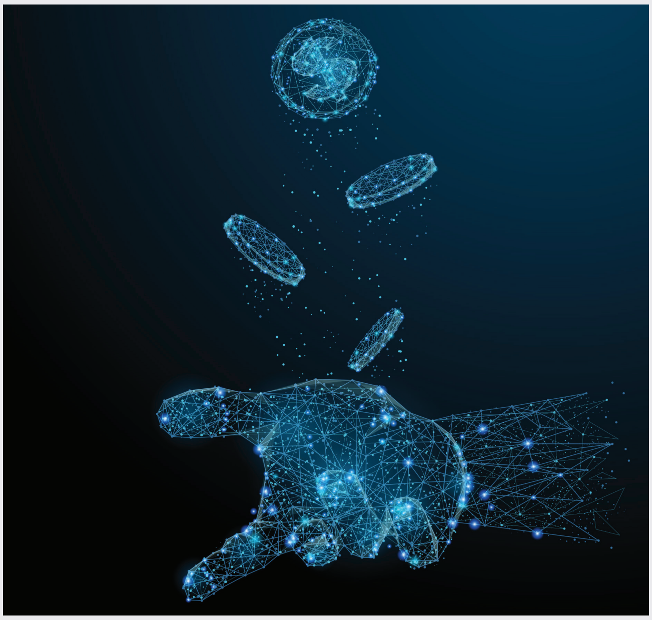
Compliance Monitor
Business intelligence | informa
www.compliancemonitor.com

A path for consumer tokens – the SEC and CFTC analysis

The demand for funding of innovative technologies has challenged financial supervisors around the globe to formulate where digital assets sit within their regulatory frameworks. **Stephen P Wink**, **David L Concannon** and **Yvette D Valdez** outline how consumer token transactions in the United States intersect with securities and commodities laws.



Increasing regulatory scrutiny of digital assets has raised the question of whether the issuance and sale of 'consumer' or 'utility' tokens – those designed for use by consumers on a distributed platform and not intended to constitute securities – will ever be possible in the United States. Recent statements of senior officials at the US Securities and Exchange Commission (the SEC) indicate a viable regulatory pathway may exist for issuing tokens that are not 'securities' subject to SEC oversight. However, issuers and intermediaries seeking to navigate the securities pathway must also remain mindful of commodities law considerations to avoid regulatory enforcement.

The SEC's evolving approach to digital assets

The SEC's approach to classifying whether a digital asset is a security derives from its application of the test set forth in *SEC v WJ Howey Co.* [1] The *Howey* test determines whether an asset constitutes an 'investment contact', one of the enumerated types of securities as defined in the securities laws. [2] The test states that an investment contract involves (i) an investment of money, (ii) in a common enterprise, (iii) in which the investor is led to expect profits, (iv) derived from the efforts of one or more third parties. [3] If the test is satisfied, it is immaterial whether the enterprise is speculative or non-speculative, or whether there is a sale of property with or without intrinsic value. [4] In short, the heart of the analysis focuses on the economic reality of the arrangement in question.

In July 2017, the SEC first applied the *Howey* test to digital assets, finding the sale of Decentralized Autonomous Organization digital tokens (DAO Tokens) was an unregistered securities offering absent a valid exemption from section 5 of the Securities Act of 1933. The report clarified that instruments having the *indicia* of investment contracts should be offered and sold in compliance with securities laws, and intermediaries for such sales, including exchanges, need to comply with the registration and other compliance requirements of these laws.

The SEC next applied *Howey* to digital assets when issuing an order (Order) instituting cease-and-desist proceedings with respect to an offering by Munchee Inc. [5] In the Order, the SEC concluded the initial coin offering for MUN Tokens was an unregistered securities offering without an available exemption, despite Munchee's argument that MUN Tokens served a utility function, in part because they were marketed as investments to persons outside Munchee's actual user base. The Order indicated that the SEC would look beyond the potential utility of a token to both the nature of an offering and the presence of investment intent among the persons participating in such offering, when determining whether a transaction may be subject to the securities laws. This analysis comported with SEC chairman Jay Clayton's contemporaneous public statements, which focused on investment participation as prompting "securities registration requirements and other investor protection provisions of our federal securities laws." [6]

Six months later, as participation in initial coin offerings (ICOs) slowed, William Hinman, director of the SEC's division of corporation finance, formulated a pathway for token transactions no longer to be characterised exclusively as securities transactions, while also reaffirming the underlying analysis of the Order. [7] During his speech at the 'Yahoo Finance All Markets Summit: Crypto', Director Hinman queried whether "a digital asset offered as a security can, over time, become something other than a security". In response, he posited that a digital asset representing a right to a financial interest in an enterprise would always remain a security, while a digital asset that, for example, is used to purchase goods or services within a sufficiently decentralised ecosystem could evolve beyond its initial classification as a security.

Director Hinman emphasised that, similar to the underlying assets in *Howey* (which were fruit trees), digital assets are not necessarily securities. Rather, in addition to the underlying rights associated with such assets, the manner of sale and a purchaser's reasonable expectations help determine whether a digital asset is a security. This rationale was underscored by Director Hinman's reference to *Gary Plastic Packaging v Merrill Lynch, Pierce, Fenner & Smith Inc*, [8] where the Second Circuit held that transactions in instruments animating a broader investment contract are subject to the securities laws. There, the court found securities laws applied because of the potential for profit from, among other things, the existence of a secondary market advertised by an issuer for an instrument that was otherwise not a security (specifically, bank certificates of deposit). In applying this rationale, Director Hinman reasoned that digital tokens sold in an offering by promoters to "develop the enterprise" will most often be a security because the efforts of promoters are the primary source of value creation in the token, and applying the securities laws in such cases helps mitigate informational asymmetries existing between promoters and investors. However, Director Hinman noted, if tokens function on a sufficiently decentralised network — that is, "where purchasers would no longer reasonably expect a person or group to carry out essential managerial or entrepreneurial efforts" — the public policy need to apply securities laws to correct the informational asymmetries is reduced.

The beginnings of a framework

Director Hinman proffered several factors for determining whether a consumer token sale may be exempt from the securities laws, focusing on the role and profit expectation of the promoter or enterprise, [9] and the design of the token. [10] Discussed below are some of these factors and component parts.

What is the role of the promoter or enterprise?

(a) Ongoing development and maintenance of the network

Director Hinman noted that a truly decentralised network, such as Bitcoin and Ethereum, does not have a single enterprise significantly or directly influencing the value of consumer tokens exchanged thereon, including through additional development and maintenance. Open source projects, where a variety of parties may contribute to the ongoing network development, clearly have a greater chance of meeting this requirement as compared to networks where the original promoter retains a significant role in ongoing network development and maintenance.

(b) Use of token sale proceeds

Using proceeds to further develop and maintain the network may demonstrate that the issuer's efforts remain central to the token's value. Conversely, using traditional financing instruments for network development may help to delineate more clearly the development efforts from a subsequent sale of tokens for use on a functioning network, thus helping support the position that the tokens themselves should not be deemed to be securities.

(c) Network governance

While stakeholder voting rights are a fundamental characteristic of a decentralised network, they are also attributes of equity securities and can militate toward concluding that particular tokens are securities if they are structured in a manner that is indicative of a central enterprise driving the token value.

(d) Robust token economy

Courts have reasoned that the existence of competing market forces is critical to distinguishing a commodity from a security, as broad market forces rather than a central party's efforts create the instrument's value. Promoting and developing such a robust economic structure may help ensure market forces drive token values independent of a promoter's efforts. This reasoning is underscored by the Ninth Circuit's findings in *Noa v Key Futures* and *SEC v Belmont Reid & Co,* each of which focused on precious metal sales and hold that the expectation of economic return based on market forces rather than a promoter's efforts does not satisfy the *Howey* test.

Is the asset designed from consumptive purposes?

(a) Functioning network

A factor closely related to the role of the promoter discussed above, though distinct, is whether the token-based network is "fully functioning or in the early stages of development" when tokens are sold. Given that most consumer products are useable when purchased, having a fully functioning token-based network prior to initiating consumer token sales supports the conclusion that "the primary motivation for purchasing the digital assets is for personal use or consumption."

(b) Secondary markets and transferability

SEC chairman Jay Clayton has noted that offerings promising purchasers the ability to sell tokens quickly on a secondary market supports the view that the token is a security. Of course, *Gary Plastics* stands for the notion that *marketing* of 'investments' based, at least in part, on potential secondary market liquidity can cause an instrument to be deemed a security. The mere existence of a secondary market, however, should not be dispositive, as there are numerous examples of secondary markets for commodities. In fact, many networks and token economies require a sort of secondary market to balance various economic demands without any one actor having to play all roles (consumer, provider, etc) on the network. Technical mechanisms may help address concerns around the establishment of a secondary market and reduce the likelihood a purchaser has the same investment motive found in *Gary Plastics*. For example, lockups can be structured so tokens are nontransferable for a certain time period or until the seller meets certain network participation obligations, and transfer restrictions may be structured to incentivise in-network transfers over out-of-network transfers.

(c) Token retention

Issuers should consider traditional equity compensation structures, rather than token compensation, for employees and advisors, particularly when the recipient cannot consume the network product or services or their allotted number of tokens. In such instances, it would be difficult to argue credibly that such tokens are not being held for investment purposes. However, such an equity compensation structure could be coupled with certain economic rights (such as dividends) and participation rights in the event of a token sale to align the interests of issuers with their employees and advisors.

(d) Token sale legal documentation

The documentation used in consumer token sales may help discourage purchasers from expecting profits, such as by including representations and warranties regarding the purchaser's intent to use the tokens on the issuer's platform and a lack of investment intent. Furthermore, issuers may choose to retain a right of first refusal for tokens a purchaser intends not to use on the issuer's network.

Pre-sale/pre-functional documentation

As a result of the foregoing legal framework and considerations, sales of tokens to fund network development (also known as prefunctional financings or presales) may constitute a securities offering. Accepting this possibility, the market has sought out new financing instruments to solve securities law issues. Although such instruments were a step towards compliance, they continue to raise other significant regulatory concerns.

Presale instruments – securities law issues

Presale instruments, including the Simple Agreement for Future Tokens (SAFT), [11] sought to comply with securities laws by separating the presale from the underlying consumer token. However, these instruments commonly present two issues. First, contemplating the contemporaneous delivery of tokens to presale purchasers and consumers upon network launch may be indicative of a securities transaction, not a consumer token launch, because under the logic of *Gary Plastic* and the *Munchee* Order the transaction was marketed to initial purchasers for investment rather than consumptive purposes. Secondly, although recent iterations acknowledge token issuances may be securities transactions, they do not address that tokens may be deemed securities and often only transferable through registered intermediaries. Where such registration is required, an issuer or platform may face a fateful decision to take the time and incur expenses to register as a broker-dealer or exchange (or alternative trading system [12]), [13] pay a third party registered intermediary, or abandon the token-based network. Furthermore, given that purchasers' investment decisions are based on the token's availability and functionality, it will remain challenging to draft appropriate disclosures in these types of instruments regarding the timing and likelihood that a token once deemed a security may transmute into a consumer token at some point in the future.

Presale instruments – commodities law issues

Beyond the securities law concerns, token presale instruments — including the SAFT — also raise commodities law concerns. Because virtual currencies are commodities, [14] a presale of consumer tokens through an instrument that provides the right to receive tokens in the future, or confers the right to exchange or convert such instrument into tokens, may be a forward contract for the sale of a commodity or a commodity option, and thus subject to regulation by the US Commodity Futures Trading Commission (CFTC) as a swap under the Commodity Exchange Act, as amended (the CEA), if an exemption is not available. [15]

Commodity forward contracts

Forward sales of commodities fall within the CEA's broad 'swap' definition, which encompasses numerous types of derivatives, and are subject to CFTC regulation absent an applicable exclusion. [16] Notably, the sale of a non-financial commodity for deferred shipment or delivery is excluded from the swap definition, so long as it is intended to be physically delivered, [17] but provided that such forward contract also qualifies as a commercial merchandising transaction (Non-Financial Forward Contract Exclusion). [18] Forward contracts purchased by investors will not qualify for the Non-Financial Forward Contract Exclusion because the purchasers are not 'commercial market participants'. [19] The SAFT and similar presale instruments are effectively a prepaid forward contract of a commodity whereby parties have agreed to a price or percentage discount on the token to be delivered at a later date, and are largely marketed to investors (*ie,* not commercial market participants). [20]

Commodity options

Later versions of the SAFT and similar presale instruments have also included convertible features, which provide investors or the issuer, as applicable, a call or put right to deliver tokens upon the consummation of a token sale at an agreed price or discount. Such an instrument may constitute a commodity option and would be subject to CFTC regulation as a swap, [21] unless an exemption applies. Trade options are generally exempt from regulation by the CFTC, other than large trader reporting requirements and the CFTC's general anti-fraud and anti-manipulation enforcement authority (the Trade Option Exemption). [22]

Unfortunately, SAFTs and similar presale instruments with such optionality features are not typically offered to commercial market participants who satisfy the Trade Option Exemption's requirement that a trade option be entered into with an offeree who is either a producer, processor or commercial user of, or merchant handling, the commodity (or products or by-products thereof) that is the subject of the option. Additionally, even if such instruments are offered to commercial market participants, these presale instruments would not necessarily satisfy the Trade Option Exemption's requirement that the offeree be entering into the commodity option solely for purposes related to its business as a commercial market participant producing, processing, using or merchandising the commodity (or products or by-products thereof) that is the subject of the option.

Hybrid instrument exemption

SAFTs and similar presale instruments, which may constitute or contain a commodity forward contract or commodity option, and may not otherwise qualify for the Trade Option Exemption or the Non-Financial Forward Contract Exclusion, are also not likely exempt from commodities law regulation under the Hybrid Instrument Exemption (defined below).

Section 2(f) of the CEA exempts a hybrid instrument [23] that is "predominantly a security" from the provisions of the CEA if, among other things, the instrument is not marketed as a contract of sale of a commodity for future delivery (or option on such a contract) subject to the CEA (the Marketing Condition) (this is known as the Hybrid Instrument Exemption). [24] Given that investors in SAFTs and similar presale instruments are motivated to purchase such instruments solely for the potential of receiving the underlying commodity (*ie*, the token) in the future, such instruments likely would not satisfy the Marketing Condition of the Hybrid Instrument Exemption.

Consequences of CFTC regulation

Because token presale instruments may have an embedded swap that does not qualify for an exemption from CFTC regulation, such instruments would be subject to the CFTC's swaps regulatory framework. In particular, in order to trade over-the-counter, swaps must be entered into between Eligible Contract Participants (ECPs). [25] While some investors may qualify as ECPs, token issuers typically fail the ECP test because they are early stage companies that do not have at least $10 million in gross assets. A swap entered into by non-ECP parties would be in violation of the CEA and CFTC regulation, and both parties could face penalties and sanctions for such actions.

Conclusion

Much has been made of the need for certainty, and perhaps even innovation, in the application of US securities and commodities laws to commercial activities relating to blockchain, cryptocurrencies and related technologies. That said, the SEC has been clear that traditional securities law principles will continue to be applied when examining token transactions. Nevertheless, there is now some reason for optimism that at least some transactions in consumer tokens may be executed without the application of federal securities laws. However, much remains unknown, including how to evaluate and weigh the factors outlined above, including what it means for a token economy to be sufficiently decentralised. Furthermore, transactions complying with securities law must also consider the application of commodities laws.

Notes

[1] 328 US 293 (1946).
[2] 15 USC §§ 77b(a)(1), 78c(a)(10).
[3] *Howey*, 328 US at 301.
[4] See *id*.
[5] See 'Order Instituting Cease-and-Desist Proceedings pursuant to section 8A of the Securities Act of 1933, Making Findings, and Imposing a Cease-and-Desist Order' (11 December 2017), *www.sec.gov/litigation/admin/2017/33-10445.pdf*.
[6] SEC, 'Statement on Cryptocurrencies and Initial Coin Offerings' (11 December 2017), *www.sec.gov/news/public-statement/statement-clayton-2017-12-11*.
[7] See William Hinman, 'Digital Asset Transactions: When Howey Met Gary (Plastic)' (14 June 2018), *www.sec.gov/news/speech/speech-hinman-061418*.
[8] 756 F 2d 230 (2d Circuit 1985).
[9] Director Hinman identified the following factors to determine the promoter or enterprise's role:

- Is there a person or group that has sponsored or promoted the creation and sale of the digital asset (the promoter), the efforts of whom play a significant role in the development and maintenance of the asset and its potential increase in value?
- Has the promoter retained a stake or other interest in the digital asset such that it would be motivated to expend efforts to cause an increase in value in the digital asset? Would purchasers reasonably believe

such efforts will be undertaken and may result in a return on their investment in the digital asset?
- Has the promoter raised funds in excess of what may be needed to establish a functional network, and, if so, has it indicated how those funds may be used to support the value of the tokens or to increase the value of the enterprise? Does the promoter continue to expend funds from proceeds or operations to enhance the functionality and/or value of the system within which the tokens operate?
- Are purchasers 'investing' — seeking a return? For example, is the instrument marketed and sold to the general public instead of to potential network users for a price that reasonably correlates with the market value of the good or service in the network?
  - Does application of the Securities Act protections make sense? Is there a person or entity that plays a key role in the profit-making of the enterprise such that disclosure of their activities and plans would be important to purchasers? Do informational asymmetries exist between the promoters and potential purchasers of the digital asset?
  - Do persons or entities other than the promoter exercise governance rights or meaningful influence?
  - Are independent actors setting the price or is the promoter supporting the secondary market for the asset or otherwise influencing trading?

[10] Director Hinman identified the following factors to determine whether an asset is designed for investment or consumptive purposes:
  - Is token creation commensurate with meeting the needs of users or, rather, with feeding speculation?
  - Is it clear that the primary motivation for purchasing the digital asset is for personal use or consumption rather than investment? Have purchasers made representations as to their consumptive, as opposed to their investment, intent? Are the tokens available in increments that correlate with a consumptive versus investment intent?
  - Are the tokens distributed in ways to meet users' needs? For example, can the tokens be held or transferred only in amounts that correspond to a purchaser's expected use? Are there built-in incentives that compel using the tokens promptly on the network, such as having the tokens degrade in value over time, or can the tokens be held for extended periods for investment?
  - Is the asset marketed and distributed to potential users or the general public?
  - Are the assets dispersed across a diverse user base or concentrated in the hands of a few that can exert influence over the application?
  - Is the application fully functioning or in early stages of development?

[11] See, *eg*, Juan Batiz-Benet, Jesse Clayburgh & Marco Santori, 'The SAFT Project: Toward a Compliant Token Sale Framework' (2 October 2017), *https://saftproject.com/static/SAFT-Project-Whitepaper.pdf* (SAFT Whitepaper).

[12] See 15 USC § 78c(a)(4)(A) (defining 'broker' as "any person engaged in the business of effecting transactions in securities for the account of others"); 15 USC § 78c(a) (5)(A) (defining 'dealer' as "any person engaged in the business of buying and selling securities . . . for such person's own account"); 15 USC § 78c(a)(1) (defining 'exchange' as "any organization, association or group of persons, whether incorporated or unincorporated, which constitutes, maintains or provides a marketplace or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange as that term is generally understood, and includes the market place and the market facilities maintained by such exchange").

[13] It is worth noting, however, that the US House of Representatives recently passed several bills aimed at improving capital formation for smaller companies. For example, the Main Street Growth Act would amend the Securities Exchange Act of 1934, as amended, to allow registration of venture exchanges that would provide trading venues tailored for smaller companies, such as blockchain-based start-ups, whose securities are considered less liquid than those of larger companies. Main Street Growth Act, HR 5877, 115th Congress (as passed by the House, 10 July 2018), *www.congress.gov/bill/115th-congress/house-bill/5877*; see Tom Zanki, 'House Passes Bill to Allow Venture Exchanges', LAW360 (11 July 2018), *www.law360.com/articles/1062096/housepasses-bill-to-allow-venture-exchanges*.

[14] Timothy Massad, chairman of the CFTC, testimony before the US Senate Committee on Agriculture, Nutrition & Forestry (10 December 2014), *www.cftc.gov/PressRoom/SpeechesTestimony/opamassad-6* (2014 Massad Senate Testimony).

[15] The CFTC regulates the swaps and futures markets, and retains general enforcement authority to police fraud and manipulation in cash or 'spot' commodities markets. See, eg, 7 USC §§ 6c(a), 9, 12(a)(5), 15; 17 CFR § 180.1; see also 'Prohibition on the Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation', 76 Fed Reg 41398 (14 July 2011), *www.gpo.gov/fdsys/pkg/FR-2011-07-14/pdf/2011-17549.pdf*. In 2014, then-CFTC chairman Timothy Massad observed that what the CFTC has referred to as virtual currencies are 'commodities' subject to provisions of the Commodity Exchange Act, as amended (the CEA), 2014 Massad Senate Testimony. Since 2015, the CFTC has been active in bringing enforcement actions when virtual currency enterprises run afoul

of regulatory requirements. See Latham & Watkins, 'CFTC Brings Significant Enforcement Action Against Online Cryptocurrency Exchange', Client Alert No 1980 (20 June 2016), *www.lw.com/thoughtLeadership/CFTC-brings-significant-enforcement-action-against-online-cryptocurrency-exchange*; Latham & Watkins, 'Enforcement Trends in Cryptocurrency', Client Alert No 1904 (9 December 2015), *www.lw.com/thoughtLeadership/lw-enforcement-trends-cryptocurrency*; Latham & Watkins, 'Cryptocurrencies Are Commodities: CFTC's First Bitcoin Enforcement Action', Client Alert No 1874 (21 September 2015), *www.lw.com/thoughtLeadership/LW-CFTC-first-bitcoin-enforcement-action*. The CFTC has also been active in enforcement against fraud and manipulation in the virtual currency 'spot' markets. See, *eg*, CFTC Release PR7714-18, 'CFTC Charges Multiple Individuals and Companies with Operating a Fraudulent Scheme Involving Binary Options and a Virtual Currency Known as ATM Coin' (18 April 2018), *www.cftc.gov/PressRoom/PressReleases/7714-18*; CFTC Release PR7614-17, 'CFTC Charges Nicholas Gelfman and Gelfman Blueprint, Inc with Fraudulent Solicitation, Misappropriation, and Issuing False Account Statements in Bitcoin Ponzi Scheme' (21 September 2017), *www.cftc.gov/PressRoom/PressReleases/pr7614-17*.

[16] See 7 USC § 1a(47)(A)(ii) ("the term 'swap' means any agreement, contract, or transaction … that provides for any purchase, sale, payment, or delivery … that is dependent on the occurrence, nonoccurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence.")

[17] Both the CEA and CFTC regulations thereunder have long recognised a forward contract exclusion from futures contracts. See 7 USC § 1a(27) ("The term 'future delivery' does not include any sale of any cash commodity for deferred shipment or delivery.") Following enactment of the Dodd-Frank Act in 2010, the sale of a non-financial commodity for deferred shipment or delivery was also excluded from the definition of 'swap' in section 1a(47) of the CEA under the Non-Financial Forward Contract Exclusion. 7 USC § 1a(47)(B)(ii).

[18] See 'Further Definition of "Swap", "Security-Based Swap" and "Security-based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping', 77 Fed Reg 48208, 48228 (13 August 2012), *www.gpo.gov/fdsys/pkg/FR-2012-08-13/pdf/2012-18003.pdf* (Products Release).

[19] As the CFTC has noted, "the underlying postulate of the [forward] exclusion is that the [CEA's] regulatory scheme for futures trading simply should not apply to private commercial merchandising transactions which create enforceable obligations to deliver but in which delivery is deferred for reasons of commercial convenience or necessity." The CFTC has expressly stated that hedge funds, acting in their capacity as investors, are not commercial market participants. Products Release, 77 Fed Reg at 48227-48229; see also 'Statutory Interpretation Concerning Forward Transactions', 55 Fed Reg 39188 (25 September 1990), *https://cdn.loc.gov/service/ll/fedreg/fr055/fr055186/fr055186.pdf*.

[20] Section 5(c) of the SAFT, which is included as Exhibit 1 to the SAFT Whitepaper, sets forth the following provision: "(c) The Purchaser has no intent to use or consume any or all Tokens on the corresponding blockchain network for the Tokens after Network Launch. The Purchaser enters into this security instrument purely to realize profits that accrue from purchasing Tokens at the Discount Price."

[21] 7 USC § 1a(47)(A)(i) ("the term 'swap' means any agreement, contract, or transaction … that is a put, call, cap, floor, collar, or similar option of any kind that is for the purchase or sale, or based on the value, of 1 or more … commodities").

[22] See 17 CFR § 32.3(c). In order to qualify as a trade option and benefit from the Trade Option Exemption, the commodity option in question must be: (i) intended to be physically settled if exercised; (ii) entered into with an offeror who is either an ECP or a producer, processor or commercial user of, or merchant handling, the commodity (or products or by-products thereof) that is the subject of the option, and such offeror is offering to enter into such option solely for purposes related to its business as such; and (iii) entered into with an offeree who is either a producer, processor or commercial user of, or merchant handling, the commodity (or products or by-products thereof) that is the subject of the option, and such offeree is entering into such option solely for purposes related to its business as such. See 17 CFR § 32.3(a).

[23] Under CFTC Rule 34.2(a), a 'hybrid instrument' is defined to include an equity or debt security with "one or more commodity-dependent components that have payment features similar to commodity futures or commodity options contracts or combinations thereof". 17 CFR § 34.2(a).

[24] Under section 2(f) of the CEA, a hybrid instrument is "predominantly a security" and exempt from the provisions of the CEA if:

(i) the hybrid instrument issuer receives payment in full of the hybrid instrument's purchase price, substantially contemporaneously with delivery of the hybrid instrument;

(ii) the hybrid instrument purchaser/holder is not required to make any payment to the issuer in addition to the purchase price described above, whether as margin, settlement payment or otherwise, during the life of the hybrid instrument or at maturity;

(iii) the hybrid instrument issuer is not subject by the instrument's terms to mark-to-market margining requirements; and
(iv) the hybrid instrument is not marketed as a contract of sale of a commodity for future delivery (or option on such a contract) subject to the CEA.
7 USC § 2(f)(2).

[25] If one or both of the parties to a swap transaction are non-ECPs, the swap must be executed on a CFTC-registered designated contract market (DCM). 7 USC § 2(e). An individual can only qualify as an ECP if such person has amounts invested on a discretionary basis, the aggregate of which is in excess of US$10 million; or US$5 million and enters into swaps in order to manage the risk associated with an asset owned or liability incurred (or reasonably likely to be owned or incurred) by such person. 7 USC § 1a(18) (defining eligible contract participant).

Stephen P Wink (stephen.wink@lw.com), **David L Concannon** (david.concannon@lw.com) and **Yvette D Valdez** (yvette.valdez@lw.com) are partners in the New York office of law firm Latham & Watkins. **Miles P Jennings** (miles.jennings@lw.com) is an associate in Latham's Silicon Valley office, while **Cameron R Kates** (cameron.kates@lw.com) and **J Ashley Weeks** (ashley.weeks@lw.com) are associates in the New York office.