

# Commodities, Derivatives and Digital Currencies

*2024 Developments in the Regulation of Financial Products Conference -  
The Catholic University of America Columbus School of Law*

Date: OCT 4, 2024

Time : 1:00 PM - 2:30 PM



# Panelists

- **Mark Ruddy**, Managing Partner, Ruddy Gregory PLLC
- **Kevin Batteh**, Partner, Delta Strategy Group
- **Connor Guerin**, Senior Investigator, FINRA, Catholic Law Student
- **Steve Humenik**, SVP, Global Head of Capital Markets, Legal & Head of Clearing, Crypto.com
- **Eric Juzenas**, Associate Director, Division of Trading and Markets, SEC

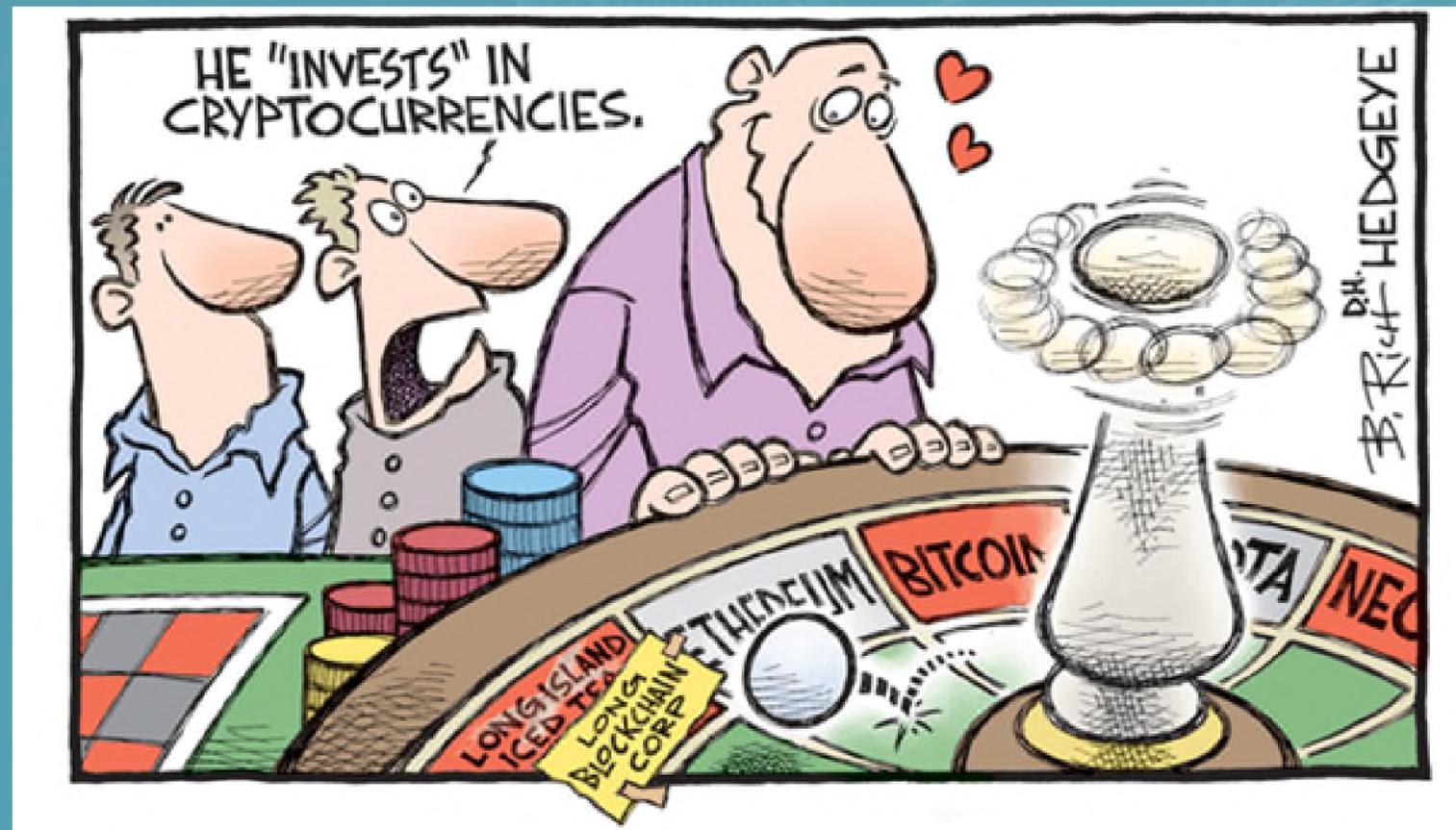


# Regulation of Cryptocurrency and Digital Assets in the US:

## Overview

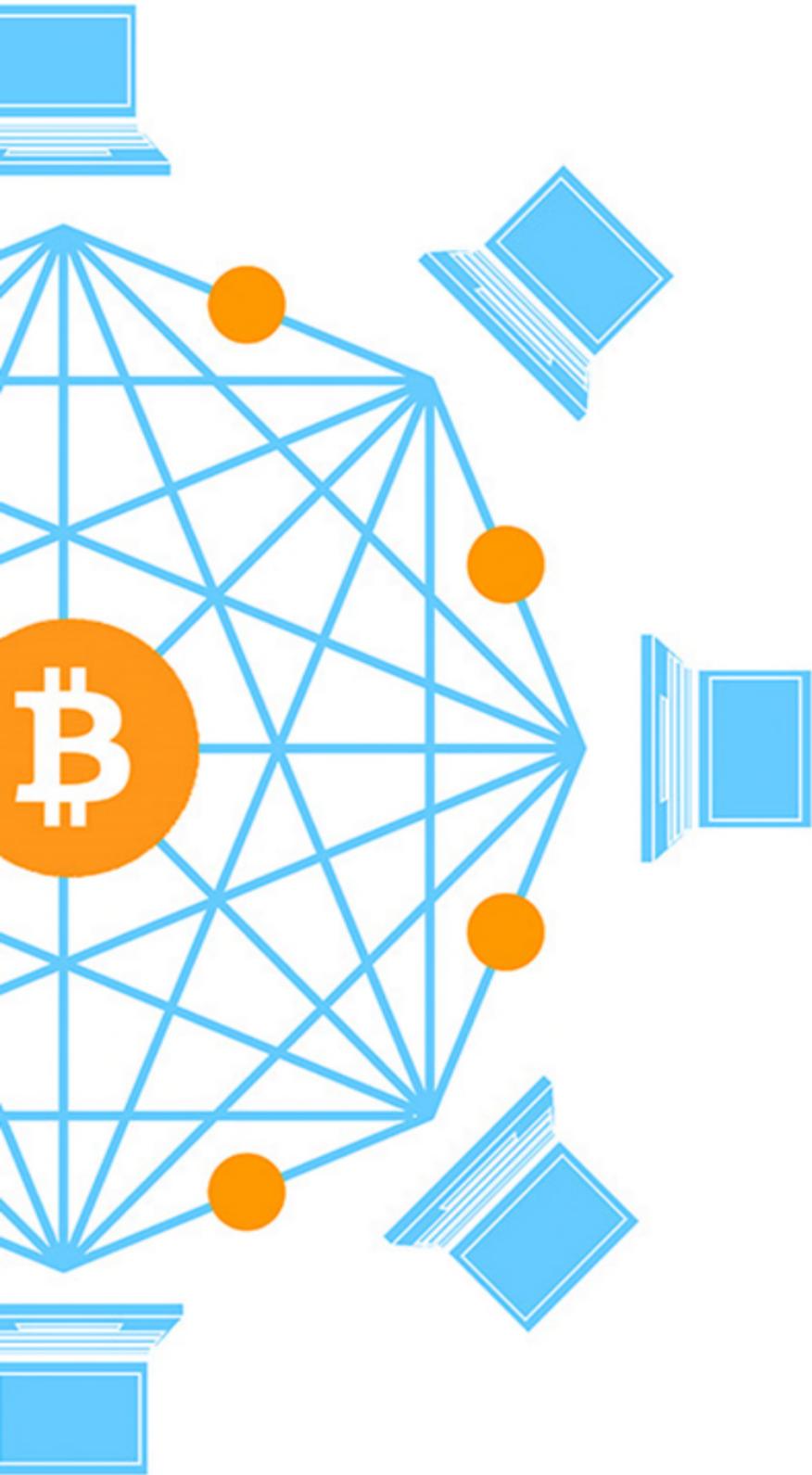
Q: Cryptocurrency vs Digital Assets: What is the distinction?

A: Cryptocurrency is a type of digital asset.



# Types of Digital Assets – Terminology

- Digital assets, Virtual assets, Crypto assets
- Digital coins, Digital tokens
- Native tokens, Utility tokens, Governance tokens
- Security tokens, Crypto-asset securities
- Cryptocurrency (e.g., bitcoin), Virtual currency, Digital currency
- Stablecoins
- Central bank digital currency (CBDC)
- Non-fungible tokens (NFTs), Asset-linked tokens



# Primary US Federal Regulators with Jurisdiction Over Parties Accessing US Markets

- **Securities and Exchange Commission (SEC)** – Investor protection, enforcement of US securities laws.
- **Commodity Futures Trading Commission (CFTC)** – Commodities, antifraud, registration of exchanges/platforms and FCMs.
- **Financial Crimes Enforcement Network (FinCEN)** – Bank Secrecy Act (BSA)/Anti-Money Laundering (AML), countering the financing of terrorism (CFT), regulation of money services businesses (MSBs), which include “money transmitters.”
- **Office of Foreign Assets Control (OFAC)** – Economic sanctions.
- **US prudential bank regulators: OCC, FDIC, Fed/FRB** – digital asset and crypto activities of banks (note November 23, 2021 joint statement).
- **US Treasury/Internal Revenue Service (IRS)** – Taxation of revenue.
- **Department of Justice (DOJ)** – Criminal enforcement



# SEC Regulation of Digital Assets

**DAO Report.** On July 25, 2017, the SEC issued a report, known as The DAO Report, which indicated that digital coins sold in ICOs may be digital asset securities subject to the federal securities laws under the Howey test.

**Is it a Security?** Before a digital token may be sufficiently “decentralized” (like bitcoin), often during its developmental stages, US securities laws may apply.

## **FinHub Framework for Analyzing Offer and Sale of Digital Assets**

On April 3, 2019, the SEC Strategic Hub for Innovation and Financial Technology (FinHub) provided guidance on the Howey elements as applied to digital assets. Among other elements, to avoid classification as a security, any economic benefit derived from appreciation in value of the digital asset must be incidental to its intended functionality (based on June 2018 speech by former Director of SEC Division of Corporation Finance William Hinman). The FinHub framework is not an official SEC rule, regulation, or statement.

# SEC Regulation of Digital Assets

## Exchange Traded Products (ETPs)

On January 10, 2024, the SEC approved Spot Bitcoin ETP applications for the first time.

Since January, the SEC has also approved Spot Ethereum ETPs which made their market debut on July 23, 2024.

BlackRock's fund iShares Bitcoin Trust was approved on September 20, 2024 and given the ticker symbol "IBIT."

ETPs are pooled investment funds that gather and invest money from investors. ETPs trade throughout the day on national securities exchanges. Institutional investors and traders now have an alternative method of exposure to the various cryptocurrencies.



# What are Blockchains?

A blockchain is a distributed database or ledger shared across a computer network's nodes. They are best known for their crucial role in cryptocurrency systems, maintaining a secure and decentralized record of transactions, but they are not limited to cryptocurrency uses. Blockchains can be used to make data in any industry immutable—meaning it cannot be altered

## SEC v. Ripple Labs, Inc.,

The SEC sued Ripple Labs in 2020, alleging that its offer and sale of the XRP token, a crypto asset based on the XRP ledger, constituted an unregistered securities offering. In July, the court issued a split ruling that the offer and sale of XRP to institutional investors was an unregistered securities offering but not the offer and sale of XRP to retail investors on crypto trading platforms or in other distributions.

It all came down to the Howey test.

**Howey test: SEC v. W.J. Howey Co., 328 U.S. 293 (1946) – Is there an investment contract?**

- **Investment of money.**
- **In a common enterprise.**
- **Reasonable expectation of profits.**
- **Based on the efforts of others – active participant or “AP.”**



**Brad Garlinghouse**  @bgarlinghouse · Jul 13, 2023 ...

The most important part of this ruling:

“XRP, as a digital token, is not in and of itself a “contract, transaction[,] or scheme” that embodies the Howey requirements of an investment contract.”

This is now a matter of law (not up for trial.)

 1.5K  9.9K  30K  3.6M  



**Brad Garlinghouse**  @bgarlinghouse · Aug 7 ...

The SEC asked for \$2B, and the Court reduced their demand by ~94% recognizing that they had overplayed their hand. We respect the Court’s decision and have clarity to continue growing our company.

This is a victory for Ripple, the industry and the rule of law. The SEC’s

[Show more](#)

 2.7K  9.3K  28K  2.4M  



## Prediction Markets

Prediction Markets are similar to futures markets for commodities or other financial asset prices. The price in a prediction market is a bet that a particular event will occur. Unlike public markets, where bets are placed indirectly on intangibles, such as government policy or the possible outcomes of an election (via the effects these things are expected to have on asset prices), prediction markets enable users to bet directly on a piece of information that they believe is valuable.

\*\*\*\*

## CFTC Regulation of Prediction Markets

CFTC Regulate Prediction Markets under the Commodity Exchange Act (CEA) Section 5c(c)(5)(C). It gives power to the CFTC to review and prohibit trade of event contracts involved with the following categories: “war, terrorism, gaming, assignation, activity that is unlawful under any federal or state law, or other similar activity determined by the Commission, by rule or regulation, to be contrary to public the interest.”

## CFTC Amendments to CEA 5c(c)(5)(C) in 2024

This summer the CFTC requested comments on a rule change to the CEA regarding events contracts. This rule change when enacted would make the following changes:

- Involved would be defined to include “related to”
- Expand the definition of gaming that would now encompass political betting
- Clarify that event contracts involving activities enumerated in Section 5c(c)(5)(C) of the CEA (e.g., “gaming”, war, terrorism, assassination) are “contrary to the public interest” and prohibited from trading or clearing. CFTC clarified that event contracts would not include economic indicators like currency.
- Provide factors used in determining whether an event contract is contrary to the public interest (e.g., national security, profiting from harm to any person).



## Background on Kalshi

**Kalshi, a prediction market, is a CFTC regulated exchange dedicated to trading on the outcome of future events, allowing people to trade on a broad range of topics. An order the CFTC issued a year ago banned KalshiEX from listing and trading binary (yes/no) event contracts based on U.S. election results. The lower court ruled in favor of KalshiEX stating that under *Loper* CFTC had exceeded its statutory authority. The District of Columbia Circuit received opposing takes on whether it should continue to stay lower court orders allowing political event contracts while it considers the CFTC's appeal. (Reply of Appellant, (KalshiEX LLC v. CFTC, No. 24-5205 (D.C. Cir. filed Sept. 14, 2024**



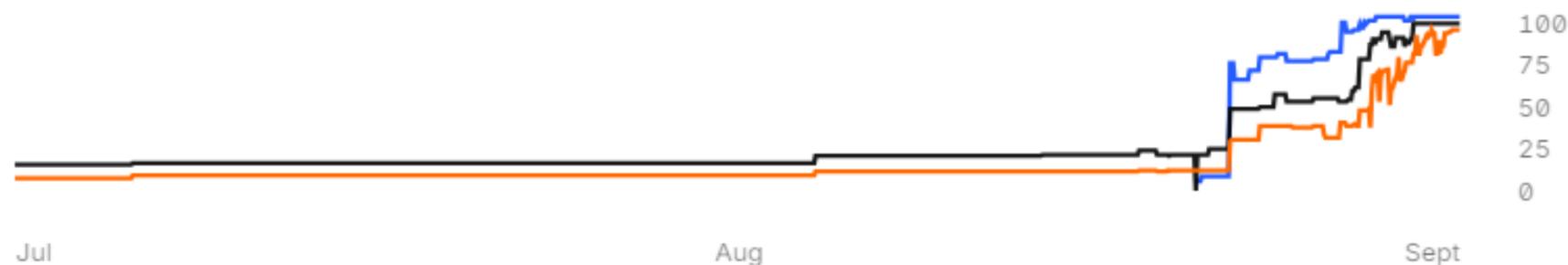
# Florida orders evacuations as Hurricane Helene reaches Cat 4

Hurricane Helene has intensified to a Category 4 storm with 130 mph winds as it nears Florida's Big Bend, the National Hurricane Center announced. According the NBC News, authorities are urging residents to evacuate immediately, warning of catastrophic storm surges and severe damage.

## Hurricane Helene category?

● Category 1 or above 99% ● Category 2 or above 99% ● Category 3 or above 99%

Kalshi



24% chance · Category 5 or above

Yes No

Weekly jobless claims fall to four-month low

Bitcoin surges to two-month high on Fed cuts, China stimulu



## US GDP growth in Q3 2024?

61% chance · Above 2.4%

Yes No



## Hurricane Helene category?

24% chance · Category 5 or above

Yes No



## Best LLM at the end of the year?

78% chance · GPT



## When will OpenAI achieve AGI?

38% chance · Before 2030

## Bitcoin Derivatives Self-Certification Process and First Bitcoin Futures Contracts

On December 1, 2017, the CFTC published a fact sheet outlining self-certification process for bitcoin-based derivatives products core principles that exchanges must use when self-certifying a new bitcoin derivatives contract to comply with CEA and CFTC regulations. On this date the CFTC also announced three exchanges self-certified new bitcoin futures contracts under these procedures.





# Self-Certification Today

The CFTC on September 12, 2024 adapted its rule for self certifications. These changes are intended to clarify terms and requirements for the entities and to help streamline the process. One change is to provide a concise explanation and analysis on both the product's terms and conditions as well as the registered entities' rules.



**Here Comes Joe...**

# President Biden's Executive Order on Responsible Development of Digital Assets

On March 9, 2022, President Biden issued an executive order (Biden EO) directing a “whole of government” effort to assess the risks and benefits of US-government sponsored digital assets and their related technology.

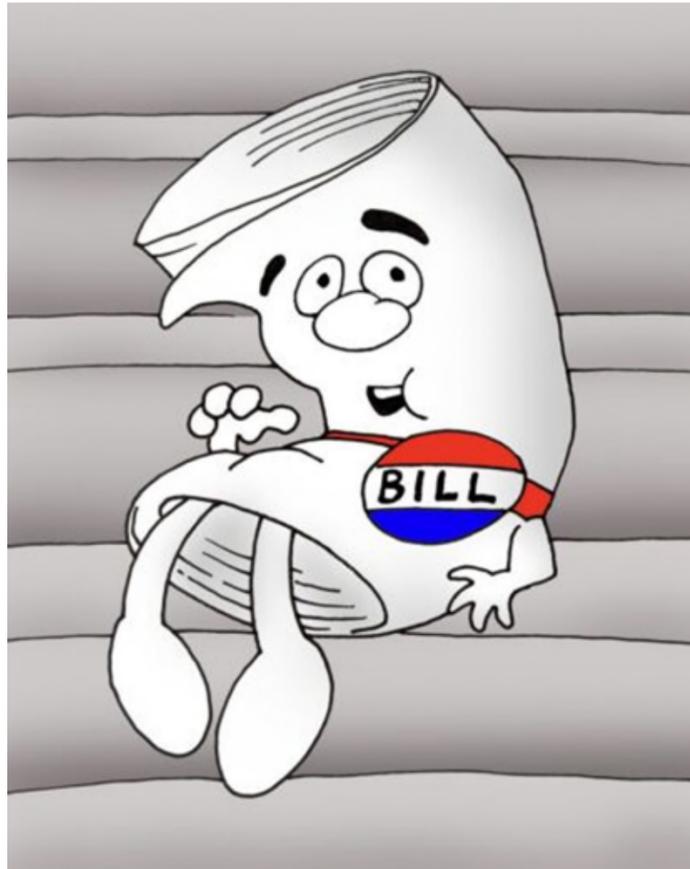
## Goals:

- Protect US consumers, investors, and businesses.
- Protect US and global financial stability and mitigate systemic risk.
- Mitigate illicit finance and national security risks posed by the use of digital assets.
- Promote US leadership in technology and economic competitiveness to reinforce US leadership in the global financial system.
- Support technological advances and ensure responsible development and use of digital assets.

The order called for research on whether a US CBDC is in the national interest and sets out six key priorities: consumer and investor protection; promoting financial stability; countering illicit finance; U.S. leadership in the global financial system and economic competitiveness; financial inclusion; and responsible innovation.



# Proposed Legislation on Digital Assets



♪ I'm just a bill, yes I'm  
only a bill

And I'm sitting here  
on Capitol Hill... ♪

# Digital Commodities Consumer Protection Act of 2022

On August 3, 2022, US Senators Debbie Stabenow (D-MI), John Boozman (R-AR), Cory Booker (D-NJ), and John Thune (R-SD) introduced legislation that would authorize the CFTC to regulate "digital commodity platforms" and "digital commodity" trading, which would give the CFTC primary oversight over most crypto trading platforms in the US and exclusive jurisdiction over "digital commodity" trades, except where a merchant or consumer is using a digital commodity solely for the purchase or sale of a good or service.

This bill is the predecessor to Senator Stabenow's proposed (but not introduced) Digital Commodity Act of 2024, which stalled this summer. Senator Boozman stated he has "outstanding concerns" over the bill, and that the legislation should not be rushed.

# Digital Commodity Exchange Act of 2022

On April 28, 2022, US Representatives Glenn Thompson (R-Pa.), Ro Khanna (D-Ca.), Darren Soto (D-Fl.), and Tom Emmer (R-Mn.) introduced the Digital Commodity Exchange Act of 2022 (DCEA), which would create a regulatory framework for digital commodity developers, dealers, and exchanges. The bill would:

- Authorize the CFTC to register and regulate trading venues offering spot or cash digital commodity markets as digital commodity exchanges (DCEs).
- Require DCEs to register with the CFTC if they want to offer leveraged trading or list for sale digital commodities that were distributed to individuals before being available to the public.
- Expand CEA self-certification process to DCEs seeking to list new digital commodities for trading.
- Permit asset-backed stablecoin operators to register with the CFTC as fixed-value digital commodity operators.
- Expand CEA definition of futures commission merchant to include entities that hold customer funds and serve as intermediaries for a registered entity in the trading of, or act as counterparties for the spot or leveraged trading of, digital commodities.
- This bill serves as the predecessor to the FIT21 bill.

# The Financial Innovation and Technology for the 21<sup>st</sup> Century Act (FIT21)

On May 22, 2024, FIT21 passed in the House of Representatives. This is the first time major digital asset legislation has passed in a chamber of Congress.

The bill separates digital assets into three categories to be subject to either SEC or CFTC jurisdiction

- “restricted digital asset” subject to SEC jurisdiction;
- “digital commodity” subject to CFTC jurisdiction; or
- “permitted payment stablecoin” subject to either SEC or CFTC jurisdiction, depending on the nature of the intermediary involved in a transaction.

# The Financial Innovation and Technology for the 21<sup>st</sup> Century Act (FIT21)

Under FIT21, a digital asset would be considered a “restricted digital asset” unless it meets the definition of a “permitted payment stablecoin,” or is self-certified as a “digital commodity.”

Whether a digital asset is considered a “digital commodity” or a restricted digital asset” is based on:

- the level of decentralization and functionality of the digital asset’s underlying blockchain system;
- the method of acquisition of the digital asset by an end user; and
- the party holding the digital asset (e.g., issuer or unaffiliated third party)

# The Financial Innovation and Technology for the 21<sup>st</sup> Century Act (FIT21)

## Stablecoins

The bill would define “permitted payment stablecoins” as digital assets issued by an issuer subject to regulation by a federal or state regulator which:

- are used or designed to be used as means of payment or settlement;
- the issuer of which (a) is obligated to redeem for a fixed monetary value or (b) represents the asset will maintain or creates the reasonable expectation that it will maintain stable value relative to a fixed amount of monetary value; and
- excludes (a) national currency or (b) securities issued by a registered investment company.

# The Financial Innovation and Technology for the 21<sup>st</sup> Century Act (FIT21)

## Digital Asset Intermediaries

FIT21 will require digital asset intermediaries to register with the SEC or CFTC, based on the type of digital asset being transacted.

- The SEC would have oversight of “qualified digital asset custodians” for “restricted digital assets” and digital asset brokers, digital asset dealers and digital asset trading systems.
- The CFTC would have oversight of “qualified digital asset custodians” for “digital commodities” and digital commodity exchanges, brokers, or dealers.
- The bill directs the SEC and CFTC to issue joint rulemaking for dual registration by intermediaries with each agency.
- Digital asset intermediaries would be subject to anti-money laundering (AML) laws and must comply as “financial institutions” under the Bank Secrecy Act (BSA).



# CFTC-SEC Joint Advisory Committee on Digital Assets

Each Commission will appoint 10 nongovernmental stakeholders to provide advice on digital asset rules, regulations, and policies. The bill directs the CFTC and SEC to jointly conduct a study to assess whether additional guidance or rules are necessary to facilitate the development of tokenized securities and derivatives products (which would represent application of blockchain technology to the broader financial market).





# Virtual Currency Tax Fairness Act

**On July 25, 2024, US Senators Kirsten Gillibrand (D-NY) and Patrick Toomey (R-Pa.) introduced the Virtual Currency Tax Fairness Act, designed to simplify the use of digital assets for everyday purchases by exempting from taxation small personal transactions using VC for goods and services under \$50.**



# Digital Asset Anti-Money Laundering Act of 2023

**On July 27, 2023, US Senators Elizabeth Warren (D-MA) and Roger Marshall (R-KS) introduced the Digital Asset Anti-Money Laundering Act of 2022 (DAAMLA), which would authorize FinCEN to designate digital asset wallet providers, miners, validators, and other select network participants as money service businesses (MSBs). This designation would require these parties to register with FinCEN and comply with AML requirements under the BSA.**



# Regulation of Cryptocurrency and Digital Assets in the US: Overview

## Regulation of Stablecoins

### What are Stablecoins?

Stablecoins are cryptocurrencies whose value is tied to that of another currency, commodity, or financial instrument. Stablecoins can be pegged to a currency like the U.S. dollar and aim to provide an alternative to the more volatile cryptocurrencies.

# Regulation of Cryptocurrency and Digital Assets in the US:

## Overview

### Regulation of Stablecoins (cont'd.)

#### TRUST Act (Toomey proposal).

On April 6, 2021, by Sen. Pat Toomey (R-PA) introduced the Transparency of Reserves and Uniform Safe Transactions (TRUST) Act, which would authorize OCC to regulate national limited payment stablecoin issuers and would permit depository institutions to issue payment stablecoins. The TRUST Act would subject all payment stablecoin issuers, including those operating as state money transmitters and those receiving a new federal license, to standardized requirements, including: disclosures regarding the reserve assets backing the stablecoin.

redemption policies.

Routine attestations by registered public accounting firms.

# Regulation of Cryptocurrency and Digital Assets in the US: Overview

## Regulation of Stablecoins (cont'd.)

### Responsible Financial Innovation Act

On October 26, 2023, US Senators Kirsten Gillibrand (D-NY) and Cynthia Lummis (R-WY) introduced the Responsible Financial Innovation Act (RFIA), which would create a regulatory framework for digital assets, including stablecoins. The legislation would permit depository institutions to issue payment stablecoins. All issuers of payment stablecoins would be required to:

- Maintain high-quality liquid assets valued at 100% of the face value of all outstanding payment stablecoins.
- Provide public disclosures on the assets backing the stablecoin and its value.
- Have the ability to redeem all outstanding payment stablecoin at par in legal tender.

# The Global Regulation of Cryptocurrency and Digital Assets

## Global standard-setting bodies

- **Financial Action Task Force (FATF)**
- **Basel Committee on Banking Supervision (BCBS)**
- **International Organization of Securities Commissions (IOSCO)**
- **Bank for International Settlements (BIS)**
- **Financial Stability Board (FSB)**



# Financial Action Task Force

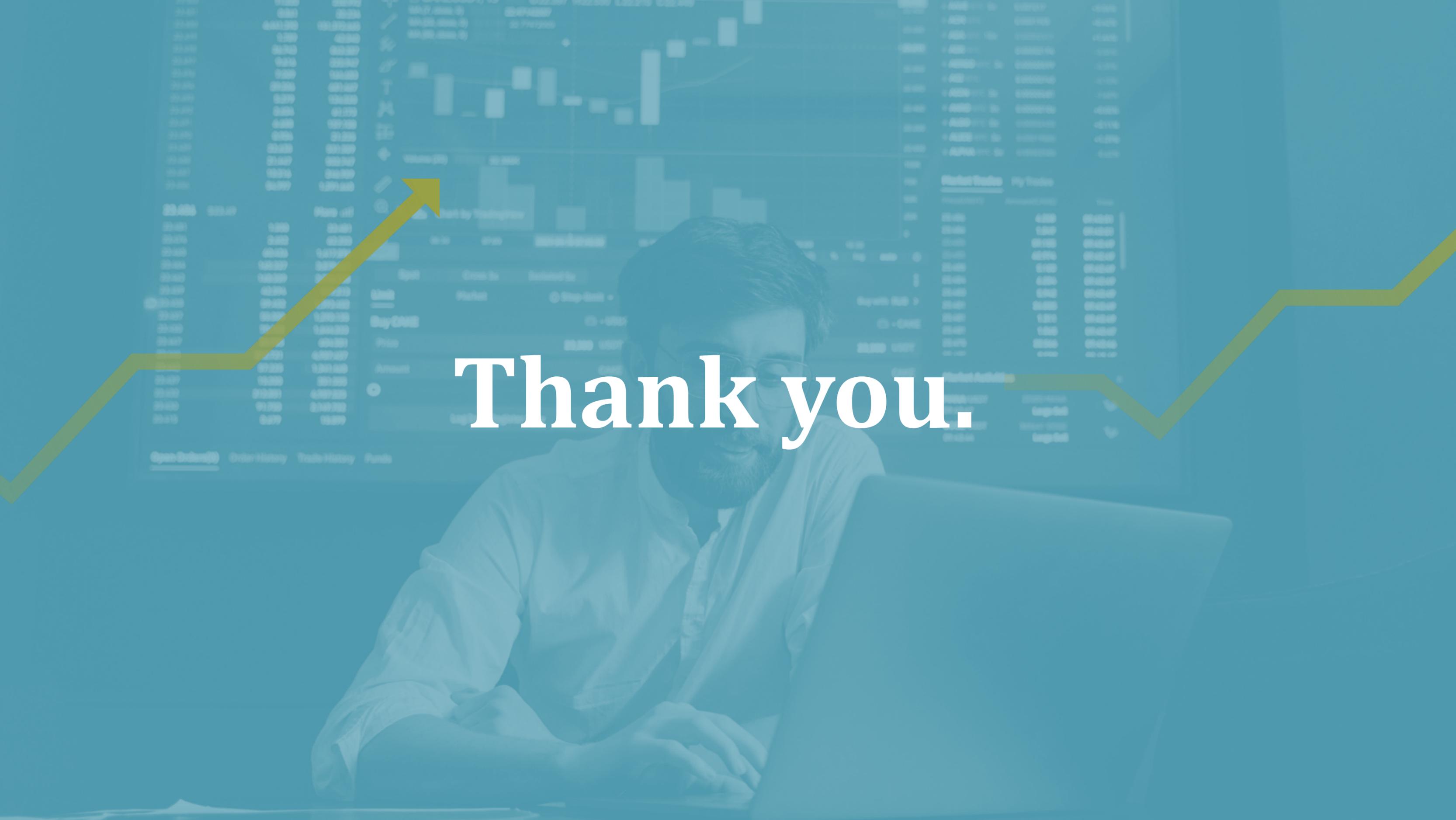
The Financial Action Task Force (FATF) leads global action to tackle money laundering, terrorist and proliferation financing. The FATF created the “Travel Rule” or Recommendation 16 which was last updated in 2021 and mandates that Virtual Asset Service Providers and financial institutions involved in Virtual Asset transfers share transaction details, such as sender and receiver information to prevent money laundering and terrorist financing.



# Basel Committee on Banking Supervision

The Basel Committee on Banking Supervision (BCBS) sets global standards for the regulation of banks. The BCBS has created a disclosure framework for banks' exposure to crypto which must be implemented by the start of 2026. Banks will be required to disclose qualitative information on their crypto activities and quantitative information on their exposure to crypto.





Thank you.