Digital and Digitized Assets:
Federal and State Jurisdictional Issues

Prepared By:

American Bar Association
Derivatives and Futures Law Committee
Innovative Digital Products and Processes Subcommittee
Jurisdiction Working Group

December 2020

DISCLAIMER AND COPYRIGHT NOTICE

The content of this White Paper and each Section in it is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting legal counsel. In addition, the content of each Section reflects the views of the authors of that Section only and does not necessarily reflect the views of their law firms, companies, clients, other lawyers in their law firms, or the other contributing authors of other Sections.

SECTION 2. COMMODITY EXCHANGE ACT AND CFTC REGULATION

Jonathan L. Marcus
Of Counsel, Skadden, Arps, Slate, Meagher & Flom LLP

Trevor A. Levine
Associate, Reed Smith LLP

Kathryn M. Trkla
Partner, Foley & Lardner LLP

Shekida A. Smith-Sandy
Associate, Perkins Coie LLP

Clifford C. Histed
Partner, K&L Gates LLP

Jeongu Gim
Associate, Skadden, Arps, Slate, Meagher & Flom LLP

Cheryl L. Isaac
Senior Counsel, Michael Best & Friedrich LLP

2020 UPDATES TO SECTION 2

Jonathan L. Marcus
Of Counsel, Skadden, Arps, Slate, Meagher & Flom LLP

Trevor A. Levine
Associate, Reed Smith LLP

Kathryn M. Trkla
Partner, Foley & Lardner LLP

Shekida A. Smith-Sandy
Associate, Perkins Coie LLP

Clifford C. Histed
Partner, K&L Gates LLP

Jeongu Gim
Associate, Skadden, Arps, Slate, Meagher & Flom LLP

1. Introduction

The CEA is a federal statute that focuses on regulating transactions and markets in derivatives, *i.e.*, contracts whose value derives from the value of a referenced underlying "commodity." Congress determined it is in the public interest to regulate derivatives markets, with an initial emphasis on exchange markets for futures on agricultural commodities, because derivatives markets are closely related to the cash markets for the underlying commodities and thus can have implications for the cash markets. Derivatives are used by many businesses to manage price or other risks associated with their activities. Businesses also may price commercial merchandizing or other transactions by reference to the prices discovered in

centralized derivatives markets, when those prices are considered reliable projections of future market value. The hedging and price discovery benefits that centralized derivatives markets provide are deemed to be in the public interest,[109] and much of the CEA framework is intended to protect the derivatives markets and related cash markets against manipulation, unwarranted price distortions, and, for derivatives on tangible commodities that settle by delivery at expiration, congestion in deliverable supplies of the underlying commodities.

The CEA grants the CFTC regulatory authority over certain categories of derivatives transactions, as well as over certain leveraged off-exchange retail transactions regardless of whether the transactions are derivatives. The scope of the CFTC's jurisdiction depends, in part, on whether the derivative or other transaction involves a "commodity." The CEA also vests the Commission with enforcement authority (but not rulemaking authority) with respect to fraud and manipulation involving cash market trading of commodities.

Notably, the CEA definition of "commodity" is broader than one might expect based on a common understanding of the term. Although there are significant issues surrounding the scope and interpretation of what the CEA definition encompasses, the definition is understood to cover securities, foreign currencies, and other financial assets, and is not limited to tangible (physical) commodities.

The CEA makes distinctions based on the type or classification of a commodity, which are relevant because the commodity classification can lead to different regulatory treatment under the statute. For example, CEA provisions allocate jurisdiction over derivatives that are based on a security or group or index of securities (or any interest therein or based on the value

[109] *See* 7 U.S.C. § 5. Over time, Congress expanded the public interest justification for regulating derivatives markets, to recognize the public interest benefits of market self-regulation and to protect financial integrity of transactions, protect against systemic risk, and protect market participants from fraud and abusive sales practices.

thereof) between the CFTC and the SEC or jointly to the two agencies. As another example, the CEA provisions regulating off-exchange retail transactions differ based on whether the commodity is a foreign currency or another type of non-security commodity. Classification as an exempt commodity (non-agricultural commodities considered non-financial in nature) or excluded commodity (considered financial in nature) is relevant to whether transactions may qualify for exclusion from futures or swaps regulation as forward contracts.

Thus, threshold questions for determining whether and how the CEA could apply to a digital or digitized asset, and transactions in the asset, include (1) whether the asset is a "commodity," as defined in the CEA, and (2) if so, how the asset is classified—in particular, whether it is a security. A digitized asset that represents a record of title to an underlying asset, *e.g.*, a token representing ownership of gold, is simply a form of electronic title document, where it is the classification of the underlying asset that is relevant. Digital assets where the token itself is the asset may be more challenging to classify as a security or non-security commodity, if the digital asset is (or aspires to be) a virtual currency or has some other type of utility function, but also may serve an initial capital raising purpose or have other characteristics associated with securities.

This Section focuses on a particular type of digital asset, virtual currencies, because the CFTC to date has asserted jurisdiction primarily over virtual currencies among digital assets. At the same time, the same principles that the CFTC applies to virtual currencies likely will apply to other digital assets.[110]

[110] *See, e.g.*, CFTC, A CFTC PRIMER ON VIRTUAL CURRENCIES (2017), https://www.cftc.gov/sites/default/files/idc/groups/public/documents/file/labcftc_primercurrencies100417.pdf [hereinafter PRIMER ON VIRTUAL CURRENCIES] ("There is no inconsistency between the SEC's analysis and the CFTC's determination that virtual currencies are commodities and that virtual tokens may be commodities or derivatives contracts depending on the particular facts and circumstances.").

The CFTC has asserted jurisdiction over virtual currency transactions in a variety of contexts, beginning with a settlement order entered between the CFTC and Coinflip, Inc. in 2015.[111] The CFTC based its assertion of jurisdiction on its position that virtual currencies are "commodities," as that term is defined in the CEA, 7 U.S.C. § 1 *et seq.*[112] The CFTC's position regarding its statutory authority over transactions involving virtual currencies has remained consistent in public statements made by CFTC Commissioners,[113] a CFTC interpretation of the

[111] *In the Matter of Coinflip, Inc.*, CFTC No. 15-29, [2015-2016 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 33,538, at 77,854 (Sept. 17, 2015) [hereinafter *Coinflip*].

[112] *Id.* at 77,855 ("Bitcoin and other virtual currencies are encompassed in the [commodity] definition and properly defined as commodities.").

[113] In December 2014, then-Chairman Timothy Massad considered whether the CFTC had regulatory authority over virtual currencies in congressional testimony before the Senate Committee on Agriculture, Nutrition, and Forestry. There, Massad explained:

> The CFTC's jurisdiction with respect to virtual currencies will depend on the facts and circumstances pertaining to any particular activity in question. While the CFTC does not have policies and procedures specific to virtual currencies like bitcoin, the agency's authority extends to futures and swaps contracts in any commodity. The CEA defines the term commodity very broadly so that in addition to traditional agricultural commodities, metals, and energy, the CFTC has oversight of derivatives contracts related to Treasury securities, interest rate indices, stock market indices, currencies, electricity, and heating degree days, to name just a few underlying products. Derivative contracts based on a virtual currency represent one area within our responsibility.

See The Commodity Futures Trading Commission: Effective Enforcement and the Future of Derivatives Regulation: Hearing before the S. Comm. on Agric., Nutrition & Forestry, 113th Cong. 20 (2014) (statement of Timothy Massad, Chairman, CFTC). CFTC Commissioners subsequently have reiterated this conclusion. *See*, *e.g.*, Giancarlo HUA Statement, *supra* note 2; J. Christopher Giancarlo, Chairman, CFTC, Keynote Address Before the ABA Business Law Section, Derivatives & Futures Law Comm. Winter Meeting, Naples, Florida (Jan. 25, 2019), https://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo63; J. Christopher Giancarlo, Chairman, CFTC, Chairman Giancarlo Statement on Virtual Currencies (Jan. 4, 2018), https://www.cftc.gov/PressRoom/SpeechesTestimony/giancarlostatement010418; J. Christopher Giancarlo, Chairman, CFTC, Giancarlo Commends SEC Chairman Clayton on ICO Statement (Dec. 11, 2017), https://www.cftc.gov/PressRoom/SpeechesTestimony/giancarlostatement121117.

Notably, in a keynote address on March 7, 2018, CFTC Commissioner Brian Quintenz not only asserted the agency's jurisdiction over digital asset derivatives, but also stated his support for an "independent, self-regulating body" for spot virtual currency transactions. Quintenz added that a self-regulatory organization for virtual currencies could "create uniform standards . . . reduce the possibility of regulatory arbitrage, and avoid duplicative regulation," which would address the concern of multiple federal and state regulators (including the CFTC) having jurisdiction over spot virtual currency transactions. *See* Brian Quintenz, Comm'r, CFTC, Keynote Address by Commissioner Brian Quintenz before the DC Blockchain Summit (Mar. 7, 2018), https://www.cftc.gov/PressRoom/SpeechesTestimony/opaquintenz8.

"actual delivery" exception to regulation of leveraged retail commodity transactions,[114] CFTC staff guidance,[115] and enforcement actions in both administrative and civil cases.[116] In May 2018, CFTC staff published guidance restating that "bitcoin and other virtual currencies are properly defined as commodities"[117]—an interpretation that a federal court accepted just months earlier.[118] The CFTC also launched LabCFTC in May 2017, which is designed to promote FinTech innovation in the markets under CFTC jurisdiction by providing a space for market participants to engage with the CFTC and potentially influence its future guidance and policy decisions over virtual currencies.[119]

---

[114] *See* Retail Commodity Transactions Involving Certain Digital Assets, 85 Fed. Reg. 37,734 (June 24, 2020) (final interpretative guidance) (interpreting 17 C.F.R. pt. 1) [hereinafter Actual Delivery Guidance]; *see also infra* Section 2.2(c).

[115] *See, e.g.*, CFTC, CFTC BACKGROUNDER ON OVERSIGHT OF AND APPROACH TO VIRTUAL CURRENCY FUTURES MARKETS (2018), https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/backgrounder_virtualcurrency01.pdf; CFTC, CUSTOMER ADVISORY: UNDERSTAND THE RISKS OF VIRTUAL CURRENCY TRADING (2017), https://www.cftc.gov/sites/default/files/idc/groups/public/@customerprotection/documents/file/customeradvisory_urvct121517.pdf; CFTC, CFTC BACKGROUNDER ON SELF-CERTIFIED CONTRACTS FOR BITCOIN PRODUCTS (2017), https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/bitcoin_factsheet120117.pdf.

[116] *See, e.g.*, *CFTC v. McDonnell*, 287 F. Supp. 3d 213 (E.D.N.Y. 2018) [hereinafter *McDonnell I*]; *In re BFXNA Inc.*, CFTC No. 16-19, [2016–2017 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 33,766 (June 2, 2016) [hereinafter *BFXNA Inc.*].

[117] CFTC Staff Advisory No. 18-14, Advisory with respect to Virtual Currency Derivative Product Listings (May 21, 2018), https://www.cftc.gov/sites/default/files/idc/groups/public/%40lrlettergeneral/documents/letter/2018-05/18-14_0.pdf. In the advisory, CFTC staff clarified its priorities and expectations with respect to new virtual currency products to be listed on a designated contract market (DCM) or swap execution facility (SEF), or cleared by a derivatives clearing organization (DCO). The advisory is intended to aid these entities in "effectively and efficiently" complying with their statutory and self-regulatory responsibilities. In light of the "significant risks associated with virtual currency markets," CFTC staff highlighted five key areas that require heightened attention when listing a new virtual currency contract on a SEF or DCM or clearing it through a DCO: (i) enhanced market surveillance, (ii) coordination with CFTC staff, (iii) large trader reporting, (iv) outreach to stakeholders, and (v) DCO risk management.

[118] *See McDonnell I*, 287 F. Supp. 3d at 213.

[119] As part of these efforts, LabCFTC issued a primer on virtual currencies, which is an educational tool for the public, not intended to offer any guidance or policy positions of the CFTC. *See* PRIMER ON VIRTUAL CURRENCIES, *supra* note 110. In November 2018, LabCFTC issued a primer on smart contracts, which is intended to help explain smart contract technology and related risks and challenges. *See* SMART CONTRACT PRIMER, *supra* note 79. One month later, LabCFTC published a request for public comments on cryptoasset mechanics and markets to help

Nevertheless, without express statutory authority over digital assets such as virtual currency, the CFTC's ability to regulate the virtual currency market necessarily depends on whether the particular virtual currency falls within the bounds of the CFTC's existing jurisdiction under the CEA. In particular, much of the CFTC's statutory authority hinges on the involvement of a "commodity."[120] Given the CFTC's longstanding interpretation that virtual currencies are commodities (implicitly, of the non-security type), many of the allegations in the CFTC's civil cases understandably are based on CEA provisions relating to the CFTC's jurisdiction over commodities.[121] Therefore, the question of whether virtual currencies are "commodities" is critical to the CFTC's larger efforts to regulate virtual currencies and, in particular, to prohibit fraud and manipulation.

If a particular virtual currency is a commodity under the CEA definition, another important jurisdictional question is triggered: whether it also is a security. Although the CFTC has jurisdiction over certain segments of the securities-based derivatives markets, the SEC, not

---

inform the CFTC in overseeing cryptocurrency markets and developing regulatory policy. *See* Request for Input on Crypto-Asset Mechanics and Markets, 83 Fed. Reg. 64,563 (Dec. 17, 2018).

[120] The CFTC may have authority over a non-commodity virtual currency to the extent it is the subject of a swap. The CEA defines "swap" in a manner that is not limited to contracts based on a commodity. Some of the provisions of the swap definition expressly list many items in addition to "commodities" (*see* 7 U.S.C. §§ 1a(47)(A)(i), (iii)), and others do not reference "commodities" at all (*see id.* §§ 1a(47)(A)(ii), (iv)).

[121] *See Coinflip*, Comm. Fut. L. Rep. (CCH) ¶ 33,538, at 77,855 (CEA section 4c(b), which restricts "any transaction involving any commodity which is . . . an 'option'"); *BFXNA Inc.*, Comm. Fut. L. Rep. (CCH) ¶ 33,766, at 79,389–90 (CEA section 2(c)(2)(D), which governs "any agreement, contract, or transaction in any commodity that is entered into with . . . a non-eligible contract participant"); *McDonnell I*, 287 F. Supp. 3d at 231; Complaint at 16, *CFTC v. My Big Coin Pay*, No. 1:18-cv-10077 (D. Mass. Jan. 16, 2018); Complaint at 15, *CFTC v. Gelfman Blueprint, Inc.*, No. 17-7181 (S.D.N.Y. Sept. 21, 2017) (CEA section 6(c)(1), which prohibits manipulative schemes and fraud "in connection [with any] contract of sale of any commodity in interstate commerce"); Complaint at 3, *CFTC v. Kantor*, No. 18-cv-2247 (E.D.N.Y. Apr. 16, 2018) (CEA section 2(e), which prohibits off-exchange retail transactions in swaps; CEA section 4d(a)(1), which prohibits soliciting or accepting orders, and accepting money, for commodity options or swap transactions without registration as a futures commission merchant). While the defendants in the initial administrative enforcement actions brought by the CFTC did not challenge the CFTC's interpretation of the commodity definition, defendants in the pending civil actions are litigating whether the relevant virtual currency is a commodity. *See infra* Section 2.3(e)(ii).

the CFTC, is responsible for oversight and regulation of the cash securities markets. The CFTC's assertion of jurisdiction over virtual currency cash markets presupposes that virtual currencies are not securities.

The Sections that follow explain the CFTC's regulatory authority over derivatives markets and certain retail transactions; the history and scope of, and interpretive issues under, the CEA's commodity definition; an examination of the CFTC's classification of virtual currencies as commodities over which it has jurisdiction; and allocation of jurisdiction between the CFTC and SEC.

2. Classification of Transactions under the CEA

The CEA regulates many (but not all) types of derivatives transactions, along with certain retail transactions that are not necessarily derivatives. The CEA imposes requirements on organized markets and clearing systems, industry professionals, and market participants with respect to different classifications of transactions, with further distinctions based on the nature of the underlying interest. The CEA approach is piecemeal, in that it prescribes separate requirements with respect to (i) contracts for the sale of commodities for future delivery (futures contracts);[122] (ii) options on commodities;[123] (iii) options on futures contracts;[124] (iv) swaps;[125] (v) over-the-counter (OTC) transactions with retail customers involving foreign currencies;[126]

[122] 7 U.S.C. § 2(a)(1). In addition to the categories identified in the text, the CEA has special provisions for regulating long-term contracts involving precious metals, referred to as "leverage contracts," but those contracts do not trade today and are not relevant for the analysis in this White Paper. The leverage contract provisions are set out in CEA section 19, 7 U.S.C. § 23.

[123] *Id.* § 6c(b).

[124] *Id.* § 2(a)(1).

[125] *Id.*

[126] *Id.* §§ 2(c)(2)(A)–(C).

and (vi) transactions in commodities that are not foreign currencies or securities with retail customers that are entered into or offered on a margined, leveraged or financed basis, unless the transaction fits within an exemption.[127]

Under this structure, the term "commodity" is one element that defines the CEA's reach over transactions and markets. Futures are defined by reference to commodities.[128] The term "commodity" also is used in the CEA's swap definition, but in sequence with other descriptive terms for permissible underlying interests. Thus, the commodity definition is relevant for purposes of understanding the broad scope of the swap definition, but arguably does not act as a limiting definitional element.

This Section explains the contours of CFTC jurisdiction over derivatives and retail transactions, and how that jurisdiction could apply to transactions involving virtual currencies. It also describes commercial forward and spot contracts that are outside the scope of CFTC regulation (but not necessarily outside the scope of its anti-fraud and anti-manipulation authority).

(a) Classifications of Regulated Transactions

A derivative is a contract whose value derives from the value of an underlying interest, such as a physical commodity, an interest rate, the economic or financial consequences of the occurrence of an event, or a security. Derivatives may take a variety of forms, and may require settlement by delivery (if held to expiration or, in the case of an option, upon exercise) of the underlying interest (which may occur via transfer of title) or by a cash payment. The following is

[127] *Id.* § 2(c)(2)(D).

[128] Conversely, as explained in Section 2.3(b) below, whether something is classified as a commodity for CEA purposes may depend on whether it is the subject of futures trading.

a high-level summary of the definitions for the different types of derivatives covered by the CEA.

Futures. The CEA does not contain a definition for the terms "futures contract" or "futures." The definitional elements are found in the CEA's grant of jurisdiction to the CFTC to regulate futures under CEA section 2(a)(1). Under that provision, futures contracts are "contracts of sale of a commodity for future delivery." The CEA does define the term "future delivery" or, more accurately, what the term does not mean, for the purpose of excluding from regulation as futures commercial merchandizing contracts for deferred delivery of a commodity.

Swaps. The term "swap" is defined in CEA section 1a(47) and CFTC Rule 1.3. The definition is broad and covers many types of derivative structures, specifically:

- Puts, calls, caps, floors, collars, or similar options on the value of one or more interest rates or other rates, currencies, commodities, securities (but options on securities also are excluded from the definition), instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind;

- Contracts for any purchase, sale, payment, or delivery (other than payment of a dividend on an equity security) that are dependent upon the occurrence, nonoccurrence, or extent of occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence (*i.e.*, event contracts or binary options);

- Executory contracts for the fixed or contingent exchange of one or more payments based on the value or level of one or more interest rates, other rates, currencies, commodities, securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind, or any interest therein or based on the value thereof, and that transfers, as between the parties to the transaction, in whole or in part, the financial risk associated with a future change in any such value or level without also conveying a current or future direct or indirect ownership interest in an asset (including any enterprise or investment pool) or liability that incorporates the financial risk so transferred, including contracts that become commonly known as one of an enumerated list of contracts such as interest rate swaps, currency swaps, agricultural swaps, or energy swaps;

- Contracts that are or in the future become commonly known to the trade as swaps;

- Security-based swap agreements that meet the definition of "swap agreement" under Section 206A of Gramm-Leach-Bliley Act,[129] a material term of which is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein; or

- Any combination or permutation of the foregoing types of contracts, including any option thereon.

The definition also contains some exclusions. Notably, security-based swaps, options on securities or a group or index of securities, and forwards on securities where the transactions are intended to be physically settled are not swaps.

Options. The term "option" is defined as a contract that is "of the character of, or . . . commonly known to the trade as, an 'option', 'privilege', 'indemnity', 'bid', 'offer', 'put', 'call', 'advance guaranty', or 'decline guaranty.'"[130] The interest underlying an option could be a commodity or another derivative, such as a futures contract or a swap. Under a typical option, the holder, or buyer, pays a premium for the right to require the counterparty, often called the "writer," to sell a commodity or other underlying interest to the option holder at a fixed strike price, in the case of a call option, or to purchase the commodity or other underlying interest from the option holder at a fixed strike price, in the case of a put option. In either case, the option holder has an "exercise right" to decide whether to require its counterparty to buy or sell the underlying interest. That right, depending upon the contract terms, may be exercisable at any time through the term of the option, during a narrowly defined time period at expiration or under other terms. An option on a commodity may be structured to require settlement by payment of cash for the difference between the strike price and current market price, in lieu of an actual sale and delivery of the commodity between the parties.

[129] 15 U.S.C. § 78c note.

[130] 7 U.S.C. § 1a(36).

(b) Primary Differences in CEA Regulation of the Different Types of Derivatives

Futures and Options on Futures. Futures and options on futures are grouped together for the same general regulatory treatment.[131] Futures and options on futures legally may be traded only on or subject to the rules of a futures exchange. The exchange must be registered with the CFTC as a DCM or, if the exchange is located outside the United States and has market participants located in the United States, it may operate under the CEA regime as an FBOT. Transactions in futures and options on futures must be centrally cleared by a derivatives clearing house. If the clearing house is clearing transactions in futures or options on futures that are listed on a DCM, the clearing house must be registered with the CFTC as a DCO. The CEA does not impose any restriction on who may trade on a DCM or FBOT.

Absent an exemption, a person that provides market participants with access to the exchanges and to their associated clearing houses must register with the CFTC as an FCM, whereas a person that assists market participants in arranging futures or options on futures transactions but does not act as a clearing intermediary may instead register with the CFTC as an IB. A person that provides trading advice to others with respect to the advisability of trading futures or options on futures generally must, absent an exemption, register with the CFTC as a CTA, and a person that forms and operates pooled investment vehicles that invest in such products generally must, absent an exemption, register with the CFTC as a CPO.

Transactions in futures and options on futures are not reported to a data repository. Information on the transactions is captured by the exchanges and clearing houses.

[131] *See* 17 C.F.R. pt. 33 (rules that the CFTC adopted pursuant to its plenary authority over options involving commodities, and that apply to options on futures).

Swaps. In contrast, swaps are not subject to an exchange-trading requirement, and not all swaps must be submitted to central clearing. The CFTC has authority to designate certain types of swaps for mandatory clearing, in which case the transactions must (absent an exemption) be centrally cleared, and also may have to be executed on a trading facility that is registered with the CFTC as a SEF or DCM. For swaps that have not been designated for mandatory clearing, counterparties may enter into transactions directly on a bilateral (*i.e.*, OTC) basis, or may voluntarily enter into transactions on a SEF or DCM if such a market is available. They also may voluntarily clear the transactions if a DCO is available that clears the type of swap.

To legally trade swaps on a SEF or bilaterally, a person must meet the definition of ECP set out in CEA section 1a(18) and CFTC Rule 1.3. If a person is not an ECP, the person generally is considered to be "retail." A person is not required to be an ECP to enter into swaps on a DCM.

For cleared swaps transactions, a person that provides clearing access to swaps counterparties must be registered as an FCM. Firms that assist counterparties in arranging swap transactions but that do not act as clearing intermediaries may do so pursuant to IB registration. A person that provides trading advice to others with respect to the advisability of trading swaps generally must, absent an exemption, register with the CFTC as a CTA, and a person that forms and operates pooled investment vehicles that invest in such products generally must, absent an exemption, register with the CFTC as a CPO.

Persons that hold themselves out as dealers or regularly enter into swaps with counterparties for their own account may have to register with the CFTC as swap dealers. Persons with substantial swap exposures may have to register with the CFTC as major swap participants.

Swap transactions must be reported to an SDR. This is the case regardless of whether the transaction is submitted to clearing.[132]

Commodity Options. The CEA grants the CFTC plenary authority to adopt rules regulating commodity options in CEA section 4c.[133] That authority does not extend to options on a security or a group or index of securities or any interest therein or based on the value thereof.[134] Commodity options also are covered by the statutory swap definition described above, and instead may be regulated under the swaps regime. The CFTC has determined to regulate commodity options under the same general rules that apply to swaps, with the exception of options on non-financial commodities under the "Trade Options Exemption."[135]

(c) Special Provisions for Regulating Retail Transactions under the CEA

Retail Forex. The CEA contains special provisions in section 2(c)(2)(B) that permit and regulate OTC trading of foreign currency futures and options on futures by retail customers, *i.e.*,

[132] If a transaction is submitted to and accepted for clearing, the resulting termination of the original transaction also must be reported to the SDR, and the DCO must report the novated trades replacing the original trade to an SDR.

[133] 7 U.S.C. § 6c(b).

[134] *See id.* § 2(a)(1)(C)(i)(I). The provision states that the CEA does not apply to options on securities or on any group or index of securities, or any interest therein or based on the value thereof. Such options also are excluded from the "swap" definition in CEA section 1a(47). Such options are included in the definitions of "security" in the Exchange Act and the Securities Act and are regulated by the SEC.

[135] As defined in CFTC Rule 32.3, a trade option is a commodity option that:

> (i) If exercised, must be settled physically, resulting in the sale and delivery of an exempt or agricultural commodity; and
>
> (ii) Is entered into between (A) an offeree (buyer) that (i) is a producer, processor, or commercial user of, or merchant handling the commodity or the products or by-products of the commodity (*i.e.*, it is a "commercial participant") and (ii) is entering into the transaction solely for purposes related to its business as such, and (B) an offeror (seller) that is either a commercial participant entering into the transaction solely for purposes related to its business or an eligible contract participant as defined in the CEA and CFTC Rule 1.3.

CFTC Rule 32.3 excludes trade options from classification as swaps and imposes substitute "light touch" regulation on the parties to such transactions.

by persons that are not ECPs as that term is defined in CEA section 1a(18) and CFTC Rule 1.3. It also contains comparable provisions in CEA section 2(c)(2)(C) that regulate trading by retail customers of any type of agreement, contract, or transaction in foreign currency, regardless of whether it could be classified as a future or a swap, if done on a leveraged, margined, or financed basis. The statutory provisions limit the persons permitted to engage in such trading with retail customers, certain of which are persons that are registered with the CFTC, such as an FCM or retail foreign exchange dealer.[136] They also authorize the CFTC to adopt rules for registering persons that act in the capacity of an IB, CTA, or CPO with respect to retail forex. The CFTC Part 5 Rules govern the retail forex activities of such persons registered with the CFTC.

Notably, the ECP definitions in CEA section 1a(18) and CFTC Rule 1.3 place a high bar for individuals to qualify, with the consequence that many individuals will be considered retail. For an individual to be considered an ECP, he or she must have amounts invested on a discretionary basis in excess of $10 million or in excess of $5 million if the individual is entering into transactions to manage risk associated with assets owned or liabilities incurred, or reasonably likely to be owned or incurred, by such individual.

Retail Commodity Transactions. CEA section 2(c)(2)(D) provides that agreements, contracts, or transactions in commodities—other than foreign currencies or securities—entered into by or offered to retail customers (non-ECPs) on a leveraged, margined, or financed basis must be regulated as or "as if" they are futures, unless covered by an exemption. As explained above, many customers who are individuals will be retail. Among other things, the "as if futures"

[136] The retail forex activities of other permissible counterparties may be regulated by other federal regulators. For example, firms registered with the SEC as broker-dealers are permitted to trade retail forex, but only as permitted and regulated by the SEC. The SEC currently prohibits broker-dealers from trading retail forex, with the effect that firms that are dually registered as broker-dealers and as FCMs are prohibited from that activity.

requirement arguably means that a non-exempt transaction may be executed only on or subject to the rules of a CFTC-regulated exchange, and persons providing services in connection with non-exempt transactions may be covered by one of the CEA's registration categories for professionals (FCM, IB, CTA, or CPO).

The CFTC has taken the position that tokens that may serve as a means of payment for goods or services as "virtual" currencies are not the same as currencies, and thus that bilateral retail transactions in virtual currencies may not occur under the rubric of the CEA's retail forex framework and instead are subject to the retail commodity transaction provisions. That is significant because retail forex transactions are not subject to the same restrictions that apply to margined, leveraged, or financed sales of commodities subject to CEA section 2(c)(2)(D).

As a threshold matter, the retail commodity provisions apply only when a party to the transaction is retail, *i.e.*, not an ECP. A second element must be present for a particular commodity sale transaction to be regulated under CEA section 2(c)(2)(D) as well: the seller must offer or execute the transaction on a leveraged or margined basis, or the transaction must be financed either directly by the seller or by a third party acting in concert with the seller. If not, then CEA section 2(c)(2)(D) is inapplicable, notwithstanding that the buyer is retail.

If both elements are present in a transaction (retail buyer; leveraged, margined, or financed transaction), there are two important exceptions under which the transaction nonetheless could occur off of a CFTC-regulated exchange (and without triggering potential FCM or other professional registration requirements).

The first exception, which receives the most attention, covers a transaction in a contract for the sale of a commodity that results in "actual delivery" of the commodity within 28 days. The CFTC has been wrestling for years with its interpretation of the term "actual delivery." In

August 2013, the CFTC issued a final interpretation of "actual delivery" in the context of CEA section 2(c)(2)(D) that generally focused on physical (tangible) commodities (the "2013 Guidance").[137] The 2013 Guidance emphasized that whether actual delivery is accomplished turns on a "functional approach" that considers facts beyond the language used by parties to the transaction. In that regard, the 2013 Guidance included a list of factors the CFTC will consider in determining whether a transaction has resulted in actual delivery. For example, actual delivery occurs if there is a transfer of title and possession of the commodity to the buyer or a depository acting on the buyer's behalf. In contrast, mere book entries and certain instances where a purchase is "rolled, offset, or otherwise netted with another transaction or settled in cash" do not constitute actual delivery.[138]

In recent years, the CFTC has focused on whether certain retail transactions in virtual currencies call for "actual delivery" and therefore are *not* required to be traded on regulated exchanges. The need to clarify the meaning of actual delivery in virtual currency transactions became more pronounced in 2016, when the CFTC brought its first enforcement action against a trading platform that offered retail commodity transactions in virtual currency without registering with the CFTC.[139] In its settlement order against Bitfinex, the CFTC took the position that delivery of bitcoin purchased with borrowed funds to a private, omnibus settlement wallet where the coins were held for the benefit of the buyer but also as collateral for the loan did not constitute actual delivery, because the buyer did not have any rights to access or use the

[137] Retail Commodity Transactions Under Commodity Exchange Act, 78 Fed. Reg. 52,426 (Aug. 23, 2013) [hereinafter 2013 Guidance].

[138] *Id.* at 52,429.

[139] *See BFXNA Inc.*, Comm. Fut. L. Rep. (CCH) ¶ 33,766.

purchased bitcoin until released by Bitfinex following satisfaction of the loan.[140] The CFTC noted that Bitfinex's "accounting for individual customer interests in the bitcoin held in the omnibus settlement wallet in its own database was insufficient to constitute 'actual delivery,'" following its position in the 2013 Guidance that "book entry" purporting to show delivery is insufficient.[141]

In March 2020, the CFTC addressed the uncertainty surrounding the concept of "actual delivery" in the context of digital asset transactions by issuing an interpretation (the "Actual Delivery Guidance").[142] More than two years earlier, in December 2017, the CFTC had issued a proposed interpretation on the same subject.[143] Consistent with the principles established in the 2013 Guidance and the litigation position taken against Bitfinex, the Actual Delivery Guidance explains that, in interpreting the term "actual delivery" for purposes of retail commodity transactions, the CFTC will employ a functional approach and examine how the transaction is marketed, managed, and performed, instead of relying solely on language used by the parties. Under the Actual Delivery Guidance, actual delivery occurs in retail virtual currency transactions when:

- a customer secures (i) possession *and* control of the entire quantity of the commodity, whether it was purchased on margin, or using leverage, or any other financing arrangement, and (ii) the ability to use the entire quantity of the commodity freely in commerce (away from any particular execution venue) no later than 28 days from the date of the transaction and at all times thereafter; and

[140] *See id*. at 79,390.

[141] *Id.* (quoting 2013 Guidance, 78 Fed. Reg. at 52,428).

[142] *See* Actual Delivery Guidance, 85 Fed. Reg. 37,734. The Actual Delivery Guidance became effective on June 24, 2020, three months after its adoption.

[143] Retail Commodity Transactions Involving Virtual Currency, 82 Fed. Reg. 60,335 (proposed Dec. 20, 2017) (to be codified at 17 C.F.R. pt. 1) [hereinafter Proposed Actual Delivery Guidance].

- the offeror and counterparty seller (including any of their respective affiliates or other persons acting in concert with the offeror or counterparty seller on a similar basis) do not retain *any* interest in, legal right, or control over any of the commodity purchased on margin, leverage, or other financing arrangement at the expiration of 28 days from the date of the transaction.[144]

The Actual Delivery Guidance provides further direction on "actual delivery" of virtual currency through illustrative examples. Some notable aspects of these examples include the following:

- Actual delivery will have occurred if, within 28 days of entering into a transaction, the virtual currency's public distributed ledger reflects the transfer of the entire quantity of the purchased virtual currency to the purchaser's blockchain address.

- Actual delivery will not have occurred if, within 28 days of entering into a transaction, the transaction is rolled, offset against, netted out, or settled in cash or virtual currency.

- When a transaction involves a depository that acts on behalf of the purchaser, three conditions must be met for actual delivery: (i) the offeror or seller has delivered the entire quantity of the virtual currency purchased into the possession of the depository; (ii) the purchaser has secured full control over the virtual currency; and (iii) the virtual currency delivered to the depository must be free of liens or other interests or legal rights of the offeror or seller 28 days after the transaction.

- A book entry made by the offeror or counterparty seller purporting to show delivery will not by itself establish actual delivery; instead, the entire quantity of the virtual currency purchased must have been delivered to the customer.[145]

The second exception from having to treat a contract for the sale of a commodity as or "as if" it were a futures contracts applies when (i) the contract creates an enforceable delivery obligation between the seller and the buyer, and (ii) the seller and the buyer have the ability to deliver and accept delivery of the commodity in connection with their respective lines of business. To date, the CFTC has declined to provide any interpretive guidance on this exception.

[144] Actual Delivery Guidance, 78 Fed. Reg. at 37,742–43.

[145] *Id.* at 37,743–44.

The focus on the commercial nature of the parties and the transaction suggests that this exception is a counterpart to the forward contract exclusions discussed below that exclude commercial merchandizing transactions from regulation as futures or swaps.

(d) Commercial Forward Contracts and Spot Contracts

The CFTC is not authorized under the CEA to adopt rules regulating trading in the cash markets for physical (or non-financial) commodities, known as forward or spot contracts or transactions, and the SEC, not the CFTC, regulates initial offerings of securities and secondary market trading of securities. The CFTC, though, does have certain authority to monitor the cash market activities of users of the derivatives markets, combined with authority to impose recordkeeping requirements on such persons relating to their cash market activities. The CFTC also has authority to require hedgers to file certain reports regarding their cash market positions and commercial operations.

Notably, the CEA makes it unlawful to manipulate or to attempt to manipulate the prices of any commodity, and vests the CFTC with authority to take enforcement action against any person that engages in such conduct. The CEA also classifies manipulation and attempted manipulation as criminal felonies, which may be prosecuted by the U.S. Department of Justice.

Commercial Forward Transactions. A forward contract is a commercial merchandizing contract between commercial parties where delivery of a non-financial commodity (such as an agricultural, energy, or metal commodity) is deferred for commercial reasons, the parties intend to make or take delivery of the commodity, and delivery routinely occurs. Forward contracts are excluded from regulation as futures pursuant to CEA section 2(a), in conjunction with section 1a(27), which provides that the term "future delivery" used in section 2(a) does not include "any sale of any cash commodity for deferred shipment or delivery." The exclusion is

not limited to forward contracts for non-financial commodities by its terms, but it historically has been applied to, and interpreted in the context of, sales of physical or tangible commodities.

The CEA swap definition expressly excludes forward contracts on "non-financial commodities" (and on securities), provided the parties intend to physically settle the transactions, with the consequence that such contracts are excluded from regulation as swaps. When the CFTC adopted its swap product definition rules in August 2012, it stated that it would interpret the forward contract exclusion from the futures and swap definitions in a consistent manner.[146]

Spot Contracts. Spot contracts are commercial contracts for the sale of a commodity for delivery within two days, or such other short timeframes consistent with applicable market convention, under which the commodity is typically delivered. Spot contracts generally are outside the regulatory ambit of the CEA (apart from the anti-fraud and anti-manipulation provisions or potential application of the retail forex or retail commodity transaction provisions described above).

(e) CFTC Registration Requirements for Virtual Currency Market Participants

Market participants that are dealing in, or providing services related to, derivatives on a virtual currency may be required to register with the CFTC. The CEA establishes different registration categories based on a participant's activities. The chart below summarizes the CEA registration categories.[147]

[146] *See* Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48,207, 48,227–28 (Aug. 13, 2012) [hereinafter Swap Definition Rule]. When it adopted the swap product definition rules, the CFTC also provided extensive interpretive guidance for determining whether contracts on non-financial commodities should be classified as excluded forward contracts. The analysis is fact intensive, based on the specific circumstances.

[147] The registration requirements in this chart presume that the virtual currencies are not securities. If the virtual currency is a security, a market participant may have to register with the SEC or, in some cases, with both the CFTC and the SEC (for example, if the derivative is a futures contract on a virtual currency that is a security).

Registration Category	Registration Requirement
Swap Dealer (SD)	An entity that either (i) holds itself out as a dealer in swaps on virtual currencies; (ii) makes a market in swaps on virtual currencies; (iii) regularly enters into swaps in virtual currencies for its own account in the ordinary course of business; or (iv) engages in activities causing it to be commonly known as a dealer or market maker in swaps on virtual currencies, must register with the CFTC and become a member of the NFA, unless certain exceptions apply. For instance, a dealer is not required to register with the CFTC if the gross notional value of its swap dealing trades, combined with those of its affiliates, over the prior 12 months is below $8 billion.[148]
Major Swap Participant (MSP)	An entity that is not an SD but maintains a position in swaps on virtual currencies that is substantial enough that the entity's default could have adverse effects on the financial stability of the U.S. banking system is required to register with the CFTC and become an NFA member.[149]
Futures Commission Merchant (FCM)	An entity that (i) "engages in soliciting or accepting orders for" futures or swaps on virtual currencies, options on futures on virtual currencies, retail off-exchange foreign exchange contracts, or swaps on virtual currencies; and (ii) in connection with those activities, accepts any money, securities, or property, or extends credit in lieu thereof to margin, guarantee, or secure the resulting trades must register with the CFTC and become an NFA member, unless an exemption applies.[150]
Introducing Broker (IB)	An entity that "engages in soliciting or accepting orders for" futures or swaps on virtual currencies but does not accept any money, securities, or property from customers, or extend credit in lieu thereof, to margin, guarantee, or secure the resulting trades must register with the CFTC and become an NFA member, unless an exemption applies.[151]
Commodity Pool Operator (CPO)	An entity that operates a commodity pool (i.e., "any investment trust, syndicate, or similar form of enterprise operated for the purpose of trading in commodity interests"), or an investment trust, syndicate, or other pooled investment vehicle that invests in derivatives on virtual currencies, must register with the CFTC and become an NFA member, unless certain exemptions apply.[152]

[148] 7 U.S.C. § 1a(49); 17 C.F.R. § 1.3.

[149] 7 U.S.C. § 1a(33); 17 C.F.R. § 1.3.

[150] 7 U.S.C. § 1a(28); 17 C.F.R. § 1.3.

[151] 7 U.S.C. § 1a(31); 17 C.F.R. § 1.3.

[152] 7 U.S.C. § 1a(11); 17 C.F.R. § 1.3.

Registration Category	Registration Requirement
Commodity Trading Advisor (CTA)	An entity that advises others on trading in futures, swaps, and other derivatives on virtual currencies for compensation or profit must register with the CFTC and become an NFA member, unless certain exemptions apply.[153]
Associated Person (AP)	An individual who solicits customers or supervises others who solicit customers on behalf of any of the registered entities above (other than SDs or MSPs) must register with the CFTC and become a member of the NFA. APs of SDs or MSPs are subject to a fitness screening.[154]

Any person registered in one of the foregoing capacities (with the exception of an AP of a swap dealer) also must become a member of the NFA.[155] NFA is a self-regulatory organization for industry professionals, created in 1976 pursuant to statutory authority.[156] It is registered with the CFTC as a "registered futures association" and is subject to CFTC oversight. Members of NFA are bound by NFA's rules, and subject to NFA's self-regulatory oversight and disciplinary authority.[157]

[153] 7 U.S.C. § 1a(12); 17 C.F.R. § 1.3.

[154] 7 U.S.C. § 1a(4); 17 C.F.R. §§ 1.3, 5.1(h)(2).

[155] *See* 17 C.F.R. §§ 3.2, 3.12. CFTC Rule 170.17, 17 C.F.R. § 170.17, provides a narrow exception to the NFA membership requirement to a person that is registered as a CTA if the person meets the criteria in CFTC Rule 4.14(a)(9), which provides that the CTA does not "[d]irect[] client accounts" or "[p]rovid[e] commodity trading advice based on, or tailored to, the commodity interest or cash market positions or other circumstances or characteristics of particular clients." 17 C.F.R. § 4.14(a)(9). Individuals who are "principals" of a registered firm also are subject to fitness screening by NFA. As defined in CFTC Rule 3.1(a), 17 C.F.R. § 3.1(a), the term covers individuals who are in a position to exercise a controlling influence over activities of the firm that are subject to CFTC regulation, such as a board member, president, chief executive officer, chief operating officer, chief financial officer, or head of a business division engaged in CFTC-regulated activities. It also covers individuals who (directly or indirectly) have a 10% or more financial or ownership interest in any class of the firm's voting securities, or have contributed 10% or more of the firm's capital.

[156] 7 U.S.C. § 21.

[157] NFA's oversight can extend to the activities of members relating to digital assets. In that regard, NFA adopted an interpretative notice that took effect on October 31, 2018, which imposes disclosure obligations on FCMs, IBs, CTAs, and CPOs regarding virtual currency derivative and underlying or spot virtual currencies.

3. The CFTC's Treatment of Virtual Currencies as Commodities

(a) The CEA "Commodity" Definition

As the structure of the CEA illustrates, determining whether the CFTC has jurisdiction over transactions involving virtual currencies in large part turns on whether they fall within the CEA's commodity definition, which defines the CEA's reach over transactions and markets. The commodity definition includes two categories, one narrow and one that potentially is very broad: (i) an enumerated list of agricultural commodities; and (ii) "all other goods and articles . . . and all services, rights, and interests . . . in which contracts for future delivery are presently or in the future dealt in" (with two limited exceptions).[158]

The definition—which has not been amended since 2010[159]—understandably does not expressly reference virtual currencies. The legislative history behind the commodity definition, however, provides insight as to whether the definition should be interpreted to contemplate including virtual currencies. The second, broad category of the commodity definition was added to the CEA in 1974, to grant the newly created CFTC expansive authority over futures markets. By establishing a far more open-ended definition of "commodity," Congress provided the CFTC substantial latitude to determine the scope of its authority through its interpretation of the flexible category. However, as illustrated by the CFTC's recent attempts to combat alleged fraud in the virtual currency markets, the CFTC's assertion of expansive authority over non-derivative markets generates interpretative issues as market participants seek clarity regarding the bounds of the CFTC's authority.

[158] 7 U.S.C. § 1a(9).

[159] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 721(a), 741(b)(10), 124 Stat. 1376, 1658, 1732 (2010).

(b) Evolution of the CEA "Commodity" Definition

Until 1974, Congress specified the bounds of commodity futures regulation through the narrow commodity definition, and expanded it over time on a commodity-by-commodity basis to regulate additional markets that Congress determined warranted regulation. Congress first enacted the Grain Futures Act in 1922[160] to regulate futures trading in "grain," which was defined by the Act to mean "wheat, corn, oats, barley, rye, flax, and sorghum."[161] In 1936, Congress replaced the Grain Futures Act with the CEA to address limitations from the use of the "grain" definition.[162] Congress replaced the term "grain" with "commodity" in an effort to make the CEA more generally applicable to any additional item that Congress later determined should be subject to futures regulation.[163] The CEA also expanded the list of commodities (and, therefore, the Commodity Exchange Authority's jurisdiction) to include cotton, rice, mill feeds, butter, eggs, and Solanum tuberosum (Irish potatoes).[164]

Over the years, Congress expanded the coverage of the CEA by amending the commodity definition to add specified commodities such as "fats and oils . . . cottonseed meal, cottonseed, peanuts, soybeans, and soybean meal" and "frozen concentrated orange juice."[165] Before

[160] Grain Futures Act, Act of Sept. 21, 1922, Pub. L. No. 67-331, 42 Stat. 998 (1922). The Grain Futures Act replaced the Future Trading Act, Act of Aug. 24, 1921, Pub. L. No. 67-66, 42 Stat. 187 (1921), which the Supreme Court found to be unconstitutional in *Hill v. Wallace*, 259 U.S. 44 (1922).

[161] 7 U.S.C. § 2 (1925).

[162] Act of June 15, 1936, Pub. L. No. 74-675, 49 Stat. 1491 (1936).

[163] *Regulation of Grain Exchanges: Hearing Before the H. Comm. on Agric.*, 73rd Cong. 11 (1934) (statement of J.M. Mehl, Assistant Chief Grain Futures Admin., U.S. Dep't of Agric.); *see also* H.R. REP. NO. 1522, at 2 (1934).

[164] 7 U.S.C. § 2 (1934 & Supp. II 1936).

[165] Act of Jul. 23, 1968, Pub. L. No. 90-418, 82 Stat. 413 (codified at 7 U.S.C. § 2 (1964 & Supp. IV v. 1 1968)).

Congress established the CFTC, however, the commodity definition covered enumerated agricultural commodities only.

The 1974 amendments reflected a notable departure from Congress's traditional approach as the new definition of "commodity" not only retained the list of agricultural commodities but added a category of goods, articles, services, rights, and interests that contemplated the CFTC's exercise of jurisdiction over additional commodities without congressional action.

The current commodity definition maintains the revised structure set by Congress in 1974:

> The term "commodity" means wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, Solanum tuberosum (Irish potatoes), wool, wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil, and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans, soybean meal, livestock, livestock products, and frozen concentrated orange juice, and all other goods and articles, except onions (as provided by section 13-1 of this title) and motion picture box office receipts (or any index, measure, value, or data related to such receipts), and all services, rights, and interests (except motion picture box office receipts, or any index, measure, value or data related to such receipts) in which contracts for future delivery are presently or in the future dealt in.[166]

The breadth of the commodity definition is evidenced by the fact that Congress has carved out only onions and movie box office receipts from the commodity definition, in 1974 and 2010,[167] respectively.

The expanded commodity definition, while granting the CFTC expansive authority over the commodity futures markets, invites questions on the limits to the CFTC's jurisdiction. This issue is most apparent in the context of novel products involving underlying interests that do not resemble the commodities enumerated in the statutory definition. Under the more expansive

[166] 7 U.S.C. § 1a(9).

[167] Dodd-Frank Act, *supra* note 159, § 721(a), 124 Stat. at 1659.

commodity definition, each novel product over which the CFTC exercises authority raises the question of whether the agency is extending its jurisdiction farther than Congress intended. This question is particularly relevant in circumstances where the CFTC is not exercising its authority in the futures or swaps markets, over which the CFTC's jurisdiction is plenary and clear,[168] but rather in the spot or cash markets, where the CFTC's authority is limited to anti-fraud and anti-manipulation enforcement, or pursuant to its authority to regulate certain retail commodity transactions.

(c) Interpretative Issue Raised by the Commodity Definition: Does a Virtual Currency Require the Existence of Overlying Futures Contracts to Be Deemed a Commodity?

As virtual currencies are not any of the enumerated agricultural commodities, whether the CFTC has jurisdiction over transactions in virtual currencies depends (with limited exception[169]) on whether they fall within any of the categories in the second portion of the definition—"goods and articles . . . [or] all services, rights, and interests . . . in which contracts for future delivery are presently or in the future dealt in." One interpretative question related to the treatment of virtual currencies under this portion of the commodity definition is whether a futures contract on a virtual currency must already exist for such virtual currency to be considered a "commodity."

There are different ways to read the second category of the commodity definition. The first, and narrowest, approach to understanding this phrase is that only goods, articles, services, rights, and interests on which a futures contract exists are "commodities" under the CEA. This reading necessarily makes the existence of futures trading on a commodity a prerequisite for the CFTC to assert its authority over something as a commodity. Accordingly, although the CEA

[168] 7 U.S.C. § 2(a)(1).

[169] As explained above, CEA regulation of swaps is not limited to swaps on commodities.

definition contemplates futures contracts that are "in the future dealt in," a commodity would not be deemed to be a "commodity" for purposes of the CEA definition until it was the subject of a futures contract.[170]

A variation of this reading is that the futures trading element qualifies only "services, rights, and interests," and not "goods and articles." If this interpretation applies, it is then necessary to determine whether a virtual currency is a good or article. If so, futures trading is not a prerequisite to classifying the virtual currency as a commodity, but if it instead is a service, right, or interest, the futures trading element is relevant.

Under a broad reading, the commodity definition encapsulates all goods, articles, services, rights, and interests on which a futures contract exists, as well as any other commodity that could be the subject of futures trading in the future.[171] Under this interpretation, the CFTC would have jurisdiction over a commodity so long as it is possible that the commodity could be the subject of a futures contract and would not necessarily require a futures market to exist prior to the CFTC asserting its jurisdiction over that commodity.

Finally, the middle-ground approach is that there needs to be an overlying futures contract, but not necessarily on the precise item, as long as there is a futures contract on another item that belongs to the same category of commodity. As explained further below in Section 2.3(e)(ii), the court in *CFTC* v. *My Big Coin Pay*[172] took this stance and held that the CFTC has enforcement jurisdiction over MBC, a virtual currency that had no overlying futures

[170] The definition's "in the future" language could be read by reference to the definition's establishment in 1974, such that Congress intended that the CFTC's jurisdiction not be limited by the futures contracts already in existence at that time but rather would extend to any commodity over which a futures contract was established thereafter.

[171] *See* CFTC, STATEMENT OF THE COMMISSION (2010), http://www.cftc.gov/ucm/groups/public/@otherif/documents/ifdocs/mdexcommissionstatement061410.pdf.

[172] *CFTC v. My Big Coin Pay, Inc.*, 334 F. Supp. 3d 492 (D. Mass. 2018).

contract, because futures contracts did exist for bitcoin, and MBC and bitcoin belonged to the same category of commodity.

Evaluating each interpretative approach through the lens of the legislative history of the commodity definition offers some additional insight, though not a clear answer as to how this condition should be understood. All four possible readings of the definition seemingly would be consistent with Congress's intent in 1974 to end its longstanding approach to specifying the bounds of commodity regulation through enumerating the commodities over which agency jurisdiction could be exercised. Even under the narrowest reading of the commodity definition, the interest underlying any futures trading that developed after 1974 would be included in the definition, thereby avoiding an outcome where expanding the CFTC's authority depends on congressional action.

The narrowest approach, however, would limit the CFTC's jurisdiction by tying the CFTC's authority directly to commodities that already are encompassed by futures trading. This outcome seemingly raises a concern similar to that which influenced Congress's first legislative approach, because the CFTC's authority would again depend on congressional action to combat fraud and manipulation with respect to a commodity that was not yet subject to a futures contract. On the other hand, the original public interest justification for regulating futures markets is based on the interrelationship between futures markets and underlying cash markets, suggesting the narrowest approach is consistent with congressional intent.

Under the expansive reading of the definition, the CFTC would not be subject to this limitation, as it would be able to regulate an emerging commodity so long as a futures market for that commodity conceivably could develop. However, the expansive reading may create as many problems as it solves. Under this reading, the CFTC's anti-fraud and anti-manipulation authority

could be read to capture *any* good, article, service, right, or interest, including those that do not necessarily have any connection to the futures markets.[173]

The middle-ground approach avoids the untenable implications of the expansive reading, but still begs the question of what items would be deemed to belong to the same "category" of commodity and thus subject to the CFTC's jurisdiction. That question could become more salient in the regulation of virtual currencies as different virtual currencies develop distinct characteristics. For example, virtual currencies may possess all or some of the characteristics of payment tokens, utility tokens, asset tokens, and hybrid tokens, and the virtual currencies' characteristics may even evolve over time.

How these interpretative issues are resolved is important to the question of whether virtual currencies are subject to the CFTC's jurisdiction under the CEA. Only one virtual currency, bitcoin, currently is the subject of exchange-listed futures trading.[174]

(d) Another Interpretative Question: If Virtual Currencies Are Commodities, What Type of Commodity Are They?

The CEA makes distinctions based on the type or classification of a commodity. It refers in various provisions to securities, foreign currencies, non-financial commodities, agricultural commodities, excluded commodities, and exempt commodities, and includes definitions of the latter two classifications.

[173] Press Release, Bart Chilton, Comm'r, CFTC, Statement on MDEX Application Regarding Box Office Receipt Contracts (June 14, 2010), https://www.cftc.gov/PressRoom/SpeechesTestimony/chiltonstatement061410.

[174] Futures generally are subject to an exchange-trading requirement. Thus, listing on a futures exchange is not an element of the futures contract definition, but a consequence that follows from classification of a contract as a futures contract. To the extent that futures trading is permitted to occur outside the exchange-trading requirement or occurs in disregard of that requirement, such trading also could provide a basis under the narrow interpretation for classifying the interests underlying such trading as commodities.

Classification of a virtual currency as a security or non-security is important, because the CEA and federal securities laws allocate jurisdiction over securities-related derivatives between (or jointly to) the CFTC and SEC, as explained more fully below. Thus, there is potential for conflicting assertions of jurisdiction over transactions in virtual currencies if the CFTC and SEC take different positions on whether a particular virtual currency is a security.

If a virtual currency is a non-security commodity, another important distinction is whether it could be considered a foreign currency. As explained above, the CFTC takes the position that virtual currencies are not currencies, with the consequence that retail transactions involving virtual currencies could not operate under the more favorable CEA framework governing retail forex, and instead must be considered under the more restrictive provisions applicable to retail commodity transactions.

If virtual currencies are not considered to be foreign currencies, that also means that physical delivery swaps involving virtual currencies are outside the scope of the Treasury Department's determination to exclude deliverable foreign exchange forwards and foreign exchange swaps from the CEA's definition of "swap." Transactions that are covered by the Treasury Department's determination would not be subject to swap regulations except for swap data reporting and business conduct standards applicable to swap dealers.[175]

The distinction between excluded commodities and exempt commodities also is relevant to the extent that it is a proxy for distinguishing financial commodities from non-financial commodities. The term "excluded commodity," added to the CEA by Congress in 2000,[176]

[175] 7 U.S.C. §§ 1a(47)(E)(iii)–(iv).

[176] Act of Dec. 21, 2000, Pub. L. No. 106-554, 114 Stat. 2763 (2000); *see also* H.R. REP. NO. 106-711, pt. 1, at 33 (2000).

means:

> (i) an interest rate, exchange rate, currency, security, security index, credit risk or measure, debt or equity instrument, index or measure of inflation, or other macroeconomic index or measure;
>
> (ii) any other rate, differential, index, or measure of economic or commercial risk, return, or value that is—
>
> > (I) not based in substantial part on the value of a narrow group of commodities not described in clause (i); or
> >
> > (II) based solely on one or more commodities that have no cash market;
>
> (iii) any economic or commercial index based on prices, rates, values, or levels that are not within the control of any party to the relevant contract, agreement, or transaction; or
>
> (iv) an occurrence, extent of an occurrence, or contingency (other than a change in the price, rate, value, or level of a commodity not described in clause (i)) that is—
>
> > (I) beyond the control of the parties to the relevant contract, agreement, or transaction; and
> >
> > (II) associated with a financial, commercial, or economic consequence.[177]

The term "exempt commodity" means "a commodity that is not an excluded commodity or an agricultural commodity."[178] This definition thus is a catchall category that includes energy interests and precious metals. Exempt commodities and agricultural commodities together generally cover commodities that are considered non-financial.

The regulatory implications of the excluded versus exempt commodity characterization are most notable where market participants are transacting in forwards or swaps based on virtual currencies. If virtual currencies are considered to be excluded commodities, the forward contract exclusions discussed above probably are not available, because the exclusion from the "swap"

[177] 7 U.S.C. § 1a(19).

[178] *Id.* § 1a(20).

definition is by its terms limited to non-financial commodities, and the exclusion from the futures definition typically is read to apply to non-financial commodities.

The CFTC's Trade Option Exemption, which excludes qualifying options from regulation as swaps, by its terms is limited to options on exempt or agricultural commodities, and thus would be unavailable for options on virtual currencies if the virtual currency is classified as an excluded commodity.[179]

Virtual currencies defy easy categorization because of their diverse characteristics and evolving uses. In the simplest reading, the term virtual currency necessarily includes the term "currency," which suggests that virtual currencies can be used as a means of payment and, as such, should be treated like a currency for regulatory purposes.[180] The CFTC nonetheless has declined to treat virtual currencies the same as currencies. Bitcoin and other virtual currencies also arguably share characteristics with precious metals, which historically have been treated as exempt commodities, due to individuals' belief in their intrinsic use and value. Virtual currencies exist in limited supply, often are capable of delivery, and are capital goods used to produce other goods and services.[181] The CFTC has not yet definitively resolved the question of whether virtual currency is an excluded or exempt commodity.

[179] 17 C.F.R. § 32.3(a). Entities that qualify for the Trade Option Exemption still must comply with certain CFTC rules, such as certain of the Part 23 rules for Swap Dealers and Major Swap Participants and the capital and margin requirements for Swap Dealers and Major Swap Participants. *See id.* § 32.3(c).

[180] Indeed, bitcoin, the leading virtual currency today, already is being used as a means of payment in some cases. *See, e.g.*, Kenneth Rapoza, *Goldman Sachs Caves: Bitcoin Is Money*, FORBES (Jan.10, 2018, 11:15 AM), https://www.forbes.com/sites/kenrapoza/2018/01/10/goldman-sachs-caves-bitcoin-is-money/.

[181] Houman B. Shadab, Regulating Bitcoin and Block Chain Derivatives, Written Statement to the CFTC Global Markets Advisory Committee 5 (Oct. 9, 2014), https://www.cftc.gov/sites/default/files/idc/groups/public/@aboutcftc/documents/file/gmac_100914_bitcoin.pdf.

When asserting that virtual currencies are commodities, though, the CFTC's statements to date suggest that it considers virtual currencies to be exempt commodities. For example, in *Coinflip*, the CFTC stated that "Bitcoin and other virtual currencies are distinct from 'real' currencies, which are the coin and paper money of the United States or another country that are designated as legal tender, circulate, and are customarily used and accepted as a medium of exchange in the country of issuance."[182] Further, the CFTC seemingly suggested that virtual currencies are exempt commodities by considering whether the bitcoin options at issue in *Coinflip* were offered pursuant to the Trade Option Exemption under CFTC Rule 32.3.[183] This apparent approach is consistent with public statements made by CFTC and SEC leadership contrasting virtual currencies with traditional currencies.[184]

In the consent order that the CFTC later entered into with Bitfinex, the CFTC similarly signaled that it may view virtual currencies as exempt, not excluded, commodities. The CFTC there referred to CEA section 2(c)(2)(D) when reasoning that the margined virtual currency transactions that were offered by Bitfinex did not qualify for an exception from CFTC jurisdiction over retail commodity transactions.[185] CEA section 2(c)(2)(D) is a provision that applies to retail commodity transactions, rather than the analogous retail foreign exchange transaction exception. By evaluating the legality of Bitfinex's virtual currency transactions by

[182] *Coinflip*, Comm. Fut. L. Rep. (CCH) ¶ 33,538, at 77,855 n.2.

[183] *Id*. at 77,856 & n.5.

[184] Jay Clayton & J. Christopher Giancarlo, *Regulators are Looking at Cryptocurrency*, WALL ST. J. (Jan. 24, 2018, 6:26 PM), https://www.wsj.com/articles/regulators-are-looking-at-cryptocurrency-1516836363 ("But cryptocurrencies lack a fundamental characteristic of traditional currencies, namely sovereign backing. They also lack other hallmarks of traditional currencies, such as governance standards, accountability and oversight, and regular and reliable reporting of trading and related financial data. Significantly, cryptocurrencies are now being promoted, pursued and traded as investment assets, with their purported utility as an efficient medium of exchange being a distant secondary characteristic.").

[185] *BFXNA Inc.*, Comm. Fut. L. Rep. (CCH) ¶ 33,766, at 79,389–90.

reference to the retail commodity provision rather than its retail foreign currency counterpart, the CFTC signaled that it may view virtual currency as an exempt commodity.

The CFTC made clear that its interpretation would apply to retail commodity transactions and would not apply to retail foreign currency transactions covered by CEA section 2(c)(2)(C) in its subsequent proposed interpretation and request for comment regarding how the "actual delivery" exception would apply to virtual currencies.[186] The CFTC explained that it considered virtual currencies to be "like many other intangible commodities that the Commission has recognized over the course of its existence (*e.g.*, renewable energy credits and emission allowances, certain indices, and certain debt instruments, among others). Indeed, since their inception, virtual currency structures were proposed as digital alternatives to gold and other precious metals."[187]

Although the principal attributes of virtual currencies are important in determining how to categorize them under the CEA, it also will be important for the CFTC to consider how any future determination compares to statements it already has made or actions it already has taken. For example, if the CFTC determined that virtual currencies are excluded commodities because of their use as a medium of exchange and payment, such a determination would seem consistent with the CFTC's prior conclusion that excluded commodities "generally are financial," whereas "exempt and agricultural commodities by their nature generally are nonfinancial."[188] On the

[186] *See* Proposed Actual Delivery Guidance.

[187] *Id.* at 60,337–38 (footnote omitted) (citing Swap Definition Rule) (discussing application of the swap forward exclusion to intangible commodities)).

[188] Swap Definition Rule, 77 Fed. Reg. at 48,232; *see also* CFTC, Excluded Commodity, CFTC GLOSSARY (last visited Nov. 11, 2020), https://www.cftc.gov/ConsumerProtection/EducationCenter/CFTCGlossary/glossary_e.html ("Excluded Commodity: In general, the Commodity Exchange Act defines an excluded commodity as: any financial instrument such as a security, currency, interest rate, debt instrument, or credit rating; any economic or commercial

other hand, the CFTC would be tasked with reconciling its decision to put virtual currencies in the same "excluded" category as fiat currencies with prior CFTC statements (some of which we have described above), as well as current positions of agencies such as the IRS and FinCEN,[189] which found virtual currencies to be dissimilar to fiat currencies, irrespective of their potential use as a payment medium.[190] The CFTC also would need to distinguish the main characteristics of virtual currency from other exempt commodities that similarly have intrinsic value in order to avoid calling into question whether other exempt commodities may fall within the excluded commodity category. Conversely, if the CFTC were to categorize virtual currencies as exempt commodities, it would need to go through a similar exercise. Further complicating the CFTC's task is the development of new types of virtual currencies that may operate like a traditional currency, such as "stablecoins" whose prices are tied to a fiat currency.

It is against this backdrop of the commodity definition—and the outstanding questions related to the scope and content of the definition—that the CFTC asserted its jurisdiction over virtual currencies. As the discussion below explains, having definitively determined that virtual currencies are commodities (implicitly as non-securities), the CFTC faces numerous challenges regarding its regulatory approach to them.

---

index other than a narrow-based commodity index; or any other value that is out of the control of participants and is associated with an economic consequence. See the Commodity Exchange Act definition of excluded commodity.").

[189] Both the IRS and FinCEN have interpreted virtual currencies not to be "currencies." *See* I.R.S. Notice 2014-21, 2014-16 I.R.B. 938; FINCEN, FIN-2013-G001, APPLICATION OF FINCEN'S REGULATIONS TO PERSONS ADMINISTERING, EXCHANGING, OR USING VIRTUAL CURRENCIES (2013), https://www.fincen.gov/sites/default/files/shared/FIN-2013-G001.pdf [hereinafter FIN-2013-G001].

[190] CFTC Staff Advisory No. 18-14, at 2 (May 21, 2018), https://www.cftc.gov/sites/default/files/idc/groups/public/%40lrlettergeneral/documents/letter/2018-05/18-14_0.pdf ("The Commission interprets the term 'virtual currency' broadly, to encompass any digital representation of value that functions as a medium of exchange and any other digital unit of account used as a form of currency.").

(e) The CFTC's Asserted Jurisdiction over Virtual Currencies as Commodities

Key regulatory consequences flow from the CFTC's determination that bitcoin and other virtual currencies are commodities, and of a type that are not securities. First, the CFTC possesses anti-fraud and anti-manipulation authority over such commodities in interstate commerce, so to the extent the CFTC finds fraud or manipulation occurring in connection with virtual currencies, it can take enforcement action. Second, the CFTC has full regulatory authority over derivatives on virtual currencies that are not securities, such as futures contracts. We discuss below the basis for the CFTC's critical determination that virtual currencies are commodities, challenges to that determination, and the responsive actions taken by the Commission.

i. Basis for the CFTC's View That Virtual Currencies Are Commodities

The CFTC initially articulated its position that virtual currencies are commodities through administrative proceedings. However, in each of those matters, the CFTC did not provide many, if any, supporting points to explain its reasoning or criteria for determining that virtual currencies were commodities. As explained below in Section 2.3(e)(ii), it was not until defendants challenged the CFTC's asserted jurisdiction in civil actions that the CFTC came forward with a more substantial explanation for its authority over virtual currencies.

In September 2015, the CFTC determined for the first time that "Bitcoin and other virtual currencies are encompassed in the [commodity] definition and properly defined as commodities" in its settlement agreement with Coinflip, Inc., a trading platform.[191] The CFTC based that conclusion on two factors: (i) the statutory definition of commodity includes "all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in," and

[191] *Coinflip*, Comm. Fut. L. Rep. (CCH) ¶ 33,538, at 77,855.

(ii) the definition of a commodity is "broad."[192] But the consent order provides no additional, more specific explanation as to why bitcoin and virtual currencies fall within the "services, rights, and interests" commodity definition category. Under the terms of the order, Coinflip agreed to cease and desist from its conduct but was not required to pay a civil monetary penalty—a relatively rare occurrence in a CFTC enforcement action. Perhaps the CFTC refrained from imposing a civil monetary penalty because this was a "first of its kind" case—the CFTC's first step in providing notice to the market of its assertion of enforcement authority over virtual currencies.

A week after the Coinflip settlement, the CFTC settled with TeraExchange, LLC, a registered SEF, regarding allegations that the SEF failed to prevent wash trading by publicizing the execution of non-deliverable forward contracts based on the value of the U.S. dollar and bitcoin without disclosing that the trades were prearranged.[193] The CFTC relied on its initial determination in *Coinflip*, stating in a footnote of its order: "Bitcoin is a commodity under Section 1a of the Act . . . and is therefore subject as a commodity to applicable provisions of the Act and Regulations."[194] The order provided no further explanation or reasoning.

In June 2016, the CFTC settled with an online platform, Bitfinex, regarding allegations that Bitfinex engaged in illegal, off-exchange retail commodity transactions without registering as an FCM.[195] Bitfinex engaged in different activities than the defendants in the first two enforcement actions. Unlike the platforms in the first two settlement orders, which involved

---

[192] *Id.* (quoting 7 U.S.C. § 1a(9); citing *Bd. of Trade of City of Chi. v. SEC*, 677 F.2d 1137, 1142 (7th Cir. 1982)).

[193] *In the Matter of TeraExchange LLC*, CFTC No. 15-33, [2015–2016 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 33,546, at 77,893–94 (Sept. 24, 2015).

[194] *Id.* at 77,894 n.3.

[195] *BFXNA Inc.*, Comm. Fut. L. Rep. (CCH) ¶ 33,766, at 77,854–55.

derivatives on virtual currencies, Bitfinex offered leveraged trading in virtual currencies, primarily bitcoin. Nevertheless, the CFTC—here too, relying simply on its previous *Coinflip* and *TeraExchange* orders—emphasized that "Bitcoin and other virtual currencies are encompassed in the definition and properly defined as commodities."[196] According to the CFTC, Bitfinex's platform constituted unlawful futures trading because it did not occur on a registered exchange.[197] Also, because Bitfinex directly accepted customer funds and trading orders, it allegedly should have registered with the CFTC as an FCM, but did not.

In September 2017, more than one year after the Bitfinex case, the CFTC filed its first virtual currency-related action in federal district court against Gelfman Blueprint, Inc. and its CEO, Nicholas Gelfman. The CFTC charged the defendants with one count of engaging in fraud by a deceptive device or contrivance, in violation of CEA section 6(c)(1) and CFTC Rule 180.1, by making written misrepresentations to their customers, failing to disclose material information to them, and misappropriating their funds.[198] The CFTC again asserted that virtual currencies are commodities, adhering to its initial position from administrative cases but similarly without much reasoning. In its complaint, the CFTC alleged in one sentence that "Bitcoin and other virtual currencies are encompassed in the definition of 'commodity' under section 1a(9) of the

[196] *Id.* at 77,855. The CFTC repeated its statements from *Coinflip* that the statutory definition of commodity includes "all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in," and that the definition of a commodity is broad.

[197] *See* 7 U.S.C. § 2(c)(2)(D)(iii) (leveraged trading of commodities that does not meet the actual delivery exception will be treated as if the trading is of futures, which must occur on a registered exchange under CEA section 4(a)).

[198] Complaint ¶¶ 81–90, *CFTC v. Gelfman Blueprint, Inc.*, No. 1:17-cv-07181 (S.D.N.Y. Sept. 21, 2017).

Commodity Exchange Act . . . ."[199] In footnote 1 of the complaint, the CFTC defined "virtual currency" the same way it had done in the *Coinflip* order.[200]

On October 12, 2017, Mr. Gelfman, acting *pro se*, filed a response to the CFTC's complaint. In the response, he asserted that the CFTC lacks jurisdiction because "[b]itcoin and other virtual currencies are not commodities under Section 1a(9) of the Act."[201] This answer was filed prior to the launch of two different exchange-traded bitcoin futures contracts in December 2017. On October 1, 2018, Mr. Gelfman's argument was rendered moot, and the case was terminated, by the filing of a Consent Order for Permanent Injunction.[202] In the "Findings of Fact" section of the Order, bitcoin was described as "a commodity in interstate commerce."[203] The "Conclusions of Law" section of the Order stated that "[v]irtual currencies such as [b]itcoin are encompassed in the definition of 'commodity' under Section 1a(9) of the Act, 7 U.S.C. § 1a(9) (2012)."[204] In addition to an injunction against committing future violations of the CEA, the Order directed Mr. Gelfman to pay $492,064.53 in restitution and a civil monetary penalty of $177,501.

Two federal courts have offered an analysis regarding how virtual currencies should be treated under the commodity definition. In *CFTC v. McDonnell*,[205] the CFTC alleged that the

[199] *Id*. at ¶ 12.

[200] *Id*. at ¶ 12 n.1.

[201] Answer at 13, *Gelfman*, No. 1:17-cv-07181 (S.D.N.Y. Oct. 12, 2017), ECF No. 12.

[202] Consent Order for Permanent Injunction, Civil Monetary Penalty, and Other Equitable Relief Against Defendant Nicholas Gelfman, *Gelfman*, No. 1:17-cv-07181 (S.D.N.Y. Oct. 2, 2018), ECF No. 33.

[203] *Id.* at 5.

[204] *Id.* at 9.

[205] *McDonnell I*, 287 F. Supp. 3d at 213.

defendants purportedly solicited customers to provide advice on trading virtual currencies, but instead misappropriated the funds and provided no advice.[206] Mr. McDonnell, who also was not represented by counsel, did not expressly assert that virtual currencies were *not* commodities, but took the position that the CFTC "possessed no enforcement jurisdiction" to bring its complaint against him.[207] The CFTC interpreted Mr. McDonnell's argument that the CFTC lacked "enforcement jurisdiction" as "suggesting that the Commission's anti-fraud enforcement authority under Section 6(c)(1) of the [CEA] and Regulation 180.1 does not reach the virtual currency-related scheme alleged."[208] In a pretrial ruling, the court rejected Mr. McDonnell's argument, explaining that the CFTC can regulate virtual currencies as commodities because (i) they are "'goods' exchanged in a market for a uniform quality and value;" (ii) they "fall well-within the common definition of 'commodity;'" and (iii) they meet the CEA's definition of commodities as "'all other goods and articles . . . in which contracts for future delivery are presently or in the future dealt in.'"[209]

Following a bench trial, the court ruled in favor of the CFTC and against Mr. McDonnell.[210] Citing its earlier ruling, the court concluded that "[v]irtual currency may be regulated by the CFTC as a commodity" and that the CFTC's "broad statutory authority . . . and regulatory authority . . . extends [*sic*] to fraud or manipulation in the virtual currency derivatives

[206] *Id*. at 229–30.

[207] Defendant's Memorandum in Support of Motion to Dismiss at 2, *CFTC v. McDonnell*, No. 18-cv-00361 (E.D.N.Y. Feb. 15, 2018), ECF No. 18-2.

[208] Plaintiff's Memorandum in Opposition to Defendant's Motion to Dismiss at 6, *CFTC v. McDonnell*, No. 18-cv-00361 (E.D.N.Y. Feb. 26, 2018), ECF No. 20.

[209] *McDonnell I*, 287 F. Supp. 3d at 228 (alteration in original) (quoting 7 U.S.C. § 1a(9)).

[210] *CFTC v. McDonnell*, 332 F. Supp. 3d 641 (E.D.N.Y. 2018) [hereinafter *McDonnell II*].

market and its underlying spot market."[211] Later in the opinion, the court commented that Bitcoin and Litecoin are virtual currencies and are commodities in interstate commerce.[212] In addition to an injunction against committing future violations of the CEA, the Order directed Mr. McDonnell to pay $290,429.29 in restitution and a civil monetary penalty of $871,287.87.[213] Mr. McDonnell did not appeal the order, and the case has concluded.

The positions summarized above provide some support for the ultimate conclusion that virtual currencies are commodities but do not resolve many interpretative questions relating to the CFTC's jurisdiction over virtual currencies. For example, although the *McDonnell* court agreed with the CFTC's position, it did not rely on the same grounds that the agency previously had stated. The CFTC previously asserted in its administrative settlements that virtual currencies fall within the definition of commodity under the CEA as part of "all services, rights, and interests . . . in which contracts for future delivery are presently or in the future dealt in."[214] Thus, there is an outstanding question regarding which of the "goods, articles, services, rights, and interests" categories apply to virtual currencies. Further, while the *McDonnell* court concluded that virtual currencies fall within the commodity definition, the court's reasoning stops short of addressing whether a virtual currency already must be subject to a futures contract in order to be a commodity. Resolving these issues will be critical in determining how far the CFTC may go in exercising its authority over virtual currencies.

---

[211] *Id.* at 651.

[212] *Id.* at 723.

[213] *Id.* at 727–28.

[214] 7 U.S.C. § 1a(9).

ii. Challenges to the CFTC's Position That Virtual Currencies Are Commodities

While the CFTC thus far has successfully asserted that virtual currencies are commodities under the CEA, the issue is far from settled. For example, the *Gelfman* defendants argued that virtual currencies are not commodities because, among other reasons, Congress has not categorized bitcoin and other virtual currencies as such, and various agencies other than the CFTC also have asserted jurisdiction over virtual currencies.[215] Although the *Gelfman* court did not rule on that issue because the case was settled, the *McDonnell* court offers a plausible rebuttal to this challenge, stating that "[u]ntil Congress clarifies the matter, the CFTC has concurrent authority, along with other state and federal administrative agencies, and civil and criminal courts, over dealings in virtual currency."[216]

A second challenge focuses on the interpretive ambiguities in the commodity definition under the CEA. "Commodity," as defined by the CEA, includes all goods, articles, services, rights, and interests "in which contracts for future delivery are presently or in the future dealt in." Even under the narrowest reading discussed above, this definition covers bitcoin because it is currently the subject of futures trading on the CME and Cboe Futures Exchange. It remains unclear, however, whether the same is true for other virtual currencies for which no futures trading currently exists. As noted in Section 2.3(c) above, the commodity definition can be read in competing ways: the first interpretation would require the existence of an overlying futures contract for the CFTC to have jurisdiction over a particular virtual currency as a commodity; the second interpretation would only require the possibility that the virtual currency would be the

[215] Answer, *supra* note 201, at 13.

[216] *McDonnell I*, 287 F. Supp. 3d at 217.

subject of a futures contract in the future; and a third, middle-ground interpretation would require that a futures contract exist on one of the virtual currencies as a category of commodity. The outcome of this interpretation carries significance, as the CFTC's authority over virtual currencies under the first interpretation would be far less clear unless and until other virtual currencies become subject to futures contracts.

The defendants in *CFTC* v. *My Big Coin Pay* urged the court to take the first approach and dismiss the case for lack of CFTC jurisdiction.[217] The case involves MBC, a virtual currency that is not bitcoin and has no overlying futures contract. The defendants argued that "[p]er the plain language of the CEA, intangible 'services, rights and interests' are only included in the CEA's definition of the term 'commodity' if there are futures contracts traded on them."[218] Because no futures contracts are traded on MBC, the defendants argued, it is not a commodity, and the CFTC has no authority to bring the action.[219]

Not surprisingly, the CFTC has supported the adoption of the second interpretive approach. In its administrative proceedings, the CFTC consistently has stated that "[b]itcoin and other virtual currencies" are properly defined as commodities—even though no futures contract existed on bitcoin or any other virtual currency when it first made that determination in

[217] Complaint, *CFTC v. My Big Coin Pay, Inc.*, No. 1:18-cv-10077 (D. Mass. filed Jan. 16, 2018). On March 7, 2019, the Department of Justice filed an unopposed motion to intervene and stay discovery in the case pending resolution of a criminal case against the *My Big Coin Pay* defendants. *See* Unopposed Motion of the United States for Leave to Intervene and for a Stay of Discovery and Memorandum in Support, *CFTC v. My Big Coin Pay, Inc.*, No. 1:18-cv-10077 (D. Mass. filed Mar. 7, 2019), ECF No. 146.

[218] Defendants' Memorandum in Support of Motion to Dismiss at 5, *CFTC v. My Big Coin Pay, Inc.*, No. 1:18-cv-10077 (D. Mass. filed May 5, 2018), ECF No. 69 (emphasis omitted).

[219] *Id.* at 6.

September 2015.[220] In *My Big Coin Pay*, the CFTC provided additional justifications for that position.

First, the Commission avoided the interpretive ambiguities and argued that MBC is a commodity regardless of whether there are futures contracts on it because it is a "good" or an "article" (a position first taken by the *McDonnell* court, not the CFTC). The Commission reasoned that the modifier "presently or in the future dealt in" applies "as a matter of syntax, punctuation, and grammar" only to "services, rights, and interests" in the definition of commodity.[221] The CFTC's argument potentially carries far-reaching consequences. If the CFTC is correct, then it can regulate cash markets for any goods or articles regardless of whether those markets are, or ever could be, connected to a futures market. Congress, however, amended the CEA to add both the goods and articles and the services, rights, and interests clauses at the same time it added the modifier regarding futures contracts. That timeline, when combined with the delineation of CFTC jurisdiction under CEA section 2(a)(1) over futures contracts and the public interest justification for regulating futures markets,[222] suggests that Congress did not intend to give the CFTC authority over commodities that would have no connection to a futures market.

Second, in the alternative, the CFTC argued that, even if the modifying clause applied to goods and articles as well, MBC and other virtual currencies are commodities because "futures contracts on the functionally similar virtual currency [b]itcoin currently are 'dealt in.'"[223] The

---

[220] *See Coinflip*, Comm. Fut. L. Rep. (CCH) ¶ 33,538.

[221] Plaintiffs' Opposition to Defendants' Motion to Dismiss at 8–9, *CFTC v. My Big Coin Pay, Inc.*, No. 1:18-cv-10077 (D. Mass. filed May 18, 2018), ECF No. 70 (citing *Barnhart v. Thomas*, 540 U.S. 20, 21 (2003), for the grammatical rule of the last antecedent under which a limiting clause is read to modify only the phrase it immediately follows).

[222] 7 U.S.C. § 2(a)(1).

[223] Plaintiffs' Opposition to Defendants' Motion to Dismiss, *supra* note 221, at 10–11.

Commission reasoned that "Congress defined commodities under the Act categorically, not by type, grade, quality, brand, producer, manufacturer, or form,"[224] and the Commission therefore has authority to regulate virtual currencies as a category of commodities given that bitcoin futures are being traded. The Commission also relied on *United States v. Valencia*, which rejected the argument that "West Coast gas" was not a commodity under the CEA because there was no futures contract for "West Coast gas."[225] The court explained that "West Coast gas" was still a commodity because "natural gas, for delivery on the West Coast or otherwise, is a commodity" in general, natural gas is "fungible," and "there is no evidence that West Coast gas could not in the future be traded on a futures exchange."[226]

While not cited by the Commission, the Fifth Circuit in *United States v. Brooks* similarly rejected the argument that only natural gas traded at Henry Hub is a commodity under the CEA because only natural gas traded at Henry Hub underlies the natural gas futures contracts traded on NYMEX.[227] The court instead held that natural gas generally is a commodity regardless of its location, because "the actual nature of the 'good' does not change."[228]

On September 26, 2018, the *My Big Coin Pay* court rejected the defendant's argument made in its motion to dismiss, ruling that at least at the pleading stage of the case, the CFTC had alleged sufficient facts for the case to move forward.[229] In so ruling, the court took the middle-

[224] *Id.* at 9.

[225] *United States v. Valencia*, No. CR.A. H-03-024, 2003 WL 23174749, at *8 (S.D. Tex. Aug. 25, 2003), *order vacated in part on reconsideration*, No. CRIM.A. H-03-024, 2003 WL 23675402 (S.D. Tex. Nov. 13, 2003), *rev'd and remanded*, 394 F.3d 352 (5th Cir. 2004).

[226] *Id.* at *8 & n.13.

[227] *United States v. Brooks*, 681 F.3d 678, 694 (5th Cir. 2012).

[228] *Id.* at 695.

[229] *CFTC v. My Big Coin Pay, Inc.*, 334 F. Supp. 3d 492 (D. Mass 2018).

ground interpretive approach to the commodity definition and held that it was sufficient at the pleading stage of the case for the complaint to allege that My Big Coin is a virtual currency and that there is futures trading in a virtual currency, namely bitcoin.[230] The court characterized the CFTC's argument in this way: "Pointing to the existence of [b]itcoin futures contracts, it argues that contracts for future delivery . . . are 'dealt in' and that My Big Coin, as a virtual currency, is therefore a commodity."[231] The court then ruled that the text of the CEA supported the CFTC's argument. The court observed that the CEA defines the term "commodity" generally and categorically, and "not by type, grade, quality, brand, producer, manufacturer, or form," agreeing with the CFTC's position that "Congress'[s] approach to defining 'commodity' signals an intent that courts focus on categories—not specific items—when determining whether the 'dealt in' requirement is met."[232] Citing the *Brooks* and *Valencia* cases, the court ruled that, "[t]aken together, these decisions align with plaintiff's argument that the CEA only requires the existence of futures trading within a certain class (*e.g.*, 'natural gas') in order for all items within that class (*e.g.*, 'West Coast' natural gas) to be considered commodities."[233] In his answer to the amended complaint, filed approximately six weeks after the denial of the motion to dismiss, defendant Randall Crater raised the following affirmative defense: "My Big Coin is not sufficiently related to [b]itcoin, the only virtual currency on which futures contracts are traded, to conclude that My Big Coin is a good, article, service, right or interest on which contracts for future delivery are

[230] *Id.*

[231] *Id.* at 496–97.

[232] *Id.* at 497.

[233] *Id.* at 498.

dealt in, and, therefore, My Big Coin is not a 'commodity' as defined in the Commodity Exchange Act."[234] The parties engaged in discovery during the following months.

On February 26, 2019, a federal grand jury in the U.S. District Court for the District of Massachusetts returned an indictment charging Randall Crater with wire fraud and money laundering in connection with his marketing and sale of My Big Coin.[235] The indictment alleges that Mr. Crater made misrepresentations to investors and misappropriated their money, but does not refer to or depend on My Big Coin's status as a commodity under the CEA. The word "commodity" does not appear in the indictment. Nine days after the indictment, the U.S. Department of Justice filed an unopposed motion to intervene in the CFTC's case and to stay discovery.[236] The court granted the motion the next day, and no substantive motions were filed or rulings made for one year.[237]

On March 9, 2020, the defendants filed in the CFTC case a motion to amend or reissue the court's September 26, 2018 order denying their motion to dismiss, and to certify the order for interlocutory appeal.[238] In the memorandum of law in support of the motion, the defendants identified the issue they wished to raise on appeal as "[w]hether a good or article, other than an enumerated agricultural product, or a service, right or interest, on which no futures contracts are

[234] Defendant Randall Crater's Answer to the Amended Complaint at 9, *CFTC v. My Big Coin Pay, Inc.*, No. 1:18-cv-10077 (D. Mass. filed Nov. 9, 2018), ECF No. 113.

[235] Indictment, *United States v. Randall Crater*, No. 1:19-cr-10063 (D. Mass. filed February 26, 2019), ECF No. 1.

[236] Unopposed Motion of the United States for Leave to Intervene and for a Stay of Discovery and Memorandum in Support, *CFTC v. My Big Coin Pay, Inc. et al.*, No. 1:18-cv-10077 (D. Mass. filed Mar. 7, 2019), ECF No. 146.

[237] Endorsed Order, *CFTC v. My Big Coin Pay, Inc. et al.*, No. 1:18-cv-10077 (D. Mass. filed Mar. 8, 2019), ECF No. 147.

[238] Defendant Randall Crater's and Relief Defendants' Notice of Motion to Amend the Court's Order Denying the Defendants' Motion to Dismiss to Certify the Order for Interlocutory Appeal, *CFTC v. My Big Coin Pay, Inc. et al.*, No. 1:18-cv-10077 (D. Mass. filed Mar. 9, 2019), ECF No. 154.

traded, is a 'commodity' as that term is defined in the Commodity Exchange Act ('CEA')?"[239] The CFTC opposed the motion, and the court denied the motion on October 29, 2020.[240] Because the CFTC case remains stayed while the criminal case is pending, and no trial date has been set in the criminal case, it is not certain when or whether the CFTC case will provide an answer to the question above.

While instructive, these cases do not resolve the interpretive ambiguities in the commodity definition. At best, they suggest that, where there are enough similarities among components of a general commodity category and one component underlies a futures contract, the CFTC may properly regulate all of those components as commodities. That, in turn, raises the question of how similar virtual currencies must be before they may be grouped together as functional equivalents of bitcoin and thus fall under the commodity definition. As explained in Section 2.3(d) above and Section 2.4 below, virtual currencies may defy easy categorization and each may have unique features that render the analogy to natural gas at different locations inapposite.

(f) The CFTC's Exercise of Anti-Fraud and Anti-Manipulation Authority over Virtual Currencies as Commodities

The CFTC is not authorized under the CEA to adopt rules regulating trading in the cash markets for commodities, known as forward or "spot" contracts or transactions. As a result, many virtual currency trading platforms operate outside of the CFTC's jurisdiction.[241] Although

[239] Memorandum of Law in Support of Defendant Randall Crater's and Relief Defendants' Motion to Amend the Court's Order Denying the Defendants' Motion to Dismiss to Certify the Order for Interlocutory Appeal at 1, *CFTC v. My Big Coin Pay, Inc. et al.*, No. 1:18-cv-10077, at 1 (D. Mass. filed Mar. 9, 2019), ECF No. 155.

[240] Order, *CFTC v. My Big Coin Pay, Inc. et al.*, No. 1:18-cv-10077 (D. Mass. filed Oct. 29, 2020), ECF No. 159.

[241] Giancarlo HUA Statement, *supra* note 2. In his testimony, Giancarlo clarified the CFTC's jurisdiction over virtual currencies: while these assets are "commodities" under the CEA, current law does not provide any U.S. federal regulator with regulatory oversight authority over spot virtual currency platforms operating in the United States or abroad. However, the CFTC does have enforcement authority to investigate through subpoena and other

spot commodity markets are not directly subject to broader CEA compliance requirements such as registration, reporting, and recordkeeping,[242] the CFTC has authority under CEA section 6(c)(1)[243] and CFTC Rule 180.1 to punish fraudulent practices and manipulation related to the commodities traded in those spaces.

CFTC Rule 180.1 states, in part:

> Prohibition on the employment, or attempted employment, of manipulative and deceptive devices.
>
> (a) It shall be unlawful for any person, directly or indirectly, in connection with any swap, or contract of sale of any commodity in interstate commerce, or contract for future delivery on or subject to the rules of any registered entity, to intentionally or recklessly:
>
> (1) Use or employ, or attempt to use or employ, any manipulative device, scheme, or artifice to defraud;
>
> (2) Make, or attempt to make, any untrue or misleading statement of a material fact or to omit to state a material fact necessary in order to make the statements made not untrue or misleading;
>
> (3) Engage, or attempt to engage, in any act, practice, or course of business, which operates or would operate as a fraud or deceit upon any person; or,
>
> (4) Deliver or cause to be delivered, or attempt to deliver or cause to be delivered, for transmission through the mails or interstate commerce, by any means of

---

investigative powers and, as appropriate, conduct civil enforcement actions against fraud and manipulation in virtual currency derivatives markets and in underlying virtual currency spot markets. *Id*. Giancarlo stated that in contrast to the spot markets, the CFTC does have comprehensive regulatory oversight over derivatives on virtual currencies traded in the United States, including registration requirements and a host of requirements for trading and market surveillance, reporting and recordkeeping, business conduct standards, capital requirements, and platform and system safeguards.

[242] The CFTC, though, does have certain authority to monitor the cash market activities of users of the derivatives markets, combined with authority to impose recordkeeping requirements on such persons relating to their cash market activities. *See, e.g.*, 17 C.F.R. § 1.31.

[243] 7 U.S.C. § 9(1) ("(1) Prohibition against manipulation. It shall be unlawful for any person, directly or indirectly, to use or employ, or attempt to use or employ, in connection with any swap, or a contract of sale of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity, any manipulative or deceptive device or contrivance, in contravention of such rules and regulations as the Commission shall promulgate by not later than 1 year after July 21, 2010, provided no rule or regulation promulgated by the Commission shall require any person to disclose to another person nonpublic information that may be material to the market price, rate, or level of the commodity transaction, except as necessary to make any statement made to the other person in or in connection with the transaction not misleading in any material respect.").

> communication whatsoever, a false or misleading or inaccurate report concerning crop or market information or conditions that affect or tend to affect the price of any commodity in interstate commerce, knowing, or acting in reckless disregard of the fact that such report is false, misleading or inaccurate. Notwithstanding the foregoing, no violation of this subsection shall exist where the person mistakenly transmits, in good faith, false or misleading or inaccurate information to a price reporting service.[244]

The CFTC's authority under CEA section 6(c)(1) and Rule 180.1 is similar to the SEC's anti-fraud authority under Exchange Act section 10(b)[245] and SEC Rule 10b-5.[246] One difference, however, is that the provisions in the CEA and CFTC Rule 180.1 do not restrict prohibited activities to those that are in themselves tied to a transaction.[247] CEA section 6(c)(1) and CFTC Rule 180.1 reach "all manipulative or deceptive conduct in connection with the purchase, sale, solicitation, execution, pendency, or termination of any swap, or contract of sale of any commodity in interstate commerce, or contract for future delivery on or subject to the rules of any registered entity."[248]

---

[244] 17 C.F.R. § 180.1(a).

[245] 15 U.S.C. § 78j ("It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . . (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." (footnote omitted)).

[246] 17 C.F.R. § 240.10b-5 ("It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, (a) To employ any device, scheme, or artifice to defraud, (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.").

[247] *See* Prohibition on the Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation, 76 Fed. Reg. 41,398, 41,399 n.6 (Jul. 14, 2011) (to be codified at 17 C.F.R. pt. 180) [hereinafter CFTC Manipulation Rule] ("Differences between the wording of Exchange Act section 10(b) and CEA section 6(c)(1) include, but are not limited to, the express prohibition of the 'attempt to use' any 'manipulative or deceptive device or contrivance' in CEA section 6(c)(1), and the absence of a 'purchase or sale' requirement in CEA section 6(c)(1).").

[248] CFTC Manipulation Rule, 76 Fed. Reg. at 41,401 ("The Commission declines to adopt the request of certain commenters to interpret CEA section 6(c)(1) as merely extending the Commission's existing anti-fraud and anti-

Nevertheless, the CFTC acknowledged some limits on its authority when finalizing CFTC Rule 180.1.[249] The preamble to the rulemaking responded to commentators' concerns that the language in the rule was so broad that it gave the CFTC limitless authority by offering examples of activities that would not be considered to be "in connection with" any swap, contract of sale of any commodity, or futures contract and, therefore, outside of the scope of the CFTC's jurisdiction.[250] The preamble further stated that the CFTC expected its authority "to cover transactions related to the futures or swaps markets, or prices of commodities in interstate commerce, or where the fraud or manipulation has the potential to affect cash commodity, futures, or swaps markets or participants in these markets."[251] On this point, the preamble concluded, "[t]his application of the final Rule respects the jurisdiction that Congress conferred upon the Commission."[252]

Recent CFTC civil cases highlight the potential issues raised when the CFTC seeks to exercise its anti-fraud and anti-manipulation authority in the context of virtual currencies and against the backdrop of its prior statements that its enforcement authority is tied to the CFTC's overall jurisdiction under the CEA. In *CFTC v. Monex*, for example, a federal judge in the

---

manipulation authority to cover swaps. Such an interpretation would be inconsistent with the language of CEA section 6(c)(1), as amended by section 753 of the Dodd-Frank Act.").

[249] *Id.* at 41,405–06.

[250] *See, e.g., id.* ("In this regard, the Commission finds the Supreme Court's decision in [*SEC v. Zandford*, 535 U.S. 813 (2002)] interpreting SEC Rule 10b-5's 'in connection with' language particularly instructive. In its opinion, the Court gave the following example to highlight the limits of SEC Rule 10b-5 applicability: If * * * a broker embezzles cash from a client's account or takes advantage of the fiduciary relationship to induce his client into a fraudulent real estate transaction, then the fraud would not include the requisite connection to a purchase or sale of securities. Likewise, if the broker told his client he was stealing the client's assets, that breach of fiduciary duty might be in connection with a sale of securities, but it would not involve a deceptive device or fraud." (second alteration in original) (footnote omitted) (citation omitted)).

[251] *Id.* at 41,401.

[252] *Id.*

Central District of California held that the CFTC may exercise its enforcement authority under CEA section 6(c)(1) only when it can show both manipulative and deceptive conduct, even though "the plain language of § 6(c)(1) suggests that Congress intended to prohibit either manipulative or deceptive conduct."[253] There, the defendants argued that CEA section 6(c)(1) confers the CFTC anti-fraud jurisdiction only where a particular commodity transaction manipulates or potentially manipulates the derivatives market.[254] The Ninth Circuit subsequently reversed the district court, rejecting Monex's argument that "stand-alone fraud claims—without allegations of manipulation—fail as a matter of law."[255]

In *McDonnell*, the court similarly disagreed with the *Monex* district court decision and allowed the CFTC's case under CEA section 6(c)(1) to continue based solely on allegations of deceptive conduct. The *McDonnell* court, after "fully consider[ing] *Monex*," held that CEA section 6(c)(1) "gives the CFTC standing to exercise its enforcement power over the fraudulent schemes alleged in the complaint."[256] In several cases, the CFTC is pursuing alleged virtual currency frauds under CEA section 6(c)(1) and CFTC Rule 180.1,[257] and the Ninth Circuit's reversal of the district court's decision in *Monex* suggests that the CFTC likely will bring these types of cases based on allegations of fraud alone, even absent proof of manipulation.

---

[253] *CFTC v. Monex Credit Co.*, 311 F. Supp. 3d 1173, 1186 (C.D. Cal. 2018), *rev'd and remanded sub nom. CFTC v. Monex Credit Co.*, 931 F.3d 966 (9th Cir. 2019), *cert. denied sub nom. Monex Deposit Co. v. CFTC*, No. 19-933, 2020 WL 3492657 (U.S. June 29, 2020).

[254] *Id.* at 1184–85.

[255] *Monex*, 931 F.3d at 969.

[256] Order at 3, *CFTC v. McDonnell*, No. 1:18-cv-00361 (E.D.N.Y. July 16, 2018), ECF No. 136.

[257] *See, e.g.*, *McDonnell*; *Gelfman*; and *My Big Coin Pay*, *supra* note 121.

Similar to the defendants in *Monex*, the defendants in *My Big Coin Pay* argued that the CFTC could not rely on its anti-fraud and anti-manipulation authority because the legislative intent behind CEA section 6(c)(1) and the CFTC's own explanation of CFTC Rule 180.1[258] did not contemplate permitting the CFTC to punish individuals and entities for general fraud where there is no evidence of market manipulation.[259] Unlike in previous cases, the CFTC stated in its complaint that the prohibited activity was a misrepresentation about the virtual currency, MBC, itself and how MBC could be used by the consumer.[260] The defendants' argument in *My Big Coin Pay* mirrors some arguments made by others that the CFTC's interpretation of its Rule 180.1 authority is more expansive in the context of virtual currencies than it has been in the past because it reaches beyond fraud or manipulation related to derivatives markets.[261]

Notwithstanding these challenges, the CFTC declared a continuing interest in policing virtual currency market participants that fall within the bounds of CFTC jurisdiction.[262] Notably,

[258] Defendants' Memorandum in Support of Motion to Dismiss, *supra* note 218, at 16 ("The CFTC stated that the fears commenters had expressed in response to the Notice of Proposed Rulemaking that 'the word "commodity" in proposed Rule 180.1 "indicates that the rule will apply to virtually every commercial transaction in the economy" are *misplaced.*'" (quoting CFTC Manipulation Rule, 76 Fed. Reg. at 41,401)).

[259] *Id.* at 15 ("The legislative history shows that these provisions were meant to combat fraudulent market manipulations—not the kind of garden variety sales puffery that the Amended Complaint alleges.").

[260] Complaint, *supra* note 217, at ¶ 60.

[261] *See* Geoffrey F. Aronow, *Is The CFTC Becoming The National Fraud Police? The CFTC Goes All In On Policing Fraud In Virtual Currencies*, 38 No. 3 FUTURES & DERIVATIVES L. REP. NL 1, at 9 (Mar. 2018) ("If the CFTC is, indeed, committed to policing fraud in the sale of virtual currency wherever the Commission may find it (with the exception of where the SEC may be able to act), the question becomes, how far is the CFTC now prepared to go in asserting broad authority to police fraud in the sale of commodities in interstate commerce?").

[262] *See, e.g.*, *State of the CFTC: Examining Pending Rules, Cryptocurrency Regulation, and Cross-Border Agreements: Hearing before the U.S. S. Comm. on Agric., Nutrition & Forestry*, 115th Cong. *9–10 (2018) (statement of J. Christopher Giancarlo, Chairman, CFTC), https://www.agriculture.senate.gov/imo/media/doc/Testimony_Giancarlo_02.15.18.pdf [hereinafter State of the CFTC] (summarizing the CFTC's current civil enforcement actions, which include not only "fail[ure] to register," but also more general allegations of "fraud, market manipulation, and disruptive trading").

the CFTC and SEC Enforcement Directors released a joint statement regarding their respective enforcement programs:

> When market participants engage in fraud under the guise of offering digital instruments—whether characterized as virtual currencies, coins, tokens, or the like—*the SEC and the CFTC will look beyond form*, examine the substance of the activity and prosecute violations of the federal securities and commodities laws. The Divisions of Enforcement for the SEC and CFTC will continue to address violations and to bring actions to stop and prevent fraud in the offer and sale of digital instruments.[263]

This statement aligns with the CFTC's position in its civil enforcement actions in 2018 as well as public statements made by CFTC Commissioners[264] and staff[265] that reiterated the CFTC's commitment to punishing bad actors in the virtual currencies markets.

(g) The CFTC's Exercise of Jurisdiction over Virtual Currencies as Retail Commodity Transactions

Classification of virtual currencies as commodities (of a type other than a currency or security) has implications for margined, leveraged, or financed transactions in virtual currencies under the retail commodity provisions of CEA section 2(c)(2)(D). As explained above in Section 2.2(c), a transaction that is within the scope of the provision is treated as or "as if" it is a futures contract, but it may be excluded from that regulatory consequence if the transaction

[263] Press Release, CFTC, Joint statement from CFTC and SEC Enforcement Directors Regarding Virtual Currency Enforcement Actions, (Jan. 19, 2018), https://www.cftc.gov/PressRoom/SpeechesTestimony/mcdonaldstatement011918 (emphasis added).

[264] *See, e.g.*, Brian Quintenz, Comm'r, CFTC, Remarks before the Eurofi High Level Seminar 2018 (Apr. 26, 2018), https://www.cftc.gov/PressRoom/SpeechesTestimony/opaquintenz11 ("From my perspective as a CFTC Commissioner, I think the area with the greatest need for enhanced regulatory certainty and oversight is the spot market. In that regard, the CFTC has undertaken an educational campaign to provide customers with information about cryptocurrencies and to warn about potential fraud in these markets. The CFTC's Division of Enforcement has aggressively targeted deception and manipulation to ensure that innocent customers are not exploited by fraudsters. And with respect to jurisdictional considerations, the CFTC has been, and continues to be, in close communication with the SEC.").

[265] *See, e.g.*, CFTC, CFTC BACKGROUNDER ON OVERSIGHT OF AND APPROACH TO VIRTUAL CURRENCY FUTURES MARKETS (2018), https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/backgrounder_virtualcurrency01.pdf.

results in "actual delivery" of the commodity within 28 days. The meaning of "actual delivery" is open to debate.

In its enforcement action against Bitfinex, the CFTC took the position (consistent with its 2013 interpretation) that delivery of bitcoin purchased with borrowed funds to a private wallet where the coins were held for the benefit of the buyer but also as collateral for the loan did not constitute actual delivery, because the buyer did not have any rights to access or use the purchased bitcoin until released by Bitfinex following satisfaction of the loan.[266] Because the transactions did not fall within the actual delivery exclusion, the CFTC determined that Bitfinex executed illegal, off-exchange transactions and also violated the CEA by acting as an unregistered FCM.

Although the CFTC faced a potential roadblock to its interpretation of the term "actual delivery" when a federal district court rejected the CFTC's position in the precious metals context in May 2018, the Ninth Circuit sided with the CFTC and overturned that decision in July 2019. In its case against Monex Credit Company,[267] the CFTC alleged that the defendants violated, among others, CEA sections 4(a) and 4d by offering precious metals off-exchange on a leveraged basis without registering with the Commission as an FCM.[268] The defendants required that customers trading on a leveraged basis ("Atlas customers") deposit funds to serve as margin for their open trading positions. The defendants also could change the margin requirements at any time in their sole discretion, and could liquidate customers' trading positions without notice in certain cases. Under the account agreement between the defendants and Atlas customers,

[266] *BFXNA Inc.*, Comm. Fut. L. Rep. (CCH) ¶ 33,766.

[267] *Monex*, 311 F. Supp. 3d at 1173.

[268] *Id*. at 1176–77.

customers with open trading positions did not take physical delivery of the metals. Instead, the metals were stored in third-party depositories, subject to contracts between the defendants and the depositories. The customers could get physical possession of the metal only if they made full payment, requested actual delivery of specific physical metals, and had the defendants ship the metals to them.[269]

Relying on the Eleventh Circuit's 2014 decision in *CFTC v. Hunter Wise Commodities*,[270] the CFTC argued that the actual delivery exception to its jurisdiction did not apply because "'actual delivery' only occurs once there has been a transfer of possession of and control over the purchased commodities."[271] In the CFTC's view, the purported delivery in the defendants' leveraged transactions was a "sham" because customer positions could be "liquidated any time and in [the defendants'] sole discretion, without notice to customers," which "deprive[d] customers of all control and authority over any metals that underlie their trading positions."[272] The *Monex* court disagreed, finding that adopting the CFTC's view would "eliminate the Actual Delivery Exception from the CEA" because all leveraged retail transactions of fungible commodities would involve at least some of the same alleged practices by the defendants.[273] The court held that the defendants' practice of delivering precious metals to third-party depositories within 28 days of their purchase by retail customers on margin fell within the actual delivery exception to the CFTC's authority.

---

[269] *Id*. at 1177–78.

[270] *CFTC v. Hunter Wise Commodities, LLC*, 749 F.3d 967 (11th Cir. 2014).

[271] *Monex*, 311 F. Supp. 3d at 1180 (citation omitted).

[272] *Id*. at 1181 (citation omitted).

[273] *Id*.

The Ninth Circuit reversed, holding that "actual delivery requires at least some meaningful degree of possession or control by the customer."[274] According to the Ninth Circuit, actual delivery does not occur when the commodity is in the broker's chosen depository, never changes hands, and is subject to the broker's exclusive control, and the customer has no "substantial, non-contingent interests."[275] The court further noted that, even if the CEA provisions on actual delivery were ambiguous, it "would find the CFTC's [2013 Guidance] persuasive."[276] Applying the guidance, the court concluded that Monex's arrangement with an independent depository for holding metals purchased on margin was "merely a book entry" that "amounts to sham delivery, not actual delivery."[277]

4. Allocation of Jurisdiction over Transactions between the CFTC and SEC

As noted above, the CEA "commodity" definition covers securities. Rather than exclude securities from the definition, Congress has allocated jurisdiction between the CFTC and SEC over derivatives based on securities or on a group or index of securities (or an interest therein or based on the value thereof), based in part on distinctions between exempted securities (as defined in the Exchange Act) and non-exempted securities, and narrow-based or broad-based indices of non-exempted securities. As a result, derivatives on a virtual currency or other digital asset that is a "security" also nevertheless may be subject to CFTC jurisdiction, but the scope of the CFTC's jurisdiction is more constrained than with respect to non-security commodities.

[274] *Monex*, 931 F.3d at 974.

[275] *Id*.

[276] *Id*. at 975.

[277] *Id*.

Securities where one or more payment components (*e.g.*, interest payments on a debt security) are linked in whole or in part to the value of a non-security commodity also raise issues of jurisdictional overlap, if the embedded commodity terms could be classified as a futures contract or another type of derivative on the commodity. The issuers of such hybrid instrument securities can control the design of the instruments to qualify for an exemption from CEA regulation under either a statutory exemption provided in CEA section 2(f) or an exemption provided in the CFTC's Part 34 Rules. If the embedded terms relate to the value of a virtual currency, and the virtual currency is a non-security commodity, the issuer will have to qualify for one of the exemptions if it wants to avoid complicated issues of how (if even possible) to comply with CEA requirements, on top of federal securities laws requirements for initial offerings and secondary market trading of securities.

The security/non-security distinction also is important more generally for determining which agency has authority over the cash market trading activities in a digital asset. The SEC, not the CFTC, is responsible for protecting cash securities markets against fraud and manipulation. Thus, beyond determining whether a digital asset is within the scope of the CEA's commodity definition, it is important to know whether the asset is a security or a non-security commodity.

The CEA and federal securities laws have been amended over the years since 1974 to address areas of competing or potentially competing jurisdictional claims between the CFTC and SEC. The two agencies also on occasion have jointly resolved jurisdictional issues, and some of those agreements have been captured in the statutory amendments, notably the terms of the Shad-Johnson Accord adopted in 1983.[278] The table at the end of this Section summarizes the

[278] The Shad-Johnson Accord was added to the CEA as part of the Futures Trading Act of 1982, which was enacted in January 1983. It incorporated into the CEA (and the federal securities laws) the terms of an agreement reached

current allocation of jurisdiction between the two agencies over trading in derivatives and in the assets underlying the derivatives.

The allocation scheme means, among other things, that if a virtual currency or other digital or digitized asset is a non-security commodity, DCMs (and FBOTs) may list futures and options on futures contracts on the token as a contract solely regulated in the normal course by the CFTC. If it is a security, though, then a futures exchange may list futures or options on futures on the token or virtual currency only as a "security futures product" under rules jointly developed and enforced by the CFTC and SEC.

Persons also may trade options on the token or virtual currency as a CFTC-regulated transaction. Transactions in options on a virtual currency that is a security, however, would be regulated by the SEC alone as securities.

Also, if a digital asset is a non-security commodity, then certain CEA and CFTC restrictions may apply to leveraged, margined, or financed transactions in the commodity, under the retail commodity provisions in CEA section 2(c)(2)(D), described above, but those provisions do not apply if the asset is a security.

Congress's allocation of jurisdiction to the CFTC and SEC described in the table below presupposes that the interest underlying a derivative is something that can fit neatly into either the security or the non-security commodity box. Bitcoin's status as a non-security commodity seems well-settled, based on the emergence of CFTC-regulated markets for bitcoin-based

---

between the respective Chairmen of the SEC and CFTC as to which agency would have jurisdiction over securities-related futures and options. Under the accord, the CFTC was given jurisdiction over futures and options on futures on exempted securities and broad-based indices of securities, and the SEC was given jurisdiction over options on all securities and all stock indices. Futures and options on futures on individual securities (other than exempted securities) and on narrow-based indices of securities (other than exempted securities) were banned, but that was intended to be temporary until the two agencies could agree on how to allocate jurisdiction. Congress tired of waiting for the CFTC and SEC to reach agreement and lifted the ban in 2000.

derivatives, regulated as futures and not security futures, or as swaps and not as security-based swaps, without any challenge from the SEC.

There can be uncertainty, though, on how to classify other virtual currencies, or other types of digital assets. Section 3 includes an analysis of whether the definition of "security" in the federal securities laws could apply to digital assets. Section 5 discusses the jurisdictional overlap issues and challenges created by uncertainty as to whether a digital asset is properly classified as a security or a non-security commodity.

Table: Allocation of Jurisdiction between the CFTC and SEC

CFTC	SEC	CFTC-SEC Jointly
Futures and Options on Futures		
Futures and options on futures on non-security commodities. Futures and options on futures on: • A broad-based index of securities.[i] • An exempted security as defined in Exchange Act section 3(a)(12).[ii] A foreign government debt security enumerated in SEC Rule 3a12-8.[iii]		Futures or options on futures on the following, regulated as security futures products: • Any security other than an exempted security[iv] or foreign government debt security enumerated in SEC Rule 3a12-8. • Any narrow-based index of securities other than exempted securities.[v] Futures on exchange-traded funds (ETFs) that passively hold non-security commodities such as gold, energy commodities, or foreign currencies are regulated as security futures, but there is an issue whether the CFTC alone should have jurisdiction over these products as futures. The CFTC issued exemptions permitting futures on commodity-based ETFs to trade as security futures products instead of treating them as futures on non-security commodities that it alone would regulate.[vi]
Options		
Options on non-security commodities—may be regulated as swaps or as trade options.[vii]	Options on:[viii] • Securities, without distinction between exempted or non-exempted. • Any group or index of securities, without distinction between broad or narrow-based or exempted or non-exempted securities, or any interest therein or based on the value thereof. Options on exchange-traded funds (ETFs) that passively hold non-security commodities such as gold, energy commodities, or foreign currencies are regulated as options on securities, but there is an issue whether the CFTC has jurisdiction over such products as options based	

CFTC	SEC	CFTC-SEC Jointly
	on the value of the underlying commodity. The CFTC has issued exemptions permitting such derivatives to trade on national securities exchanges, regulated as options on securities.[ix] Options on foreign currencies when listed on a national-securities exchange (otherwise regulated by the CFTC).[x]	
Swaps / Security-Based Swaps		
Swaps based on a non-security commodity, including options on a non-security-commodity Swaps based on: • A broad-based index of securities[xi] or • An exempted security as defined in Exchange Act section 3(a)(12).[xii] Options on securities or an index of securities are excluded from the swap definition and are regulated by the SEC.	Security-based swaps, i.e., swaps based on: • Any security other than an exempted security or foreign government debt security enumerated in SEC Rule 3a12-8 or • Any narrow-based securities index.	Mixed swaps, *i.e.*, security-based swaps with a component based on the value of one or more interest rates or other rates, currencies, commodities, instruments of indebtedness, indices, quantitative measures, other financial or economic interest or property of any kind (other than a single security or narrow-based security index), or the occurrence, nonoccurrence, or the extent of occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence not related to a single company or issuer.[xiii]
Hybrid Securities		
	If the conditions for the exclusion in CEA section 2(f) or the CFTC Part 34 Rules are met, the SEC will regulate securities with one or more payments indexed to the value, level, or rate of, or providing for the delivery of, one or more non-security commodities (hybrid instruments).	If the conditions for the exclusion in CEA section 2(f) or the CFTC Part 34 Rules are met, both agencies potentially could assert jurisdiction over securities with one or more payments indexed to the value, level, or rate of, or providing for the delivery of, one or more non-security commodities.
Cash Market Transactions		
Retail leveraged, margined, or financed transactions in commodities that are not securities or foreign currencies. Retail leveraged, margined, or financed transactions in foreign currencies offered by futures commission merchants or retail foreign exchange dealers.	Spot and forward transactions in securities. Retail leveraged, margined, or financed transactions in foreign currencies offered by broker-dealers. (SEC currently prohibits such activity.)	

[i] The CEA does not define the term broad-based security index, but it does define the term narrow-based security index, in CEA section 1a(35). An index is narrow-based if: (i) it has nine or fewer component securities; (ii) it has a single component security that comprises more than 30% of the index weighting; (iii) its five highest weighted component securities comprise in aggregate more than 60% of the index weighting, or (iv) its lowest weighted component securities that compromise in aggregate 25% of the index weighting have an aggregate dollar value of average daily trading volume of less than $50 million (or $30 million if the index has 15 or more component securities). The CFTC and SEC have jointly adopted rules defining the methodology for applying the statutory criteria. *See* 17 C.F.R. §§ 41.11, 41.12. In addition, they have jointly adopted rules defining the criteria for an index comprised of debt securities to be classified as non-narrow, and have agreed, pursuant to joint orders, to apply alternative criteria for classifying a volatility index as non-narrow.

[ii] The term exempted securities is defined in Exchange Act section 3(a)(12). 15 U.S.C. § 78c(a)(12). For purposes of allocating jurisdiction over futures and options on futures over exempted securities, the CEA limits the term to the definition as in effect on the date of enactment of the Futures Trading Act of 1982, but excluding municipal securities. 7 U.S.C. § 2(a)(1)(C)(iv). The Exchange Act definition includes U.S. government securities and any securities designated as exempted securities by the SEC by rule or regulation. Exchange Act section 3(a)(12) refers to "government securities" as defined in Exchange Act section 3(a)(42). That definition covers, *e.g.*, securities that are direct obligations of the United States or whose obligations are guaranteed as to principal or interest by the United States.

[iii] The SEC, in Rule 3a12-8, has designated debt obligations issued by the governments of 21 countries as exempted securities for the purpose of permitting futures contracts on such instruments to trade on U.S. futures exchanges (*i.e.*, designated contract markets) under the CEA regulatory framework. 17 C.F.R. § 240.3a12-8.

[iv] 7 U.S.C. § 2(a)(1)(D). The statutory provisions limit the securities underlying a security futures product to common stock "or such other equity securities" as the SEC and CFTC may agree. Pursuant to that authority, the two agencies issued orders permitting security futures on (1) American depositary receipts [Joint Order Granting the Modification of Listing Standards Requirements under Section 6(h) of the Securities Exchange Act of 1934 and the Criteria under CEA Section 2(a)(1) of the CEA, Exchange Act Release No. 44725 (Aug. 20, 2001), https://www.sec.gov/rules/other/34-44725.htm]; and (2) shares of exchange-traded funds, trust issued receipts, and registered closed-end investment companies [Joint Order Granting the Modification of Listing Standards Requirements Under Section 6(h) of the Securities Exchange Act of 1934 and the Criteria Under Section 2(a)(1) of the CEA, Exchange Act Release No. 46090, 67 Fed. Reg. 42,760 (June 25, 2002)]. They also each adopted a rule permitting security futures on individual debt securities. 17 C.F.R. §§ 41.21, 240.6h-2.

[v] 7 U.S.C. § 2(a)(1)(D).

[vi] The first was issued in 2008, covering futures on a gold ETF that the OneChicago Exchange proposed to list. Order exempting the trading and clearing of certain products related to SPDR® Gold Trust Shares Exemption Order, 73 Fed. Reg. 31,981 (June 5, 2008) [hereinafter SPDR Exemption Order].

[vii] The swap definition in CEA section 1a(47) includes options on commodities (as well as options on "interest or other rates, currencies . . . securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind"). The CFTC also has separate plenary authority to regulate options involving commodities under CEA section 4c(b). As explained above, the CFTC regulates commodity options as swaps, with the exception of trade options.

[viii] 7 U.S.C. § 2(a)(1)(C)(i)(I) provides that the CEA does not apply to options on securities or on any group or index of securities, or any interest therein or based on the value thereof. Such options also are excluded from the CEA "swap" definition in 7 U.S.C. § 1a(47). In contrast, such options are included in the definitions of "security" in the Exchange Act and the Securities Act.

[ix] The first was issued in 2008, covering listed options on a gold ETF. SPDR Exemption Order, 73 Fed. Reg. 31,981.

[x] 7 U.S.C. § 2(c)(2)(A)(iii).

[xi] The CFTC's jurisdiction over swaps on a broad-based securities index is circuitous, via cross-reference in the CEA swap definition to the broad definition of "security-based swap agreements" in section 206A of the Gramm-Leach-Bliley Act (15 U.S.C. § 78c note) in conjunction with Exchange Act provisions limiting the scope of security-

based swaps to swaps on a narrow index of securities and excluding such swaps from the security-based swap agreement definition. The Gramm-Leach-Bliley Act provision defines the term security-based swap agreement to mean "a swap agreement (as defined in Section 206A) of which a material term is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein." This definition, and the related swap agreement definition, were added to the Gramm-Leach-Bliley Act as part of the CFMA amendments enacted in 2000 and thus pre-date the Dodd-Frank amendments. The elements of the Exchange Act definition of security-based swap covering index products are limited by their terms to indexes that are a "narrow-based security index." 15 U.S.C. §§ 78c(a)(68)(A)(ii)(I), (III). The exclusion of security-based swaps from the separate definition of security-based swap agreement is set out in Exchange Act section 3(a)(78)(B), 15 U.S.C. § 78c(a)(78)(B).

[xii] The CFTC's jurisdiction over swaps on exempted securities comes about through an exclusion in the Exchange Act definition of the term security-based swap for swaps on exempted securities. 15 U.S.C. § 78c(a)(68); *see also* 7 U.S.C. § 1a(43) (cross-referencing the Exchange Act definition).

[xiii] *See* Swap Definition Rule, 77 Fed. Reg. at 48,291 ("The category of mixed swap is described, in both the definition of the term 'security-based swap' in the [Securities] Exchange Act and the definition of the term 'swap' in the CEA, as a security-based swap that is also based on the value of 1 or more interest or other rates, currencies, commodities, instruments of indebtedness, indices, quantitative measures, other financial or economic interest or property of any kind (other than a single security or a narrow-based security index), or the occurrence, nonoccurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence (other than an event described in subparagraph (A)(ii)(III) [of section 3(a)(68) of the Exchange Act]). A mixed swap, therefore, is both a security-based swap and a swap." (second alteration in original) (footnote omitted)).