



By Electronic Submission

July 24, 2023

Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: KalshiEx, LLC's Self-Certified Proposed Political Event Contract

Dear Mr. Kirkpatrick:

Better Markets¹ appreciates the opportunity to comment on the Commission's review of KalshiEX, LLC's proposed congressional control contract under CFTC Regulation 40.11.²

BACKGROUND

On July 19, 2022, KalshiEX, LLC ("Kalshi") submitted a proposal ("Original Proposed Contract") to the CFTC seeking review and approval of a new binary event contract, which Kalshi titles "the 'Will <party> be in control of the <chamber of Congress>?' Contract." Kalshi's Original Proposed Contract was a binary (all-or-nothing) option contract whose payout was contingent on whether a particular political party will control Congress at a particular time.

¹ Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

² 17 CFR § 40.11, *Review of event contracts based upon certain excluded commodities*; U.S. COMMODITIES FUTURES TRADING COMMISSION, *CFTC Announces Review and Public Comment Period of KalshiEx Proposed Congressional Control Contracts Under CFTC Regulation 40.11* (June 23, 2023), <https://www.cftc.gov/PressRoom/PressReleases/8728-23>

On May 16, 2023, after receiving public notice from several news outlets that the Commission was going to deny its Original Proposed Contract³, and after receiving public advice from Commissioner Pham that it should withdraw its proposal⁴, Kalshi withdrew its bid. Less than 30 days later, on June 12, 2023, Kalshi officially notified the Commission that it was self-certifying a political control event contract (“Self-Certified Contract”). Kalshi’s Self-Certified Contract is substantially similar to the Original Proposed Contract, albeit with certain discernible differences. In response to Kalshi’s notification, on June 23, 2023, the Commission announced that it has commenced a review of the Self-Certified Contract in accordance with CFTC Regulation 40.11(c).

The proposed Self-Certified Contract should not be approved based on several legal and policy grounds because it would (1) violate the statutory and regulatory framework applicable to event contracts; (2) constitute “gaming” under state and federal law; (3) undermine public faith in our markets and elections; and (4) fail to serve the primary purpose of the futures markets as a viable hedging and price discovery mechanism. Although the Commission has previously allowed several non-profit ventures to offer trading on similar political event contracts under specific and limited circumstances, Kalshi’s proposal constitutes a significant departure from previous precedent. Never before has the Commission allowed a for-profit venture to operate in this sensitive arena, fraught with the potential for abuse.

The proposal suffers from multiple fatal flaws. Kalshi’s scant publicly available submission lacks sufficient detail to enable a full and meaningful assessment of the proposed Self-Certified Contract. However, on the available record, meager though it is, the Commission must conclude that the contract would violate the law, pose a serious threat to investors, and fail to serve the legitimate hedging and price discovery functions of the markets it regulates. As a legal matter, Kalshi’s event contract involves, relates to, or at the very least is similar to “gaming” and an activity that is unlawful in numerous states across the country. That must bear heavily on the Commission’s decision and indeed prove dispositive. The CFTC must be mindful that the wrong decision by the CFTC here could de facto preempt innumerable state laws in ways that Congress

³ Lydia Beyoud, *CFTC Poised to Deny US Political Gambling Before November Polls*, Bloomberg (Oct. 28, 2022), <https://www.bloomberg.com/news/articles/2022-10-28/cftc-poised-to-deny-us-political-gambling-before-november-polls?sref=mQvUqJZj>. See also Nick Baker, *CFTC Staff Recommends Rejecting Kalshi’s US Election Contracts*: Bloomberg, (October 28, 2022), <https://www.coindesk.com/policy/2022/10/28/cftc-staff-recommend-rejecting-kalshis-us-election-contracts-bloomberg/>

⁴ Declan Harty, *CFTC’s Pham: Kalshi should withdraw election betting bid*, PoliticoPro (Nov. 08, 2022), <https://subscriber.politicopro.com/article/2022/11/cftc-commissioner-kalshi-should-withdraw-election-betting-bid-00065579>. See Better Markets Ethics Complaint Regarding CFTC Commissioner Caroline Pham’s Apparent Public Disclosure of Highly Confidential, Nonpublic, Internal, Factual and Legal Discussions Regarding the Pending Application of KalshiEx, LLC (Dec. 8, 2022), https://bettermarkets.org/wp-content/uploads/2022/12/Better_Markets_Letter_CFTC_Ethics_Complaint_Pham.pdf; see also Better Markets Ethics Complaint Regarding CFTC Commissioner Caroline Pham’s Apparent Public Disclosure of Highly Confidential, Nonpublic, Internal, Factual and Legal Discussions Regarding the Pending Application of KalshiEx, LLC (Dec. 12, 2022), <https://bettermarkets.org/wp-content/uploads/2023/06/LTR-CFTC-Inspector-General-re-Pham-12-12-22-.pdf>.

clearly did not intend. In addition, the contract is susceptible to manipulation, further endangering investors and the integrity of the markets.

This proposal would contribute to the deeply troubling trend toward the “gamification” and “retailization” of finance. In this increasingly common pattern, everyday consumers and investors are lured into new financial products and services by claims that the offerings represent beneficial “democratization” and “innovation.” Yet as we have seen with the “digital engagement practices” that fueled the meme stock frenzy,⁵ and even more so in the market for cryptocurrencies, the result is typically massive wealth accumulation for a few sponsors and issuers and massive losses suffered by the vast majority of investors.⁶

Democracy and elections are foundational principles for our country and are not appropriate subjects for gaming, gambling and betting. Given the use and abuse of social media in the gambling space⁷ and the A.I. in the political space⁸, allowing gambling on U.S. elections will invite if not incentivize more interference, abuse, and misconduct as gamblers seek to effect political outcomes to maximize their winnings. Even relatively small amounts of spending on negative attack ads can help swing a close race, local elections, and primaries with low turnout, especially if done in the last few days before an election when there is little if any time for a meaningful response.⁹ Imagine what damage an AI deepfake video, supercharged by viral social media, could do if a gambler wanted to try to increase the odds of winning his or her bet in the days before an election. The truth will not catch up to the lie before the votes - and die - are cast.

⁵ See generally Dennis M. Kelleher, Jason Grimes, and Andres Chovil, *Securities—Democratizing Equity Markets With And Without Exploitation: Robinhood, Gamestop, Hedge Funds, Gamification, High Frequency Trading, And More*, 44 W. NEW ENG. L. REV. 51 (2022).

⁶ There are numerous additional downsides that should be considered. See, e.g., Madison Darbyshire, *Traders phone up gambling helplines as game-like broker apps spread*, the Financial Times (Oct. 6, 2021) (“Helplines of gambling addiction recovery groups have been ringing with a new kind of caller: day traders. The rise of mobile brokerage applications outfitted with prompts, animations, rewards, and digital flourishes have brought the feel of investing platforms closer to online sports betting and gambling.”), available at <https://www.ft.com/content/8f9bbc77-06b1-4fbd-8b7e-6e381ba038a7>; Scott Chipolina and Oliver Barnes, *‘There needs to be a health warning’: How crypto trading can lead to addiction*, the Financial Times (June 2, 2023) (“Debate over whether the sector should come under scope of financial services or be treated like gambling.”), available at <https://www.ft.com/content/0f879851-5c74-42ef-914b-154cd4e9a881>.

⁷ Jared Diamond, *A Reporter’s Tweet Moved NBA Draft Odds. He Also Works for a Gambling Company*, The Wall Street Journal, (June 24, 2023), https://www.wsj.com/sports/basketball/nba-draft-shams-charania-the-athletic-fanduel-84e9ccc4?mod=hp_featst_pos5

⁸ Emily Birnbaum and Laura Davison, *AI Is Making Politics Easier, Cheaper and More Dangerous*, (July 11, 2023), <https://www.bloomberg.com/news/features/2023-07-11/chatgpt-ai-boom-makes-political-dirty-tricks-easier-and-cheaper?srd=premium&sref=mQvUqJZj>

⁹ While Kalshi’s proposed Self-Certified Contract is nominally limited to the change in partisan control of Congress, we would anticipate that, if allowed by the CFTC, Kalshi and others would quickly offer similar contracts on all sorts of elections from the local level to the Presidency.

Given all these factors and the negative impact that the commodification of our electoral process would have on the integrity of our democracy, we urge the Commission to reject Kalshi's Self-Certified Contract.

Legal Context

The Commodity Exchange Act (“CEA”) Section 5c(c)(5)(C) prohibits the listing of agreements, contracts, transactions, or swaps in an excluded commodity.¹⁰ Section 5c(c)(5)(C)(i) of the CEA prohibits event contracts that “involve, relate to, or reference” terrorism, assassination, war, gaming, or an activity that is unlawful under any State or Federal law.¹¹ The legislative history of CEA Section 5c(c)(5)(C) indicates that CFTC should consider whether the event contract as a whole involves activities listed under Section 5c(c)(5)(C)(i).

In 2011, the Commission promulgated Regulation 40.11 to implement Section 5c(C)(5)(C) of the CEA.¹² Regulation 40.11(a)(1) prohibits the listing of an agreement, contract, or transaction “that involves, relates to, or references” terrorism, assassination, war, gaming, or an activity that is unlawful under any State or Federal law.¹³ Because not all undesirable contracts may fall neatly within the specific categories listed in Regulation 40.11(a)(1), CFTC Regulation 40.11(a)(2) includes a provision that prohibits event contracts involving an activity that is “similar to” the activities enumerated in 40.11(a)(1), so long as the Commission determines the contract to be “contrary to the public interest.”¹⁴

Regulation 40.11(c) provides for a 90-day review period for any such contract that the Commission determines may involve gaming or any of the other activities referenced in Regulation 40.11(a)(1).¹⁵

Prior Commission Approaches

Historically, the CFTC has permitted binary event contracts only under conditions more limited and tightly controlled than those of the Kalshi contract. In 1993, CFTC staff issued a no-action letter to the Iowa Electronic Markets (“IEM”), an academic prediction market run by the

¹⁰ 7 U.S.C. § 7a-2(c)(5)(C). The Commodities Exchange Act (CEA) is codified at 7 U.S.C. § 1 *et seq.*

¹¹ 7 U.S.C. § 7a-2(c)(5)(C)(i).

¹² Provisions Common to Registered Entities, 76 Fed. Reg. 44776, 44785 (July 27, 2011).

¹³ 17 C.F.R. 40.11(a)(1).

¹⁴ 17 C.F.R. 40.11(a)(2).

¹⁵ 17 C.F.R. 40.11(c).

University of Iowa’s Tippie College of Business in conjunction with several other universities.¹⁶ Among the event contracts available for trading on the IEM are political event contracts regarding partisan control of the United States Congress. The CFTC’s staff no-action letter allowed the IEM to continue offering its political event contracts, but with several restrictions. First, the no-action was premised on the IEM’s academic purpose and operation as a non-profit entity. Second, neither the IEM nor the University of Iowa charges any commissions or receives a return in connection with its operation, and IEM does not realize a financial profit or suffer loss as a result of the transactions.

In December 2011, the North American Derivatives Exchange (“NADEX”) submitted a proposal to the CFTC seeking approval of five new political event contracts relating to the political control of the United States Congress and the Presidency.¹⁷ On April 2, 2012, the CFTC issued an order prohibiting NADEX from listing its proposed political event contracts.¹⁸ In its order, the CFTC found that the contracts, which would have paid out based upon the outcome of US federal elections, “involved[] gaming” and were contrary to the public interest under CEA Section 5c(c)(5)(C)(i). In its analysis, the CFTC determined, among other things:

- (1) “the unpredictability of the specific economic consequences of an election means that the Political Event Contracts cannot reasonably be expected to be used for hedging purposes;”
- (2) “there is no situation in which the Political Event Contracts’ prices could form the basis for the pricing of a commercial transaction involving a physical commodity, financial asset or service, which demonstrates that the Political Event Contracts have no price basing utility;” and
- (3) “the Political Event Contracts can potentially be used in ways that would have an adverse effect on the integrity of elections, for example by creating monetary incentives to vote for particular candidates even when such a vote may be contrary to the voter’s political views of such candidates.”¹⁹

¹⁶ CFTC No-Action Letter, CFTCLTR No. 93-66, 1993 WL 595741 (June 18, 1993), <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrllettergeneral/documents/letter/93-66.pdf>.

¹⁷ U.S. COMMODITIES FUTURES COMMISSION, *CFTC Commences 90-day Review of NADEX’s Proposed Political Event Derivatives Contracts* (Jan. 5, 2012), <https://www.cftc.gov/PressRoom/PressReleases/6163-12>.

¹⁸ U.S. COMMODITIES FUTURES COMMISSION, *Order Prohibiting the Listing or Trading of Political Event Contracts*, <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>.

¹⁹ *Id.*

In 2014, the CFTC staff issued a no-action letter to PredictIt, operated by researchers at the Victoria University of Wellington, allowing its political event contracts to operate in the United States provided that it met certain conditions. Among these conditions were that the market must:

- be small-scale and not-for-profit;
- be operated for academic and research purposes only;
- be overseen by faculty at the University, without receipt of separate compensation;
- be limited to 5,000 traders per contract, with an \$850 investment limit per participant in any contract;
- not offer brokerage services or charge commissions to participants;
- utilize a third-party service provider to perform know-your-customer (“KYC”) due diligence on its participants; and
- only charge those fees necessary to cover the costs of implementing the KYC process, regulatory compliance, and basic expenses necessary to operate the proposed event contract market.

In August 2022, however, the CFTC staff informed PredictIt that it had violated the no-action letter, that it was withdrawing the no-action letter, and instructed the company to wind down its operation of the political event contracts by February 2023.²⁰

The Kalshi Contract

Kalshi’s Original Proposed Contract provided that it was their intention to impose a position limit of \$25,000. However, in Kalshi’s new Self-Certified Contract, it is the exchange’s intention to increase the position limit as follows:

- (i) The Position Limit for Individuals shall be \$125,000 per Member; and \$250,000 for those with demonstrated established economic hedging need;
- (ii) The Position Limit for Entities shall be \$5,000,000 per Member; and \$10,000,000 for those with demonstrated established economic hedging need;
- (iii) The Position Limit for Eligible Contract Participants shall be \$50,000,000 per Member; and \$100,000,000 for those with demonstrated established economic hedging need.

Kalshi’s Self-Certified Contract provides that a claim for a purported need for economic hedging by an individual, entity, or eligible contract participant member may be demonstrated to Kalshi according to the means and methods established by Kalshi. Whether a member has demonstrated

²⁰ U.S. COMMODITIES FUTURES COMMISSION, *CFTC Staff Withdraws No-Action Letter to Victoria University of Wellington, New Zealand Regarding a Not-For-Profit Market for Certain Event Contracts* (Aug. 4, 2022), <https://www.cftc.gov/PressRoom/PressReleases/8567-22>.

that it has a sufficiently established an economic hedging need is determined solely at Kalshi's discretion. Furthermore, the Self-Certified Contract provides little information on the fees and commissions Kalshi charges on its platform, stating only the following:

“Members will be charged fees in accordance with Rule 3.6 of the Rulebook. Fees are charged in such amounts as may be revised from time to time to be reflected on the Exchange's Website.”

As with its Original Proposed Contract, Kalshi does not include a copy of the Rulebook referenced in its submission, leaving readers and possibly the Commission itself without key information regarding the specifics of its fee structure or Kalshi's unilateral, subjective power to change any and all provisions. Finally, Kalshi does not presently allow leveraged or margined trading on its platform, but it reserves the right to change this policy in the future, as it, of course, can change any of its other policies, procedures or statements.

If approved, Kalshi's proposal would represent a significant departure from the fundamental and historical underpinnings of the futures markets. The fundamental purpose of the derivatives market is to provide a means of hedging risk and price discovery for commercial enterprises, not to enable mass speculative gambling among retail traders.²¹ While limited speculation is permitted to provide additional liquidity necessary to enable derivatives markets to perform their important historic functions, the markets overseen by the CFTC are not — and never were — intended as casinos or predominantly speculative vehicles.²² Nor were our elections intended to be commodified, commercialized, and gambled upon *en masse* with the mere click of a button.

The Commission has appropriately identified several areas of interest in the 24 questions it posed for public comment.²³ We hope our comments assist the Commission as it reviews this proposal.

¹³ See Timothy E. Lynch, *Derivatives: A Twenty-First Century Understanding*, 43 LOY. U. CHI. L. J. 1 (2011) (“[E]nabling hedging is the *raison d'être* for the existence of derivatives, and without this characteristic, it is doubtful that the modern derivatives industry would have developed.”); Lynn A. Stout, *Derivatives and the Legal Origin of the 2008 Credit Crisis*, 1 HARV. BUS. L. REV. 1 (2011); Miriam A. Cherry & Robert L. Rogers, *Prediction Markets and the First Amendment*, 2008 U. ILL. L. REV. 833, 838 (2008) (distinguishing the information-aggregating function of prediction markets from the price discovery function of other traditional markets); COMMODITIES FUTURES TRADING COMMISSION, *The Economic Purpose of Futures Markets and How They Work*, <https://www.cftc.gov/LearnAndProtect/AdvisoriesAndArticles/economicpurpose.html>.

²² See generally Lynn A. Stout, *How Deregulating Derivatives Led to Disaster, and Why Re-Regulating Them Can Prevent Another*, 1 LOMBARD ST. 4 (July 2009).

²³ COMMODITIES FUTURES TRADING COMMISSION, *Questions on the KalshiEX, LLC “Will <party> be in control of the <chamber of Congress> for <term>?” Contracts for Public Comment*, <https://www.cftc.gov/media/8801/DMOKalshiQuestions062323/download>

COMMENTS

I. The Submission fails to provide sufficient information to allow meaningful public comment or appropriate review by the Commission.

As a threshold matter, the Self-Certified Contract from Kalshi is grossly deficient and has to violate the Administrative Procedures Act (“APA”) that requires enabling meaningful public comment. It is largely opaque, providing remarkably scant detail about the material features of the contract. In short, it fails to supply enough information that might enable the Commission or interested members of the commenting public to fully evaluate the contract. Even if the Commission believes that it has sufficient information from Kalshi’s public and confidential submissions, that is inadequate because the Commission has deprived itself of the benefit of informed, meaningful public comment on the material aspects of the proposed Self-Certified Contract. This is a key reason that the APA requires agencies like the CFTC to seek, obtain, and take into account public comment.

Kalshi’s Self-Certified Contract fails to provide sufficient detail regarding several key issues surrounding the contract. As discussed above, Kalshi’s submission includes no specific details regarding the fee structure it would charge its users, stating only that users will be charged fees according to its own “Rulebook,” which Kalshi fails to include with its publicly available submission.²⁴ The Self-Certified Contract application also does not offer a description of how margin will be handled under the contract.

More significantly, the Self-Certified Contract conspicuously omits any assessment of the actual impact of that trading activity, either on investors or those who may have attempted to use those contracts to, for example, hedge a risk. Finally, information regarding the Self-Certified Contract’s risk mitigation analysis and price-basing utility, as well as any additional considerations related to the Self-Certified Contract is not available to be reviewed for public comment for it is supposedly included in confidential appendices of Kalshi’s submission. Notwithstanding Kalshi’s representations, as deficient and incomplete as they are, Kalshi could possibly materially change any term, policy, or practice after receiving Commission approval of its contract.²⁵

1. Kalshi failed to properly comply with the submission requirements provided in CFTC regulation 40.2(a)(3).

In its Self-Certified Contract submission, Kalshi used language that appears to certify that the event contract complies with the CEA and CFTC regulations. However, in the actual

²⁴ As noted above, even the minimal information that is publicly available is subject to our serious concerns surrounding Kalshi’s reservation of the right to alter the terms of the contract in the future.

²⁵ Kalshi’s ability to change the contract in the future is a major concern even if such future alterations are subject to Commission approval. Regardless of that approval process for later changes, the public (and the Commission itself) are now being asked to evaluate a contract with terms that may essentially be inaccurate, to the extent Kalshi already harbors the intention to change them in the future.

certification document required under Regulation 40.2(a)(3)(iv), Kalshi did not certify that the event contracts comply with the CEA and CFTC regulations. In fact, Kalshi only included language in the certification document from regulation 40.2(a)(3)(vi) which certifies that Kalshi posted a notice of pending product certification with the CFTC and a copy of the submission on its Website.

In contrast, Kalshi's previous self-certified event contracts with different underlying subject matters all contained a statement certifying the compliance of their contracts with CEA and CFTC regulations along with a signature from a representative. However, Kalshi did not do the same in its Self-Certified Contract. With this apparent omission, this is a de facto admission by Kalshi that its Self-Certified Contract does not comply with the CEA and CFTC regulations. Regardless, Kalshi has failed to meet the necessary regulatory requirements for self-certifying its political control event contract. The CFTC should require Kalshi to remove its political control contracts due to its failure to comply with the regulatory requirements put in place to ensure legal compliance and protect market integrity.

II. The Commission should prohibit trading of the Self-Certified Contract because it conflicts with the intent of the Commodity Exchange Act, violates the letter of the Commission's rules against event contracts, and is contrary to the public interest.

The Commission should reject Kalshi's Self-Certified Contract because it conflicts with the letter and spirit of the Commodity Exchange Act, Commission Rule 40.11, and the public interest. Section 5c(c)(S)(C) of the Commodity Exchange Act provides, in pertinent part:

(C) SPECIAL RULE FOR REVIEW AND APPROVAL OF EVENT CONTRACTS AND SWAPS CONTRACTS.—

(i) EVENT CONTRACTS.—In connection with the listing of agreements, contracts, transactions, or swaps in excluded commodities that are based upon the occurrence, extent of an occurrence, or contingency (other than a change in the price, rate, value, or levels of a commodity described in section 1a(2)(i) [2] of this title), by a designated contract market or swap execution facility, the Commission may determine that such agreements, contracts, or transactions are contrary to the public interest if the agreements, contracts, or transactions involve—

- (I) activity that is unlawful under any Federal or State law;
- (II) terrorism;
- (III) assassination;
- (IV) war;
- (V) gaming; or
- (VI) other similar activity determined by the Commission, by rule or regulation, to be contrary to the public interest.

- ii. PROHIBITION.—No agreement, contract, or transaction determined by the Commission to be contrary to the public interest under clause (i) may be listed or made available for clearing or trading on or through a registered entity.

Following these Dodd-Frank amendments to the CEA, the Commission promulgated Rule 40.11,²⁶ pertaining to event contracts. In that rule, the Commission wisely chose to exercise the authority from Congress to impose an outright ban on gaming contracts or similar contracts that are contrary to the public interest. The rule provides as follows:

§ 40.11 Review of event contracts based upon certain excluded commodities.

(a) *Prohibition.* A registered entity shall not list for trading . . . any of the following:

- (1) An agreement, contract, transaction, or swap based upon an excluded commodity, as defined in Section 1a(19)(iv) of the Act, that involves, relates to, or references terrorism, assassination, war, gaming, or an activity that is unlawful under any State or Federal law; or
- (2) An agreement, contract, transaction, or swap based upon an excluded commodity, as defined in Section 1a(19)(iv) of the Act, which involves, relates to, or references an activity that is similar to an activity enumerated in § 40.11(a)(1) of this part, and that the Commission determines, by rule or regulation, to be contrary to the public interest.

A. The proposed Self-Certified Contract involves, relates to, or is similar to, gaming, which is condemned under the CEA, prohibited under the Commission’s rules, and outlawed in several states.

Kalshi’s Self-Certified Contract is substantially similar in all material respects to the NADEX contracts, which the Commission appropriately denied because they were, involved, related to, or were similar to gaming and because they were illegal under state law.

1. The Kalshi contract involves gaming.

As the CFTC determined in its response to NADEX’s 2012 proposal for binary event contracts, political event contracts involve or are similar to “gaming.”²⁷ Here too, Kalshi’s virtually identical political event contract is gaming, involves gaming, relates to gaming, or is “similar to”

²⁶ 17 C.F.R. § 40.11.

²⁷ See U.S. COMMODITY FUTURES TRADING COMM’N, *Order Prohibiting the Listing or Trading of Political Event Contracts*, (Apr. 2, 2012), <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>.

gaming within the meaning of CEA § 5cI(5)(C)(i) and Commission Regulation 40.11(a)(1). It, therefore, falls squarely under the Commission’s regulatory prohibition, as authorized under the terms of the CEA.

Like NADEX’s proposal in 2012,²⁸ Kalshi now proposes to list a binary (all-or-nothing) event contract whose payoff is contingent upon the election of representatives to the United States Congress, such that one political party gains “control” — or a voting majority — of a chamber of Congress for a particular congressional term. Participants in such political prediction markets place a sum of money at risk, with the payout based on the market’s assessment of the probability of each outcome. If a participant “predicts” correctly, they are rewarded monetarily. Conversely, if they predict incorrectly, their position will lose monetary value.

The conclusion that the Kalshi Self-Certified Contract, and the NADEX contract before it, are, involve, relate to, or are similar to “gaming” follows from an analysis of both federal and state law.²⁹ With respect to federal law, although “gaming” is not defined in either the CEA or CFTC regulations, the Commission previously relied on the Unlawful Internet Gambling Enforcement Act in its prior finding that NADEX’s similar political event contracts constituted “gaming” under the CEA and Commission Rule 40.11.³⁰ The Unlawful Internet Gambling Enforcement Act defines the terms “bet or wager” as:

“the staking or risking by any person of something of value upon the outcome of a contest of others, a sporting event, or a game subject to chance, upon an agreement or understanding that the person or another person will receive something of value in the event of a certain outcome.”³¹

Clearly, Kalshi’s proposed event contracts fall squarely within this definition — namely, “*the staking or risking by any person of something of value upon the outcome of a contest of others.*”³² Although neither the Unlawful Internet Gambling Enforcement Act nor the Commodity Exchange

²⁸ For a discussion of the Commission’s treatment of the NADEX contracts, see Dave Aron & Matt Jones, *States’ Big Gamble on Sports Betting*, 12 UNLV GAMING L. J. 53, 75–76 (2021).

²⁹ For a discussion of prior CFTC consideration and analysis of event contracts and “gaming,” *see id.*, at 71–86.

³⁰ U.S. COMMODITY FUTURES TRADING COMM’N, *Order Prohibiting the Listing or Trading of Political Event Contracts*, (Apr. 2, 2012), <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>; The Unlawful Internet Gambling Enforcement Act is codified at 31 U.S.C. § 5361 *et seq.*

³¹ 31 U.S.C. § 5362(1)(A) (emphasis added); *see also* Christine Hurt, *Regulating Public Morals and Private Markets: Online Securities Trading, Internet Gambling and the Speculation Paradox*, 86 B.U. L. REV. 371 (2006); Dave Aron & Matt Jones, *States’ Big Gamble on Sports Betting*, 12 UNLV GAMING L. J. 53, 67–86, 71 (2021) (discussing the CEA’s application to event contracts).

³² Relatedly, the traditional common law definition of “gaming” includes three elements: consideration, prize, and chance, all of which are present in prediction markets. *See* Tom W. Bell, *Gambling for the Good, Trading for the Future: The Legality of Markets in Science Claims*, 5. CHAP. L. REV. 159, 165-166 (2002).

Act defines the term “contest,” the Cambridge English Dictionary provides the following definition:

“a competition to do better than other people, esp. to win a prize or achieve a position of leadership or power: **‘In the last election, he survived a close contest against a political newcomer.’**”³³

Moreover, as observed by the CFTC in its 2012 order against the NADEX proposal, numerous states’ gambling laws expressly link the terms “gaming” or “gambling” with betting or wagering upon the outcome of an election:

“[S]everal state statutes, on their face, link the terms gaming or gambling (which are used interchangeably in common usage, dictionary definitions and several state statutes) to betting on elections, and state gambling definitions of ‘wager’ and ‘bet’ are analogous to the act of taking a position in the Political Event Contracts.”³⁴

This is no less true now than it was in 2012, and there is no reason why the Commission should now find otherwise.

While some contend that political event contracts cannot be or involve “gaming” because prediction markets contain an element of skill as opposed to mere chance, the statutory definition of “bet or wager” above lists “a game subject to chance” in the disjunctive and but one of several examples, not a necessary element. That political prediction markets contain an element of skill — i.e., informational or predictive superiority — makes them no more distinct from gaming than does a professional poker player’s expertise make their profession distinct from gambling. Both at the blackjack table and in a prediction market, skill will aid the participants. But in both cases, significant elements of uncertainty and chance preside over the endeavor that are outside the control of the participants, rendering the activity one that is, involves, relates to — or is at least similar to — “gaming” for purposes of the CEA.³⁵

Proponents of Kalshi wrongfully claim that the language and structure of Section 5cI(5)(C)(i) make clear that the scope of the Commission’s discretionary review is narrowly

³³ THE CAMBRIDGE ENGLISH DICTIONARY, *Contest* (emphasis added), <https://dictionary.cambridge.org/us/dictionary/english/contest>.

³⁴ U.S. COMMODITY FUTURES TRADING COMM’N, *Order Prohibiting the Listing or Trading of Political Event Contracts*, (Apr. 2, 2012), <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>.

³⁵ See Ryan P. McCarthy, *Information Markets as Games of Chance*, 155 U. PA. L. REV. 749, 770 (2007); Thomas Lee Hazen, *Disparate Regulatory Schemes for Parallel Activities: Securities Regulation, Derivatives Regulation, Gambling, and Insurance*, 24 ANN. REV. BANKING & FIN. L. 375, 401-12, 416-18 (2005) (comparing investing, hedging, insurance, and gambling as risk-taking activities).

focused on the nature of the contract's underlying event, not on trading in the contract itself. Because elections do not fit within any of the enumerated activities, they claim that the Commission should not impede self-certification of the political control contract.³⁶ However, the legislative history of CEA Section 5c(c)(5)(C) makes clear that the relevant question for the Commission in determining whether a contract involves one of the activities enumerated in CEA Section 5c(c)(5)(C)(i) is whether the contract, considered as a whole, involves one of those activities.³⁷ As mentioned previously, the Self-Certified Contract proposed by Kalshi should be rejected by the Commission since the whole contract can be categorized as a form of gaming. On Kalshi's exchange, customers will voluntarily bet money based on the outcome of a competitive political election.

2. The Kalshi contract involves an activity that is unlawful under state law.

As a separate matter, the Commission also rejected the NADEX contract because it plainly involved, related to, or referenced an activity that was unlawful under numerous states' laws. The same is true with respect to the Kalshi contract, a separate factor that is also dispositive under Rule 40.11(a)(1).³⁸ Placing a bet or wager on the outcome of an election is civilly or criminally unlawful in well over a dozen states nationwide.³⁹ For decades, states have long asserted their right to protect

³⁶ See Dissenting Statement of Commissioner Caroline D. Pham Regarding the Review and Stay of KalshiEX LLC's Political Event Contracts, <https://www.cftc.gov/sites/default/files/filings/ptc/23/06/ptc0612232837.pdf>

³⁷ See In the Matter of the Self-Certification by North American Derivatives Exchange, Inc., available at <https://www.cftc.gov/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>

³⁸ See, e.g., NV REV. STAT. § 293.830 (2014) ("Any person who makes, offers or accepts any bet or wager upon the result of any election, or upon the success or failure of any person or candidate . . . is guilty of a gross misdemeanor."); TN CODE § 2-19-129 (2014) ("A person commits a Class C misdemeanor if such person makes any bet or wager of money or other valuable thing upon any election."); 720 ILL. COMP. STAT. ANN. 5/28-1 (2011) ("A person commits gambling when he . . . [m]akes a wager upon the result of any game, contest, or any political nomination, appointment or election . . ."); NEB. REV. STAT. § 28-1101(4) (2011) ("A person engages in gambling if he or she bets something of value . . . upon the outcome of a game, contest, or election . . ."); N.M. STAT. ANN. § 44-5-10 (1978) ("Bets and wagers on an election authorized by the constitution and laws of the United States, or by the laws of this state, are gaming within the meaning of this chapter [on gambling debts and losses.]; N.D. CENT. CODE ANN. § 12.1-28-01 (West 2011) ("Gambling' means risking any money . . . upon . . . the happening or outcome of an event, including an election . . . over which the person taking the risk has no control."). See also GA. CODE ANN. § 16-12-21(a)(2) (West 2011) ("A person commits the offense of gambling when he . . . [m]akes a bet upon the result of any political nomination, appointment, or election . . ."); MISS. CODE ANN. § 97-33-1 (2011) ("If any person . . . shall wager or bet . . . upon the result of any election . . . he shall be fined in a sum not more than Five Hundred Dollars . . ."); S.C. CODE ANN. § 16-19-90 (2011) ("Any person who shall make any bet or wager of money . . . upon any election in this State shall be guilty of a misdemeanor . . ."); TEX. PENAL CODE ANN. § 47.02(a)(2) (West 2011) ("A person commits an offense if he . . . makes a bet on the result of any political nomination, appointment, or election . . .").

³⁹ See NATIONAL CONFERENCE OF STATE LEGISLATURES, *Wagering on Elections? Not a Smart Bet* (Sept. 17, 2014), <https://www.ncsl.org/blog/2014/09/17/wagering-on-elections-not-a-smart-bet.aspx>.

the integrity of their elections by prohibiting placing wagers on the outcome of an election.⁴⁰ In the absence of finding a public interest, the Commission should not preempt these states' longstanding, deeply rooted concerns by granting KalshiEx — a profit-driven venture — license to profit from speculation on the outcome of our elections.

B. The Contract is otherwise contrary to the public interest.

1. The proposed event contract is readily susceptible to manipulation.

Kalshi's political event contract runs afoul of the CFTC's Core Principles applicable to Designated Contract Markets — namely, Core Principle #3's requirement that a contract must not be “readily subject to manipulation.”⁴¹

Political prediction markets operate in a shrouded space that would readily lend itself to manipulation and other forms of abusive activity. It raises the specter of political insiders privy to non-public information — say, internal polling or campaign finance data — wielding their informational advantage to profit at the expense of others.⁴² And it would be susceptible to other classic forms of market manipulation. After all, “parties with an interest in the outcome have an incentive, whenever possible, to move the odds prices in their preferred direction.”⁴³

In her 2009 Harvard Law Review article “Prediction Markets and Law: A Skeptical Account,” Professor Rebecca Haw Allensworth detailed how bad actors might manipulate prediction markets:

Prediction markets are vulnerable to manipulation, although scholars do not agree on how serious the problem is. Information market traders can gain from manipulations in two ways. First, they could profit by artificially lowering the trading price temporarily and purchasing shares to be sold at a higher price when the market returns to ‘normal.’ Second, they could try to affect the informational value of the market. For example, a candidate's supporter could purchase his shares at an inflated value, raising the perceived odds that he would win the election, and (hopefully) getting more voters to jump on the putative bandwagon. At least in the

⁴⁰ See generally Paul W. Rhode & Koleman S. Strumpf, *Historical Presidential Betting Markets*, 18 J. OF ECON. PERSP. 127 (2004) (outlining the history of election wagering in America).

⁴¹ See COMMODITIES FUTURES TRADING COMMISSION, *Designated Contract Markets (DCMs)*, <https://www.cftc.gov/IndustryOversight/TradingOrganizations/DCMs/index.htm>.

⁴² See Alex Altman, *Political Betting Market Raises Questions About Insider Trading*, TIME (Oct. 6 2015), <https://time.com/4062628/fantasy-sports-predictit-political-forecasting/>.

⁴³ Paul W. Rhode & Koleman S. Strumpf, *Manipulating Political Stock Markets: A Field Experiment and a Century of Observational Data 2* (Jan. 2007) (unpublished manuscript, available at <https://economics.yale.edu/sites/default/files/files/Workshops-Seminars/Economic-History/rhode-051116.pdf>).

short term, manipulators have succeeded in artificially inflating or deflating the prices of securities in information markets. In 2004, TradeSports's election prediction market fell victim to two 'sustained attempts' at manipulation, which resulted in 'large price changes that do not appear to have been based on any information.'⁴⁴

Similarly, in one study, titled "Affecting Policy by Manipulating Prediction Markets: Experimental Evidence," researchers found experimental evidence demonstrating how a highly motivated actor can manipulate prediction markets, thereby undermining their predictive reliability:

We find clear evidence that highly incentivized manipulators can destroy the predictive power of an information market. That is, we have identified a case where manipulators do cause human forecasters to make predictions that are no better than random guessing would generate showing that prediction markets can be manipulated. Further, our results show that the effects of introducing manipulators are due to more than just the large influx of liquidity in the market. This finding demonstrates that policy makers should not indiscriminately rely upon market predictions, but rather need to consider the incentives and wherewithal of potential manipulators. Our results are also suggestive that the possibility of such manipulators may also be sufficient to undermine the market aggregation of information.⁴⁵

With Kalshi allowing single contracts of \$100,000,000 and aggregate amounts at risk almost certain to be in the tens if not hundreds of billions of dollars, the incentive to interfere with and manipulate the political events are likely to prove overwhelming so some number of gamblers.

Kalshi's submission (or at least the part available to the public) does not explain how it will identify and eliminate manipulation risks. Given the many ways one could conceivably influence or manipulate a prediction market to their advantage,⁴⁶ the Commission should not allow the adoption of political event contracts as Kalshi proposes.

⁴⁴ Rebecca Haw Allensworth, *Prediction Markets and Law: A Skeptical Account*, 122 HARV. L. REV. 1217 (2009).

⁴⁵ Deck, *infra* n. 46, at 61.

⁴⁶ See, e.g., Brad Plumer, *How to Swing the Prediction Markets and Boost Mitt Romney's Fortunes*, THE WASHINGTON POST (Oct. 23, 2012), <https://www.washingtonpost.com/news/wonk/wp/2012/10/23/how-to-manipulate-prediction-markets-and-boost-mitt-romneys-fortunes/>; Alex Klein, *InTrade And Jon Huntsman: Why the Media's Faith in the Internet Betting Ring Is Foolish*, THE NEW REPUBLIC (Jun. 21, 2011), <https://newrepublic.com/article/90371/intrade-and-jon-huntsman-president-odds-republican-nomination>. See generally Kloker, Simon and Kranz, Tobias T., *Manipulation In Prediction Markets – Chasing The Fraudsters*. In PROCEEDINGS OF THE 25TH EUROPEAN CONFERENCE ON INFORMATION SYSTEMS (ECIS), Guimarães, Portugal, June 5-10, (2017) (pp. 2980-2990), <http://aisel.aisnet.org/ecis2017rip/47>; Cary Deck, Shengle Lin, & David Porter, *Affecting Policy by Manipulating Prediction Markets: Experimental Evidence*,

2. Kalshi’s proposed for profit contract would fail to provide the consumer protections and academic benefits provided by other non-profit prediction markets.

The fact that some other event contract platforms have been allowed to operate does not support the approval of the Kalshi submission. Those other platforms were readily distinguishable and were subject to multiple important limitations and conditions. Unlike the Iowa Electronic Markets⁴⁷ — and, until recently, PredictIt⁴⁸ — Kalshi is a for-profit entity established and motivated to maximize financial gain. Moreover, unlike non-profit prediction markets, Kalshi would face significant commercial pressure to extract wealth from its users through high transaction, commission, withdrawal, and other fees, as well as creating and offering a proliferation of other contracts, presumably enabling betting on virtually all other elections in the U.S. and elsewhere. Kalshi’s submission proposal provides little assurance that it will not do so, outlining no specific details regarding its fees, commission policies, or business plans.

In contrast, the conditions of the no-action letter granted to the Iowa Electronic Markets state that its prediction market is run on a not-for-profit basis, no commissions are charged to users, and its administrators do not receive a return in connection with the site. Moreover, traders are limited to position limits of well under \$1,000. Until recently, the political prediction market PredictIt — a non-profit project run by academics from the Victoria University of Wellington in New Zealand — likewise operated with similar restrictions protecting traders and guaranteeing researchers access to its data.⁴⁹ These contracts are a far cry from Kalshi’s proposed Self-Certified Contract. The Commission’s recent withdrawal of PredictIt’s no-action letter only intensifies concerns surrounding the appropriateness of allowing even non-profit research enterprises to operate event contract platforms, let alone the one advanced by Kalshi.

3. Kalshi’s proposed contract would redirect capital from productive uses into highly speculative markets and would undermine public trust in our elections.

85 J. ECON. BEHAV. & ORG. 48 (2013) (“[W]e present evidence from the lab indicating that single-minded, well-funded manipulators can in fact destroy a prediction market’s ability to aggregate informative prices and mislead those who are making forecasts based upon market predictions.”).

⁴⁷ See IOWA ELECTRONIC MARKETS, <https://iemweb.biz.uiowa.edu/>; CFTC No-Action Letter, CFTCLTR No. 93-66, 1993 WL 595741 (June 18, 1993), <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrllettergeneral/documents/letter/93-66.pdf>.

⁴⁸ See Declan Harty, *No Future: Regulator Orders Political Prediction Market to Shut Down in U.S.*, POLITICO (Aug. 09, 2022), <https://www.politico.com/news/2022/08/09/no-future-regulator-orders-political-betting-market-to-shut-down-in-u-s-00050238>.

⁴⁹ See Declan Harty, *Washington Weighs Plan to Let Americans Wager on Elections*, POLITICO (Sep. 5, 2022), <https://www.politico.com/news/2022/09/05/voters-betting-elections-trading-00054723>.

Kalshi's contract would redirect capital that could otherwise be productively deployed in the public securities markets and elsewhere into a highly speculative and risky market that serves little if any economic purpose, just like traditional gambling.⁵⁰ Such markets prey on unwary traders and typically serve to enrich the few at the expense of the many.⁵¹ What is more, this speculative market runs contrary to the fundamental and historical purposes underlying the derivatives market — namely, to hedge commercial risks and assist in price discovery. Indeed, if anything, the so-called market that would be created by Kalshi's Self-Certified Contract would appear to increase risk rather than hedge or alleviate it.

And it does so at the steep cost of jeopardizing the integrity of and public faith in our elections. Whether through mere perception or through other means, there is little doubt that the mass commodification of our democratic process would raise widespread concerns about the integrity of our electoral process. Putting aside the significant issues of whether such markets could inspire vote-switching and other nefarious conduct, the mere impact on the public's perception of our democracy is cause enough to conclude that it is decidedly not in the public interest.

A. CFTC Regulation 40.11(a)(2) includes a very important catch-all provision.

Because not all contracts that would clearly be contrary to the public interest may fall neatly within the specific categories listed, CFTC adopted a regulation, 40.11(a)(2), that prohibits event contracts involving an activity that is “similar to” the activities enumerated in 40.11(a)(1), so long as the CFTC determines the contract to be “contrary to the public interest.”⁵² This provision serves as a clear recognition that there are simply some types of trading that society can and must consider off limits.⁵³

For example, betting via event contracts on where the next school shooting will be or how many school children will be murdered in the next school shooting are not enumerated and therefore it could be argued not prohibited. However, few would doubt that such betting should be prohibited because such a contract would “involve, relate to, or reference” assassination. But

⁵⁰ See Christine Hurt, *Regulating Public Morals and Private Markets: Online Securities Trading, Internet Gambling, and the Speculation Paradox*, 86 B.U. L. REV. 371, 373-74 (2006) (“[G]ambling is viewed as an enterprise of chance that encourages [participants] . . . to divert useful capital into a chaotic system whereby an undeserving few reap ill-gotten gains while the vast majority foolishly lose.”); Lynn A. Stout, *Why the Law Hates Speculators: Regulation and Private Ordering in the Market for OTC Derivatives*, 48 DUKE L.J. 701, 715 (1999) (“Common law courts regarded speculation as a type of wagering rather than a useful form of economic commerce.”); Thomas Lee Hazen, *Disparate Regulatory Schemes for Parallel Activities: Securities Regulation, Derivatives Regulation, Gambling, and Insurance*, 24 ANN. REV. BANKING & FIN. L. 375, 377 (“In contrast to investing, hedging and insurance, gambling is not generally viewed as a productive activity or one that provides any benefit to society beyond its entertainment value.”).

⁵¹ See Jon Kimball & David Rees, THE WASHINGTON POST, *We Made Thousands On This Website. But We're Still Happy It's Shutting Down* (Aug. 25, 2022), <https://www.washingtonpost.com/opinions/2022/08/25/predictit-gambling-political-prediction-markets/>.

⁵² 17 C.F.R. 40.11(a)(1).

⁵³ 17 C.F.R. 40.11(a)(2).

it's not difficult to anticipate a lawyer's argument that a school shooting actually did not "involve, relate to, or reference" assassination, at least not in a narrow traditional sense. No one, however, could argue that such a contract would be "similar to" assassination and thereby properly prohibited as contrary to the public interest. Regarding Kalshi's Self-Certified Contract, in addition to being unlawful under a number of state and federal laws and prohibited gaming (either directly or because it "involves" and "relates to" gaming), it should also be prohibited because it is similar to gaming and therefore should be rejected as contrary to the public interest.

B. Congress did not intend for the CFTC to police elections.

Widespread gambling on our elections through the simple click of a button is far removed from the purpose, function, and importance of the electoral processes. Such activities undermine the sanctity and democratic value of elections, turning them into speculative spectator sports. Better Markets agrees with the statements made by Chair Behnam regarding the new and entirely different role the CFTC would have to assume if political contracts were allowed.⁵⁴

The prospect of the CFTC assuming the role of an "election cop" raises valid concerns about the misalignment of that role with the CFTC's mandate and with the original intent and objectives set forth by Congress. This situation presents not only legal implications but also broader policy considerations. It prompts questions regarding the suitability of this financial regulatory body being heavily involved in overseeing and policing gambling on the country's electoral processes. Therefore, it is important for the CFTC to carefully evaluate all these implications and potential consequences when it deliberates on whether to allow a political event contract in the derivatives marketplace.

III. The Submission cannot and will not serve a meaningful hedging or price discovery function.

The legislative history of CEA Section 5c(c)(5)(C) makes clear Congress's intent to restore the economic purpose test that was used by the CFTC to determine whether a contract was contrary to the public interest pursuant to CEA Section 5(g) prior to its deletion by the Commodity Futures Modernization Act of 2000. The restored economic purpose test calls for an evaluation of an event contract's utility for hedging and price discovery purposes. The unpredictability of the specific,

⁵⁴ Tracey Alloway and Joe Weisenthal, Transcript: CFTC Chair Rostin Behnam on the Fight to Regulate Crypto, A live Odd Lots interview from the ISDA annual meeting, (May 18, 2023), <https://www.bloomberg.com/news/articles/2023-05-18/transcript-cftc-chair-rostin-behnam-on-the-fight-to-regulate-crypto?sref=mQvUqJZj> stating, "Imagine a situation where we have alleged fraud or alleged manipulation of an election and someone coming to the CFTC and say, "You know, you have a contract listed on an election in, you know, X district in Y state, and we believe there was fraud, because of hardware, software, news, you name it." Right? "You need to police that fraud." So without being too indirect, what I'm trying to say is the CFTC could end up being an election cop, and I don't think that's what Congress meant or intended for us to do. And I think that raises for me personally, and I can't speak for the commission or my colleagues, a lot of legal questions and policy questions about whether or not you would want a financial regulator that's very interesting policing elections."

concrete economic consequences of an election (or change in partisan control of Congress) means that the political event contracts cannot reasonably be expected to be used for hedging purposes. The political event contracts' prices could not form the basis for the pricing of a commercial transaction involving a physical commodity, financial asset or service, which demonstrates that the political event contracts have no price-basing utility.

While the contract would pose significant threats to the public interest, as demonstrated above, Kalshi's proposed contracts would not perform any countervailing function that these markets were created for and intended to serve. Specifically, they cannot serve the futures markets' fundamental purpose as a meaningful hedging or price discovery mechanism. The proposal thus poses serious risks without benefits, a lose-lose proposition.

As the Commission itself observed in its previous review of NADEX's political event contracts,⁵⁵ the consequences of political control of Congress are too uncertain to provide a meaningful hedging function, for significant uncertainty still surrounds whether control of Congress will translate into any specific policy outcome or whether and to what extent such policy outcomes would influence commodity-related risks. For example, just because a party running on a tax reform platform gains control of Congress does not mean that this party can and will muster the support to pass their desired specific tax changes, much less whether or not a President would then sign such a law.⁵⁶ This calls into question the efficacy of a political event contract for purposes of hedging against tax risk. The same uncertainty applies to the impact of an election on any policy.

History is littered with innumerable examples of campaign promises, however genuine, being utterly meaningless once a person or party is elected or in control of one or both houses of Congress. As the old saying goes, "too many in this town mistake majority for control." Partisan majorities do not mean control and neither majorities nor control mean that some specific legislative item or agenda has any chance of passing or not, much less becoming law. The proponents of the Self-Certified Contract are ignoring these well-known, longstanding facts. The unsupported and unsupportable claims of a hedging purpose for the Self-Certified Contract are nothing but a smokescreen to get the CFTC to allow gaming and gambling on U.S. elections.

Moreover, the burden is on Kalshi to also specify why and exactly how the alleged hedging benefits of the proposed contract cannot be adequately addressed by existing hedging instruments.

⁵⁵ COMMODITIES FUTURES TRADING COMMISSION, *Order Prohibiting the Listing or Trading of Political Event Contracts* (Apr. 2, 2012) ("[T]he unpredictability of the specific economic consequences of an election means that the Political Event Contracts cannot reasonably be expected to be used for hedging purposes."), <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>.

⁵⁶ See, e.g., Marianna Sotomayor & Leigh Ann Caldwell, *House GOP Tries to Embark on a United Front as Expected Rifts Loom*, THE WASHINGTON POST (Sep. 23, 2022) ("Pleasing the factions will be a difficult job for anyone in leadership unless the possible majority margin is large enough to deter members from advancing their will — a tension often seen this term among Democrats who have only a four-vote margin."), <https://www.washingtonpost.com/politics/2022/09/23/house-gop-tries-embark-united-front-expected-rifts-loom/>.

Kalshi's submission fails to carry this burden. More specifically, Kalshi has failed to demonstrate why existing hedging mechanisms more tailored to the particularized risks a hedger arguably faces — such as a sector-specific fund, for example — are inferior to Kalshi's proposed contract. Ultimately, political risk itself must be disaggregated into other, more specific, concrete risks. And to the extent that any more specific risks flow from the change in control of a congressional chamber, they are more appropriately hedged by instruments other than the Self-Certified Contract.

IV. Legalizing gambling on elections will be a dramatic policy change with potentially grave national implications.

While Kalshi's Self-Certified Contract is nominally limited to the change in partisan control of Congress, it can be anticipated that, if allowed, Kalshi and others would quickly offer similar contracts on all sorts of elections from the local level to the Presidency. Thus, the proposal, if approved or otherwise allowed to go into effect, would almost certainly usher in widespread betting on elections throughout America.

Legalizing gambling on U.S. elections – de facto or otherwise -- would be a dramatic policy change with potentially grave national implications. The consequences of gambling on elections are far-reaching and alarming. Given the use and abuse of social media in the gambling space⁵⁷ and artificial intelligence (AI) in the political space⁵⁸, allowing gambling on U.S. elections will invite if not incentivize more interference, abuse, and misconduct as gamblers seek to effect political outcomes to maximize their winnings. As noted above, when \$100,000,000 bets are allowed and billions of dollars are at stake, this is inevitable. It would also be reasonable to think that with this much money at stake that organized crime syndicates would get involved in what has historically been a lucrative activity for them, i.e., gambling.

Elected officials rely not only on free and fair elections to engender faith in the outcomes of elections, but elections are the foundation of American democracy. Gambling on elections would create very powerful incentives for bad actors, or even those just looking to make a quick buck, to interfere with our elections and try to sway voters outside of the democratic process. For example, it is easy to imagine how AI or social media might be manipulated to quickly circulate false and misleading information within hours or days of an election that could move enough votes to change the election's results.

⁵⁷ Jared Diamond, A Reporter's Tweet Moved NBA Draft Odds. He Also Works for a Gambling Company, (June 24, 2023), https://www.wsj.com/sports/basketball/nba-draft-shams-charania-the-athletic-fanduel-84e9ccc4?mod=hp_featst_pos5

⁵⁸ Tiffany Tsu and Steven Lee Myers, A.I.'s Use in Elections Sets Off a Scramble for Guardrails, Gaps in campaign rules allow politicians to spread images and messaging generated by increasingly powerful artificial intelligence technology, (June 25, 2023), <https://www.nytimes.com/2023/06/25/technology/ai-elections-disinformation-guardrails.html?smid=nytcore-ios-share&referringSource=articleShare>

As Bloomberg News reported on July 12, 2023, “AI is making politics easier, cheaper and more dangerous,” including:

“AI holds the potential to supercharge the dissemination of misinformation in political campaigns. The technology is capable of quickly creating ‘deepfakes,’ fake pictures and videos that some political operatives predict will soon be indistinguishable from real ones, enabling miscreants to literally put words in their opponents’ mouths. Deepfakes have plagued politics for years, but with AI, savvy editing skills are no longer required to create them.”⁵⁹

As a result, deepfake videos are already being deployed to impact voters, as Bloomberg pointed out:

“In March [2023], an anonymous Twitter user posted an altered video that went viral, purporting to show Biden verbally attacking transgender people. Another one, circulate widely by a right-wing US pundit, appeared to show Biden ordering a nuclear attack on Russia and sending troops to Ukraine.”⁶⁰

Allowing gambling on elections will make the dangers of AI and interference in elections much worse, more likely, and gravely consequential. Given the current environment where many Americans already question the integrity of U.S. elections, this would be adding fuel to the fire at the worst possible time.

As betting apps proliferate on mobile phones, widespread gambling on our elections through the simple click of a button is far removed from the purpose, function, and importance of the electoral processes. Such activities undermine the sanctity and democratic value of elections, turning them into speculative spectator sports. Moreover, the prospect of the CFTC assuming the role of an “election cop” raises very serious concerns about the misalignment of that new and unprecedented role with the CFTC’s historic mission and mandate as established by Congress. The CFTC is not designed, intended, set up, or funded to regulate gambling activities.

In short, Kalshi’s proposal would distort the fundamental and historical purposes of the futures markets — namely, to aid hedging and price discovery among commercial enterprises — while ushering in a flood of retail traders to enter a quintessentially speculative market with the prospect of suffering substantial losses.⁶¹ As noted at the outset of this letter, this proposed contract would further contribute to the trend toward the “gamification” and “retailization” of finance. In

⁵⁹ Emily Birnbaum and Laura Davison, AI Is Making Politics Easier, Cheaper and More Dangerous, Voters are already seeing AI-generated campaign materials — and likely don’t know it, (July 11, 2023), <https://www.bloomberg.com/news/features/2023-07-11/chatgpt-ai-boom-makes-political-dirty-tricks-easier-and-cheaper?srnd=premium&sref=mQvUqJZj>

⁶⁰ *Id.*

⁶¹ *See supra* notes 21–22, 50 and accompanying text.

this increasingly common pattern, everyday consumers and investors are lured into new financial products and services, justified by claims that the offerings represent beneficial “democratization” and “innovation.” Yet as we have seen again and again—with the “digital engagement practices” that fueled the meme stock frenzy, and even more so in the market for cryptocurrencies—the result is typically massive wealth accumulation for a few sponsors and issuers and massive losses suffered by the majority of investors.⁶²

The futures markets were not established as a new type of casino but to facilitate the provision of essential goods to Americans by enabling commercial entities to manage the price risk associated with their productive commercial activities.⁶³ There is no credible evidence that Kalshi’s proposed Self-Certified Contract will serve these critical functions, but little question that it will pose serious threats to investors, markets, and our democracy. Given what is at stake, we urge the Commission not to approve Kalshi’s contract.

CONCLUSION

We hope these comments are helpful as the Commission finalizes the proposal.

Sincerely,



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⁶² See generally Dennis M. Kelleher, Jason Grimes, and Andres Chovil, *Securities—Democratizing Equity Markets With And Without Exploitation: Robinhood, Gamestop, Hedge Funds, Gamification, High Frequency Trading, And More*, 44 W. NEW ENG. L. REV. 51 (2022).

⁶³ See generally Christine Hurt, *Regulating Public Morals and Private Markets: Online Securities Trading, Internet Gambling and the Speculation Paradox*, 86 B.U. L. REV. 371 (2006).