Public Statements & Remarks

Dissenting Statement of Commissioner Summer K. Mersinger Regarding Proposed Rulemaking on Event Contracts

May 10, 2024

I support the Commission[1] undertaking a rulemaking on event contracts, which is long overdue. During my tenure on the Commission, I have consistently called for a rulemaking process to establish a framework for the Commission to exercise the discretionary authority with respect to event contracts that Congress granted to the agency in our governing statute, the Commodity Exchange Act ("CEA").[2]

Unfortunately, though, I cannot support this particular proposed rulemaking (the "Proposal"). At first blush, it appears to be "much ado about nothing,"[3] as it seems to do little more than rubber-stamp what the Commission has already said and done. Upon closer inspection, though, it is a "wolf in sheep's clothing"[4] because where the Proposal departs from our past practice, it lays the foundation to prohibit entire categories of potential exchange-traded event contracts whose terms and conditions the Commission has never even seen.

In planting the seeds of future bans of countless event contracts, sight unseen, the Proposal—

- Exceeds the legal authority that Congress granted the Commission in the CEA;
- Relies heavily on a brief snippet of legislative history consisting of a colloquy between two Senators – cherry-picking parts of the colloquy it likes, while ignoring other parts of the same colloquy;
- Resurrects an "economic purpose test" for evaluating the public interest that was based on a provision of the CEA that was repealed by Congress nearly a quarter-century ago;
- Fails to do the hard work of analyzing the unique nature of event contracts, which are different in kind from traditional derivatives contracts more familiar to the agency;
- Relies on unsupported conjecture, treats similar circumstances differently, and raises more questions than it answers; and
- Flies in the face of the CFTC's mandate to promote responsible innovation as Congress directed in the CEA.

My dissent should not be taken as an indication that I am a fan of all event contracts. But it is hard not to conclude from the multitude of defects in this Proposal that its significant overreach is motivated more by a seemingly visceral antipathy to event contracts than by reasoned analysis.

It does not matter whether we think event contracts are a good idea or a bad idea; the Commission must exercise its authority with respect to event contracts within the scope of the CFTC's legal authority, and must appropriately implement the authority that Congress has provided us. This Proposal fails both tests.

I. Event Contracts in Brief

CEA Section 5c(c)(5)(C), which was added to the CEA in 2010 by the Dodd-Frank Act,[5] permits the Commission to prohibit an event contract from being listed for trading on an exchange[6] if: 1) the contract involves one of five enumerated activities *(i.e.,* activity that is unlawful under Federal or State law; terrorism; assassination; war; or gaming); and 2) the Commission determines that the contract is contrary to the public interest. CEA Section 5c(c)(5)(C) also provides that the Commission may determine, by rule or regulation, that an event contract involves "other similar activity" to the five enumerated activities, which would subject event contracts involving that similar activity to the "contrary to the public interest" standard.[7]

Congress in CEA Section 5c(c)(5)(C) did not decree that event contracts involving enumerated activities are contrary to the public interest *per se*. Rather, if an event contract involves an enumerated activity, the Commission "may" determine that it is contrary to the public interest and prohibited from trading – which necessarily indicates that the Commission also has the discretion to determine that it is not.

A year after enactment of the Dodd-Frank Act, the Commission adopted CFTC Rule 40.11[8] to implement the CEA's new event contract provisions.[9] It is Rule 40.11 that the Commission is now proposing to amend.

II. The Proposed Definition of "Gaming" is Significantly Overbroad

Neither the CEA nor the Commission's rules define the term "gaming." In the Rule 40.11 Adopting Release implementing CEA Section 5c(c)(5)(C), the Commission acknowledged that "the term 'gaming' requires further clarification," and said that the Commission may issue a future rulemaking concerning event contracts that involve "gaming."[10]

I agree that, 13 years later, it is long past time for the Commission to do so. But, the Proposal's definition of "gaming" is much too broad.

1. The Proposal Sweeps in the Universe of Every "Occurrence or Non-Occurrence in Connection With a Game

The proposed definition of "gaming" includes both the outcome of a game and the performance of one or more competitors in a game. So far, so good.

But it then tacks on an additional category of "any other occurrence or non-occurrence in connection with" a game. The all-encompassing nature of the phrase "any other occurrence or non-occurrence" is self-evident. And that universality is further reinforced by its attachment to the "in connection with" wording.

The motivation for this expansive wording in the Proposal is likely that, where the phrase "in connection with" appears in various enforcement provisions of the CEA, the Commission interprets it "broadly, not technically or restrictively."[11] And the Proposal gives no indication that it should be interpreted any differently here. In fact, the Proposal (at page 29) goes so far as to say that staking or risking something of value on a contingent event "in connection with" a game "would be as much of a wager or a bet on the game . . . as staking or risking something of value on the outcome of the game . . . would be."

Under this incredibly far-reaching formulation, there are countless "occurrence[s] or non-occurrence[s] in connection with" a game that the Proposal would deem to be "gaming." Obvious examples include event contracts involving the attendance at a baseball or football game, or whether a particular nation will be selected to host a soccer World Cup. These would clearly be "in connection with" the underlying baseball, football, or soccer games – but there is no reason why staking something of value on those contingent events should be treated the same as staking something of value on the outcome of those games.

Indeed, there is no better illustration of the overbreadth of the "in connection with" aspect of the proposed "gaming" definition than the Proposal's own example (at page 32) of "whether a particular individual will attend a game." It is difficult to fathom why an event contract involving whether Taylor Swift will attend a Kansas City Chiefs football game should constitute "gaming" – and impossible to understand why the Proposal treats similar things differently, since whether she attends a Beyoncé concert would not constitute "gaming."

I acknowledge that it might be appropriate to extend the definition of "gaming" to include events that can affect the outcome of a game or the performance of a competitor in a game. Event contracts involving, say, whether an injury to Shohei Ohtani would prevent him from playing in the World Series, or involving the score of a football game at halftime, might be examples of this. But to broadly define as "gaming" every "occurrence or non-occurrences in connection with" a game – regardless of whether it has any bearing on the outcome of the game or the performance of a competitor in the game – is wholly unwarranted.

2. Elections and Awards are Not "Gaming"

The Proposal rubber-stamps two prior Commission Orders that found that event contracts involving political control or elections are "gaming,"[12] essentially repeating the same discussion from those Orders – and then throwing awards into its "gaming" definition as well. Yet, this definition is inconsistent with the legislative history of CEA Section 5c(c)(5)(C) – legislative history on which, for other issues discussed below, the Proposal relies heavily.

That legislative history consists of a colloquy between Senators Blanche Lincoln and Dianne Feinstein. Senator Lincoln was then the Chair of the Senate Committee on Agriculture, Nutrition, and Forestry, which is the CFTC's authorizing committee.

In the colloquy, the Senators talked about "gaming" only in the limited context of sporting events. In responding to Senator Feinstein's question about the CFTC's authority under Section 5c(c)(5)(C) to determine that a contract is a "gaming" contract, Senator Lincoln said that "[i]t would be quite easy to construct an 'event contract' around sporting events such as the Super Bowl, the Kentucky Derby, and Masters Golf Tournament."[13] Thus, Senator Lincoln clearly associated "gaming" with sporting events, *i.e.,* games.[14]

But rather than remain true to the legislative history that equated "gaming" with only sporting events, the Proposal broadly sweeps all "contests" into its definition of "gaming." And it then concludes that elections and awards are "contests" and, therefore, "gaming" – even though neither Senator Lincoln nor Senator Feinstein ever mentioned elections or awards (or "contests," for that matter).

The Proposal attempts to squeeze elections and awards into the "gaming" category through the following tortured chain of reasoning:

- Gaming means gambling;
- Some State statutes link gambling to betting or wagering on contests; therefore,
- Contests (including elections and awards) constitute gaming.

Yet, one has to ask: If Congress had intended for elections and awards to be enumerated activities, is it more likely that Section 5c(c)(5)(C) would have:

- Included elections and awards in its list of enumerated activities; or
- Enumerated "gaming" and hoped the Commission would—
    - Define "gaming" to include "contests;" and
    - Consider "contests" to include elections and awards?

Congress easily could have included elections and awards as enumerated activities, but it did not. Confronted with this Congressional silence, I do not believe the Commission can simply decree that elections and awards are enumerated activities. And this is especially the case when Congress in CEA Section 5c(c)(5)(C) provided the Commission with a ready-made process for determining, through a rulemaking proceeding, whether contests, elections, and/or awards are similar to the enumerated activities, including "gaming."

I am baffled at why the Commission is tying itself into knots by trying to reason its way from "gaming" to "gambling" to "contests" to elections and awards, rather than simply do what Congress said it could do: consider whether elections and awards are similar to "gaming" (or another enumerated activity). This is not a matter of form over substance. Approach matters when it comes to exercising our authority under the CEA, and I cannot support the Proposal's approach to stretch the statutory term "gaming" to include elections and awards.

III. The Commission Lacks Legal Authority to Determine in Advance that Entire Categories of Event Contracts are Contrary to the Public Interest

The overbreadth of the Proposal's "gaming" definition would suffice for me to dissent. But the Proposal's most brazen overreach is its determination, in advance, that every event contract that involves an enumerated activity is automatically contrary to the public interest – regardless of the terms and conditions of that contract.

The Proposal would prohibit these contracts – sight unseen – through the shortcut of declaring entire categories of event contracts to be contrary to the public interest. But the Commission lacks legal authority under the CEA to make public interest determinations by category.

The Proposal's justification for its approach (at page 37) is that "the statute does not require this public interest determination to be made on a contract-specific basis." This is backwards. The CFTC is a creature of statute, and has only the authorities granted to it by the CEA. There is no provision in CEA Section 5c(c)(5)(C) for public interest determinations regarding event contracts involving enumerated activities to be made by category. Accordingly, the Commission cannot claim that authority through the *ipse dixit* of "Congress didn't say we couldn't."

This is not a mere question of what procedure to follow. The Proposal would allow the Commission to make the substantive policy determination that entire categories of event contracts, regardless of their terms and conditions, are contrary to the public interest. And the consequences of such a determination are severe – a complete prohibition on exchanges' ability to list event contracts, and on market participants' ability to trade them. If Congress had intended for the Commission to wield this immense authority, surely it would have said so.

In fact, in another CEA provision similar to CEA Section 5c(c)(5)(C) that also was added by the Dodd-Frank Act, Congress did say so. CEA Section 2(h)(2)(A)(i) specifically states that the Commission shall review "each swap, or any group, *category*, type, or class of swaps to make a determination as to whether the swap or group, *category*, type, or class of swaps should be required to be cleared."[15] Thus, when it enacted the Dodd-Frank Act, Congress knew how to tell the Commission that it could make a determination on either an individual or categorical basis when it wanted to do so.[16] In contrast, Congress did not say in CEA Section 5c(c)(5)(C) that the Commission could make public interest determinations for event contracts by category.

The Proposal's premise is that a grant of authority to make a determination about one thing necessarily includes authority to make a determination about a category of such things – *unless* Congress says otherwise. But if that were the case, then there was no need for Congress to tell the Commission in CEA Section 2(h)(2)(A)(i) that it could make mandatory swap clearing determinations either by individual swap or by category.[17] The Proposal's determination would render statutory text in CEA Section 2(h)(2)(A)(i) mere surplusage in violation of established canons of statutory construction.[18] It also would violate the canon of statutory construction that provisions enacted as part of the same statute (here, the Dodd-Frank Act) should be construed in a similar manner.[19]

In the absence of any statutory text in CEA Section 5c(c)(5)(C) like that in CEA Section 2(h)(2)(A)(i), I cannot accept that Congress silently authorized the CFTC to make life easier for itself through the shortcut of making impactful determinations that entire categories of event contracts are contrary to the public interest and thus are prohibited from trading on exchanges.

IV. Even if there is Legal Authority, the Proposal Fails to Justify Making Advance Public Interest Determinations by Category – For a Host of Reasons

Even if the Commission has legal authority to make public interest determinations for event contracts by category, the Proposal is wholly unpersuasive in its attempt to justify doing so. There are a multitude of failings.

1. There is No Basis to Resurrect the Repealed "Economic Purpose Test," Which Shouldn't be Applied to Event Contracts in Any Event

The Proposal would ban entire categories of event contracts as being contrary to the public interest based largely on the proposition that they fail the "economic purpose test." There are four significant problems with this approach.

Congressional Intent: First, the Proposal relies on a single, ambiguous, passage in the legislative history to conclude that Congress intended, for purposes of a public interest review of an event contract, to resurrect the "economic purpose test" that the Commission once used to determine whether a futures contract was contrary to the public interest – until Congress repealed that public interest requirement in 2000.[20]

The Proposal's resurrection of the "economic purposes test" is based entirely on this one passage in the colloquy between Senator Dianne Feinstein and Senator Blanche Lincoln:

> Mrs. Feinstein: . . . Will the CFTC have the power to determine that a contract is a gaming contract if the predominant use of the contract is speculative as opposed to hedging or economic use?
>
> Mrs. Lincoln: That is our intent. The Commission needs the power to, and should, prevent derivatives contracts that are contrary to the public interest because they exist predominantly to enable gambling through supposed event contracts. It would be quite easy to construct an 'event contract' around sporting events such as the Super Bowl, the Kentucky Derby, and Masters Golf Tournament. These types of contracts would not serve any real commercial purpose. Rather, they would be used solely for gambling.[21]

To be clear, the Dodd-Frank Act did not codify the Commission's prior "economic purpose test." And I cannot accept the Proposal's assertion that this isolated colloquy between two Senators establishes an intent by the whole of Congress that the Commission conduct its public interest reviews of event contracts based on an "economic purpose test" that the Commission had withdrawn as a result of the repeal (by the whole of Congress) of the statutory provision it implemented a decade earlier.

After all, neither Senator Feinstein nor Senator Lincoln used the term "economic purpose test" or referred to the Commission's Guideline No. 1 that set out that test. As someone who spent over a decade working in Congress, and who was present on the Senate floor for countless colloquies and even had a hand in preparing talking points for similar floor discussions, I am confident that if the Senators believed we should resurrect the "economic purpose test," they would have said just that.

Difference in Kind: Second, the "economic purpose test" was designed for traditional futures contracts that have been listed and traded on exchanges for decades.[22] These contracts differ in kind from event contracts, which typically are structured as binary (yes/no) options.

The two prongs of the "economic purpose test," which the Proposal adopts as a primary basis for prohibiting entire categories of event contracts as being contrary to the public interest, evaluate: 1) the contract's utility for price basing; and 2) whether the contract can be used for hedging purposes. Yet, the Commission itself has previously recognized the difference between event contracts and the traditional futures contracts for which the "economic purpose test" was developed. In a Concept Release issued in 2008, the Commission stated that "[i]n general, event contracts are neither dependent on, nor do they necessarily relate to, market prices or broad-based measures of economic or commercial activity," and elaborated as follows:

> Since 2005, the Commission's staff has received a substantial number of requests for guidance on the propriety of offering and trading financial agreements that may primarily function as information aggregation vehicles. These event contracts generally take the form of financial agreements linked to eventualities or measures that neither derive from, nor correlate with, market prices or broad economic or commercial measures.[23]

In other words, the Proposal would ban entire categories of event contracts largely on the basis of price basing and hedging requirements that event contracts (described in the Concept Release as "information aggregation vehicles") likely – because of their very structure – have little chance of satisfying.

This problem is compounded by the fact that under the Proposal, some event contracts that fail to satisfy the "economic purpose test" would be banned, while other contracts failing the test would not. For example, the Proposal's statement (at page 52) that "most contracts falling within the proposed definition of 'gaming' would have no underlying cash market with bona fide economic transactions to provide directly correlated price forming information" is equally true of weather-related event contracts – but those contracts would not be banned.

Since the weather is not an enumerated activity, event contracts involving the weather can trade because they are not subject to a public interest review under CEA Section 5c(c)(5)(C). Thus, the Proposal's reliance on the "economic purpose test" means that exchanges can list for trading event contracts (such as those involving weather) that the Commission believes are contrary to the public interest – which I find untenable.

These are the inevitable results of imposing an "economic purpose test" on event contracts that was not designed for event contracts. Certainly, a rulemaking proceeding could be appropriate to fully explore the economic attributes of event contracts, and to consider how to incorporate such attributes into a public interest review that is tailored to the nature of event contracts. But, that is not this Proposal.

Government paternalism: Third, the Proposal asserts (at page 50) that "the economic impact of an occurrence (or non-occurrence) in connection with a contest of others, or a game of skill or chance . . . generally is too diffuse and unpredictable to correlate to direct and quantifiable changes in the price of commodities or other financial assets or instruments, limiting the hedging and price-basing utility of an event contract involving such an occurrence."

But to say that there are limits to the hedging utility of an event contract is simply a statement that the contract may not be a particularly good hedging vehicle. Market participants should be permitted to make their own choices about what financial products meet their hedging needs. It is not the CFTC's role to deny them that choice altogether because we feel a given product's hedging value is "limited."

The "Economic Purpose Test" Was Not Applied to Categories of Contracts: Fourth, even assuming that the "economic purpose test" is an appropriate part of a public interest analysis for event contracts, it does not support making public interest determinations for event contracts by category – because the Commission applied its "economic purpose test" to the terms and conditions of individual contracts. The Commission's Guideline No. 1 provided that *"[i]ndividual contract terms and conditions* must be justified" in order for an exchange to demonstrate that it met the "economic purpose test."[24]

The Commission took no shortcuts in applying its subsequently withdrawn "economic purpose test" to futures contracts. It did not group contracts into categories (such as all futures contracts on wheat, corn, gold, or silver) in evaluating the public interest through its "economic purpose test." Rather, the Commission looked at each contract's "individual contract terms and conditions" to make that determination. If the Proposal is going to (incorrectly) adopt that "economic purpose test" in determining whether an event contract is contrary to the public interest, then it should apply that test the same way.

2. The Proposal's Application of Other Factors Falls Far Short of Justifying its Prohibition Entire Categories of Event Contracts

Aside from the "economic purpose test," the Proposal points to a hodgepodge of other factors to try to justify prohibiting entire categories of event contracts, whose terms and conditions the Commission has never seen, from being traded on exchanges. But its discussion of these factors is conjectural and without evidentiary support, calls into question other contracts that are trading on regulated exchanges, and raises more questions than it answers. Taken as a whole, the Proposal falls far short of justifying the shortcut of prohibiting entire categories of event contracts (even assuming the Commission has the legal authority to do so).

Examples of these defects in the Proposal abound, but I will focus here on just a few:

Hopelessly Impractical: The category of activities illegal under State law demonstrates the type of problems inherent in determining that all event contracts in a category are contrary to the public interest. Some activities are illegal in some States, but not others. Yet, the Proposal does not provide any guidance on several obvious questions: Is an event contract automatically contrary to the public interest if it involves an activity that is illegal in only a single State – and if so, why? Or, if not, then how many States have to declare an activity illegal before the automatic prohibition on event contracts involving that activity is triggered? More than half? States comprising a certain percentage of the country's population?[25]

The problem is exacerbated by the Proposal's suggestion that the prohibition of event contracts can hinge on decisions by judges. Is this reference limited to Supreme Courts of the States? Or would a ruling by a lower court of a State that a particular activity is illegal trigger an automatic determination that an event contract involving that activity is contrary to the public interest? What if that decision is appealed?

While I have focused here on the category of event contracts involving activities illegal under State law, these types of practical questions are a foreseeable and inevitable result of any determination that an entire category of event contracts is contrary to the public interest. I recognize that a contract-specific approach to making public interest determinations regarding event contracts may be difficult and resource-intensive for the CFTC. But aside from my view that a contract-specific approach is required by the CEA, it also is a better approach from a policy perspective precisely because it would permit the CFTC to consider these practical questions in the context of the specific circumstances applicable to a particular event contract. We do not get to override a requirement under the law because it will be hard or require more work for us.

Absolutism Based on Conjecture: Another defect in the Proposal is illustrated by the following (at page 50): "*Generally speaking*, the Commission believes that something of value is staked or risked upon an occurrence (or non-occurrence) in connection with a contest of others, or a game or [sic] skill or chance, for entertainment purposes – in order wager [sic] on the occurrence. As such, the Commission believes that contracts involving such occurrences are *likely* to be traded predominantly 'to enable gambling' and 'used predominantly by speculators or participants not having a commercial or hedging interest' . . ." (Emphasis added; footnote omitted)

These assertions are entirely conjectural, as the Proposal does not cite any support for these statements. One can readily envision an event contract involving whether a particular US city will be awarded the summer or winter Olympic games in a given year, which would be used by hotel and restaurant owners, as well as other businesses, that would make money if their city gets the Olympics but not if the Olympics are awarded elsewhere. Such an event contract would not necessarily be used predominantly for entertainment or speculative purposes.

Indeed, the quoted text itself uses wording like "[g]enerally speaking" and "likely," which is an acknowledgement that its conclusions are not universally true. A belief for which no evidence is cited, and that is acknowledged not to be true across-the-board, cannot justify an absolutist determination that all event contracts involving an activity are automatically contrary to the public interest, nor can it justify a prohibition on trading all event contracts in that category.

Calling into Question Traditional Futures Contracts: I agree that an event contract involving the outcome of a sporting event, and that allows players or coaches to trade that contract, would be contrary to the public interest. But consistent with its overreach, the Proposal also concludes that even where the terms and conditions of such a contract prohibit such persons from trading, the contract is nonetheless contrary to the public interest. The Proposal's stated rationale (at page 51) is that "the athlete or coach would potentially have a platform – for example, access to media, combined with public perception as an authoritative source of information regarding the team – that could be used to disseminate misinformation that could artificially impact the market in the contract for additional financial gain."

The same can be said of many traditional exchange-traded futures contracts. For example, oil companies (or companies in the agricultural or metals sectors, or other energy companies) also have "access to media, combined with public perception as an authoritative source of information regarding" the oil (or other) industry, "that could be used to disseminate misinformation that could artificially impact the market in the contract for additional financial gain." And yet, exchanges are permitted to list oil futures for trading (in fact, oil companies are permitted to trade them).

The Proposal offers no explanation for why a possible incentive to spread misinformation should render all event contracts involving sporting events (or occurrences or non-occurrences in connection with sporting events) contrary to the public interest when traditional futures contracts with the same incentive are not. A contract-specific public interest analysis, by contrast, could take into account the terms and conditions of a particular event contract – such as whether athletes and coaches can trade, or whether there are guardrails against the spread of misinformation – to determine whether the threat of misinformation in that contract is such that it is contrary to the public interest.

Fallacies Concerning the CFTC's Regulatory and Enforcement Roles: The Proposal raises in alarmist tones the red herring that sweeping public interest determinations are necessary so that the CFTC does not get drawn into a regulatory or enforcement role for which it is not well-equipped. For example, the Proposal says (at page 44) that one factor that may be relevant in evaluating whether event contracts are contrary to the public interest is the extent to which they "would draw the Commission into areas outside of its primary regulatory remit."[26] Other examples are: 1) the statements (at page 55) relating to event contracts involving elections that the Commission "is not tasked with the protection of election integrity or enforcement of campaign finance laws;" and 2) the statement (in the first sentence of footnote no. 127) that "the oversight function in this area [regarding elections] is best reserved for other expert bodies."

To be clear: The CFTC does not administer, oversee, or regulate elections, sporting events, gambling, or any other activity or event discussed in the Proposal – and that will not change with respect to any event contract that is found not to be contrary to the public interest. Rather, the CFTC would exercise its exact same authorities under the CEA that it does with respect to all other derivatives contracts.

Nor would the CFTC become some type of "election cop." After all, the CFTC has anti-fraud and anti-manipulation enforcement authority with respect to futures contracts on broad-based security indices, but that does not mean the CFTC regulates the securities markets or that it is tasked with the protection of the integrity of the securities markets or enforcement of securities laws – the Securities and Exchange Commission ("SEC") does all that. The CFTC similarly has enforcement authority with respect to natural gas and electricity since there are futures contracts on those commodities, but that does not mean the CFTC regulates the transmission of natural gas or electricity or that it is tasked with the protection of the integrity of physical natural gas or power markets, or enforcement of the Natural Gas Act or the Federal Power Act – the Federal Energy Regulatory Commission ("FERC") does all that.

The same is true with respect to an event contract that is not contrary to the public interest and thus is permitted to trade on a regulated exchange. As the Supreme Court has stated: "This Court's cases have consistently held that the use of the words 'public interest' in a regulatory statute is not a broad license to promote the general public welfare. Rather, the words take meaning from the purposes of the regulatory legislation."[27] If a particular event contract involving elections were found not to be contrary to the public interest and thus permitted to trade, the CFTC would have absolutely no authority to administer, oversee, or regulate the elections that are the subject of that contract, or to enforce any campaign finance laws. Its authority would extend only so far as is the case with respect to all commodities underlying derivatives contracts within our jurisdiction, as provided by Congress in the CEA.

Why This is Important: I can understand why some might ask: You have been pleading for an event contracts rulemaking for some time now, and here it is – so what is the problem? The problem is this: CFTC Rule 40.11(a)(1) already prohibits the listing and trading of any event contract involving an enumerated activity. As I explained in my Kalshi Dissenting Statement:

> Rule 40.11 contradicts the statute. CEA Section 5c(c)(5)(C) grants the Commission discretion to determine *whether* [an exchange's] event contract that involves an enumerated activity is contrary to the public interest. CFTC Rule 40.11(a), by contrast, provides that [an exchange] "*shall not* list for trading" a contract that involves . . . an enumerated activity (emphasis added). Read literally, Rule 40.11(a) removes entirely the flexibility that Congress granted the Commission to evaluate [exchange] event contracts from a public interest perspective.[28]

Rather than fix this problem, though, the Proposal doubles down on it. By making categorical public interest determinations in advance, the Proposal would impermissibly transform the two-step analysis that Congress provided for event contracts into a single step. It would transmogrify the *discretion* that Congress gave the Commission to determine that an event contract involving an enumerated activity is contrary to the public interest into a *mandate* that it do so.

The Proposal actually is quite candid in acknowledging that it would re-write CEA Section 5c(c)(5)(C). It states (at page 38): "If, as proposed, [Rule 40.11] is amended to include a categorical public interest determination with respect to contracts involving each of the Enumerated Activities, the Commission would not, going forward, undertake a contract-specific public interest analysis as part of a review . . . Rather, the focus of any such review would be to evaluate whether the contract involves an Enumerated Activity, in which case, it may not be listed for trading . . ."

If Congress had intended that every event contract involving an enumerated activity is automatically contrary to the public interest and prohibited from trading, it could have provided for such a single-step process in CEA Section 5c(c)(5)(C). But it did not do that, and instead provided that even if an event contract involves an enumerated activity, the Commission cannot prohibit the contract without exercising its discretion in a second step of determining that the contract is contrary to the public interest. The Commission can't short-circuit the process that Congress established by determining that an event contract is contrary to the public interest – in advance and without knowing the contract's terms and conditions – simply because that makes things easier for the agency.

Granted, the Proposal makes categorical public interest determinations only for the activities enumerated in CEA Section 5c(c)(5)(C). I admit that I am not going to lose sleep over a determination that all event contracts involving terrorism, assassination, and war are contrary to the public interest.

But this is where the "wolf in sheep's clothing" arrives. While this Proposal only addresses event contracts involving enumerated activities, it sets the precedent for how the Commission can handle event contracts involving other activities that it determines are similar to enumerated activities, too.

If the Proposal is adopted as final, then at any time in the future, the Commission could determine that other activities are similar to enumerated activities – and could then determine that every event contract involving that activity is automatically contrary to the public interest (and therefore prohibited from trading) regardless of its particular terms and conditions. And given all the deficiencies in this Proposal's categorical public interest determinations discussed above, that appears to be a low bar to clear.

V. Portions of the Proposal are Inaccurate or Extremely Weak, or Make No Sense

The fact that certain portions of the Proposal are inaccurate, extremely weak, or simply make no sense suggests that it either was hastily prepared, or is motivated primarily by the sheer hatred that the Commission seems to bear towards event contracts. Here are a few examples:

--The Proposal says (at page 44) that "the public good" is a relevant factor for consideration in an evaluation of whether an event contract is contrary to the public interest. It makes no sense that the Commission should consider "the public good" in evaluating whether a contract is contrary to "the public interest." This is tautological – "the public good" and "the public interest" mean the same thing.

--The Proposal's statement (at pages 39-40) that in the colloquy, Senators Feinstein and Lincoln "discussed the Commission's authority, prior to the enactment of the Commodity Futures Modernization Act of 2000 ('CFMA'), 'to prevent trading that is contrary to the public interest" is incorrect. Senators Feinstein and Lincoln did not "discuss" the Commission's pre-CFMA authority. Senator Feinstein referenced it in asking a question, but Senator Lincoln (the Committee Chair) did not talk about it – in fact, she did not even mention the CFMA.

--Footnote no. 49 cites the CFTC Reauthorization Act of 2019 as support for the Proposal's view that an erroneous reference to a non-existent CEA Section 1a(2)(i) in CEA Section 5c(c)(5)(C) was intended by Congress to refer to CEA Section 1a(19)(i) instead, since the bill included a provision to replace the reference to Section 1a(2)(i) with a reference to Section 1a(19)(i). But an amendment in a bill introduced in a subsequent Congress (nine years later) sheds no light on what was intended by the Congress that enacted the statutory provision in question – especially when the referenced bill was not enacted and nothing has happened on it during the ensuing five years.

VI. Certain Implementation Timeline Provisions in the Proposal are Ill-Advised

Implementation Timeline: As discussed above, I do not support the proposal to determine that all event contracts involving enumerated activities are contrary to the public interest. But if the Commission decides to do so, I oppose applying that determination to contracts that are already listed for trading as of the date of publication of final rule amendments in the Federal Register.

It is my hope that there would be few such contracts. But for any contracts that would be impacted, the Proposal is pollyanaish in its rosy view that "a 60-day implementation period for these contracts will minimize any market disruption that might be caused by the rule amendments." For one thing, given the Proposal's repeated emphasis (at pages 29, 33, and 54) that its examples of activities that constitute "gaming" under the proposed definition are non-exclusive, I am dubious that exchanges and traders necessarily will know exactly which existing event contracts the Commission believes are now suddenly prohibited.

Beyond that, this aspect of the Proposal is fundamentally unfair. At any time during the 13 years since its adoption of Rule 40.11, the Commission could have concluded that a given event contract involving an enumerated activity is contrary to the public interest. Exchanges and market participants that have listed and traded an event contract in good faith reliance on the fact that the Commission had not determined the contract to be contrary to the public interest should not pay the price (literally) for the Commission's inaction by having to halt trading in a fixed amount of time because the Commission has finally gotten around to it.

This would be the antithesis of "good government." Accordingly, I do not believe that any rule amendments finalized as part of this rulemaking should apply to an event contract that is listed and available for trading as of the date of their publication in the Federal Register.

VII. Conclusion

Rather than undertake a rulemaking process to do the hard work of building a framework for evaluating event contracts pursuant to CEA Section 5c(c)(5)(C), the Commission squandered the 14 years since that provision was enacted as part of the Dodd-Frank Act. While the Commission is now proposing an event contract rulemaking, that hard work still has yet to be done. Instead, the Commission is skipping right over building a proper framework – and simply proposing to prohibit contracts outright.

This result seems preordained, given the hostility that the Commission has displayed toward event contracts since the enactment of the Dodd-Frank Act. This Proposal rubber-stamps the Commission's two prior Orders finding proposed event contracts to be contrary to the public interest. In addition, it continues the "tradition" of stretching a solitary, cryptic colloquy to form the basis for evaluating whether event contracts are contrary to the public interest through the "economic purpose test" that: 1) is not mentioned in the statute; 2) had previously been withdrawn due to Congress' repeal of the CEA provision it implemented; 3) was not designed for this type of contract; and 4) many event contracts, due to their structure, likely will be unable to meet.

And now the Proposal goes even further, adopting an overly broad definition of "gaming" and declaring entire categories of event contracts to be contrary to the public interest, sight unseen. The Commission's legal authority to make such determinations by category is questionable, at best; that it is inappropriate from a policy perspective cannot reasonably be questioned.

The Proposal flatly contravenes Congress' direction in the CEA that the CFTC "promote responsible innovation."[29] The unmistakable take-away for exchanges is not to expend resources developing an innovative event contract because the Commission will go to great lengths to find that it is contrary to the public interest and prohibit it from trading.[30]

I want to be very clear: My dissent should not be taken as an endorsement of the wisdom of event contracts generally, or of any event contract in particular. Rather, it reflects my application of Congress' direction to the Commission in CEA Section 5c(c)(5)(C). Whatever we may think of event contracts, we cannot re-write the CEA to claim an authority that Congress did not give us because we have been derelict in applying the authority that Congress did give us. Nor should we be prohibiting an event contract without a proper showing that it involves an enumerated activity and is contrary to the public interest based on the application of well-defined factors to the particular terms and conditions of that particular contract.

Because this wolf in sheep's clothing fails on many levels for the foregoing reasons, I respectfully dissent.

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[1] This Statement will refer to the agency as the "Commission" or "CFTC." All web pages cited herein were last visited on May 9, 2024.

[2] *See* Dissenting Statement of Commissioner Summer K. Mersinger Regarding Order on Certified Derivatives Contracts with Respect to Political Control of the U.S. Senate and House of Representatives (September 22, 2023), available at https://www.cftc.gov/PressRoom/SpeechesTestimony/mersingerstatement092223 (https://www.cftc.gov/PressRoom/SpeechesTestimony/mersingerstatement092223) ("Kalshi Dissenting Statement"); and Dissenting Statement of Commissioner Summer K. Mersinger Regarding Commencement of 90-Day Review Regarding Certified Derivatives Contracts with Respect to Political Control of the U.S. Senate and House of Representatives (June 23, 2023), available at https://www.cftc.gov/PressRoom/SpeechesTestimony/mersingerstatement062323 (https://www.cftc.gov/PressRoom/SpeechesTestimony/mersingerstatement062323).

[3] Shakespeare, William, 1564-1616, *Much Ado about Nothing,* London, New York (Penguin, 2005).

[4] Aesop's Fables, *The Wolf in Sheep's Clothing* (1867).

[5] Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law No. 111-203, 124 Stat. 1376 (2010) ("Dodd-Frank Act").

[6] CEA Section 5c(c)(5)(C) applies to event contracts listed for trading by two types of exchanges (designated contract markets ("DCMs") and swap execution facilities ("SEFs")), as well as the clearing of event contracts by derivatives clearing organizations ("DCOs"), all of which must register with, and are regulated by, the CFTC. For convenience, this Statement will refer simply to "exchange trading" of event contracts.

[7] CEA Section 5c(c)(5)(C)(i); 7 U.S.C. § 7a-2(c)(5)(C)(i).

[8] CFTC Rule 40.11, 17 C.F.R. § 40.11.

[9] *See* Provisions Common to Registered Entities, 76 Fed. Reg. 44776 (July 27, 2011) ("Rule 40.11 Adopting Release").

[10] *Id.* at 44785.

[11] *See* Prohibition on the Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation, 76 Fed. Reg. 41398, 41405 (July 14, 2011) (citing the U.S. Supreme Court's decision in *SEC v. Zandford*, 535 U.S. 813 (2002), interpreting the "in connection with" language in SEC Rule 10b-5, 17 C.F.R. § 240.10b-5, as "particularly instructive"; in *Zandford,* the Supreme Court broadly equated the "in connection with" language with the word "coincide" and the phrase "not independent events," *id.* at 820-822).

[12] *See* Order Prohibiting North American Derivatives Exchange's Political Event Derivatives Contracts (April 2, 2012), available at https://www.cftc.gov/PressRoom/PressReleases/6224-12 (https://www.cftc.gov/PressRoom/PressReleases/6224-12); and Order In the Matter of the Certification by KalshiEX LLC of Derivatives Contracts with Respect to Political Control of the United States Senate and United States House of Representatives (September 22, 2023), available at https://www.cftc.gov/PressRoom/PressReleases/8780-23 (https://www.cftc.gov/PressRoom/PressReleases/8780-23).

[13] *See* 156 Cong. Rec. S5906-07 (daily ed. July 15, 2010) (statements of Senator Dianne Feinstein and Senator Blanche Lincoln), available at https://www.congress.gov/111/crec/2010/07/15/CREC-2010-07-15-senate.pdf (https://www.congress.gov/111/crec/2010/07/15/CREC-2010-07-15-senate.pdf) ("Feinstein-Lincoln colloquy").

[14] The Senator's view is consistent with the natural interpretation of the word "gaming" as meaning the staking of money on the outcome of a game. For example, Cambridge Dictionary defines "gaming" in terms of games: "The risking of money in games of chance, especially at a casino; gaming machines/tables." *See* "gaming" definition, CAMBRIDGE DICTIONARY, available at https://dictionary.cambridge.org/us/dictionary/english/gaming (http://www.cftc.gov/exit/index.htm?https://dictionary.cambridge.org/us/dictionary/english/gaming).

[15] CEA Section 2(h)(2)(A)(i), 7 U.S.C. § 2(h)(2)(A)(i) (emphasis added). For convenience, the text will refer only to CEA Section 2(h)(2)(A)(i), although the Dodd-Frank Act also used this same wording explicitly authorizing the Commission to make determinations by category in CEA Sections 2(h)(2)(B)(i), (ii), (iii)(II), and (E); 2(h)(3)(A), (B), (C)(i), (C)(ii), and (D); and 2(h)(4)(B), (B)(iii), (C)(i), and (C)(ii), 7 U.S.C. §§ 2(h)(2)(B)(i), (ii), (iii)(II), and (E); 2(h)(3)(A), (B), (C)(i), (C)(ii), and (D); and 2(h)(4)(B), (B)(iii), (C)(i), and (C)(ii).

Of particular interest is CEA Section 2(h)(4)(B)(iii), 7 U.S.C. § 2(h)(4)(B)(iii), which provides that to the extent the Commission finds that a particular swap or category (or group, type or class) of swaps would be subject to mandatory clearing but no DCO has listed the swap or category (or group, type, or class) of swaps for clearing, the Commission "shall . . . take such actions as the Commission determines to be necessary and *in the public interest*, which may include requiring the retaining of adequate margin or capital by parties to the swap, group, *category*, type, or class of swaps." (Emphasis added) Here, unlike with respect to event contracts, Congress explicitly told the Commission that it could make a public interest determination either individually or by category.

[16] Similarly, in another CEA provision added by the Dodd-Frank Act, Congress told the Commission that it could exempt swaps or other transactions from position limits either individually or by class. *See* CEA Section 4a(7), 7 U.S.C. § 6a(7) ("The Commission . . . may exempt . . . any swap or class of swaps . . . or any transaction or class of transactions from any requirement it may establish . . . with respect to position limits").

[17] Nor can authority to make categorical determinations be found in the CEA's grant of general rulemaking authority in CEA Section 8a(5), 7 U.S.C. § 12a(5), which provides that the Commission may adopt such rules as, "in the judgment of the Commission, are reasonably necessary to effectuate any of the provisions or to accomplish any of the purposes of" the CEA. Again, if that were the case, then there was no need for Congress to tell the Commission in CEA Section 2(h)(2)(A)(i) that it could make mandatory swap clearing determinations either by individual swap or by category, nor was there any need for Congress to tell the Commission in CEA Section 4a(7) that it could exempt swaps or other transactions from position limits requirements either by individual transaction or by class.

[18] *See, e.g.*, *Dep't of Agric. Rural Dev. Rural Hous. Serv. v. Kirtz*, 601 U.S. 42, 53 (2024) (stating proper respect for Congress cautions courts against lightly assuming statutory terms are superfluous or void of significance); *City of Chicago, Illinois v. Fulton*, 592 U.S. 154, 159 (2021) (specifying the canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme).

[19] *See Turkiye Halk Bankasi A.S. v. United States*, 598 U.S. 264, 275 (2023) (The Court has a duty to construe statutes and not isolated provisions, and such construction must occur within the context of the entire statutory scheme.).

[20] Before 2000, CEA Section 5(g) required that futures contracts not be contrary to the public interest. The Commission interpreted this statutory public interest standard to include the "economic purpose test." *See* Request for Comments Respecting Public Interest Test, Guideline on Economic and Public Interest Requirements for Contract Market Designations, 40 Fed. Reg. 25849 (June 19, 1975) ("Guideline No. 1"). In 2000, Congress repealed Section 5(g) of the CEA and its public interest requirement in the Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763 (2000) ("CFMA"). As a result, the Commission withdrew Guideline No. 1.

[21] *See* Feinstein-Lincoln colloquy, n.13, *supra*.

[22] The CFTC's Guideline No. 1, including its "economic purpose test," applied to futures contracts. *See* Guideline No. 1, 40 Fed. Reg. at 25850 ("The Commission is inviting comment . . . to assist the Commission in determining whether the *futures contracts* of [certain exchanges] meet the public interest requirements for contract market designation . . ."), and at 25851 (an exchange "should at this time affirm that *futures transactions* in the commodity for which designation is sought are not, or are not reasonably expected to be, contrary to the public interest") (emphases added). And the Feinstein-Lincoln colloquy makes clear that CEA Section 5c(c)(5)(C) was drafted with futures contracts in mind. Senator Lincoln cited terrorist attacks, war and hijacking as examples of events that "pose a real commercial risk to many businesses in America," but stated that "*a futures contract* that allowed people to hedge that risk [of terrorist attacks, war, and hijacking] . . . would be contrary to the public interest." Feinstein-Lincoln Colloquy, n.13, *supra* (emphasis added).

[23] Concept Release on the Appropriate Regulatory Treatment of Event Contracts, 73 Fed. Reg. 25669, 25669-25670 (May 7, 2008). More specifically, the Concept Release noted that: 1) event contracts based on environmental measures (such as the volatility of precipitation or temperature levels) or environmental events (such as a specific type of storm within an identifiable geographic region) will "not predictably correlate to commodity market prices or other measures of broad economic or commercial activity;" and 2) event contracts based on general measures (such as the number of hours that U.S. residents spend in traffic annually or the vote-share of a particular candidate) "do not quantify the rate, value, or level of any commercial or environmental activity," and that contracts on general events (such as whether a Constitutional amendment will be adopted) "do not reflect the occurrence of any commercial or environmental event." *Id.* at 25671.

[24] Guideline No. 1, 40 Fed. Reg. at 25850 (emphasis added). *See also id.* at 25851 ("The justification of *each contract term or condition* must be supported by appropriate economic data") (emphasis added).

[25] The Proposal justifies its category-based approach regarding activity that is illegal under State law (at pages 48-49) on the grounds that it "eliminates the possibility that the Commission would have to serve . . . as arbiter of a state's own public interest determination . . . in recognizing specific activity as causing, or posing, public harm." But unless the activity is illegal in all 50 States, then in determining that an event contract involving an activity illegal in some States is automatically contrary to the public interest, the Commission is inherently "serv[ing] as arbiter" of the determination by all the other States that the activity does not cause, or pose, public harm.

[26] Since the CFTC has a narrow "regulatory remit" restricted to regulating derivatives markets, this factor presumably could support finding that virtually every event contract is contrary to the public interest.

[27] *NAACP v. Federal Power Commission,* 425 U.S. 662, 669 (1976). The Court went on to explain: "Congress in its earlier labor legislation unmistakably defined the national interest in free collective bargaining. Yet it could hardly be supposed that, in directing the Federal Power Commission to be guided by the 'public interest,' Congress thereby instructed it to take original jurisdiction over the processing of charges of unfair labor practices on the part of its regulatees." *Id.* at 671. Similarly, it could hardly be supposed that, in directing the CFTC to be guided by the "public interest" in evaluating event contracts, Congress thereby instructed it to take original jurisdiction over the regulation or enforcement of laws relating to elections, sporting events, gambling, or any other activity or event.

[28] *See* Kalshi Dissenting Statement, n.2, *supra.*

[29] CEA Section 3(b), 7 U.S.C. § 5(b). The Proposal claims (at pages 7, 17, and 20) that it would help to support responsible market innovation. I do not agree that prohibiting broad categories of innovative event contracts supports responsible market innovation.

[30] In this regard, the Proposal even undermines the CFTC's commitment to its own stated Core Value of being "Forward-Thinking" (*i.e.,* challenging ourselves to stay ahead of the curve). CFTC Core Values, Forward-Thinking, available at https://www.cftc.gov/About/AboutTheCommission (https://www.cftc.gov/About/AboutTheCommission).

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