

March 20, 2018

VIA ELECTRONIC SUBMISSION

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Comments on the Proposed Interpretation, *Retail Commodity Transactions Involving Virtual Currency* (RIN 3038-AE62)

Dear Mr. Kirkpatrick:

I. INTRODUCTION

On behalf of The Commercial Energy Working Group (the "**Working Group**"), Eversheds Sutherland (US) LLP submits this letter in response to the request for public comment set forth in the Commodity Futures Trading Commission's ("**CFTC**" or "**Commission**") Proposed Interpretation, *Retail Commodity Transactions Involving Virtual Currency* ("**Proposed Interpretation**").¹

The Working Group is a diverse group of commercial firms in the energy industry whose primary business activity is the physical delivery of one or more energy commodities to others, including industrial, commercial, and residential consumers. Members of the Working Group are producers, processors, merchandisers, and owners of energy commodities. Among the members of the Working Group are some of the largest users of energy derivatives in the United States and globally. The Working Group considers and responds to requests for comment regarding regulatory and legislative developments with respect to the trading of energy commodities, including derivatives and other contracts that reference energy commodities.

¹ Proposed Interpretation, *Retail Commodity Transactions Involving Virtual Currency*, 82 Fed. Reg. 60,335 (Dec. 20, 2017), <http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2017-27421a.pdf>.

II. COMMENTS OF THE WORKING GROUP

The Working Group commends the CFTC's continued efforts to promote market stability and transparency while facilitating innovation and advancements in market operations. In this respect, the Working Group appreciates that the CFTC recognizes that the blockchain technology underlying virtual currency has the "potential to yield notable advancements in applications of financial technology."² Given the potential implications, the Working Group welcomes the opportunity to comment on the Proposed Interpretation, which was issued to provide the CFTC's view regarding the meaning of "actual delivery" in the context of retail commodity transactions in virtual currency, as the term is used in Commodity Exchange Act ("**CEA**") Section 2(c)(2)(D)(ii)(III)(aa).^{3,4}

Members of the Working Group see potential in distributed ledger technology to enhance the sale, movement, storage, and processing of commodities. To that end, the Working Group encourages the Commission to carefully craft rules for the direct or indirect trading of virtual currencies or other digital assets based upon blockchain or other distributed ledger technologies. Such rules should not hinder the adoption of blockchain technology for use in other aspects of commodities trading or in other areas of the commodities value chain.

A. Application of the CFTC's Interpretation Should Be Limited to the Analysis of Retail Commodity Transactions in Virtual Currency

The CFTC should explicitly limit the application of concepts developed from the Proposed Interpretation to the analysis of retail commodity transactions in virtual currency. While such interpretations may inform the analysis of other types of transactions, they should not constrain or otherwise control the analysis. In particular, the Working Group recommends the CFTC state that the interpretations do not control the legal analysis for the following types of transactions:

² Proposed Interpretation at 60,338.

³ *Id.* at 60,337.

⁴ Pursuant to the Proposed Interpretation, the following two primary factors would need to be met to demonstrate "actual delivery" of retail commodity transactions in virtual currency:

- (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 leverage, or any other financing arrangement, and (ii) use it freely in commerce (both within and away from any particular platform) no later than 28 days from the date of the transaction; and
- (2) 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) not retaining any interest in 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.

Id. at 60,339.

- transfers of digital assets between eligible contract participants or eligible commercial entities;⁵
- transactions for physical commodities effected through blockchain or other distributed ledger technologies; or
- trading of environmental commodities (e.g., renewable identification numbers (“**RINs**”) or renewable energy credits (“**RECs**”).

This recommendation from the Working Group promotes the avoidance of unforeseen consequences. The CFTC faces a difficult task in implementing the CEA as technology changes and trading evolves. However, general interpretations have the potential to overlook important technical or subtle variances between different types of transactions. The CFTC’s interpretation should not hinder the commodity markets exploration of how blockchain and other distributed ledger technologies can be harnessed to enhance the trading, movement, storage, and processing of commodities. In a sense, if the CFTC were to explicitly limit its interpretation to retail commodity transactions involving virtual currencies, it would promote the policy of “do no harm.”

B. Support for the Non-Exclusive Examples

The Working Group supports the non-exclusive examples provided in the Proposed Interpretation, which further clarify the meaning of “actual delivery” in the context of retail commodity transactions in virtual currency. Specifically, the Working Group supports these non-exclusive examples because: (i) they appropriately provide guidance on how the CFTC intends to assess whether retail commodity transactions in virtual currency⁶ result in actual delivery; and (ii) the non-exclusive examples are generally consistent with the approach taken by the CFTC in previous guidance on the meaning of “actual delivery” in the context of retail commodity transactions.⁷ The Working Group preliminarily views such examples as not constraining the use of distributed ledger technology to facilitate the trading, movement, storage, or processing of other commodities, whether traded through blockchain or otherwise.

The Working Group supports the CFTC’s functional approach to assessing whether there has been a “real and immediate” transfer of the commodity to a buyer or its agent, as the CFTC discussed in the *Bitfinex* order.⁸ That approach largely is an assessment of the relevant facts and circumstances to determine whether a buyer acquires possession and

⁵ CEA Section 2(c)(2)(D) applies to any agreement, contract, or transaction in any commodity that is entered into with, or offered to, a person that is **neither an eligible contract participant nor an eligible commercial entity** “on a leveraged or margined basis, or financed by the offeror, the counterparty or a person acting in concert with the offeror or counterparty on a similar basis.” Proposed Interpretation at 60,336.

⁶ The Working Group recognizes that the Proposed Interpretation focuses on retail commodity transactions in virtual currency whereby an entity or platform offers margin trading or otherwise facilitates the use of margin, leverage, or financing arrangements for their retail market participants. See *id.* at 60,337.

⁷ See generally Interpretation, *Retail Commodity Transactions Under Commodity Exchange Act*, 78 Fed. Reg. 52,426 (Aug. 23, 2013), <http://www.cftc.gov/idc/groups/public/@Irfederalregister/documents/file/2013-20617a.pdf>.

⁸ See *In re BFXNA INC. d/b/a Bitfinex*, CFTC Docket No. 16-19, 2016 WL 3137612, at *4 (June 2, 2016).

control of a commodity. In the context of retail commodity transactions in virtual currency, the Working Group proffers no view as to whether or not a seller's retention of an interest in the conveyed commodity is appropriate.

However, the Working Group recommends that the CFTC reserve for a separate, subsequent interpretation the following question: does a seller's retention of an interest in a digital asset in a non-retail blockchain transaction prevent the conclusion that actual delivery had occurred? It is foreseeable that a commodity seller might retain a security interest in the related digital asset.

In a departure from the Working Group's request in this letter to limit any final interpretation to retail commodity transactions in virtual currency, the Working Group requests that the CFTC clarify some dicta in the *Bitfinex* order regarding book-entry transfers. In the *Bitfinex* order, the CFTC draws a distinction between "actual delivery" and "constructive delivery."⁹ The *Bitfinex* order, citing the *Hunter Wise* decision, states:

"the electronic transfer of documents indicating control or possession" without physical transfer of the commodity "is by any definition constructive, rather than actual."¹⁰

The CFTC should carefully and explicitly clarify that title transfer through a book-entry system operated by a disinterested third party can constitute "actual delivery."¹¹ In the context of intangible commodities, the above referenced quote leaves some question as to whether such book-entry transfer is sufficient for "actual delivery." The clarification would make it unnecessary for market participants in other types of transactions that settle through book-entry to draw legal distinctions from the facts of *Hunter Wise* and the CFTC's reasoning in *Bitfinex*.¹²

There is a present need to add clarity regarding delivery through a book-entry system. Transactions for many commodities, such as RINs, may settle through a central registry. Also, in the context of electronic warehouse receipts and other forms of documents of title (which might be "tokenized"), it is possible that ownership of commodities transfers even though the actual physical commodities do not even move.

C. Actual Delivery Period (Response to Question 1 of the Proposed Interpretation)

With respect to Question 1 in the Proposed Interpretation, the Working Group does not have an opinion at this time regarding the appropriate length of time for the actual delivery period for retail commodity transactions in virtual currency. However, the Working Group would like to take this opportunity to emphasize that outside of the context of retail

⁹ *Bitfinex*, 2016 WL 3137612, at *4 (referencing *CFTC v. Hunter Wise Commodities, LLC*, 749 F.3d 967, 978-9 (11th Cir. 2014)).

¹⁰ *Bitfinex*, 2016 WL 3137612, at *4 (citing *Hunter Wise*, 749 F.3d at 979).

¹¹ The CFTC goes on in *Bitfinex* to state that "sham" delivery, such as when a seller merely notes a transfer on its own books, is a form of "constructive delivery" and is not "actual delivery." *Bitfinex*, 2016 WL 3137612, at *4. The Working Group agrees with this conclusion and this sense of the term "constructive delivery."

¹² In *Hunter Wise*, the book-entry system was part of a scheme to profit from off-exchange transactions in various precious metals.

commodity transactions in virtual currency, the actual delivery period for purposes of CEA Section 2(c)(2)(D)(ii)(III)(aa) should remain at the current 28-day period even where the same or a similar technology (*i.e.*, blockchain or distributed ledger technology) is used as part of a transaction. The 28-day period has become a well-recognized standard, affording legal certainty to trading parties when contracting.¹³ The Working Group is hesitant to support any effort by the CFTC to encourage Congress to amend the timelines for actual delivery under CEA Section 2(c)(2)(D).

D. Title (Response to Question 8 of the Proposed Interpretation)

Question 8 of the Proposed Interpretation concerns the concept of “title” in the determination of actual delivery of a virtual currency. The Working Group particularly recommends for the CFTC to (i) limit any further interpretation on the indicia of title with respect to virtual currency to delivery of virtual currencies in retail commodity transactions and (ii) explicitly state that other concepts and indicia of title for digital assets could apply for the trading of such assets. We also remind the CFTC that any further clarification of “title” to virtual currencies (or any other digital asset) should account for the distinction between legal ownership and beneficial ownership.

E. Depository and Full Control (Response to Question 5 and Question 6 of the Proposed Interpretation)

The Working Group submits in respect of Question 5 that the only qualification necessary for a depository for the limited purpose of effecting actual delivery of virtual currency or a digital asset is that such depository (i) expressly holds such assets for the benefit of the receiving counterparty and (ii) agrees to accept orders with respect to such assets from the receiving counterparty or, if a written account control agreement is in place, from a creditor to the receiving counterparty (provided that such creditor is not the delivering counterparty). The Working Group also submits that the control over digital assets held by a depository as specified in clause (ii) immediately above constitutes a sufficient definition of “full control” over a digital asset held by a depository, as contemplated by Question 6. Further criteria should not be adopted by the Commission, particularly for purposes of contemplating actual delivery of digital assets in respect of commodity-related transactions.

F. Digital Assets as Securities (Response to Question 9 of the Proposed Interpretation)

In response to Question 9 of the Proposed Interpretation, the Working Group supports the view that, if a token sponsor has represented that its tokens constitute securities, then the trading of such tokens should be jurisdictional to the Securities and Exchange Commission. However, in other cases, the CFTC **may** have jurisdiction unless another exemption or exception applies. That is to say, the characterization analysis should not be framed as a binary outcome: a security or, because the digital asset is not a security, a commodity. More generally, each token should be reviewed for attendant facts and circumstances, which analysis may support the token as something other than a security or a commodity. At the highest level, the CFTC’s final interpretation with respect to retail

¹³ The Working Group acknowledges that other delivery periods may correspond to operational realities for other commodities, but discourages the Commission from promulgating different time periods that would move away from a single, well understood, and easily implemented standard.

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commodity transactions in virtual currency should not constrain future innovation around other digital assets and how such assets are traded or regulated.

III. CONCLUSION

The Working Group appreciates this opportunity to provide input on the Proposed Interpretation and respectfully requests that the comments set forth herein are considered.

If you have any questions, please contact the undersigned.

Respectfully submitted,
/s/ David T. McIndoe
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