By Electronic Submission

October 28, 2024

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

Re: KalshiEx, LLC's Rule Certification Submission No. 2409-1100-4224-55

Dear Mr. Kirkpatrick:

Better Markets[1] appreciates the opportunity to comment[2] on the Commodity Futures Trading Commission's (the "CFTC" or "Commission") review of KalshiEX, LLC's Submission No. 2409-1100-4224-55 (the "Submission")[3] pursuant to CFTC Regulation 40.6(c)(2).[4] Kalshi's Submission raises serious concerns about the potential erosion of market transparency, facilitation of pre-arranged trades, and risk of creating unfair trading environments—issues that pose significant threats to market integrity and fair competition. We respectfully urge the Commission to reject Kalshi's Submission. The introduction of opaque, RFQ-based trading channels and facilitation of private negotiations would set a dangerous precedent, undermining transparency and market integrity. Approving this Submission risks compromising the CFTC's commitment to protecting the public interest and could transform the DCM landscape into an environment that

---

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

2 *CFTC Requests Public Comment on a Rule Certification Filing by KalshiEX LLC* (September 26, 2024), https://www.cftc.gov/PressRoom/PressReleases/8983-24.

3 KalshiEx, LLC's Rule Certification Submission No. 2409-1100-4224-55 (September 11, 2024), *available at* https://www.cftc.gov/filings/orgrules/rules0911245779.pdf.

4 17 CFR § 40.6(c)(2).

privileges a few at the expense of many. To maintain a fair, competitive, and transparent market, it is imperative that the Commission upholds regulatory standards and rejects Kalshi's proposal.

COMMENTS

I. Kalshi's Submission is inconsistent with Designated Contract Market Core Principle 9, which governs market transparency and price discovery.

Kalshi's proposed introduction of a Request for Quote (RFQ) functionality in the Submission raises serious concerns regarding compliance with Designated Contract Market (DCM) Core Principle 9,[5] which mandates that DCMs maintain a competitive, open, and efficient trading mechanism that supports and protects the price discovery process.

The RFQ system proposed by Kalshi would allow market participants seeking to initiate a trade (Requesters) to privately communicate with one or more potential counterparties (Quoters) by providing quotes in response to the Requester's inquiry.[6] These bilateral, pre-execution communications occur outside of the public view, preventing other market participants from accessing critical pre-trade information.

The CFTC hosted a roundtable in 2012, during which participants emphasized balancing flexibility and transparency to support market liquidity and innovation.[7] Pre-execution transparency, however, fosters greater price competition, increases liquidity, and creates more efficient markets.[8] Kalshi's RFQ system, by facilitating private negotiations between Requesters and Quoters, compromises this transparency, impeding the competitive and open price discovery process essential for market integrity. Without transparency, the market's ability to function efficiently and fairly is fundamentally weakened, reducing confidence in its fairness.[9]

A. Violations of Market Transparency Requirements

---

5 7 U.S.C. 7(d)(9).

6 KalshiEx, LLC's Rule Certification Submission No. 2409-1100-4224-55 (September 11, 2024), *available at* https://www.cftc.gov/filings/orgrules/rules0911245779.pdf

7 CFTC Staff to Host a Public Roundtable to Discuss Proposed Regulations Implementing Core Principle 9 for Designated Contract Markets (June 5, 2012), *available at* https://www.cftc.gov/PressRoom/Events/opaevent_cftcstaff060512.

8 Mattmann, Brian, *The Benefits of Pre-Trade Transparency: A Cross-Market Comparison Between the U.S. and Swiss Corporate Bond Markets* (May 2023). *available at* http://dx.doi.org/10.2139/ssrn.4437804.

9 Investopedia, *Market Efficiency Explained: Differing Opinions and Examples* (April, 2, 2022), *available at* https://www.investopedia.com/terms/m/marketefficiency.asp.

The CFTC's letter dated September 24, 2024,[10] identified Kalshi's Submission as "novel and complex" and flagged it as potentially inconsistent with § 38.500 of the Commission's regulations,[11] which codified DCM Core Principle 9 requiring that DCMs provide mechanisms for transparent and competitive trading. By permitting private communications invisible to the broader market, Kalshi's proposed RFQ system prevents other participants from contributing to or benefiting from the price discovery process.

The lack of public visibility into RFQ communications contradicts CFTC regulation § 38.500, which mandates that DCMs ensure transparent systems that allow all participants equal access to price-related information, fostering fair competition. Kalshi's proposed RFQ system bypasses this by allowing private, pre-execution negotiations, preventing price discovery from occurring in a fully open and public manner. This closed-loop system creates an information asymmetry, where only a select few participants have access to quote data, allowing them to make more informed trading decisions while other market participants are left in the dark. This selective access not only distorts competitive balance but also undermines the market's ability to function efficiently and fairly, as all participants must have access to the same information for a truly competitive and transparent trading environment.

B. Erosion of Price Discovery and Liquidity Fragmentation

Price discovery is the process through which markets aggregate and reflect the collective judgment of participants regarding the value or outcome of an event or contract. In the context of event contracts, where outcomes are tied to specific events rather than traditional financial instruments, a transparent and open market is essential to ensure that prices reflect the true market sentiment and expectations about those events.

Kalshi's Submission fragments this process by enabling Requesters to privately negotiate with Quoters, bypassing the centralized order book, which is designed to collect and disseminate price information to all participants. By facilitating these private negotiations, the RFQ functionality isolates price information, depriving the broader market of the opportunity to aggregate and reflect this information in a public forum. This is particularly harmful in event contracts, where access to accurate information about expected outcomes is critical for all participants to form a competitive and transparent price.

Without full transparency, market prices may no longer reflect the true consensus of event outcomes, leading to inefficiencies in assessing probabilities and potential impacts of these events. As liquidity is drawn into these private negotiations, the liquidity available in the centralized market is diminished, further weakening the market's ability to function effectively. This fragmentation of liquidity not only harms price discovery in event contracts but also disadvantages participants who are excluded from these private negotiations, leading to an uneven playing field.

---

[10] CFTC's Letter to Kalshi, *Notification of Stay: Kalshi Submission No. 2409-1100-4224-55* (September 24, 2011), *available at* https://www.cftc.gov/sites/default/files/filings/documents/2024/orgdcmkexkalshiexsta240925.pdf

[11] 17 CFR § 38.500.

As liquidity becomes increasingly concentrated in private negotiations, participants in the centralized market may face wider bid-ask spreads and higher transaction costs, further exacerbating inefficiencies. The resulting fragmentation undermines the accuracy and robustness of the event contract market, ultimately increasing costs for all participants and creating less efficient and more costly trading conditions.

C. Undermining Confidence in Market Integrity

A core function of any DCM is to maintain public confidence in the integrity of its markets.[12] Event contract markets, in particular, thrive on transparency, fairness, and open competition, all of which are essential to the price discovery process and the accurate reflection of market sentiment regarding specific events. The introduction of opaque trading channels, such as Kalshi's RFQ system, undermines these values by creating an environment where certain participants can benefit from exclusive access to price information.

When some participants negotiate privately while others are excluded, it fosters a perception of unfairness, which erodes confidence in the market. In event contract markets, where participants rely on transparent access to event-related data for informed decision-making, this perception of unfairness is even more damaging. Over time, reduced confidence leads to decreased participation by traders who feel disadvantaged, further fragmenting liquidity and harming market efficiency.

As fewer participants engage in the centralized market, the overall competitiveness and robustness of the event contract market diminishes. Reduced participation weakens liquidity and amplifies inefficiencies in price discovery, leaving the market vulnerable to wider bid-ask spreads and higher transaction costs. This lack of transparency also increases the risk of market manipulation, as participants with exclusive access to information may exploit their advantage at the expense of others.

In the long term, allowing opaque systems to operate diminishes trust in the market's fairness, ultimately harming the health and sustainability of the event contract marketplace. A market perceived as favoring select participants will struggle to maintain liquidity, reduce volatility, and attract new traders, compromising its long-term integrity.

II. Kalshi's Submission facilitates pre-arranged trades and abusive practices by allowing participants to negotiate trades privately without sufficient oversight, creating market manipulation and regulatory evasion opportunities.

The Commission's letter highlights concerns related to DCM Core Principles 2 and 12,[13] which require DCMs to implement robust measures to prohibit pre-arranged trades and other abusive trading practices. Kalshi's RFQ functionality, which allows private pre-execution communications, introduces significant risks of facilitating pre-arranged trades under the guise of

---

12 Core Principles and Other Requirements for Designated Contract Markets, 77 Fed. Reg. 36612 (June 19, 2012), available at https://www.govinfo.gov/content/pkg/FR-2012-06-19/pdf/2012-12746.pdf

13 7 U.S.C. 7(d)(2) and 7 U.S.C. 7(d)(12).

anonymity and bilateral negotiation. The RFQ system, as described in the Submission, fundamentally conflicts with **CFTC regulations §§ 38.150(a)(3), 38.152, 38.650, and 38.651**, which explicitly require DCMs to implement measures to prohibit abusive trading practices such as pre-arranged trades.[14]

While the Submission provides that the RFQ system operates within regulatory parameters,[15] the nature of pre-execution communications inherently encourages behavior that § 38.152[16] of the Commission's regulations seeks to prevent. Specifically, the possibility of conducting private negotiations without real-time market scrutiny significantly increases the risk of regulatory evasion. Such opaque trading environments could enable market participants to engage in pre-arranged trades that undermine competitive market conditions, harming other participants and compromising market integrity.

A. Potential for Regulatory Arbitrage and Market Manipulation

If the Commission approves this Submission, it would establish a deeply troubling precedent, paving the way for other DCMs to introduce opaque trading mechanisms under the guise of so-called 'innovation.' This would open the door to regulatory arbitrage, where DCMs prioritize the convenience of a select few traders over the integrity of the marketplace.

Moreover, Kalshi's RFQ system is a perfect recipe for market manipulation, allowing privileged participants to exploit selective access to quote information and private negotiations while sidelining genuine market participants. These risks fly in the face of the Core Principles, which demand transparent markets free from manipulation. Approving this Submission would make it easier for certain participants to engage in quote manipulation or other abusive practices, further distorting the market for everyone else. The Commission's duty is to protect the market's integrity and the public, not to rubber-stamp mechanisms that could turn the marketplace into a playground for insiders at the expense of fairness, transparency, and competition.

B. Governance and Surveillance Concerns

Kalshi's Submission raises additional concerns about whether adequate governance measures are in place to monitor and prevent misconduct in the RFQ process. Given the private nature of pre-execution communications, it remains unclear whether Kalshi has implemented sufficient oversight to monitor these exchanges in real-time.

The lack of transparency for other market participants, combined with the increased risk of pre-arranged trades, creates an environment highly vulnerable to manipulative behavior. Without appropriate oversight and surveillance, the RFQ system creates a perception of unfairness and favoritism, which can erode public confidence and ultimately harm the market's health.

---

14 17 CFR § 38.150(a)(3), 17 CFR § 38.152, 17 CFR § 38.650, and 17 CFR § 38.651, respectively.

15 KalshiEx, LLC's Rule Certification Submission No. 2409-1100-4224-55 (September 11, 2024), *available at* https://www.cftc.gov/filings/orgrules/rules0911245779.pdf.

16 17 CFR § 38.152.

C. Concerns Regarding the Quote Acceptance Process

The proposal also introduces a feature where, if the Quoter does not confirm a quote within 30 seconds, the RFQ is treated as void.[17] While this time limit may seem reasonable, it could allow market participants to exploit this feature by selectively allowing quotes to expire when conditions change unfavorably.

This introduces a risk of market manipulation, where participants can withdraw from commitments with little to no consequence, which undermines the reliability and efficiency of the market.

CONCLUSION

We hope these comments are helpful.

Sincerely,

Cantrell Dumas
Director of Derivatives Policy

Better Markets, Inc.
2000 Pennsylvania Avenue, NW
Suite 4008
Washington, DC 20008

cdumas@bettermarkets.org
http://www.bettermarkets.org

17 KalshiEx, LLC's Rule Certification Submission No. 2409-1100-4224-55 (September 11, 2024), *available at* https://www.cftc.gov/filings/orgrules/rules0911245779.pdf.