primitive and despite the name 'smart' they are not really smart and do not use AI. So, what is a smart contract? How do they work? Let's find the answer through the following article!

What are smart contracts?

The term was first used in the 1990s by computer scientist and cryptographer Nick Szabo.

In the article 'Smart Contracts: Building Blocks for Digital Markets', scientist Szabo described smart contracts as 'new institutions and ways to formalize these […] digital revolution'. He calls them "intelligent" because their functionality is superior to the traditional paper-based version, without implying that they use artificial intelligence.

In fact, the most basic example of a smart contract is that of a vending machine. When the buyer meets the conditions of the 'contract' by putting money in the machine, it automatically follows the terms of the agreement and delivers the product. Of course, more complex forms of smart contracts are used to exchange blockchain-based cryptocurrencies.

Szabo goes on to define a smart contract as 'a set of promises, specified in digital form, consisting of multiple protocols by which the parties act on these promises'.

How do smart contracts work?

Thus, their main function is to fulfill certain terms, such as transferring funds from one party's wallet to another. In other words, if 'x' occurs, then step 'y' is executed as a response. The smart contract itself is then replicated through a number of blockchain nodes, benefiting from the security and immutability that blockchain provides.

How 'smart' are smart contracts?

Szabo's decision to emphasize that smart contracts are not really "smart" is significant. Smart contracts may be smarter than traditional paper-based versions, able to automatically perform some pre-programmed steps, but they still cannot parse the subjective terms of the contract.

This means that the tasks that smart contracts can perform are actually quite rudimentary. Although smart contracts will become more complex and capable of settling many transactions with high difficulty as the adoption of blockchain technology expands, it will still be many years before smart contracts can define the subjective legal criteria.

Currently, smart contracts are best suited for two types of transactions found in many contracts: Ensuring that payments are made when specific conditions are met, and imposing financial penalties if certain conditions are not met. response.

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