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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).

Dear Chairman and Commissioners:

This comment urges approval of KalshiEx, LLC's ("KalshiEX" or "Kalshi") proposed Congressional Control Contracts pursuant to Commodity Futures Trading Commission Regulation 40.11(c).

I am a former Commissioner of the United States Securities and Exchange Commission (1985-1990).[1] I am currently the W.A. Franke Professor of Law and Business (Emeritus) at Stanford University where I have served since leaving the SEC in 1990, and am also Senior Faculty of the Rock Center on Corporate Governance. My scholarship has been published in the Harvard, Yale, and Stanford law reviews, and my areas of specialization include financial market regulation, fraud, corporate governance, and venture capital.

When considering the public policy implications of the proposed contract, it is constructive for the Commission to recognize the robust information environment in which the contract proposes to trade. In particular, there is no shortage of commentary and prediction relating to the outcome of federal elections in general, or the prospects for control of either house of Congress in particular. The proposed contract will thus not be introduced in an information vacuum. The contract's implications for the public interest are therefore most accurately appreciated by considering the marginal effects that its introduction would have over and above the robust information sources already present in the market, and that will continue to be vigorously exercised if the contract is approved.

Significantly, dozens of polls seek to measure and predict the outcome of Congressional elections by district and in the aggregate. These polls include Quinnipiac,[2] ABC/Washington Post[3],

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[1] The views expressed in this comment are my own and do not reflect, nor should they be ascribed to, the views or positions of any other organization with which I may be affiliated.
[2] Quinnipiac University, "Poll Results", https://poll.qu.edu/poll-results
[3] Washington Post-ABC News Poll, https://www.washingtonpost.com/wp-srv/politics/polls/postabcpoll_031012.html

New York Times/Siena,[4] Ipsos,[5] and Emerson College.[6] For example, a recent Emerson College poll found Senator Raphael Warnock trailing his challenger Herschel Walker for the Georgia Senate seat by two points.[7] Other Senate races, such as the one in Pennsylvania, have been similarly well-polled with Emerson College[8] polling joining similarly reputable Susquehanna Polling & Research and giving Lieutenant Governor John Fetterman a modest margin over his challenger, Mehmet Oz.[9]

Many commentators and consultants also predict Congressional campaign outcomes, again on a district-by-district basis, as well as for Congress as a whole. These commentators include the Cook Political Report,[10] Data for Progress,[11] Politico[12] and Frank Luntz.[13] Steve Shepard of Politico, as an example, rates the Senate as a "toss up" but projects that Republicans are "likely" to take control of the House.[14] Meanwhile, the Cook Political Report rates nine of the thirty-five Senate seats up for re-election as Safe Democrat, three as lean Democrat, four as lean Republican, and fifteen as Safe Republican.[15]

Some analysts construct statistical models that rely on polling data to aggregate this information and to generate quantitative predictions of likely electoral outcomes. The most famous of these models is, perhaps, operated by FiveThirtyEight,[16] but there are many prominent alternatives, including models generated by the Economist[17] and the New York Times.[18] FiveThirtyEight, as of September 11, 2022, projected a 74% probability that Republicans would take control of the House, and a 69% probability that Democrats would control the Senate.[19] The Economist also projects a 74%

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[4] The New York Times/Siena College Research Institute July 5-7 2022.
https://int.nyt.com/data/documenttools/us0722-crosstabs-nyt071122/33ffa85627ee4648/full.pdf

[5] Ipsos. "Political and Public Opinion Polling". https://www.ipsos.com/en/political-and-public-opinion-polling

[6] Emerson College Polling. https://emersoncollegepolling.com/

[7] See https://emersoncollegepolling.com/georgia-2022-walker-holds-two-point-lead-over-warnock-in-tight-senate-race-kemp-leads-abrams-by-four/

[8] See https://emersoncollegepolling.com/pennsylvania-2022-fetterman-holds-four-point-lead-over-oz-for-us-senate-shapiro-leads-mastriano-by-three/

[9] See https://www.politicspa.com/susquehanna-poll-fetterman-holds-five-point-lead-on-oz-49-44/111648/

[10] Cook Political Report, https://www.cookpolitical.com/

[11] Data for Progress, "Elections", https://www.dataforprogress.org/elections

[12] Politico. "2022 Election Forecast", https://www.politico.com/2022-election/race-forecasts-ratings-and-predictions/

[13] Frank Luntz, "What Happened When 7 Trump Voters and 6 Biden Voters Tried to Find Common Ground". NEW YORK TIMES (Jul. 28, 2022), https://www.nytimes.com/interactive/2022/07/28/opinion/focus-group-political-division.html

[14] See, Politico Forecast, September 11, 2022, available at https://www.politico.com/2022-election/race-forecasts-ratings-and-predictions/

[15] See https://www.cookpolitical.com/ratings/senate-race-ratings

[16] FiveThirtyEight, "2022 election forecast", https://projects.fivethirtyeight.com/2022-election-forecast/senate/?cid=rrpromo

[17] The Economist, "How The Economist presidential forecast works", THE ECONOMIST (2020), https://projects.economist.com/us-2020-forecast/president/how-this-works

[18] See https://www.nytimes.com/live/2020/presidential-polls-trump-biden

[19] See https://projects.fivethirtyeight.com/2022-election-forecast/house/; and https://projects.fivethirtyeight.com/2022-election-forecast/senate/

probability that Republicans will control the House, but generates a higher 78% probability that Democrats will control the Senate.[20]

Other analysts build models that rely on economic or other macro criteria to predict the outcome of federal elections, including presidential and congressional campaigns. For instance, Yale Professor Ray Fair,[21] Google's Patrick Hummel and Microsoft Research's David Rothschild[22] all have developed models along these lines. London School of Economics' Torun Dewan and Harvard's Kenneth Shapsle reviewed the vast literature surrounding these fundamentals models (including political science game theoretic models of elections) and found dozens of models, which encompass a wide variety of modeling choices.[23] For example, as of July 28, Fair's model projected that Democrats will receive 47% of the two-way House vote in the 2022 midterm election.[24]

Prediction markets based on federal elections are active abroad and easily accessed by US persons. At Britain's BetFair, more than $250 million was traded on the US election as of the Wednesday before election day, with another $150 million expected over the following few days.[25] Several other sites, including Ireland's Paddy Power (now owned by BetFair) and UK's LadBrokes saw millions in trading as well.[26] Polymarket's 2020 presidential election market supported more than $10 million in trading.[27] Many US residents access these markets using a variety of affordable VPNs, and the predictive probabilities implied by trading in these markets are obvious to all. Recent prices on Betfair imply a 68% probability that Democrats retain control of the Senate and a 74% probability that Republicans take control of the House, with roughly $400,000 wagered on the outcome of Senate races and $300,000 wagered on House races.[28] At Ladbrokes, prices imply a 56% probability that Democrats retain control of the Senate and a 75% probability that Republicans take control of the House.[29]

There is no shortage of press commentary that reviews and aggregates these different perspectives into a single overarching theme. The New York Times recently published a roundup of

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[20] Split Decision, The Economist, Sept. 10, 2022, at 25.

[21] Ray C. Fair, "Predicting Presidential Elections and Other Things", 2002. https://fairmodel.econ.yale.edu/rayfair/pdf/vote.pdf

[22] Patrick Hummel and David Rothschild, "Fundamental models for forecasting elections at the state level", ELECTORAL STUDIES (2014), https://www.sciencedirect.com/science/article/abs/pii/S0261379414000602#!

[23] Torun Dewan and Kenneth Shepsle, "Political Economy Models of Elections", ANNUAL REVIEW OF POLITICAL SCIENCE (2011), https://www.annualreviews.org/doi/10.1146/annurev.polisci.12.042507.094704

[24] See https://fairmodel.econ.yale.edu/vote2020/indexne1.htm

[25] Chris Isidore. "$284 million has already been wagered by British bettors on the US election outcome". CNN (October 30, 2020), https://www.cnn.com/2020/10/30/business/us-presidential-election-wagering-record/index.html

[26] "Betting sites see record wagering on US presidential election", CNBC (Nov. 7, 2016), https://www.cnbc.com/2016/11/07/betting-sites-see-record-wagering-on-us-presidential-election.html

[27] Polymarket, "Will Trump win the 2020 US presidential election", https://polymarket.com/market/will-trump-win-the-2020-us-presidential-election

[28] See https://www.betfair.com/exchange/plus/politics/market/1.179673535

[29] See https://sports.ladbrokes.com/event/politics/international/us-elections/2022-house-elections/234135146/all-markets

the prognostications of election "soothsayers."[30] Such coverage is common at leading media sources, including the Washington Post,[31] Politico,[32] and the Wall Street Journal.[33]

Finally, overt and entirely legitimate efforts by millions of people seek legally and powerfully to influence the outcome of federal elections. Editorial boards, columnists, and armies of influencers, endorsers, and campaign contributors all strive to tilt election outcomes. Presidential candidates in 2020 spent north of $4 billion,[34] and Congressional candidates spent a further $4 billion,[35] all raised from more than four million donors.[36]

The public interest benefits of introducing Kalshi's contract in this environment are palpable and easily enumerated.

First, Kalshi's proposed contract will identify all market participants and subject them to know-your-customer and anti-money laundering requirements. The contract will generate audit trails and all transactions will be transparent to regulators. In contrast, alternative data sources operate with varying degrees of transparency and disclosure, and many are not subject to direct federal regulatory oversight. Federal authorities, for example, neither know the identities or incentives of persons who respond to polls, nor can audit or validate the numerous statistical models that operate in this space. Indeed, First Amendment considerations properly limit the government's ability to monitor and control alternative predictive information sources. In contrast, Kalshi's contract will have a level of transparency and regulatory compliance unequaled by any of these other predictive sources. The processes by which Kalshi generates its predictive information will also be fully transparent to regulators and market participants alike, and will be subject to careful scrutiny. Kalshi will thus add a differentiated and regulated voice to predictive public information flows.

Second, numerous observers have commented on the possibility that polling data are becoming less reliable either because respondents are unwilling to respond truthfully to pollsters or

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[30] Blake Hounshell, "Why the Soothsayers Are So Puzzled by This Year's Midterms", NEW YORK TIMES (Aug. 8, 2022), https://www.nytimes.com/2022/08/08/us/politics/midterm-election-democrats-republicans-predictions.html

[31] Annie Linskey and Michael Scherer, "Democrats see the once unthinkable: A narrow path to keeping the House", WASHINGTON POST (Aug. 27, 2022), https://www.washingtonpost.com/politics/2022/08/27/democrats-republicans-house-midterms/

[32] Myah Ward, "Election forecasters rethink their ratings", POLITICO (Aug. 25, 2022), https://www.politico.com/newsletters/politico-nightly/2022/08/25/election-forecasters-rethink-their-ratings-00053839

[33]John McCormick. "Independent Voters Now Tilting Toward Democrats in Midterm Elections, WSJ Poll Finds", WALL STREET JOURNAL (Sep. 1, 2022), https://www.wsj.com/articles/democratic-midterm-prospects-improve-as-races-heat-up-wsj-poll-finds-11662024601

[34]Federal Election Commission, "Statistical Summary of 24-Month Campaign Activity of the 2019-2020 Election Cycle", https://www.fec.gov/updates/statistical-summary-24-month-campaign-activity-2019-2020-election-cycle/#:~:text=Presidential%20candidates%20raised%20and%20spent,2019%20through%20December%2031%2C%202020.

[35] Id.

[36] OpenSecrets, "Donor Demographics", https://www.opensecrets.org/elections-overview/donor-demographics?cycle=2020&display=G

because the evolution of internet and cellphone communications introduces bias into polling practices.[37] Kalshi's market is not as vulnerable to these concerns because Kalshi market participants have powerful incentives to accurately predict election outcomes. Expressing any other incentive would be financially costly and adverse to the trader's financial interests. From that perspective, knowledgeable observers interested in adjusting for biases that might be influencing polling practices have incentives to express their adjustment factors by participating in the Kalshi contract, and thereby informing the rest of the market of these adjustment factors.

Third, by operating a differentiated market in which knowledgeable observers can express predictive judgments in an incentive compatible manner, free of biases that can influence other predictive methodologies, Kalshi's contract will add to the competitiveness, accuracy, and transparency of all predictive forms of expression in the marketplace.

Fourth, concerns that a contract like Kalshi's might be used for manipulative purposes are easily exaggerated. Persons interested in manipulating markets have little incentive to identify themselves to federal authorities who can quickly respond with civil or criminal sanctions. Persons interested in manipulating federal elections will find it far more rational to launch social media disinformation campaigns or other forms of deception than to participate in a contract market where they must identify themselves and know that their every move is monitored by regulatory authorities. Further, because of the ambiguous relationship between turnout and perceived position in a campaign, it is far from clear how persons interested in manipulating an election would participate in the Kalshi market. Would a person favoring Candidate X want to inflate the probability that Opponent Y will prevail, and thereby attempt to stimulate more X supporters to show up at the polls? Or, would the person favoring Candidate X want to deflate the probability that Opponent Y will prevail in order to dishearten Candidate Y's supporters and suppress opponent turnout? And, if market participants seek, for partisan reasons, to tilt the market one way or another, they will be entirely unable to prevent counterparties from entering the market to offset their non-market-based efforts to influence Kalshi's predictive estimates. Indeed, they woud be creating profitable trading strategies for their opponents – hardly an outcome they would welcome. The optimal strategy for a potential manipulator is thus far from clear, and this ambiguity very substantially diminishes concern that the Kalshi market will be used for manipulative purposes. Indeed, given the ambiguous electoral consequences of efforts to influence pricing of the Kalshi contract, a person interested in promoting one candidate over another would likely find it far more rational simply to contribute to the favored candidate's campaign where the effect of the contribution is far less ambiguous.

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[37]Joseph P. Williams, "The Problem with Polls", US NEWS (Sep. 28, 2015), https://www.usnews.com/news/the-report/articles/2015/09/28/why-public-opinion-polls-are-increasingly-inaccurate; Jemima McEvoy. "2020 Election Polls Were the Least Accurate In Decades—Mostly For Underestimating Trump, Report Finds". FORBES (Jul. 19, 2021), https://www.forbes.com/sites/jemimamcevoy/2021/07/19/2020-election-polls-were-the-least-accurate-in-decades-mostly-for-underestimating-trump-report-finds/?sh=4cf10fe56318; Nate Cohn, "Yes, the Polling Warning Signs are Flashing Again", NEW YORK TIMES (Sep.. 12, 2022), https://www.nytimes.com/2022/09/12/upshot/polling-midterms-warning.html?campaign_id=9&emc=edit_nn_20220912&instance_id=71706&nl=the-morning&regi_id=159018825&segment_id=106056&te=1&user_id=399100d1a84e7cf6e6483cec4f676104; David Leonhardt, "Are the Polls Wrong Again?", NEW YORK TIMES (Sep.12, 2022), https://www.nytimes.com/2022/09/12/briefing/polling-midterms-republicans-democrats.html

Fifth, the electorate's view of the likely outcome of an election will not be determined exclusively by the pricing of the Kalshi contract. Voters retain access to multiple sources of predictive information, as described above, and will discount Kalshi's predictive information, to the extent appropriate, in light of all other predictive information sources that are active in the market.

Sixth, the extent to which the public is willing to rely on the predictive information generated by the Kalshi contract will be codetermined by the level of confidence the Kalshi contract generates in its integrity. The greater the public's confidence in the integrity of the information generated by the contract, the greater the reliance the public will place on the contract, and the more valuable the contract to society and to its sponsors. The contract's sponsors thus have intrinsic incentives to operate the market without bias or favor to any side of any contract, and to assure that the contract's predictive results are as unbiased and accurate as possible. It is unclear that every other voice in the market for predictive information has equivalently neutral incentives.

I trust that these observations are helpful to the Commission in its deliberations and would be happy to respond to any inquiries that the agency might wish to pose as part of its deliberative process.

With best regards,

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Law and Business, Emeritus