SIG
SUSQUEHANNA

July 8, 2024

*VIA Electronic Submission*

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: 17 CFR Part 40 Event Contracts; Comment for Proposed Rule 89 FR 48968

Dear Mr. Kirkpatrick:

Susquehanna International Group, LLP ("SIG")[1] appreciates the opportunity to comment on the Commodity Futures Trading Commission's ("CFTC" or the "Commission") proposed amendments to part 40 of the CFTC's regulations as set forth in the notice of proposed rulemaking dated May 10, 2024 (the "Notice"). In pertinent part, the Notice sets forth several questions that relate to the utility of contracts involving "gaming" and asks whether a blanket prohibition of such contracts is warranted. As a longstanding market maker of exchange traded derivative instruments, we believe that the types of contracts that the Notice now defines as gaming can provide businesses legitimate hedging opportunities and that the public interest would be very much served by allowing for a regulated market to trade them upon. Therefore, for the reasons set forth below, we strongly urge the CFTC to reconsider its position and the proposed ban of all gaming contracts.

As an initial matter, the Notice asks for public comments regarding the CFTC's newly proposed definition of "gaming" as "the staking or risking by any person of something of value upon: (i) the outcome of a contest of others; (ii) the outcome of a game involving skill or chance; (iii) the performance of one or more competitors in one or more contests or games; or (iv) any other occurrence or non-occurrence in connection with one or more contests or games." While we defer to the comments submitted by licensed sportsbooks and legal experts as to what should be considered "gaming," SIG would note that the CFTC's proposed definition appears to be overly broad. SIG's understanding of "gaming"—which the CFTC notes is used "interchangeably" with the terms "gambling," "betting," or "wagering"— has always been that it involves an activity wherein a person takes on financial risk wholly unrelated to any other business activity. As such, if a trader risks something of value upon "the outcome of a contest of others" in the interest of hedging

1 SIG affiliated companies have operated as registered market makers and broker/dealers in the U.S. securities and futures markets for over 30 years and collectively participate in a significant percentage of daily consolidated volume in exchange listed products.

a legitimate business risk, that trade should not be prohibited as a *de facto* "bet" or "wager" under Section 5c(c)(5)(C) of the Commodity Exchange Act or the unrevised CFTC Rule 40.11.

While the Notice concedes that the proposed definition of "gaming" would prohibit some legitimate hedging activity for entities "for whom a particular occurrence in connection with a game or contest have more direct and more predictable outcome," the Notice downplays this inclusion by finding that these contracts generally "cannot [be] reasonably expected to be 'used for hedging and/or price basing on more than an occasional basis.'" SIG respectfully disagrees with this conclusion. For example, contracts that relate to the outcome of a sporting event (*e.g.*, the winner of a National Football League game) could help manage the financial risk and variance inherent to sportsbook operators whose business is inextricably tied to predicting the outcome of certain games or contests. They can (and do) face significant financial risk in their operations if their retail customers heavily favor one side of an event. In that instance, operators are forced to either change the "price" of the event to an undesirable amount to discourage additional participation or to stop accepting wagers on the event entirely. If the CFTC were to allow for a regulated derivative market offering contracts related to the outcome of an event, however, the sportsbook that has reached its risk limit would be able to hedge that risk to the market at an efficient price, balance its books, and continue accepting wagers from retail customers in a regulated environment. As legalized and regulated sports betting continues to grow in the United States, sportsbooks looking for an opportunity to hedge legitimate business risk to a sophisticated counterparty based upon the outcome of a game or contest alone would occur on "more than an occasional basis."

Even setting aside licensed sportsbooks, the Notice concludes that the "broader universe of market participants . . . are most likely to trade such contract for entertainment purposes only[.]" This finding, however, fails to appreciate the economic ecosystem centered around American sports. In addition to sportsbooks, there are myriad local businesses that have a substantial financial interests tied to the outcome of these contests. This includes not just stadium and arena owners that need to anticipate staffing needs in their venues, but also countless hotels, restaurants, and other local businesses that stand to generate a great deal of revenue if their local sports team qualifies to host additional playoff games or has a particularly successful season. Even more ancillary businesses, such as parking lot operators close to stadiums, see uncertain spikes in revenue when attendance to local sporting events increase or for each additional playoff game. Certainly, when a team is having an exciting, winning season, more fans will attend games and thereby frequent local establishments. Unfortunately, there is no traditional financial tool that could allow these businesses to hedge the uncertainty of a team winning a game or playoff series. Unlike a retail customer, entities are almost universally restricted from utilizing a licensed sportsbook to hedge this type of risk. If, however, these contracts were made available on a regulated market, these business owners—like a farmer using a listed future to hedge a crop harvest—could protect against the downswing in revenue if a local team's season were to end unexpectedly early.

The above justification for permitting trading of at least some regulated gaming contracts applies with even greater force to those contracts based upon the outcome of a political contest—which the Notice would now expressly consider "gaming" in proposed CFTC Rule 40.11(b)(2). While SIG has submitted multiple comment letters addressing this exact issue—filed as public comments for Industry Filings 22-002 and 23-01—we would still take this opportunity to reiterate our view that contracts regarding the outcome of political elections serve a vital purpose in allowing investors to hedge against unwanted risk created by elections in a manner closely resembling commonly used financial products.

As previously explained, market participants already adjust their trading strategies in response to electoral outcomes as different governments have substantially different policies. While there is some uncertainty regarding the exact manifestation of specific policies, election contracts allow a market participant—and the market as a whole—to forecast the implications associated with one candidate's agenda and then react to the possible outcome of an election. In this manner, the directional effect of a given government certainly "correlate[s] to direct and quantifiable changes in the price of commodities [and] other financial assets or instruments[.]" For example, one candidate may be more likely than another to impose strict environmental regulations that would raise operational costs and associated prices in certain energy industries. By trading election outcome contracts, businesses could alleviate the risk of increased energy costs by trading a contract with a party more willing to bear that risk.

Moreover, our experience over decades in the financial industry suggests that traditional instruments are insufficient to fully hedge the risks that arise from these fluctuations in government policy. Many products do not have futures markets associated with them. As a result, market participants that face idiosyncratic policy risk are forced to use imperfect exchange-traded products that do not fully reduce their unwanted risk. This void in options leaves many businesses and investors exposed to unmitigated risk. Regulated election contracts, on the other hand, could be used to efficiently hedge business risks in the same manner as other successfully listed hedging products. Just as a financial institution uses listed futures to hedge a portfolio of investment products, another business applying the same general risk management goal could hedge a candidate's prospective tax hike using regulated election contracts.

Lastly, the Notice poses several concerns with respect to election integrity. Specifically, the Notice speculates that permitting trading on these contracts could "raise unique additional public interest concerns relating to election integrity and the perception of election integrity[.]" While many other commentators have weighed in regarding the social significance of these contracts' hedging utility and their resistance to manipulation, SIG would just emphasize that vast amounts of US election-related trading already occur in the status quo and, to date, have not caused any integrity-related concerns. This fact should not only highlight the clear demand that exists for these products but also underscore that bringing this activity to the onshore, regulated, and taxed market could significantly alleviate that concern. Even if the CFTC does not wish to "find itself investigating the outcome of an election," allowing for an onshore trading environment would give those agencies that are "tasked with the protection of election integrity or enforcement of campaign finance laws," such as the Federal Election Commission, more information to do their jobs while also providing market protection for the many that could avail themselves of these hedging tools.

In conclusion, SIG strongly recommends that the CFTC reconsider its position on a prohibition of "gaming" contracts. There are numerous types of contracts that would fall under the CFTC's broad definition that could provide an active, competitive hedging market to the benefit of a multitude of stakeholders. Permitting even some of these contracts—such as those discussed above—would serve as an invaluable financial tool that even institutional investors may use to balance otherwise unchecked risk.

Sincerely,

David Pollard,
Head of Strategic Planning