September 16, 2022

SUBMITTED VIA CFTC PORTAL
Secretary of the Commission
Office of the Secretariat
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Review of KalshiEx LLC's proposed Congressional Control Contracts pursuant to Commodity Futures Trading Commission Regulation 40.11(c).

I'm a founder and angel investor from the Bay Area. SVAngel, my investment firm, has had the privilege of working with several hundred companies over the last 30 years, across dozens of different industries. These partners include firms like Google, Facebook, Coinbase, and Stripe. I'm also an advocate for more government action surrounding gun control, served as Vice Chairman of UCSF Medical Foundation, and have sat on the development committees of institutions like UCLA, Packard Children's Hospital, and the Tiger Woods Foundation, which aims to promote children's health and education.

I appreciate the CFTC requesting the public's input into these contracts so that I and others have the opportunity to weigh in on their value. The CFTC's products underlie the global financial system by providing risk management policies for many different sectors. Consequently, I pay close attention to the space. Kalshi's contracts would meet a demand from the market for both hedging and pricing purposes, and provide an invaluable public service to compete with polling and other forecasts. I strongly encourage the Commission to approve Kalshi's contract for listing by October 28th in time for the midterm elections.

Hedging and price basing (economic) utility

Kalshi's contract would provide meaningful risk mitigation for small businesses and households. In my experience as an investor and advisor to so many companies and small, growing businesses, I've seen first hand people struggling with these risks. The product proposed by Kalshi would go a long way towards managing these risks.

More specifically, the CFTC has solicited public comment regarding whether the outcomes of elections are "predictable" in order to serve as effective hedging tools. They are. The evidence is extensive and hard to ignore.

This is not a secret. Investment banks hire whole divisions to estimate the impact elections will have on their clients. This data is also published publicly on occasion, or discussed by the financial press (Slate: "Wall Street Says You Should Short Mexico to Prepare for Trump").[1] While some headlines refer to presidential outcomes, plenty detail very specific Congressional outcomes, like when, in 2020, Bank of America provided roadmaps for each type of partisan outcome (one party controls all of government, divided government, et cetera). There, they wrote that full Democratic control of government would lead to $2-2.5 trillion in stimulus compared to a Biden win with a divided Congress ($0.5-1 trillion) or a Trump win with a divided Congress ($1.5-2 trillion). They also detailed impacts to specific sectors, like businesses exposed to Chinese trade, in each scenario.[2]

Academics consistently discuss the link between changes in partisan control of Congress, and changes in polling, with consistent effects on financial markets, suggesting significant hedging and repricing by the market to manage risks arising from upcoming shifts in control of Congress.

CEOs also frequently flag electoral risk as it relates to their bottom line in earnings calls. According to Factset, more than a third of earnings calls in Q3 2020 mentioned the word "election".[3] I encourage Commissioners and staff to see these discussions. Concerns about a particular Congressional outcome are particularly relevant for energy, health care, and financial firms. Comments by several businesses and individuals have also testified to the importance of hedging elections in their lives and businesses.

If the market is engaging in significant extant hedging activity, then it is not deniable that an election event contract contains significant hedging utility and it is reasonably likely that the contract will be used for hedging. The hedging use of this contract is so obvious that it would satisfy even the CFTC's proposed test of "market demand exists."

I also note that concerns along the lines of whether elected officials actually successfully implement their goals and policies are incorrect. As discussed above, markets and businesses react to risks of political control, so clearly political control risks have impacts, and these risks can be managed. Further, this is not different from many other existing CFTC products. Basis risk is normal in many derivative products, like hurricane or housing price index futures. There's no guarantee that a drop in the Case-Shiller housing price index (whose futures are listed on the Chicago Mercantile Exchange) will actually reduce asset value or cash flows for an investor or homeowner. Nonetheless, the CFTC permitted these valuable market innovations to be listed.

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[1] Banks suggest shorting peso to hedge against a Trump win. (slate.com)
[2] Bérengère Sim. 2020. "Bank of America wrote a massive 92-page report on election's impact — here's what investors need to know." Financial News.
[3] More Than One Third of S&P 500 Companies Are Discussing the Election on Q3 Earnings Calls (factset.com)

I also note that a commenter saying "I could not or would not use this contract to hedge" should have little consequence. There is certainly no requirement that everyone be able to use the contract to hedge, only that it can reasonably be used for hedging. All of the comments demonstrating how the contract can be used for hedging directly address the question and demonstrate that the contract can and will be used for hedging.

Question seven asks whether the risks that elections portend can be hedged using other products. I am not aware of another circumstance where this logic was used to potentially deny a product with legitimate hedging purposes. Though I can imagine many such instances (such as hedging the risk of government benefits being taken away), the contract itself would still be valuable to isolate risk (rather than be subject to the risks of other assets) and produce significant price basing benefits uniquely.

Public interest

In addition to furthering the public interest by introducing an important hedging tool, the markets will further the public interest by providing an important data point that will help researchers and policy makers. PredictIt has been cited by many prominent scholars and government officials. Its markets are frequently referred to by the political media and leading thinkers to get a non-partisan view of the likelihood of an election's outcome. Examples include its markets being consistently referenced as informative and useful by major, credible news organizations like CNN, CNBC, Politico, Bloomberg, The Economist, The Wall Street Journal, The Washington Post, and The New York Times, across sections like *The Upshot*, *DealBook*, opinion columns, and the technology section.[4][5][6][7] In addition, it has repeatedly been cited by prominent political officials and thinkers. Examples include economists like Jason Furman, previously President Obama's Council of Economic Advisors; Nobel Laureate Paul Krguman, a Professor at The Graduate Center and a columnist for *The New York Times*; and data scientists/reporters like Nate Silver, founder and editor-in-chief of *FiveThirtyEight*.[8][9][10] The fact that PredictIt has such power in the political press, despite its position and trader limits, is indicative of the incredible interest and social value in providing event contracts on elections to the public.

Academic researchers have used PredictIt's data (a good in and of itself), finding that it has a variety of public issues. Hundreds of papers on economics, finance, and political science use PredictIt's data to study prediction markets and their connection to political outcomes and traditional asset and currency markets. Examples include:

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[4] La Monica. "Joe Biden's Fed conundrum: Stick with Jerome Powell or let him go?" 2021. CNN Business.
[5] Heath. "These gamblers are putting money on the outcome of the impeachment inquiry." 2019. Washington Post.
[6] Contrera. "Here's how to legally gamble on the 2016 race." 2016. Washington Post.
[7] https://www.nytimes.com/search?query=PredictIt
[8] https://twitter.com/NateSilver538/status/1242845027014971394
[9] https://twitter.com/jasonfurman/status/1460404350975680514
[10] https://twitter.com/paulkrugman/status/1177602108763316227?lang=en

- Berg and Chambers (2016) found that using prediction markets, including PredictIt, increased user interest in civics and user news consumption.[11]
- Miller (2021) found that PredictIt is better at election forecasting than traditional methods of forecasting.[12]
- French (2020) created an election prediction model using PredictIt that outperforms many traditional methods of forecasting.[13]

Finally, the CFTC asked if this situation is any different than in 2012, when it previously ruled on similar contracts. Event contracts were extremely limited in practice in 2012. In 2008, when it sought public comment on event contract regulation, the Commission acknowledged its extremely limited experience with event contracts. In fact, it admitted its only experience was with Iowa Electronic Markets, for which it had given two no-action letters in the 1990s. Between then and the Nadex order, the only event contracts that were certified with the Commission were a small number of economic indicators from Nadex itself and motion picture box office contracts, which were swiftly banned by Congress. That being said, the concept of election event contracts was so natural to the Commission such that even at that time, the Commission used the example of a presidential election binary to explain event contracts to the public![14] Event contracts were so limited in 2012 that regulation 40.11–which was the justification for rejecting Nadex's contracts–was only published the day before the Nadex order. Kalshi's proposal provides a prime opportunity for the Commission to make a decision more in line with the public's interest and law.

Innovation

The fact that these contracts are innovative is not a reason to prohibit the contract. Many innovative products have become staples of the markets and have encouraged significant economic growth. In the past, for example, basic agricultural futures and index-settled products were once considered to be devoid of hedging utility and be pure gaming products. Today, those products are cornerstones of the global financial system. It is critical for government agencies to rely on evidence and testimony from potential hedgers and others rather than speculation or knee-jerk skepticism to novel products like Kalshi's. This means considering their testimony, looking at the experiences of other nations, and the large value that election markets have had for academics and the public.

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[11] Berg & Chambers. *Bet Out the Vote: Prediction Markets as a Tool to Promote Undergraduate Political Engagement*. 2018. Journal of Political Science Education.
[12] Miller. *Predicting the 2020 Presidential Election*. 2020. Data Science Quarterly.
[13] Franch. *Political preferences nowcasting with factor analysis and internet data: The 2012 and 2016 US presidential elections*. 2021. Technological Forecasting and Social Change.
[14] Federal Register :: Concept Release on the Appropriate Regulatory Treatment of Event Contracts

As discussed above, Kalshi’s contract submission does already have significant market hedging activity. However, I’m concerned that it could stifle innovation to require this of proposals, especially as outlined in questions eight and nine. Question eight specifically requests whether the Commission should consider requiring applicants to provide ‘demonstrated need’ of hedging and then asking if some percent of market participants must be legitimately hedging. Both of these standards would be very damaging towards responsible innovators. A ‘demonstrated need’ standard could make it more difficult for participants to bring products to market that potentially disrupt and compete with existing products, or which serve a niche that has yet to, but will, be filled. In addition, there is no way for a registrant to prove in advance of listing (nor does there exist a mechanism by which the Commission could reasonably guess) what percent of its participants would be hedging as opposed to speculating. It seems perverse to prevent would-be hedgers from using a product that would benefit them on the basis that too many others would use it for speculation. It would be disappointing to see these novel standards applied to Kalshi’s contract as precedent for future submissions.

Question nine then goes on to ask whether and how the Commission should consider the contract’s availability towards retail investors should affect their analysis. The Commission should not punish the contract for being more accessible, not less, to investors. Although retail investors are smaller, they are affected just as much by macro-political level events as large businesses. Retail investors can hedge all the same, and are no more likely to engage in speculation as large-dollar institutions (many of whom specialize in such behavior).

Kalshi’s contract is a potentially powerful tool for the market. I look forward to the Commission's decision.