

Bitcoin: Currency, Property, and Now, Commodity

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In September 2015, the Commodity Futures Trading Commission (CFTC) issued an order filing and settling charges against a cryptocurrency company for conducting commodity options-related activity without complying with applicable regulations. The order finds that Coinflip, Inc., a San Francisco-based company, operated Derivabit, an online exchange offering to connect buyers and sellers of bitcoin option contracts, without maintaining the appropriate registrations. Although the ruling may not be particularly profound, it likely puts to rest the uncertainty over how bitcoins themselves (or any other virtual currency) should be classified under the Commodities Exchange Act (CEA) for regulatory purposes. The order defines “virtual currencies” as “a digital representation of value that functions as a medium of exchange, a unit of account, and/or a store of value, but does not have legal tender status in any jurisdiction” and confirms that all virtual currencies, at least insofar as they fall within that definition, are classified as commodities under the CEA. Based on this classification, the CFTC enforced certain CEA provisions and other regulations against Derivabit in the same manner as it would enforce those rules against an exchange dealing in run-of-the-mill commodity options or swaps. The CFTC’s order could have sweeping effects on the trade and use of virtual currencies. Under rules adopted by the CFTC pursuant to Dodd-Frank, it is unlawful for any person in connection with any “contract of sale of any commodity” to engage in fraud or manipulative behavior, regardless of whether such activities have a nexus to a commodities-based derivatives market. By classifying virtual currencies as commodities, the CFTC is thus allowing for the possibility that it could assert its anti-fraud authority over virtual currency transactions in the cash market, such as transactions on a bitcoin exchange, even where the transactions have no plausible connection to a derivatives market. The order also leaves open the possibility that the CFTC could attempt to assert its anti-fraud authority over ‘blockchain 2.0’ applications, which require the transmission of nominal amounts of virtual currency to facilitate a non-monetary goal, such as the creation and enforcement of a smart contract. It remains to be seen, however, just how far the CFTC may seek to use its anti-fraud authority, if at all, to police users of virtual currencies. Although the future legal treatment of virtual currencies is ultimately unknown, one thing is certain: as virtual currency technology continues to develop at breakneck pace, virtual currency innovators must keep abreast of the rapidly developing legal landscape.

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