How the Digital Commodities Consumer Protection Act of 2022 would broaden the CFTC’s authority to regulate cryptocurrencies and other digital assets

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The total market capitalization of the global cryptocurrency market has returned to $1.1 trillion, despite a bleak performance in June. It's estimated that one in five Americans has used or traded digital assets. Given the value of this market and the volume of American participation, legislators continue to introduce bills aimed at regulating cryptocurrency markets.

Earlier in June, Senators Kirsten Gillibrand (D-NY) and Cynthia Lummis (R-WY) introduced the Responsible Financial Innovation Act (the RFIA), which proposed to address significant issues arising at the intersection of traditional financial regulation and digital asset innovation across taxation, securities, banking and consumer protection. One method the RFIA proposed to accomplish this was to give the Commodity Futures Trading Commission (the CFTC) clear authority over applicable digital asset spot markets, thereby affecting digital assets that met the definition of a commodity, such as
bitcoin and ether.

A bill introduced on August 3—the Digital Commodities Consumer Protection Act of 2022 (DCCPA)—borrowed language from the RFIA but also introduced its own concepts, which could grant the CFTC increased control over this asset class. As discussed below, the DCCPA, introduced by US Senators Debbie Stabenow (D-MI), chair of the Senate Committee on Agriculture, Nutrition, and Forestry, and John Boozman (R-AR), ranking member, along with Senators Cory Booker (D-NJ) and John Thune (R-SD), would aim—like the RFIA—to close regulatory gaps between state and federal regulation of cryptocurrencies, but to varying degrees.

Characteristics of DCCPA

The core proposals of the DCCPA are to:

- Close regulatory gaps by requiring all digital commodity platforms (defined to mean a person that is one or more of the following: digital commodity broker, a digital commodity custodian, a digital commodity dealer, a digital commodity trading facility) to register with the CFTC
- Require digital commodity platforms to prohibit abusive trading practices, eliminate or disclose conflicts of interest, maintain sufficient financial resources, have strong cybersecurity programs, protect customer assets and report suspicious transactions
- Require digital commodity platforms to adhere to advertising standards and disclose information about digital commodities and their risks, bringing greater transparency and accountability to the marketplace
- Authorize the CFTC to impose user fees on digital commodity platforms to fully fund its oversight of the digital commodity market
- Direct the CFTC to examine racial, ethnic and gender demographics of customers participating in digital commodity markets and use that information to inform its rulemaking and provide outreach to customers and
- Recognize that other financial agencies have a role in regulating digital assets that are not commodities, but function more like securities or forms of payment.

Comparing RFIA and DCCPA

In general, the DCCPA could give the CFTC broader discretion in regulating cryptocurrency markets than the RFIA. For example, the DCCPA would grant the CFTC a greater ability to interpret exactly which kinds of assets constitute those subject to the CFTC’s oversight.

The RFIA defined certain cryptocurrencies under the Commodities Exchange Act (the Act) as “digital assets,” meaning “a natively electronic asset that confers economic, proprietary, or access rights or powers; and is recorded using cryptographically secured distributed ledger technology, or any similar analogue.” The DCCPA, in contrast, proposes to defined certain cryptocurrencies under the Act as “digital commodities,” meaning, “a fungible digital form of personal property that can be possessed and transferred person-to-person without necessary reliance on an intermediary.” “Digital commodities” would include “property commonly known as cryptocurrency or virtual currency, such as Bitcoin and Ether” and would exclude “an interest in a physical commodity; a security; a digital form of currency backed by the full faith and credit of the United States; [with an exception], an instrument regulated by the [CFTC] pursuant to any provision of the Act other than section 2(c)(2)(F); or any other instrument that the [CFTC] determines not to be a digital commodity.”

Where the RFIA explicitly defines the rights that an electronic asset must confer to be regarded as a “digital asset,” the DCCPA leaves the interpretation of which rights must be conferred in a larger degree to the CFTC by describing “digital commodities” as “personal property” rather than, “a natively electronic asset that confers economic, proprietary, or access rights or powers.”

Still, even though the definition of digital commodity excludes securities, the definition does not explicitly answer when digital assets might constitute a security, unlike the RFIA. This could create tension between the SEC and CFTC over jurisdiction of this asset class based on the SEC’s application of the Howey test, potentially resulting in more of this asset class being classified as securities.

In addition to wider latitude to interpret which cryptocurrencies constitute assets subject to the CFTC’s jurisdiction, the DCCPA also grants CFTC broader discretion in regulating digital asset exchanges, which grants it greater control over how such assets are traded. For example, the RFIA explicitly prohibits digital asset exchanges from permitting “trading in a digital asset, if it is reasonably likely that the transaction history of the digital asset can be fraudulently altered by any
person or group of persons acting collectively; or functionality or operation of the digital asset can be materially altered by any group or group of persons under common control." The RFIA continues to establish specific considerations for the digital asset exchange to use when evaluating whether the above description is satisfied. In contrast, while the DCCPA also “permit[s] trading only in transaction in digital commodities that are not readily susceptible to manipulation,” it does not explicitly prompt the digital asset exchange on how it must evaluate this question. Accordingly, while the DCCPA is aimed at regulating the cryptocurrency marketplace, it generally does so with a looser touch than the RFIA.

As shown through these two examples, the DCCPAs broader language generally marks the DCCPA as more ambitious in terms of what regulatory authorities it may grant the CFTC, by virtue of the greater room it provides for the agency to interpret the legislation and create regulations enforceable against entities operating under its oversight.

Either bill would strengthen CFTC’s powers in the crypto marketplace

While each of these bills would give the CFTC a different degree of discretion, the CFTC will become a stronger regulatory force in cryptocurrency markets if either bill passes. Market participants are encouraged to monitor developments related to the trading of cryptocurrencies to ensure their trading practices remain consistent with current rules.

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