August 8, 2024

Commodity Futures Trading Commission (CFTC)
Three Lafayette Centre
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Washington, DC 20581

Dear Chairman Behnam and the Honorable Commissioners of the CFTC,

Thank you, Mr. Chairman and Commissioners, for your dedicated service to our country. I appreciate the hard work that goes into your role as regulators. As a former Chairwoman of the Senate Agriculture Committee, and one of the primary authors of the Commodity Exchange Act (CEA) provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank), I write to provide my formal comments on the proposed rule PR 8907-24 , relating to Event Contracts, which was issued by the Commodity Futures Trading Commission (the "CFTC"') on May 10, 2024.

I. Introduction

Our derivatives markets are crucial for the American economy. As you know, they allow businesses and individuals alike to hedge risks, express market views, and discover prices. Without these markets, we'd struggle to effectively and efficiently manage economic risks and remain competitive.

I am deeply troubled by the recent proposal put forth by the CFTC, the federal agency that is tasked with administering the CEA. In prohibiting broad categories of contracts, the CFTC's proposal relies heavily on a 2010 Senate colloquy between me and the late Senator Feinstein for support. But the CFTC proposal goes well beyond what we intended. This heavy-handed proposal to ban markets, rather than regulating them, risks undermining the core principles that underpin our financial markets – principles we strived to uphold through carefully crafted legislation that encourages innovation and provides consumer protections.

Of course, there are instruments that should not be traded on any financial market. Instruments about war, terrorism, and assassination might be inappropriate for the markets. This is precisely why we included rules in the CEA that give the government authority to prohibit contracts about war, terrorism, and assassination. We also believed that our futures markets are not meant for gambling, and so we also gave the government the authority to prohibit gambling contracts about games like the Super Bowl, the Kentucky Derby, and the Masters Tournament. But outside these narrow categories, the law is clear that the CFTC has the responsibility to regulate contracts, not ban them.

Now, however, the CFTC is attempting to prohibit all sorts of financial instruments – from instruments that have any relation to sports, such as attendance and ratings of a championship game, to instruments involving political elections, to contracts about the Nobel Prize. As the CFTC sees it, these are "gaming" contracts, and therefore fall under the prohibition we drafted in 2010.

However, it is my view that this interpretation entirely misses the mark. The law was meant to capture recreational gambling on sporting events and casino-type activities, not the Nobel Prize in Physics or the outcome of major elections. These events are nothing like the Super Bowl, the Kentucky Derby, or the Masters Tournament. If we had intended to include these events, we would have done so explicitly. We did not, because those events – unlike the result of a sports match – have real and significant economic consequences. Prohibiting futures contracts on those events would therefore inhibit the sort of legitimate economic activity that our markets are designed to promote. Further, it would push this existing legal economic activity to unregulated, offshore markets with little to no consumer protections.

By defining "gaming" so broadly, the CFTC's proposed rule casts a dangerous shadow over the entire industry. Speculating has risks, but it is not recreational gambling. Taking a position on a future event with commercial significance, in a commercial manner, is not recreational gambling. Consider a small business owner, for example, who owns a sports bar in a city whose baseball team is doing well. If they hire more staff in anticipation of their team making it far into the playoffs with the accompanying packed nights at the bar, they have not "gambled". Rather, they have made a prudent, speculative, and commercial investment for a real economic purpose. Buying a contract that pays out if their team falls short of the playoffs isn't gambling, either. This is a prudent investment that allows the bar owner to hedge their risk of a potential economic loss if the team's season doesn't go as hoped. Or let's consider someone who is bullish on the prospects of a new technology who invests in companies that are developing that hardware or software. They have not gambled either; they have invested in a speculative position. How about a farmer or a rancher that speculates on the future price of rice, corn, or cattle on the futures markets? They are certainly not gambling. The opportunity to hedge risk should not be limited to the wealthiest individuals and corporations who can access these types of innovative risk management products through large investment banks.

Under the CFTC's proposed rule, sensible, commercial activity would be categorized and prohibited as gambling. That doesn't only blur the lines between gambling and legitimate commercial activity, it obliterates it. The foundational premise of the CFTC's new rule is that it equates all legitimate commercial speculative activity with gambling. The early history of markets was replete with similar accusations that markets were nothing but gambling dens. That accusation has since been disproven by the unparalleled economic growth made possible by our financial markets, and especially by our derivatives markets.

American futures markets are strong and resilient, and they support a strong and resilient economy. The strength and vitality of our markets rest on two fundamental pillars: robust regulation and broad participation. The role of U.S. regulators is absolutely crucial. The FTX collapse clearly illustrates what happens without strong regulator intervention. The CFTC's proposal to prohibit markets is not regulating them; it is a failure to regulate. This is the opposite of what I intended with Dodd-Frank. My intention was to create a robust framework for regulating markets, not ban entire markets. I am proud of what our work on this financial reform legislation accomplished, and I am hopeful the CFTC will reconsider its current proposal on event contracts.

II. Specific points of concern

The CFTC's proposal misinterprets my colloquy on several key points.

a. Definition of Gaming

The CFTC's proposed definition of gaming misinterprets the intent of my 2010 Senate colloquy. The CFTC rule proposes to classify trades as gaming based on the *subject of the trade*. Trades that are on a specific subject -- and the CFTC identifies four subjects --- are classified as gaming, and trades on other subjects are not gaming. That means that the dividing line between gaming and how the CFTC defines the opposite of gaming is simply the subject of the trade.

In the CFTC's proposal, the *only* distinction the CFTC is proposing between gaming and economic trading is what the subject of the trade is. Looking at the trader, the facility, the ecosystem surrounding the trade, is irrelevant. For the CFTC to argue that the only discerning difference between gaming activity and economic trading activity is the subject of the "bet" is contrary to my intent in the statutory provisions of Dodd-Frank, contrary to the experience of the industry, and contrary to my 2010 colloquy. Under the CFTC's proposal, gaming encompasses three topics, none of which are in the statute we drafted and none of which are in my colloquy with Senator Feinstein. Instead, the CFTC proposes to adopt definitions of gambling from unrelated laws. And, at this, the proposal is misguided. The intent of the statute was never to establish "taboo" topics that are gambling. The intent of the statute was to give the CFTC authority to distinguish between gambling for entertainment and economic trading.

The dividing line between recreational gambling and economic trading that occurs on derivatives markets is not the *subject* of the trade; it is the *activity*. The *activity* that we intended to keep out of the futures markets is recreational gambling for entertainment. The gaming that we referred to in the statute describes a recreational activity that is for entertainment. The CFTC's proposal to define gaming simply based on the subject of the trade is contrary to my intent.

You may remember that in our 2010 colloquy, we specifically highlighted the Super Bowl. People gamble on who will win the Super Bowl and the event has enormous economic consequences that can create risk that can be hedged, managed, and transferred. One event – like the Super Bowl – can be the subject of both gambling *and* legitimate economic activity. The difference between the two is that economic trading is not done for recreation and gambling for entertainment is for recreation. The CFTC's proposal to define gaming solely based on the *subject* of the trade abandons the regulatory responsibility to investigate and ascertain the financial utility and purpose of economic trading. It calls the legitimacy of all derivatives markets into question. This was not my intent and is contrary to our colloquy.

In addition to the concerns with the CFTC's overall proposed definition of gaming, the specific definitions it proposes are also questionable. The CFTC's proposal looked to the dictionary definition of gambling, but the proposal ignored the obvious, and intended, definition: to play a game for money. In fact, nearly every definition of "gaming", which is the word we used in the statute, incorporates the idea of 'playing a game.' The gambling that we referred to in our colloquy was clear on this point, and that is why we used the examples like the Super Bowl. The CFTC's incredibly broad proposal, to sweep up events like elections and the Nobel Prize for physics in the definition of gaming, goes way too far. Elections are not games. I think that, now, at this time in history, it is especially apparent that elections are not games.

b. Blanket Prohibitions

The CFTC proposes a blanket prohibition on all contracts that have, as their *subject*, one of the activities we enumerated in the statute, as opposed to contract specific determinations. This is contrary to the plain language of the statute, and most certainly contrary to my intent. The statute is intended to give the CFTC authority to make determinations about specific contracts that are listed, not adopt blanket prohibitions.

One of the hallmarks of the derivatives markets is the presumption that the market, not the government, should be choosing how they hedge their risks, what data to ingest, and what to trade. It is not the government's role to be picking winners and losers in our financial markets.

Our intent with the provisions of Dodd-Frank were to recognize that there may be *instances* where an event contract should not be listed, but these instances are narrow. Only if the CFTC determines that a contract is contrary to the public interest is a specific contract prohibited. That determination must be made on a contract-by-contract basis.

We are living in a time of significant global unrest. Does it make sense that the CFTC can foresee that *every* event contract that related to the subject of war is contrary to the public interest? We did not suggest that every single contract which referenced war would forever be contrary to the public interest. If we did, we would have forbidden those contracts altogether, but that is not how we approached the issue.

Congress said that event contracts on the enumerated activities *may* be contrary to the public interest. The CFTC's proposal to ban entire categories of contracts, and not make a contract-by-contract determination of public interest, is inconsistent with what we intended in the statute.

c. Purpose of the Derivatives Markets

I am particularly concerned by the CFTC's interpretation of the derivatives industry concepts of hedging, price formation, price-basing, and speculating. In justifying its blanket ban over contracts that fit its proposed definition of gaming, the CFTC says that "The Commission believes that the economic impact of an occurrence (or non-occurrence) in connection with a contest of others, or a game of skill or chance—including the outcome of such contest or game—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." The CFTC, therefore, believes that the outcome of an election, for example, does not pose risk to market participants that can be hedged.

This is simply untrue. Elections have enormous economic impacts and pose enormous economic risks to all sorts of parties, from individuals to small businesses to trade associations to large corporations. The reasoning that the CFTC uses to conclude that event contracts will have limited hedging utility and price-basing utility is mistaken.

The derivatives markets are successfully used to hedge by transferring risk. Risk is not limited to changes in the price of some commodity, it is much broader than that. Dodd-Frank itself is a testament to the complexity of the economy, and the *risks of a complex and interconnected global economy*. The CFTC's assumption that elections don't pose direct financial risks is false, and its dismissal of the broader risks associated with elections is wrong too. Risks that market participants face, however diffuse, can be effectively managed by transferring the risk using event contracts.

Additionally, the CFTC ignores one of the historical uses of the derivatives markets. The derivatives markets have historically been utilized as aggregators of market sentiment. Prices form as participants express their opinion on the market, and the data is used by the marketplace as a gauge of market sentiment. Event contracts provide a very useful mechanism for the market to express their opinion on future events. The data that can come from these event contracts, or prediction exchange contracts, can be very valuable. And it is a hallmark of the derivatives industry that market participants can decide what information is useful to them and what is not useful.

Similarly, the CFTC's concern that the information the market would be using to determine its view of a fair price "differs from the informational sources used for pricing the vast majority of commodities underlying Commission-regulated derivatives contracts (e.g., government issued crop forecasts, weather forecasts, federal government economic data, market derived supply and demand metrics for commodities, market-based interest rate curves)" is misplaced. Although the CFTC does not fully articulate what the exact significance of this difference is, the implication is that the price-basing process won't work for event contracts. This underestimates the broad inputs that markets use to price many traditional commodities, such as oil and gold, where participants use broad inputs to determine future market prices and predict future market demand. These inputs are much greater than the price of the spot market commodity. This is certainly true for equity index futures. Most importantly, it ignores the power of American markets and their adeptness at ingesting information. The CFTC's premise –that there is insufficient reliable information to form prices – is unfortunately misguided.

All this reasoning is used in the CFTC's proposal to support the conclusion that contracts it proposes to classify as gaming, such as election contracts, will not be used for hedging or price basing. This is untrue. Elections do pose risks, and individuals and businesses should have a means to hedge that risk. It is not credible to say that data on what the market thinks about the likely outcome of elections is not incredibly economically important. I hope that the CFTC remembers the early days of some of the other products it regulates and the lessons that it learned: markets take time to develop; speculators play an incredibly important role in that development; American markets are very well functioning and – perhaps most importantly - it's the markets that should decide which contracts succeed. The CFTC should let the markets thrive under careful oversight and consumer protections.

III. Conclusion

As our economy becomes ever more complex, the risks that events pose to a broad range of market participants becomes more acute. It is critical to have the ability to manage a wide variety of risks and to aggregate market sentiment. The derivatives markets are ideal for this. The CFTC is the right regulator for the job. The CFTC should embrace the role that Congress has given to it, foster innovation, and keep America's financial markets at the forefront of responsible innovation in a competitive global economy.

Sincerely,

Blanche L Lincoln

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