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CFTC Proposes Interpretation to Address Cryptocurrency Delivery Questions

On December 15, 2017, the U.S. Commodity Futures Trading Commission (“CFTC”) issued its proposed interpretation¹ of the term “actual delivery” in the context of virtual currency retail commodity transactions. **Comments to the proposed interpretation are due to the CFTC by March 20, 2018.**

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The CFTC has exclusive jurisdiction to regulate commodity futures, options on futures and all derivatives within the definition of “swap.” Further, Section 2(c)(2)(D) of the Commodity Exchange Act (the “CEA”) grants the CFTC oversight authority over any transaction in a commodity that is entered into (a) with or offered to a person who is not an eligible contract participant or eligible commercial entity (a “retail customer”), (b) on a leveraged, margined or financed basis and (c) that does not result in “actual delivery” of the commodity within 28 days.² Such transactions are referred to as “retail commodity transactions” and are treated the same as futures contracts, meaning that they are not only subject to the CFTC’s anti-fraud and anti-manipulation authority, but that they must also be traded on registered futures exchanges.³

In August 2013, the CFTC released an interpretation of the term “actual delivery” that contained a list of relevant factors and examples (the “2013 Guidance”).⁴ The 2013 Guidance distinguishes “actual delivery” of commodities from situations where the underlying commodity has not actually left the seller’s control (referred to as “constructive delivery”). The examples set forth in the 2013 Guidance all require that actual delivery “involve transfer of title and possession of the commodity to the purchaser or a depository acting on the purchaser’s behalf.”⁵

In 2015 the CFTC found that virtual currencies are properly defined as commodities under the CEA and CFTC regulations.⁶ In 2016, the CFTC brought an enforcement action against an unregistered platform that offered virtual currency to retail customers on a leveraged, margined or financed basis on grounds that the virtual currency purchased was not actually delivered.⁷ With the December 2017 proposed interpretation, the CFTC aimed to clarify its construal of the term “actual delivery” with respect to virtual currency and seek comment from the public on various issues and questions created by the evolving and growing industry.

In the proposed interpretation, the CFTC did not provide a bright line definition of “virtual currency,” but rather stated broadly that, in the context of the proposal,

¹ Commodity Futures Trading Commission, Retail Commodity Transactions Involving Virtual Currency, 82 Fed. Reg. 60335 (Dec. 20, 2017); available at www.gpo.gov/fdsys/pkg/FR-2017-12-20/pdf/2017-27421.pdf (hereafter, the “Proposed Interpretation”).

² CEA Section 2(c)(2)(D)(ii)(III)(aa).

³ CEA Section 2(c)(2)(D); *see also* CEA Sections 4(a), 4(b), 4b.

⁴ *See* Retail Commodity Transactions under the Commodity Exchange Act, 78 Fed. Reg. 52426 (Aug. 23, 2013).

⁵ Proposed Interpretation at 60337.

⁶ *See* In re Coinflip, Inc., d/b/a Derivabit, and Francisco Riordan, CFTC Docket No. 15-29 (Sept. 15, 2015).

⁷ *See* In re BFXNA INC. d/b/a BITFINEX, CFTC Docket No. 16-19 (June 2, 2016) (consent order). The actual delivery exception was not met by the platform because the offering entity “held the purchased bitcoins in bitcoin deposit wallets that it owned and controlled.”

virtual or digital currency: (e)ncompasses any digital representation of value (a “digital asset”) that functions as a medium of exchange, and any other digital unit of account that is used as a form of a currency (i.e., transferred from one party to another as a medium of exchange); may be manifested through units, tokens, or coins, among other things; and may be distributed by way of digital “smart contracts,” among other structures.⁸

The CFTC stated that it will continue to follow the interpretation of “actual delivery” set forth in the 2013 Guidance and assess whether actual delivery has occurred by examining if:

1. A customer has the ability to (i) take possession and control of the entire quantity of the commodity (whether it was purchased on margin or using leveraging or financing) and (ii) use the commodity freely in commerce no later than 28 days from the transaction date; and
2. The offeror and counterparty seller (and the affiliates of each) do not retain any interest in, or control over, any of the commodity purchased at the end of the 28-day period.⁹

The proposed interpretation also set forth several examples (summarized below) that apply the above guidelines to virtual currency transactions:

- Actual delivery *will* have occurred if, within the 28-day window, there is a record of the transfer on the relevant publicly distributed ledger or blockchain of the entire amount of the purchased virtual currency being completely transferred from the counterparty seller to the purchaser in accordance with the above rules (or, in the case where a third-party intermediary is employed, a record of the two complete transfers).
- Actual delivery *will* have occurred if, within the 28-day window: (i) the entire amount of the virtual currency purchased has been delivered into the possession of a depository (*i.e.*, a wallet or similar storage system) that is not owned, operated or controlled by the counterparty seller or its affiliates, which depository has agreed with the purchaser to hold the virtual currency as agent without regard to any interest asserted by the counterparty seller; (ii) the counterparty seller has transferred title to the purchaser; (iii) the purchaser has secured complete control over the virtual currency; and (iv) no liens or other interests of the seller resulting from the use of margin, leverage or financing will continue past the end of the 28-day window.
- Actual delivery *will not* have occurred (i) if evidenced only by a book entry by the offeror or counterparty seller that delivery has been made (*i.e.*, there needs to be a record made on a publicly distributed ledger or a depository transfer); or (ii) if, within the 28-day window, the transaction is rolled, offset against, netted out or settled in cash or another virtual currency between the two parties.¹⁰

In addition to inviting general comment on the proposed interpretation, the CFTC requested input on several specific questions stemming from the new territory. They include such topics as how to ensure “full control” by a purchaser (possession of a unique cryptographic key?); how to clarify the meaning of “depository”; whether to create certain registration exemptions so not to discourage virtual currency platforms; whether to amend the 28-day delivery period (as virtual currency transactions should take much less time to deliver); and how to interpret the scope of the U.S. Securities and Exchange Commission’s jurisdiction over virtual currency units that are deemed to be securities.

Please contact [Deborah Monson](#), [Jeremy Liabo](#), [Anne Fox](#), [William Schoenfeld](#) or the Ropes & Gray attorney who usually advises you with any questions you may have or if you would like additional information.

⁸ Proposed Interpretation at 60338.

⁹ Id at 60339.

¹⁰ Id at 60340.