

Emerging Market Trends in Derivatives Industry

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In the post-pandemic world, several trends are developing that will fundamentally change the way financial market participants manage commercial risk or trade traditional and rapidly evolving novel assets, while new classes of participants are necessitating a fundamental rethink of how Federal and State regulators ensure safety and soundness of U.S. financial markets. This article identifies these trends and explores how these changes are likely to affect future regulations and compliance needs.

Proliferation of “Commodities”

The legal definition of “commodity” in the Commodity Exchange Act (“**CEA**”)[1] is being stretched far beyond what anyone would have imagined 13 years ago when it was last significantly amended,[2] let alone 100 years ago when the CEA’s predecessor legislation was first enacted.[3] This categorical expansion has huge implications for all participants in derivatives markets, as well as on the jurisdictional boundary between the two main market regulators in the United States – *i.e.*, the Commodity Futures Trading Commission (“**CFTC**”) and the Securities and Exchange Commission (“**SEC**”).

The term “commodity” is a term of art defined in the CEA; however, since inception, the scope of the term has expanded from primarily the grains to first include other agricultural products and then to include energy resources, precious metals, financial instruments and now digital assets. As the economy grows and more participants enter the markets, the scope of what constitutes a “commodity” will continue expanding and has recently started to include event outcomes, such as football games,[4] or real estate and art auctions, which raise the question of what is gaming, betting or hedging and speculation.

However, figuring out the legal nature of novel products, such as digital assets, can be difficult until Congress amends the CEA and provides greater clarity on the distinctions between securities, commodities, bank-regulated instruments and other novel products.[5] Meanwhile, the CFTC and the SEC continue to try to guide the marketplace. For example, the SEC’s Division of Corporate Finance just recently opined on whether stablecoins are “securities.”[6]

There are significant practical implications depending on the outcome of “commodity” classification, which include whether the CEA’s federal preemption applies, the SEC’s jurisdiction is triggered, whether State gambling and bucket shop rules apply,[7] how these instruments will be treated in bankruptcy, and to what extent the Uniform Commercial Code (“**UCC**”) will apply.[8] One thing is certain, there will be much greater diversity in “commodities” in the near future.

“Retailification” of Commodity Markets

Commodity derivatives markets have traditionally been driven by professional participants, such as large farmers and commodity traders, as well as registered and regulated entities.[9] With the advent of crypto contracts, this has changed – the volumes of derivative transactions are increasingly being driven by retail traders (*i.e.*, by non-

professional participants). Interestingly, however, the trend toward greater retail participation in derivatives markets is pronounced not only with digital assets, but in all other “traditional” commodity classes. This generational shift means that the CFTC and the National Futures Association (“**NFA**”) will have to pivot to focus more on consumer protection issues because regulators cannot rely solely on market intermediaries and financial infrastructure providers to be responsible for protecting retail participants (who are increasingly using innovative technology and, e.g., the mobile apps to trade futures contracts).

Ironically, as the retail volume and demand has increased, and more swaps are being cleared, the number of registered futures commission merchants (“**FCMs**”) until very recently has been significantly dwindling. However, in the past year the trend has clearly reversed – and the demand for traditional registered FCMs and introducing broker (“**IB**”) services started to grow with the realization that a registered FCM or an IB is an entry point into futures trading for retail participants.^[10]

Even though the proposed Digital Assets Structure legislation will create several specific categories for digital assets intermediaries and trading venues, most likely these new entities will be registered, licensed and supervised based on the well-established practices with respect to already existing registered categories of market participants and financial infrastructure providers.

Drive to Accommodate Retail Participants

Given that retail participants can trade margined or leveraged commodities only on exchanges, i.e., DCMs, there is an increasing pressure on DCMs to broaden their access points for retail participants who are interested in not just digital assets, but also more traditional commodity transactions and are utilizing decentralized finance (“**DeFi**”) platforms. Conversely, unregistered platforms, such as DeFi, are under an increasing pressure to register as DCMs to sufficiently address and accommodate continuously growing retail demand in commodity contracts that qualify as “futures contracts.”

To accommodate an increasing volume of retail participants, one of the tools that is being considered is the creation of fully margined and self-liquidating accounts, where retail market participants can bypass an intermediary, such as a registered FCM, and essentially become self-clearing members of clearing houses, i.e., derivatives clearing organizations (“**DCOs**”). It is likely that the CFTC will eventually bless these structures (e.g., allowing retail participants placing smaller lot futures trades on an app on their mobile phones at any time of the day). Of note, micro-sized contracts geared toward retail participants are already rapidly gaining in popularity.

After U.S. Congress finalizes its legislation on stablecoins and digital assets infrastructure and markets, the CFTC and the SEC will have to promulgate a number of new regulations, in great part addressing further protections to retail participants. It is only a matter of time when that happens.

Fractionalization and Specialization of Derivatives Contracts

Increasing sophistication in risk management demands a greater variety of risk management, speculative and liquidity tools that can address a wider diversity of derivatives contracts offered on DCMs, the smaller (micro) sizes of these contracts as well as longer (as well as shorter) duration^[11] (i.e., as compared to “industrial”-size contracts entered into by professional participants on traditional commodities for periods of months driven by production and natural commodity cycles). The move toward more bespoke and smaller-size contracts, as well as toward zero-day settlement vs. perpetual contracts, is indicative of the greater participation in such transactions by retail participants, which will continue and will pressure the CFTC to further refine its DCM self-certification process for futures contracts and options.

Markets are also experiencing an explosion in the varieties of assets that are being digitally tokenized in order to facilitate on blockchain trading by greater numbers of participants. Going far beyond turning carbon credits into digital tokens, the marketplace now has native tokens that are themselves HELOCs, auto titles and property titles – all created and traded exclusively on a chain. Tokens have also been introduced that represent money market funds, ETFs, bonds, precious metals, as well as fine art and other collectibles.^[12] All of these new products will need to be given a new level of recognition and legal protection. If, or more likely when, the CFTC receives the grant of exclusive regulatory jurisdiction (in addition to its already existing enforcement jurisdiction) over spot digital assets, this will be a paradigm shift in market regulation.^[13]

Erosion of Traditional Regulated Categories / Disintermediation

Financial engineers today are developing novel structures to meet customer demands, which include DeFi platforms, decentralized autonomous associations (“**DAOs**”) offering commodity contracts traded on the blockchain, as well as the use of Artificial Intelligence (“**AI**”). As a result, a single entity may simultaneously meet the characteristics of a DCM / SEF, DCO, an IB or an FCM, a swap data repository (“**SDR**”) and a swap dealer (“**SD**”) or a security-based SD offering its services seamlessly across the globe. This means that the 100 year-old traditional regulatory approach implemented by the SEC and the CFTC is not flexible enough to properly regulate these new hybrid structures. So, regulators and the SROs will have to come up with a new regime to comprehensively regulate and effectively supervise these business arrangements. On May 5, the House of Representatives introduced a discussion draft of a market structure bill to help provide direction to the regulators on digital assets,^[14] which is an important step toward conceptualizing these new structures.

The trend of traditional financial services being disrupted by financial innovation is not limited to digital assets and commodities and securities. Throughout the financial sector, the promises of technology are transforming how banks and non-banks alike are offering everything from payments to deposits to personal financial management. From a regulatory standpoint, this has led to renewed interest that the prudential bank regulators, especially the Office of the Comptroller of the Currency (“**OCC**”), with its chartering authority, approve special-purpose chartered banks that would only carry out a limited number of banking functions. Additionally, Acting Comptroller Rodney Hood has expressed that one of the OCC’s priorities is to further support the ability of banks generally to partner with fintechs, especially in the retail sector and as it relates to money transfers.

Reevaluation of the Term - “Gaming”

Distinction between “gambling” or “gaming” and trading commodities for a legitimate business purpose (and what a legitimate economic interest is) is at the heart of the CEA and has been argued in courts long before the enactment of the CEA in 1921 or the establishment of the CFTC in 1974.^[15] The industry, the regulators and courts will continue grappling with these concepts and where the line lies delineating gambling, as is evidenced by recent litigation involving “event contracts,”^[16] as well as recent CFTC proposed rulemaking on “event contracts” and an attempt to define what “gambling” is.^[17] One thing is certain, “event contracts” and prediction markets are here to stay, and the definition and common public understanding of what gaming and gambling are in 2025 differs markedly from what was commonly understood just a few years ago. It is clear that the CFTC, and possibly Congress, will have further regulatory action on this class of contracts.

Increased Trading Efficiency and 24/7/365 Trading Flow

Increased trading efficiency and greater availability of real-time payments are just some of the benefits that could be possible as a result of a greater use of digital assets in the marketplace. When commodities are traded as tokens on the blockchain, for example, trading can occur 24/7/365 and need not be restrained by market hours and banking days. This is because blockchain technology achieves final settlement by definition when a token is exchanged from one party to the next, instantly at the speed of the internet, not the traditional banking system.

Similarly, if stablecoins are being used to pay for the purchase and redemption of the value of tokens, then as soon as a transaction is completed on the blockchain, then payment also achieves final settlement.

The CFTC has recently published a Request for Comment on 24/7 trading of DCMs, which is intended to match retail demand for continuous trading sessions (e.g., in perpetuums on cryptos).^[18] One thing is clear – if one DCM / SEF starts 24/7/365 trading, and if at least one DCO accommodates clearing of continuous markets, all other exchanges and trading venues will have to offer same functionalities; likewise, FCM or SDs will not be able to opt out from these markets because they will have exposures created over holidays and weekends and they would not be able to ignore them. In tandem, regulations, supervision and the entire U.S. financial infrastructure will need to quickly adapt to accommodate continuous transaction flow in practically infinite supply of various products. It is clear that this change is imminent.

Enforcement Priorities

The new leadership of the CFTC and the SEC (as well as the Department of Justice (“**DOJ**”)) have emphasized that enforcement priorities will be on the protection of retail participants and the public at large from fraud and manipulation, and that there will be no regulation by enforcement or prosecution.^[19] Furthermore, there will be less of a need to regulate by enforcement if Congress finalizes its legal framework for stablecoins and digital assets and there will be clear guidance on these markets from the CFTC and the SEC.

At the same time, the CFTC's enforcement lawyers are increasingly reading from the SEC's rulebook, and the previously insider trading cases involving commodities are now commonplace, as are enforcement cases involving disclosures. Inevitably, retail participation will necessitate that the CFTC utilize similar tools as those used by the SEC to protect retail capital markets.

Accordingly, it is expected that enforcement will be of different quality and will target different market actors both on the CFTC and the SEC side.

Conclusion

It is clear that in the next few years U.S. (and world) commodity and commodity and security derivatives markets will be fundamentally different. It is likely that retail participants will be day-trading on their mobile phones numerous futures and options contracts (including micro- and perpetual futures) 24/7/365 and that tokenized assets will be transferred instantaneously to collateralize these trades. There will be several new categories of registered market participants (e.g., digital asset and digital commodity intermediaries and platforms and AI-driven advisers) in addition to traditional brokers and FCMs who will accommodate this trading flow. Increased risks to institutional and retail market participants will be (hopefully) matched with greater sophistication of regulators, SRO's and DOJ's enforcement departments. In other words, no asset and no commodity and no market utility will remain unaffected by these rapidly emerging trends.

[1] See 7 U.S.C. § 1a(9).

[2] The Dodd-Frank Wall Street Reform and Consumer Protection Act 124 Stat. 1376-2223, (2010) significantly amended the CEA in 2010.

[3] See, first the Future Trading Act of 1921 (declared unconstitutional), and then enacted as the Grain Futures Act of 1922, 7 U.S.C. § 1 (1922).

[4] See e.g., Kalshi, LLC v. CFTC, Appeal from Case No. 1:23-cv-03257 (May 5, 2025).

https://storage.courtlistener.com/recap/gov.uscourts.cadc.41256/gov.uscourts.cadc.41256.01208736517.1_1.pdf

[5] See e.g., the Discussion Draft of the proposed Digital Assets Market Structure legislation introduced on May 5, 2025 in the House. <https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=409719>

[6] <https://www.sec.gov/newsroom/speeches-statements/statement-stablecoins-040425>

[7] For example, if more previously-recognized as gaming contracts are traded on a federally-registered commodity exchange, there will be less volume in economically similar contracts that would be subject to individual States' jurisdiction and more traded on federally-preempted commodity exchanges, i.e., designated contract markets ("DCMs"). Admittedly, this shift in venue and jurisdictional reach will translate into enormous savings and convenience for individual traders.

[8] The UCC has been recently amended to add a digital asset focused article, Article 12 which defines and covers Controllable Electronic Records.

[9] E.g., "eligible commercial entities" under § 1a(17) of the CEA, or "eligible contract participants" under § 1a(18) of the CEA.

[10] Because retail participants can only trade futures contracts (i.e., cannot trade swaps), and the futures contracts can only trade on registered commodity exchanges, and because only registered FCM can facilitate such trading, by necessity retail participants must open futures trading accounts with the FCMs. Several recent CFTC enforcement actions sanctioning unregistered FCMs, IBs, swap execution facilities ("SEFs") and DCMs had clearly reconfirmed this point.

[11] See, e.g., CFTC's Request for Comment involving perpetual contracts, published on April 21, 2025.

[12] See, e.g., <https://www.congress.gov/crs-product/IF12670>

[13] See, digital assets and crypto legislation in the US. Senate and House – each of these proposed drafts extends CFTC's exclusive jurisdiction over spot (non-derivatives) markets in these commodities.

[14] See, https://financialservices.house.gov/uploadedfiles/tbaa_xml.pdf

[15] See, e.g., Chicago Board of Trade v. Christie Grain & Stock Co., 198 U.S. 236 (1905).

[16] See note 3 above citing Kalshi

[17] See, e.g., CFTC proposed rule on event contracts issued on May 10, 2024, Event Contracts, Notice of Proposed Rulemaking, 89 FR 48968 (June 10, 2024).

[18] See, CFTC Request for Comment on 24/7 Trading, published April 21, 2025.

[19] See Memorandum for All Employees, Office of the Deputy Attorney General, Ending Regulation by Prosecution, April 7, 2025, issued in response to President Donald J. Trump's Executive Order 14178 Strengthening American Leadership in Digital Financial Technology, issued January 23, 2025..