

DIGITAL ASSET DEVELOPMENTS: U.S. COMMODITY FUTURES TRADING COMMISSION ASSERTS THAT TETHER IS A COMMODITY

To Our Clients and Friends:

On Friday October 15, 2021, the Commodity Futures Trading Commission (CFTC) issued an enforcement order (Tether Order) against the issuers of the U.S. dollar Tether token (USDT), a leading stablecoin, and fined those issuers \$41 million for making untrue or misleading statements about maintaining sufficient fiat currency reserves to back each USDT “one-to-one.”^[1] In so doing, the CFTC asserted that USDT is a “commodity” under the Commodity Exchange Act (CEA).

The Tether Order is significant for few reasons. First, it marks the first U.S. enforcement action against a major stablecoin. Second, the CFTC has now asserted that it has some enforcement authority over stablecoins, just at the time that the Biden Administration is gearing up its regulatory approach to digital currencies in general and stablecoins in particular. Securities and Exchange Commission (SEC) Chair Gary Gensler stated earlier this year that he believed that certain stablecoins, such as those backed by securities, are securities,^[2] and the President’s Working Group on Financial Markets will soon be issuing a report on stablecoins.^[3] Third, the CFTC’s assertion that USDT is a commodity signals that stablecoins that are backed one-to-one with fiat currency are not securities and therefore are not directly subject to the SEC’s jurisdiction.

CFTC Legal Authority

Although the CFTC is principally a regulator of the markets for commodity futures and derivatives such as swaps, it does have certain enforcement authority over commodities in the cash markets (*i.e.*, spot commodities). Section 6(c)(1) of the Commodity Exchange Act, provides that it is “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, . . . any manipulative or deceptive device or contrivance, in contravention of such rules and regulations as the Commission shall promulgate.”^[4] The CFTC has promulgated regulations pursuant to Section 6(c)(1), which render unlawful intentional or reckless statements or omissions “in connection with . . . any contract of sale of any commodity in interstate commerce.”^[5] When those regulations were promulgated, the CFTC stated that “[it] expect[ed] to exercise its authority under 6(c)(1) 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.”^[6]

Tether Order

Prior to the Tether Order, the CFTC had asserted that some digital assets are commodities.^[7] The Tether Order definitively states that USDT is a commodity (and, in dicta, asserts that bitcoin, ether, and litecoin are commodities as well). It then alleges that the issuers of USDT made material misstatements under Section 6(c)(1) of the CEA and its implementing regulations regarding whether USDT was backed on a one-to-one basis with fiat currency reserves and whether this reserving would undergo regular professional audits, and the issuers made material omissions regarding the timing of one of the reserve reviews that USDT issuers did take.^[8] Without admitting or denying the CFTC’s findings and conclusions, the USDT issuers consented to the entry of a cease-and-desist order and civil money penalty of \$41 million.^[9]

Conclusion

The recent past has seen the explosive growth of the digital asset markets, with regulators globally seeking to catch up. In the United States, the challenge has been, in the absence of new legislation, to make digital asset transactions fit within existing regulatory schemes. Much initial regulation has been at the state level; most federal financial regulators have initially been attempting to regulate through enforcement. Now, however, there is the prospect of overlapping federal regulation, particularly with respect to stablecoins. The Tether Order comes at a time when media outlets have reported that the U.S. Department of Treasury will be working with U.S. financial regulators to issue a broad report on stablecoins, including how stablecoins should be regulated. And although the CFTC has taken its position on USDT, it is currently still unclear how other U.S. regulators will view stablecoins and other digital assets.

[1] *In the Matter of Tether Holdings Limited, Tether Operations Limited, Tether Limited, and Tether International Limited*, CFTC Docket No. 22-04 (Oct. 15, 2021), available at <https://www.cftc.gov/media/6646/enftetherholdingsorder101521/download>.

[2] Gary Gensler, SEC Chair, “Remarks Before the Aspen Security Forum” (August 3, 2021).

[3] See, e.g., Michelle Price, “Explainer: How the U.S. Regulators Are Cracking Down on Cryptocurrencies,” Reuters, September 24, 2021.

[4] 7 U.S.C. § 9(1).

[5] 17 C.F.R. § 180.1(a)(2).

[6] CFTC, Final Rules: Prohibition on the Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation, 76 *Fed. Reg.* 41,398, 41,401 (July 14, 2011).

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[7] *See, e.g., In re Coinflip, Inc.*, CFTC No. 15-29, 2015 WL 5535736, at * 2 (Sept. 17, 2015) (stating that bitcoin is properly defined as a commodity within the meaning of the CEA).

[8] Tether Order at 8-9.

[9] Also on October 15, the CFTC entered into a consent order with Bitfinex, a leading digital currency exchange that has many management and operational interlocks with the USD Tether issuers, for allegedly permitting U.S. customers that were not eligible contract participants to engage in leveraged, margined or financed commodity transactions that were not carried out on a designated contract market (*i.e.*, a CFTC registered futures exchange) in violation of the CEA's requirements, and acting as a futures commission merchant (FCM) without being registered with the CFTC as such. The CFTC further asserted that Bitfinex had violated a 2016 CFTC order that had commanded it to cease-and-desist from such activity. Without admitting or denying the CFTC's findings and conclusions, Bitfinex consented to the entry of the new cease-and-desist order and a \$1 million fine. *See In the Matter of iFinex Inc., BFXNA Inc., and BFXWW Inc.*, CFTC Docket No. 22-05 (Oct. 15, 2021), available at <https://www.cftc.gov/media/6651/enfbfxnaincorder101521/download>.



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