

Regulation of Event Contracts Markets

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I. Introduction

An event contract is a derivative that yields payment based on the result of an event, occurrence, or value. The Commodity Futures Trading Commission (“CFTC” or “Commission”) has stated that 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.”² An event contract market is a forum for trading such contracts.

A significant number of event markets are structured as “binary option” contracts, which pay out a fixed amount based upon the occurrence or non-occurrence of a particular specified event.³ In a 2008 Concept Release, discussed further *infra*, the CFTC identified three broad categories of event contracts: (1) contracts based on narrow commercial measures and events; (2) contracts based on certain environmental measures and events; and (3) contracts based upon general measures and events.⁴ The CFTC’s experience to date with event contract markets was with the Iowa Electronic Markets which had been operated by the University of Iowa since it received no action relief in 1992 to operate an event contract market for academic purposes relating to political events, as well as submarkets relating to corporate earnings and economic indicators.⁵ In 1999, the Chicago Mercantile Exchange (“CME”) began listing derivatives about weather events. ⁶ Notably, the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”) prohibited the listing of contracts relating to movie box office sales.⁷

II. CFTC Jurisdiction

A. Commodity Exchange Act & Commodity Futures Modernization Act of 2000

The Commodity Exchange Act (“CEA”) grants exclusive jurisdiction to the CFTC over commodity futures and options.⁸ The Commodity Futures Modernization Act of 2000 (“CFMA”) amended the CEA, including by adding that off-exchange trading in “excluded commodities”

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² Concept Release on the Appropriate Regulatory Treatment of Event Contracts, 73 Fed. Reg. 25669, 25670 (May 7, 2008).

³ *Id.*

⁴ *See id.*

⁵ CFTC Staff Letter, CFTCLTR No. 93-66 [1992-1994 Transfer Binder] Comm. Fut. L. Rep. CCH ¶ 25.785 (June 18, 1993).

⁶ *See Weather Products*, CME GROUP, <https://www.cmegroup.com/trading/weather/> (last visited Mar. 25, 2023)

⁷ 7 U.S.C. § 13-1 (2010).

⁸ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No 111-203, 124 Stat. 1735 § 745(5)(C) (codified at 7 U.S.C. § 2(a)(1)(A)).

between certain “eligible contract participants” are generally not subject to the CEA.⁹ The CFMA defined “excluded commodity” as: (A) an interest rate, exchange rate, currency, security, security index, credit risk or measure, debt or equity instrument, or index or measure of inflation; (B) any other rate, differential, index, or measure of economic or commercial risk, return or value that (i) is not within the control of any party to the relevant contract, agreement, or transaction; or (ii) is not based in substantial part on the value of a limited number of commodities not described in (A) that have a finite supply; or (C) an occurrence, extent of an occurrence, or contingency, beyond the control of the parties to the relevant contract, agreement, or transaction.¹⁰

The CFMA also amended the CEA by deleting Section 5(g), which provided that the CFTC “could not designate a board of trade as a contract market unless the board of trade affirmatively and pro-actively demonstrated that transactions in their contracts ‘will not be contrary to the public interest.’”¹¹ In a 2008 Concept Release, discussed further *infra*, the CFTC stated the public interest test under former Section 5(g) included an “economic purpose” test, under which exchanges were required to show that a proposed contract could be used for hedging, price basing, or both.¹² The CFMA implemented in the place of any express “public interest” or “economic purpose” requirement, the Core Principles that DCMs are required to abide by.¹³

B. 2008 Concept Release

On May 1, 2008, the CFTC’s Division of Market Oversight (“DMO” or the “Division”) issued a Concept Release entitled *Concept Release on the Appropriate Regulatory Treatment of Event Contracts*,¹⁴ in response to requests for clarification of the scope of the part of definition of excluded commodity including “an occurrence, extent of an occurrence, or contingency, beyond the control of the parties to the relevant contract, agreement, or transaction.” The Concept Release requested public comment on a number of questions related to the regulation of event contracts, including: what public interests are served by event contracts traded for information aggregation purposes and how those interests are consistent with the public interest goals of the CEA; what calculations, analyses, variables, and factors could be used to determine the social value of information that may be discovered through event contracts trading and whether this should factor into determining whether the CFTC regulates the markets; if event contracts are within the CFTC’s jurisdiction; whether there should be exemptions or exclusions applied to event contracts, if they are within CFTC jurisdiction; how the CFTC should address the potential gaming aspects of some event contracts and possible preemption of state gaming laws; and various questions related to

⁹ Commodity Futures Modernization Act, Pub. L. No. 106-554 § 103(d)(1) (2000).

¹⁰ Commodity Futures Modernization Act, Pub. L. No. 106-554, 114 Stat. 2763A-371 § 101(13) (2000).

¹¹ H.R. Rep. No. 975, 93 Cong. (1974); Concept Release on the Appropriate Regulatory Treatment of Event Contracts, 73 Fed. Reg. 25669, 25672 (May 7, 2008). For additional analysis, *see* Katherine Cooper, The History of the Economic Purpose and Public Interest Tests, ABA Derivatives & Futures Law Committee 2023 Winter Meeting: Innovative New Products Panel (Jan. 6, 2022).

¹² *See* Concept Release on the Appropriate Regulatory Treatment of Event Contracts, 73 Fed. Reg. 25669, 25672 (May 7, 2008); *see also* Statement of Commissioner Brian D. Quintenz on ErisX RSBIX NFL Contracts and Certain Event Contracts, CFTC (Mar. 25, 2021), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/quintenzstatement032521>.

¹³ *See* 7 U.S.C. § 7. *See* Katherine Cooper, The History of the Economic Purpose and Public Interest Tests, ABA Derivatives & Futures Law Committee 2023 Winter Meeting: Innovative New Products Panel (Jan. 6, 2022).

¹⁴ Concept Release on the Appropriate Regulatory Treatment of Event Contracts, 73 Fed. Reg. 25669 (May 7, 2008).

implementation of a regulatory scheme for event contracts. Thirty-two comment letters were filed in response to the questions presented in the Concept Release, including comments from the Board of Directors for Iowa Electronic Markets, Intrade the Prediction Market Limited, the Coalition for Internal Markets, and the Centre for Financial Market Integrity.¹⁵ The general tone of the comment letters, ranging from small to very large companies and exchanges, were supportive of the idea that event contracts markets serve legitimate economic purposes.¹⁶

C. Futures Contracts on Domestic Box Office Receipts

On March 9, 2010, Media Derivatives, Inc. (“MDEX”) requested approval of futures and binary option contracts which would settle based on opening weekend revenues for the movie *Takers*.¹⁷ Shortly thereafter, on March 30, 2010, Cantor Exchange (“Cantor”) requested approval of domestic box office receipt futures contracts based on revenue from the first four weeks following release of the movie *The Expendables*.¹⁸ Both requests underwent review by the Commission, during which time then-Director of DMO Richard Shilts released a public statement discussing the MDEX and Cantor contracts.¹⁹ Regarding the CFTC’s review of those contracts, Mr. Shilts noted that: “the primary focus of the [CFTC] staff’s review of contract filings is to ensure that the contract is not readily susceptible to manipulation ([CEA] Core Principle 3) and that the contract has speculative position limits or position accountability rules that minimize the susceptibility to manipulation ([CEA] Core Principle 5),” in addition to issues raised in public comments. Notably, Mr. Shilts stated that:

... the Core Principle requirements for DCM contracts were added to the CEA in 2000 by the Commodity Futures Modernization Act. At that time, the CFMA repealed that section of the Act which embodied a public interest requirement that in turn included an economic purpose test. Under the economic purpose test, exchanges could only list for trading contracts that could be used on more than an occasional basis for hedging or price-basing purposes. As a result of the changes of the CFMA, staff does not routinely consider the economic purpose served by proposed contracts in its reviews. However, in view of the comments expressed by interested parties and several commissioners related to the potential hedging uses of the contracts, staff will consider the potential hedging utility of the proposed contracts.

¹⁵ See Comment File 08-004, Concept Release on the Appropriate Regulatory Treatment of Event Contracts (May 7, 2008), available at <https://www.cftc.gov/LawRegulation/PublicComments/08-004.html>. The relevant businesses of some of the noted commenters are discussed in further detail *infra*, including Intrade the Prediction Market Limited and Iowa Electronic Markets.

¹⁶ See generally *id.*

¹⁷ See Statement of Richard Shilts, Director, Division of Market Oversight on Meeting of the Commodity Futures Trading Commission to Discuss: Futures and Binary Options Based on Box Office Receipts (May 19, 2010), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/shiltstatement051910>.

¹⁸ See *id.*

¹⁹ See *id.*

On June 14, 2010, the CFTC approved the contracts requested for review by MDEX²⁰, followed by approval of the Cantor contracts on June 28, 2010.²¹ At this point, contracts based on domestic box office receipts were permitted under the CEA, pursuant to the CFTC's approval orders. However, on July 21, 2010, Dodd-Frank was enacted, including a provision that amended the CEA to prohibit futures contracts on motion picture box office receipts.²²

D. Commodity Exchange Act Section 5c(c)(5)(C)

The 2008 financial crisis was the catalyst for a reevaluation of derivatives regulation. Dodd-Frank introduced a comprehensive overhaul and reorganization of the U.S. financial regulatory system. Section 745²³ of Dodd-Frank added Section 5c(c)(5)(C) to the CEA,²⁴ pertaining to review of the listing of event contracts by entities registered with the CFTC as designated contract markets (“DCMs”) and swap execution facilities (“SEFs”). Section 5c(c)(5)(C) gives authority to the CFTC to determine that an event contract in excluded commodities referencing terrorism, assassination, war, gaming, any activity unlawful under state or federal law, or “other similar activity” is contrary to the public interest, and thus may be prohibited by the CFTC.²⁵

E. Regulation 40.11

On July 27, 2011, the CFTC promulgated Regulation 40.11 pursuant to its authority under Section 5c(c)(5)(C) of the CEA.²⁶ Regulation 40.11(a) prohibits CFTC-registered entities from listing or accepting for clearing event contracts in excluded commodities that reference terrorism, assassination, war, gaming, any activity unlawful under state or federal law, or that reference “an activity that is similar to” those activities and that the CFTC determines to be “contrary to the public interest.”²⁷ Regulation 40.11(c) provides for a 90-day review period for the CFTC to determine whether a contract proposed by a DCM violates Regulation 40.11(a).

Regulation 40.11 creates an outright prohibition of futures contracts involving activities specified in Regulation 40.11(a), as compared to CEA Section 5c(c)(5)(C) granting the CFTC the *authority* to prohibit such contracts.²⁸ Regarding Regulation 40.11, the CFTC has stated that

²⁰ See CFTC, Statement of the Commission (June 14, 2010), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@otherif/documents/ifdocs/mdexcommissionstatement061410.pdf>.

²¹ See CFTC Response to Request by Cantor Exchange for review and approval of the *The Expendables* futures contract. (June 28, 2010), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@otherif/documents/ifdocs/cantorfuturesdbororder062810.pdf>.

²² See 7 U.S.C. § 13–1.

²³ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No 111-203, 124 Stat. 1735 § 745 (2010).

²⁴ 7 U.S.C. § 7a–2(c)(5)(C).

²⁵ See *id.*

²⁶ 17 C.F.R. § 40.11.

²⁷ 17 C.F.R. § 40.11(a)(1)–(2).

²⁸ For additional analysis, see Katherine Cooper, The History of the Economic Purpose and Public Interest Tests, ABA Derivatives & Futures Law Committee 2023 Winter Meeting: Innovative New Products Panel (Jan. 6, 2022).

DCMs may submit a particular event contract or other product to the CFTC for approval pursuant to CFTC Regulation 40.3,²⁹ or self-certify a new product under Regulation 40.2.³⁰

III. CFTC Regulation and Actions

A. Iowa Electronic Markets

In 1992 and again in 1993, the CFTC issued no action letters allowing the University of Iowa to operate the event contracts market Iowa Electronic Markets (“IEM”).³¹ IEM is a limited market known for the trading of contracts based on the results of presidential and other elections, which “originated as an experimental and academic program at the University of Iowa.”³² Pursuant to the CFTC’s no action letter, IEM has since been permitted to operate subject to certain conditions, such as limiting access to each of its submarkets to between 1,000 and 2,000 traders, and providing that individual traders in one submarket may only risk between five and five hundred dollars.³³ Additionally, the University and those Governors and Directors working on IEM may not receive profit or compensation related to the trading on IEM, as the CFTC’s no action relief was based in part on the University of Iowa’s representations that IEM would operate for only academic purposes.³⁴

B. NADEX

In December 2011, the North American Derivatives Exchange (“NADEX”), a CFTC-regulated Designated Contracts Market (“DCM”) self-certified a series of political events contracts related to the results of the U.S. federal elections in 2012, pursuant to Regulation 40.2. On April 2, 2012, the CFTC issued an order that prohibited NADEX from listing the relevant political event contracts, having determined that the contracts involved “gaming” and were contrary to the public interest under Section 5c(c)(5)(C) of the CEA.³⁵ The CFTC order stated that the relevant question in determining whether a contract involves one of the activities enumerated in Section 5c(c)(5)(C) is “whether the contract, considered as a whole, involves one of those activities.”³⁶ The order pointed to the connection between the terms “gaming” or “gambling” to betting on elections, and noted that state gambling definitions of “wager” and “bet” are “analogous to the act of taking a position” in political event contracts.

Notably, the NADEX order found that the “legislative history of CEA Section 5c(c)(5)(C) indicates Congress’s intent to restore, for the purposes of that provision, the economic purpose test

²⁹ See 17 C.F.R. § 40.3.

³⁰ See 17 C.F.R. § 40.2.

³¹ See Andrea M. Corcoran, CFTC No-Action Letter rf05-003 (June 18, 1993). The 1993 Letter superseded a more limited letter issued in 1992.

³² *Id.* at 1.

³³ *Id.* at 6.

³⁴ *Id.*

³⁵ CFTC Order Prohibiting the Listing or Trading of Political Event Contracts, In re Self-Certification by North American Derivatives Exchange, Inc. of Political Event Derivatives Contracts and Related Rule Amendments under Part 40 of the Regulations of the Commodity Futures Trading Commission (April 2, 2012), available at <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf>.

³⁶ *Id.* at 2.

that was used by the Commission to determine whether a contract was contrary to the public interest pursuant to CEA Section 5(g) prior to its deletion” by the CFMA.³⁷ The order also found that the CFTC has discretion to consider other factors when determining whether an event contract is contrary to the public interest, then stated that political event contracts “can potentially be used in ways that would have adverse effect on the integrity of elections.”³⁸

C. Intrade

On November 26, 2012, the CFTC filed a civil complaint against Intrade the Prediction Market Limited (“Intrade”) and Trade Exchange Network Limited (“TEN”), two Irish companies, with violating the Commission’s ban on off-exchange options trading by offering commodity option contracts to and soliciting, accepting, and confirming the execution of orders from U.S. customers.³⁹ According to the CFTC complaint, Intrade and TEN operated an online prediction market trading website from September 2007 to June 25, 2012, through which U.S. customers were able to trade options products subject to the CFTC’s off-exchange options trading prohibition.⁴⁰ The relevant contracts included binary options relating to the future prices of gold and crude oil, future changes to the U.S. unemployment rate, and U.S. gross domestic product figures.⁴¹ The CFTC also alleged that TEN violated a 2005 CFTC order that found TEN engaged in prior, similar conduct, and required TEN to cease and desist from violations of the CEA and CFTC regulations.⁴²

On August 3, 2015, the U.S. District Court for the District of Columbia entered an order for summary judgment in favor of the CFTC on two of the three Counts in the complaint.⁴³ Count I of the complaint alleged violations of Section 4c(b) of the CEA, which prohibits entering into options contrary to any rule promulgated by the CFTC, and CFTC Regulation 32.11, which prohibits solicitation or acceptance of orders in connection with the purchase or sale of any commodity option.⁴⁴ The District Court found that there was no genuine issue of material fact that the contracts in question fit within the statutory and regulatory definitions of “commodity options” subject to Section 4c(b) and Regulation 32.11.⁴⁵ Count II of the complaint alleged violations of Section 6c of the CEA, which gives authority to the CFTC to issue injunctions for engaging in a practice constituting a violation of the CEA, any CFTC regulation, or any CFTC order.⁴⁶ TEN argued that it did not violate the 2005 CFTC order because it had deconsolidated into three separate

³⁷ *Id.* at 3.

³⁸ *Id.* at 4.

³⁹ See Press Release, CFTC Release No. 6423-12, CFTC Charges Ireland-based “Prediction Market” Proprietors Intrade and TEN with Violating the CFTC’s Off-Exchange Options Trading Ban and Filing False Forms with the CFTC (Nov. 26, 2012), available at <https://www.cftc.gov/PressRoom/PressReleases/6423-12>.

⁴⁰ See Complaint, SEC v. Trade Exch. Network Ltd., 12-cv-1902 (D.D.C. Nov. 26, 2012).

⁴¹ See *id.* at 3. While Intrade also traded political event contracts, the CFTC’s complaint specifically addressed contracts referencing the future prices of gold and crude oil, future changes to the U.S. unemployment rate, and U.S. gross domestic product figures.

⁴² *Id.* at 2.

⁴³ See Memorandum Opinion: Summary Judgment, SEC v. Trade Exch. Network Ltd., 12-cv-1902 (D.D.C. Aug. 3, 2015).

⁴⁴ See *id.* at 7.

⁴⁵ *Id.*

⁴⁶ See *id.* at 13.

entities in 2007, one of which was Intrade.⁴⁷ The District Court found that TEN and Intrade were operating as a common enterprise, and thus were jointly and severally liable for violating the 2005 order.⁴⁸

D. Victoria University of Wellington (New Zealand)/PredictIt – No Action Letter

On October 29, 2014, the CFTC’s Division of Market Oversight issued a no action letter allowing Victoria University of Wellington, New Zealand (“Victoria University”) to operate a small scale event contracts market offering such contracts to U.S. persons, without registering with the CFTC as a DCM, SEF, or foreign board of trade (“FBOT”).⁴⁹ Pursuant to CFTC Letter 14-130, Victoria University was permitted to operate PredictIt for U.S. persons, an event contracts market consisting of a submarket for political event contracts and a submarket for economic indicator contracts.⁵⁰ Victoria University already operated a similar platform in New Zealand called iPredict. Victoria University indicated that the information gathered through trading of the contracts would be used for educational and research purposes, and the no action letter stated that the University operate the market as a not-for-profit, that to keep the market small scale traders would have a position/investment limit of only \$850 per contract. This amount was essentially an inflation-adjustment to the limit that imposed by the IEM no action letter, discussed *supra*, 20 years earlier. Another limitation was that there could only be 5,000 traders per submarket at any time, among other conditions.⁵¹ The PredictIt site is currently operationally supported by Aristotle International, Inc. (“Aristotle”), a U.S.-based political campaign, finance, and payments technology provider.

E. Aristotle International Section 4(c) Petition

On May 20, 2019, Aristotle, the company that has provided systems development, know your customer (“KYC”) and anti-money laundering (“AML”) compliance and other administrative and support services to Victoria University in the operation of PredictIt, filed a petition (the “Petition”) requesting that the CFTC develop a regulatory regime for event contracts markets, pursuant to its authority under Section 4(c) of the CEA, to allow event contracts to trade on CFTC-registered platforms.⁵² The Petition argues that event contracts “serve an information aggregation function for members of the public—academics, companies, and governments—who use them to further their research, manage their business operations, and set policy.”⁵³ Arguments made in the Petition regarding the information aggregation function of event contracts markets are based upon the results of trading and academic research gained from trading on PredictIt. For example, the Petition discusses how one study found that event contracts markets are more accurate with half the forecast error compared to traditional public opinion election polls.⁵⁴ The

⁴⁷ *Id.* at 13–14.

⁴⁸ *Id.* at 15.

⁴⁹ See Vincent McGonagle, CFTC No-Action Letter 14-130 (October 29, 2014), available at <https://www.cftc.gov/csl/14-130/download>.

⁵⁰ See *id.*

⁵¹ See *id.*

⁵² See Petition Pursuant to Section 4(c) of the Commodity Exchange Act for Action on Event Markets (May 20, 2019).

⁵³ *Id.* at 7.

⁵⁴ *Id.* at 8.

Petition also discusses how businesses incorporate the prices of event markets into their decision making, providing the example of how Hewlett-Packard used internal event markets to forecast sales of its printers and found that the markets outperformed the company's official forecasts.⁵⁵ Another included example is that Goldman Sachs reported that it relied on event markets, including markets compiled by PredictIt, "to forecast stock market turmoil as a result of the U.S. midterm elections."⁵⁶ Finally, regarding the use of event contracts markets by government bodies to better set policy, the Petition notes that the Department of Defense's blue-sky research agency planned to sponsor prediction markets on questions of military interest in 2001, and that the National Science Foundation issued a grant to set up event contracts markets relating to synthetic biology in 2009.⁵⁷

The Petition discusses the economic purpose of event contracts, arguing that such markets serve the purpose of price discovery, similar to futures and swaps markets, and should not be considered "gaming" under CEA Section 5c(c)(5)(C) or Regulation 40.11.⁵⁸ The Petition argues that the underlying economic value of event contracts markets, in particular the ability to inform business decisions in interstate commerce, distinguishes them from sports betting and "gaming."⁵⁹ The Petition notes that event contracts markets were not fully considered when the CEA and its subsequent amendments were drafted, and that there has been no clear regulatory framework promulgated for those markets.⁶⁰ The Petition expresses the view that the CFTC is the proper regulator for non-security-based event contracts, and that the Commission should develop a regulatory framework tailored specifically to the unique characteristics of event contracts markets including the creation of a separate regulatory category.⁶¹ The Petition explains that the limitations placed on event contracts markets through no action relief prevents such markets from attracting sufficient liquidity and scale to achieve their full potential.⁶²

F. FTX

FTX Trading Ltd. ("FTX"), the non-U.S. based entity and now-bankrupt company known for its former operation of a cryptocurrency exchange, operated political event contracts markets relating to the 2020 U.S. presidential election and reportedly on the U.S. presidential election results in 2024.⁶³ The relevant futures trading products that FTX offered were called "TRUMP," "BIDEN," "BERNIE," "BLOOMBERG," "PETE," and "WARREN," and allowed users to use

⁵⁵ *Id.*

⁵⁶ *Id.* at 9.

⁵⁷ *Id.* at 9.

⁵⁸ *Id.* at 22.

⁵⁹ *Id.* at 29.

⁶⁰ *Id.* at 13.

⁶¹ *Id.* at 18.

⁶² *Id.* at 17.

⁶³ See Marie Huillet, *You Can Now Use Cryptocurrency to Trade 'TRUMP-2020' Futures*, COINTELEGRAPH (Feb. 7, 2020), available at <https://cointelegraph.com/news/you-can-now-use-cryptocurrency-to-trade-trump-2020-futures>; see also Zack Voell, *Crypto Traders Bet on US Election as FTX Prediction Markets Hit Record Volumes*, COINDESK (Oct. 16, 2020, 11:06 AM), available at <https://www.coindesk.com/markets/2020/10/16/crypto-traders-bet-on-us-election-as-ftx-prediction-markets-hit-record-volumes/>.

cryptocurrency to bet on the outcome of the presidential election in 2020.⁶⁴ Notably, at the time when the TRUMP product was being offered, FTX had stated on its website that “ignoring fees, inefficiency, and spread, the price of one TRUMP contract equals the president’s expected chances of reelection,” with the contracts settling at \$1 if then-President Donald Trump won reelection, and at \$0 if Joe Biden won the race.⁶⁵ Additionally, in 2021 FTX offered trading of futures contracts relating to the reelection of Brazilian president Jair Bolsonaro.⁶⁶ Similarly to the TRUMP contract, “Bolsonaro 2022” was slated to settle at \$1 if Bolsonaro won reelection, and \$0 if he did not.⁶⁷ None of the political event contracts offered by FTX were permitted to be traded by residents of the U.S.⁶⁸

G. ErisX

On December 14, 2020, Eris Exchange (“ErisX”) self-certified⁶⁹ a series of event contracts relating to points scored in national football league (“NFL”) games, offered only to Eligible Contract Participants (“ECPs”), meaning retail persons and “persons seeking to profit based upon the outcome of particular sporting events” would not be able to trade the contracts. ErisX argued that the relevant contracts had a hedging potential for sportsbook operators, and provided vendors and stadium owners the opportunity to hedge commercial risk associated with low game attendance.⁷⁰

On December 23, 2020, the CFTC issued a 90-day stay of the listing of the ErisX event contracts, pending a review by the agency as well as a public comment period.⁷¹ Following the public comment period, the CFTC circulated a draft order which would find that the ErisX event contracts involved “gaming” and were contrary to the public interest, and thus prohibit their trading. ErisX withdrew its self-certification submission following circulation of the draft order,

⁶⁴ See Marie Huillet, *You Can Now Use Cryptocurrency to Trade ‘TRUMP-2020’ Futures*, COINTELEGRAPH (Feb. 7, 2020), available at <https://cointelegraph.com/news/you-can-now-use-cryptocurrency-to-trade-trump-2020-futures>; see also @FTX_Official, TWITTER (Feb. 10, 2020, 3:42 AM), https://twitter.com/FTX_Official/status/1226788534951927809.

⁶⁵ See Sebastian Sinclair, *FTX Raises ‘TRUMP’ Futures Margins as Price Suggests Lower Expectations of Election Win*, COINDESK (Oct. 30, 2020, 7:11 AM), available at <https://www.coindesk.com/markets/2020/10/30/ftx-raises-trump-futures-margins-as-price-suggests-lower-expectations-of-election-win/>.

⁶⁶ See Jamie Crawley, *New FTX Derivative Lets Traders Bet on Re-Election of Brazil’s Bolsonaro*, COINDESK (May 17, 2021, 10:41 AM), available at <https://www.coindesk.com/markets/2021/05/17/new-ftx-derivative-lets-traders-bet-on-re-election-of-brazils-bolsonaro/>; see also @SBF_FTX, TWITTER (May 15, 2021, 3:43 AM), https://twitter.com/SBF_FTX/status/1393472143862624262.

⁶⁷ *Id.*

⁶⁸ See Yilun Cheng, *FTX users can now trade reelection futures contract for President Trump*, YAHOO (Feb. 6, 2020), available at https://www.yahoo.com/video/ftx-users-now-trade-reelection-193448641.html?guccounter=1&guce_referrer=aHR0cHM6Ly93d3cuZ29vZ2xlLmNvbS8&guce_referrer_sig=AQAAIHL1K7VPUa7k0VNxeWWPredfZpyPpnOjA7T76qIo7Qz39TewrdJuS4naOJJIGV9XHY_1HKb_1-Yuk2ncaF1sg1ABo_AsitRxELUjr1bs-InHuQ2FIlalo5HeEGcsoOEuar1W85afrxQ6G2yzOxu8nMQEq2cEJi0YDmPIr9r5_TC.

⁶⁹ See ErisX, CFTC Regulation 40.2(a) Certification. Notification Regarding the Initial Listing of Eris Exchange RSBIX NFL Futures (Eris Exchange Submission #2020-11E) (Dec. 14, 2020).

⁷⁰ *Id.* at 6.

⁷¹ See Press Release, CFTC Release No. 8345-20, *CFTC Announces Review of RSBIX NFL Futures Contracts Proposed by Eris Exchange, LLC* (Dec. 23, 2020), available at <https://www.cftc.gov/PressRoom/PressReleases/8345-20>.

and thus no final CFTC order was issued. However, CFTC Commissioners Brian Quintenz and Dan Berkovitz each released comprehensive public statements on the ErisX self-certification submission. While taking different positions on the specific ErisX filing, they both presented detailed explanations of why the CFTC should not be obstructing the development of non-traditional event contract markets. However, it was clear that the Chair and a majority of Commissioners would have objected to the regulated trading of the ErisX contracts pursuant to both Section 5c(c)(5)(C) of the CEA and Regulation 40.11.⁷²

Commissioner Quintenz’s statement highlights an inconsistency between Regulation 40.11’s blanket prohibition of certain futures contracts that CEA Section 5c(c)(5)(C) merely grants the CFTC the authority to prohibit, and argues that Regulation 40.11 is invalid.⁷³ Additionally, Commissioner Quintenz’s statement speculates that the relevant CFTC authority pursuant to CEA Section 5c(c)(5)(C) may be an unconstitutional delegation, without an intelligible principle to guide the agency.⁷⁴ Finally, regarding the circulated draft order, Commissioner Quintenz argued that the order was arbitrary and capricious, pointing to its placement of the burden on ErisX to show that the relevant contracts would have hedging utility in order to pass the economic purpose test; failure to properly consider public comments and resulting denial of due process to ErisX; defining “gaming” in an arbitrary manner; and using impermissible tests when evaluating the public interest utility of the contracts.⁷⁵

Commissioner Berkovitz would have found that the ErisX contracts should not be permitted to be traded due to lack of showing the contracts’ hedging utility, and because ErisX impermissibly planned to offer the contracts only to ECPs.⁷⁶ Pursuant to an analytical framework of first determining whether a contract “involves” a prohibited activity, and second whether the contract is contrary to the public interest, Commissioner Berkovitz would have found that the ErisX contracts involved “gaming,” and that there was insufficient evidence of their hedging utility under the economic purpose test.⁷⁷ Finally, Commissioner Berkovitz argued that ErisX’s plan to offer its political event contracts to only ECPs would be a violation of the Core Principles applicable to DCMs, specifically the requirement that DCMs provide impartial access to their markets.⁷⁸

H. Polymarket

On January 3, 2022, the CFTC filed and settled charges with Polymarket,⁷⁹ a decentralized, non-custodial betting platform, for offering off-exchange event contracts without registered as a

⁷² For additional analysis, *see* Katherine Cooper, The History of the Economic Purpose and Public Interest Tests, ABA Derivatives & Futures Law Committee 2023 Winter Meeting: Innovative New Products Panel (Jan. 6, 2022).

⁷³ *See* Statement of Commissioner Brian D. Quintenz on ErisX RSBIX NFL Contracts and Certain Event Contracts, CFTC (Mar. 25, 2021), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/quintenzstatement032521>.

⁷⁴ *See id.*

⁷⁵ *See id.*

⁷⁶ *See* Statement of Commissioner Dan M. Berkovitz Related to Review of ErisX Certification of NFL Futures Contracts, CFTC (Apr. 7, 2023), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement040721>.

⁷⁷ *See id.*

⁷⁸ *See id.*

⁷⁹ The CFTC order was against Blockratize, Inc., a Delaware-registered corporation doing business as Polymarket.

DCM or SEF.⁸⁰ Specifically, the CFTC order found that Polymarket began operating an event contracts market in mid-2020, publicly offering the opportunity to buy and sell binary options contracts relating to event such as: (1) “Will [Ethereum] be above \$2,500 on July 22?”; (2) “Will the 7-day average COVID-19 case count in the U.S. be less than 15,000 for the day of July 22?”; and (3) “Will Trump win the 2020 presidential election?”⁸¹ According to the CFTC, these contracts constituted swaps under the Commission’s jurisdiction, and thus could not be offered except by the CFTC-registered exchange.⁸² Pursuant to the order, Polymarket paid a civil penalty of \$1.4 million, and was required to wind down activity on Polymarket.com that was not in compliance with the CEA and CFTC regulations.⁸³

I. Kalshi

On July 20, 2022, the CFTC-registered DCM KalshiEX LLC (“Kalshi”) submitted a series of proposed political event contracts for approval by the CFTC pursuant to Regulation 40.2.⁸⁴ The contracts were binary options based on the question: “Will [political party] be in control of the [chamber of Congress]?” and would pay out based upon the party affiliation of the Speaker of the U.S. House of Representatives or the President Pro Tempore of the U.S. Senate.⁸⁵ Kalshi argued that Regulation 40.11 did not apply because the relevant contracts did not reference gaming nor any unlawful activity.⁸⁶ Additionally, Kalshi argued that the relevant contracts could be used to hedge economic and commercial consequences of elections, while not threatening the integrity of U.S. elections.⁸⁷ Kalshi also pointed to the fact that other similar political event contracts were permitted to be offered to persons in the U.S. on platforms that were not regulated exchanges and instead subject to limitations under no action relief.⁸⁸

On August 26, 2022, the CFTC issued a 90-day stay of the listing of the Kalshi event contracts, pending agency review and a public comment period, during which the CFTC sought commentary on questions such as whether the Kalshi contracts involved “gaming” or similar activity.⁸⁹ In her dissenting statement on the 90-day stay, CFTC Commissioner Caroline Pham commented, “Rule 40.11(a)(2) is not operative until the Commission promulgates a rule or regulation to determine that an activity that is ‘similar to’ an enumerated activity is contrary to the

⁸⁰ See Press Release, CFTC Release No. 8478-22, CFTC Orders Event-Based Binary Options Markets Operator to Pay \$1.4 Million Penalty (Jan. 2, 2022), available at <https://www.cftc.gov/PressRoom/PressReleases/8478-22>.

⁸¹ *Id.*

⁸² *See id.*

⁸³ *See id.*

⁸⁴ See KalshiEX LLC - Commission Regulation 40.3(a), Voluntary submission of new products for Commission review and approval, regarding the “Will <party> be in control of the <chamber of Congress>?” Contract, (July 19, 2022), available at <https://www.cftc.gov/sites/default/files/filings/ptc/22/08/ptc082422kexdc001.pdf>.

⁸⁵ See Press Release, CTC Release No. 8578-22, *CFTC Announces Review and Public Comment Period of KalshiEx Proposed Congressional Control Contracts Under CFTC Regulation 40.11* (Aug. 26, 2022), available at <https://www.cftc.gov/PressRoom/PressReleases/8578-22>.

⁸⁶ See KalshiEX LLC - Commission Regulation 40.3(a), Voluntary submission of new products for Commission review and approval, regarding the “Will <party> be in control of the <chamber of Congress>?” Contract, (July 19, 2022), available at <https://www.cftc.gov/sites/default/files/filings/ptc/22/08/ptc082422kexdc001.pdf>.

⁸⁷ *See id.*

⁸⁸ *See id.*

⁸⁹ See Press Release, CTC Release No. 8578-22, *CFTC Announces Review and Public Comment Period of KalshiEx Proposed Congressional Control Contracts Under CFTC Regulation 40.11* (Aug. 26, 2022), available at <https://www.cftc.gov/PressRoom/PressReleases/8578-22>.

public interest, therefore, Rule 40.11(a)(2) does not apply to the political event contracts.⁹⁰ There were 201 comments filed regarding the Kalshi contracts, including from large industry participants such as the Futures Industry Association, Aristotle International Inc., and Intercontinental Exchange, as well as from small industry participants, private citizens, and groups of professors and academic researchers.⁹¹ Many of the comments offered support for the CFTC allowing the listing of the Kalshi contracts.⁹² Many comments also asked that the CFTC provide regulatory clarity in the event contracts markets.⁹³ The CFTC has yet to act regarding its review of the Kalshi political event contracts.

J. PredictIt – Revocation of No Action Relief

On August 4, 2022, the CFTC announced that DMO was revoking its previously issued no action relief relating to PredictIt, based on Victoria University not complying with the conditions of the Division’s no action letter.⁹⁴ The Division did not provide details about the non-compliance. The revocation ordered that all listed contracts and positions on PredictIt be closed or liquidated, and PredictIt’s operations be shut down, by 11:59 PM EST on February 15, 2023.⁹⁵ In response, Aristotle International, along with a group of PredictIt traders and academics who utilize the trade data in their research and curriculums, filed suit in the U.S. Federal District Court for the Western District of Texas against the CFTC, seeking an injunction to prevent the agency from shutting down PredictIt while the company challenges the decision to revoke no action relief.⁹⁶ On December 23, 2022, the plaintiffs filed a notice of appeal in the Western District of Texas, arguing that inaction by the District Court for three months following initial filing in September 2022 was “constructive denial” of their motion.⁹⁷

On January 18, 2023, the U.S. Court of Appeals for the Fifth Circuit scheduled a hearing for oral arguments in the case, for February 8, 2023, denying the CFTC’s motion to dismiss the appeal.⁹⁸ On January 26, 2023, the Fifth Circuit also granted an injunction allowing PredictIt to continue offering the trading of political event contracts past the February 15 deadline indicated in the CFTC’s revocation letter, while its challenge of the CFTC’s action is ongoing.⁹⁹ A panel of

⁹⁰ See Dissenting Statement of Commissioner Caroline D. Pham Regarding the Review and Stay of KalshiEX LLC’s Political Event Contracts, CFTC (Aug. 26, 2022), available at

<https://www.cftc.gov/PressRoom/SpeechesTestimony/phamstatement082622>.

⁹¹ See Comments for Industry Filing 22-002, Review and Public Comment Period of KalshiEx Proposed Congressional Control Contracts Under CFTC Regulation 40.11 (Aug. 26, 2022), available at <https://comments.cftc.gov/PublicComments/CommentList.aspx?id=7311>.

⁹² See generally *id.*

⁹³ See generally *id.*

⁹⁴ See Press Release, CTC Release No. 8578-22, *CFTC Announces Review and Public Comment Period of KalshiEx Proposed Congressional Control Contracts Under CFTC Regulation 40.11* (Aug. 26, 2022), available at <https://www.cftc.gov/PressRoom/PressReleases/8578-22>.

⁹⁵ See *id.*

⁹⁶ *Clarke v. CFTC*, No. 22-vs-909 2022, WL 16545967 (W.D. Tex. Sept. 9, 2022).

⁹⁷ See *Clarke v. CFTR*, No. 22-51124 (5th Cir. Feb. 8, 2023).

⁹⁸ See *Fifth Circuit Grants Injunction Allowing PredictIt Market to Continue Operating*, GLOBENEWSWIRE (Jan. 26, 2023, 10:05 PM), available at <https://www.globenewswire.com/news-release/2023/01/27/2596580/0/en/Fifth-Circuit-Grants-Injunction-Allowing-PredictIt-Market-to-Continue-Operating.html>.

⁹⁹ See *id.*

three Fifth Circuit judges heard oral arguments in the case on February 8, 2023. The parties now await a decision.

On March 2, 2023, the CFTC, through the Division of Market Oversight, sent a new letter to Victoria University indicating that it was retracting the August 4, 2022 letter that revoked the Victoria University/PredictIt no action relief.¹⁰⁰ The new letter identified alleged non-compliance with the requirements of the CFTC's 2014 no action letter relating to PredictIt.¹⁰¹ The letter indicates the continued view for the PredictIt market to cease trading, but asks Victoria University to respond to the letter before the CFTC such action is finalized¹⁰². The CFTC also petitioned the Fifth Circuit to vacate the pending case, arguing that the case is moot due to the prior August 4, 2022 letter being retracted.¹⁰³ The Plaintiffs filed a reply brief, with the Fifth Circuit now considering the mootness issue raised by the CFTC.

¹⁰⁰ See Notice to Traders, PREDICTIT, available at <https://www.predictit.org/platform-announcements>.

¹⁰¹ See *id.*

¹⁰² VUW provided a timeous response to the CFTC on April 5, 2023.

¹⁰³ See Katryna Perera, *CFTC Tells 5th Circ. To Reject PredictIt's Injunction Bid*, LAW360 (Feb. 2, 2023, 10:26 PM), available at <https://www.law360.com/articles/1572019/cftc-tells-5th-circ-to-reject-predictit-s-injunction-bid>.