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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: Questions on the KalshiEX, LLC “Will <party> be in control of the <chamber of Congress>?”
Contracts for Public Comment**

Dear Chairman and Commissioners of the Commodity Futures Trading Commission:

We respectfully submit this comment letter in response to the Commission’s request for public comments. DLx Law is a boutique law firm with expertise in federal and state securities laws, financial regulatory laws, general corporate matters, and start-up and venture financing, among other areas. We regularly advise clients in matters relating to the use of novel technologies and business models, including businesses that utilize blockchain technology, and are proud to be ranked as a “Band 2” practice in the United States by independent ranking firm Chambers & Partners for FinTech Legal: Blockchain & Cryptocurrencies. We acted as counsel to KalshiEx, LLC (“Kalshi”) in connection with the submission of its initial application to operate as a designated contract market (“DCM”) overseen by the Commodity Futures Trading Commission (the “Commission” or “CFTC”), and we currently represent Kalshi in certain matters.

We are writing to support the Commission’s prompt approval of the congressional control contracts proposed by Kalshi for listing on their contract market (the “Kalshi Platform”). The Kalshi Platform is a federally regulated DCM for contracts based on the outcomes of a wide range of selected events with economic or commercial relevance (known as “event contracts”). For the reasons set forth in this letter, we are of the view that the proposed congressional control contract entitled “Will <party> be in control of the <chamber of Congress>?” (the “Proposed Event Contract”) does not contravene the provisions of 17 C.F.R. § 40.11(a) and should be approved.

I. Legal framework

The Commodity Exchange Act (the “CEA”) regulates the trading of commodity futures in the United States. Under the CEA, the CFTC may determine that an event contract is “contrary to the public interest” and prohibit it from being listed for trading, if the contract involves one of six enumerated



activities.¹ The Commission’s implementing regulation for this provision is detailed in 17 C.F.R. § 40.11(a), entitled “Review of event contracts based upon certain excluded commodities,” which prohibits the listing for trading:

“(1) An agreement, contract, transaction, or swap based upon an excluded commodity, as defined in Section 1a(19)(iv) of the Act, that involves, relates to, or references terrorism, assassination, war, gaming, or an activity that is unlawful under any State or Federal law; or

(2) An agreement, contract, transaction, or swap based upon an excluded commodity, as defined in Section 1a(19)(iv) of the Act, which involves, relates to, or references an activity that is similar to an activity enumerated in § 40.11(a)(1) of this part, and that the Commission determines, by rule or regulation, to be contrary to the public interest.”²

As discussed below, the Proposed Event Contract (i) does not involve, relate to, or reference “gaming” or an activity that is “unlawful under any State or Federal law,” and (ii) should not be considered “contrary to the public interest” within the meaning of § 40.11(a)(2). Therefore, we believe that the Commission should approve the Proposed Event Contract for trading on the Kalshi Platform.

II. The Proposed Event Contract does not involve “gaming,” or an activity that is otherwise “unlawful under State or Federal law”

Federal Laws

As observed in the Nadex Order,³ the closest federal definition of “gaming” can be found in the federal statute which prohibits the funding of unlawful internet gambling.⁴ There, the federal statute defines a “bet or wager” as “the staking or risking by any person of something of value upon the outcome of a contest of others, a sporting event, or a game subject to chance...”⁵

A. Critical Impact of Economic Utility

The recurring theme in the case law in the United States considering whether activities with an aleatory element constitute “wagering” is that, when the underlying activity either does not have any extrinsic economic purpose, such as pure pastimes like casino games, or constitutes some type of diversion that may have relevance to the participants in the scheme but no outside economic consequence, such as sporting events, wagering is found. While an aleatory element can also be identified in many other

¹ Those six enumerated activities are: “(I) activity that is unlawful under any Federal or State law; (II) terrorism; (III) assassination; (IV) war; (V) gaming; or (VI) other similar activity determined by the Commission, by rule or regulation, to be contrary to the public interest.” 7 U.S.C. § 7a-2(c)(5)(C)(i)(I)-(VI).

² 17 C.F.R. § 40.11(a).

³ CFTC Order Prohibiting the Listing or Trading of Political Event Contracts (Apr. 2, 2012), available at <https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf> (the “Nadex Order”).

⁴ 31 U.S.C. § 5361 *et seq.*

⁵ 31 U.S.C. § 5362(1)(A). The same statute also specifically excludes various activities and transactions from the definition of “bet or wager,” including “any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act” and other derivative instruments. See 31 U.S.C. § 5362(1)(E).



contractual relationships, including most commodities futures and options contracts, where the underlying purpose of the contract is a commercial one (or, in the case of contracts traded on markets and cleared through clearing organizations, the contract can reasonably be used for *bona fide* hedging and price-basing purposes), wagering is generally not found, and a further analysis of the aleatory elements is not undertaken.⁶ A similar rule requiring an underlying “insurable interest” is applied in the context of insurance contracts.⁷

While not all activity that contains aleatory elements, such as games of skill like poker or daily fantasy sports, will be considered “gambling” or “gaming”,⁸ where the activity does not have any reasonably foreseeable economic consequence or significance, it will generally face a very high degree of scrutiny from courts.⁹ Alternatively, traditional activities such as insurance, the secondary trading of securities, and many commercial derivatives contracts that have a clear commercial or economic purpose are generally recognized as not involving “gambling”.¹⁰ This is particularly the case where it can be shown that the contracts are being used, at least in part, for legitimate hedging of pre-existing risks.

The underlying question of the Proposed Event Contract – which party will be in control of either chamber of the Congress – has deep implications on legislation and policymaking in almost all industries, and hence foreseeable risks and economic consequences. For example, it is reported that over fifty million people in the U.S. participated in government assistance programs.¹¹ Party control of the Congress directly correlates with the existence and the amount of various government benefits and subsidies – whether tax credits, food stamps, Medicaid, Covid-19 assistance, or anything else – all of which significantly impacts the well-being of each individual and household that participate. Congressional control by one political party or the other poses significant risks as to the viability of any one of these government benefits and subsidies. And any changes to these government assistance programs could affect the recipient’s financial situation immediately.

Similarly, businesses, especially those in regulated industries, such as education, energy, and healthcare, are directly impacted by federal regulation and other Congressional policies. For example, as different parties take different positions on environmental policies, any changes to the existing environmental policy will immediately impact the supply chain, costs, and demand in the energy industry, all of which have direct economic consequences. Congressional control by one political party or the other thus poses significant risks that could impact almost all participants in the space. In fact, individuals and businesses often make economic decisions in anticipation of changes of Congressional party control,

⁶ Examples of leading scholarship in this area include: Thomas Lee Hazen, *Disparate Regulatory Schemes for Parallel Activities: Securities Regulation, Derivatives Regulation, Gambling and Insurance*, 24 ANN. REV. BANKING & FIN. L. 375 (2005); Lynn A. Stout, *Why the Law Hates Speculators: Regulation and Private Ordering in the Market for OTC Derivatives*, 48 DUKE L. J. 701 (1999) (“Stout”); and Timothy E. Lynch, *Coming Up Short: The United States’ Second-Best Strategies for Corraling Purely Speculative Derivatives*, 36 CARDOZO L. REV. 545 (2014).

⁷ See McCall, Brian Michael, *Gambling on Our Financial Future: How the Federal Government Fiddles While State Common Law Is a Safer Bet to Prevent Another Financial Collapse*, ARIZONA STATE L. J., VOL. 46 (2014).

⁸ See, e.g., *Las Vegas Hacienda v. Gibson*, 359 P.2d 85, 87 (Nev. 1961) (“The test of the character of a game is not whether it contains an element of chance or an element of skill, but which is the dominating element.”).

⁹ For a detailed discussion of the challenges faced by daily fantasy sports platforms, which closely resemble event contract markets but without the “economic purpose” element, see John T. Holden & Ryan Rodenberg, *Modern Day Bucket Shops? Fantasy Sports and Illegal Exchanges*, 6 TEX. A&M L. REV. 619 (2019).

¹⁰ See Stout, *supra* note 6 at 724.

¹¹ See 21.3 Percent of U.S. Population Participates in Government Assistance Programs Each Month (May 28, 2015), available at <https://www.census.gov/newsroom/archives/2015-pr/cb15-97.html>.



whether making a large purchase, entering into long-term or short-term contracts, expanding the business in certain areas, or incurring new loans. In all of these cases, the risk of change is of great economic importance to many households and businesses that the Proposed Event Contract could provide a hedging function for. In fact, the hedging utility of the Proposed Event Contract is similar to the hedging function of insurance products, the secondary trading of securities, and many other commercial derivatives contracts in that each has a clear commercial or economic purpose and is not considered “gaming.” The Proposed Event Contract squarely passes the economic purpose test.

B. Dominant Factor Test

Where questions about the appropriate characterization of partially aleatory activities arise, courts and regulators in the U.S. generally apply the “Dominant Factor Test,”¹² which states that chance needs to be the “dominant factor” in determining whether an activity constitutes gambling or wagering.

In the case of the Proposed Event Contract, chance will not be the dominant factor in determining traders’ economic exposure. To the contrary, traders are able to access vast amounts of available, reliable and relevant data regarding election sentiment, from a wealth of public opinion polls, recordings and transcripts of debates, and observations about changing regional and national economic conditions to informal information sources such as the perspectives of media pundits, conversations in barber shops and beauty salons, and even the tone of late-night comedy routines. A trader’s outcome on positions in the Proposed Event Contract will be driven primarily by the research she conducts and not on simple chance.

State Laws

In the Nadex Order, the Commission observed that (i) several state statutes¹³ on their face link the terms “gaming” or “gambling” to betting on elections, and (ii) state law definitions of the terms “wager” and “bet” were analogous to the act of taking a position in those contracts proposed to be listed.

In response to the first part of the observation raised by the Commission, as an initial matter, many state statutes,¹⁴ when referencing elections, specifically reference the outcome of one election. For example, the Nebraska statutory provision provides that a person is engaged in gambling if betting “upon the outcome of a game, contest, or election”;¹⁵ North Dakota statute defines gambling as the risking of thing of value upon “the outcome of an event, including an election or sporting event”;¹⁶ the South Carolina statutory provision prohibits betting “upon any election in this State”;¹⁷ and Texas prohibits making a bet “on the result of any political nomination, appointment, or election”.¹⁸

In those states with statutes that prohibit betting on elections, these statutes address betting on a specific election, which arguably is intended to be limited to local elections in the respective states, as

¹² See, e.g., *Las Vegas Hacienda v. Gibson*, 359 P.2d 85, 87 (Nev. 1961).

¹³ The CFTC cited various state statutes, including: 720 Ill. Comp. Stat. Ann. 5/28-1; Neb. Rev. Stat. Ann. § 28-1101; N.M. Stat. Ann. § 44-5-10; N.D. Cent. Code Ann. § 12.1-28-01; Ga. Code Ann. § 16-12-21; Miss. Code. Ann. § 97-33-1; S.C. Code Ann. § 16-19-90; Tex. Penal Code Ann. § 47.02.

¹⁴ *Id.*

¹⁵ Neb. Rev. Stat. Ann. § 28-1101(4).

¹⁶ N.D. Cent. Code Ann. § 12.1-28-01.

¹⁷ S.C. Code Ann. § 16-19-90.

¹⁸ Tex. Penal Code Ann. § 47.02(a)(2).



clearly provided in the South Carolina Code.¹⁹ In contrast, the question underlying the Proposed Event Contract relates to the cumulative results of hundreds of separate elections through States and electoral districts of the United States. The combined outcome of multiple, geographically dispersed elections is not a subject covered in any of the State statutes discussed above.

In fact, although states may have a legitimate interest in eliminating the risk of manipulation that is potentially present in a contract relating to a single local election, states do not have a demonstrable interest in a contract relating to the aggregate result of *all local elections*, whether inside or outside of the state. This point is made particularly clear by the South Carolina Code²⁰ which specifically prohibits only betting on election results in the state of South Carolina; the collective election results across the country and the party control of either chamber of the Congress should not be of interest or concern to any given state. Despite certain state statutes on their face linking the terms “gaming” or “gambling” together with betting on elections, the aggregate election result, which is the underlying question of the Proposed Event Contract, should not be interpreted to be subject to these state statutes.

Notwithstanding the above, as discussed earlier, the Proposed Event Contract serves a clear commercial or economic purpose, and thus should not be considered “gaming” or “gambling” or otherwise an illegal activity for no reason other than the fact that certain state statutes link “gaming” or “gambling” to betting on elections on its face.

Furthermore, considering the second part discussed in the Nadex Order drawing an analogy to “wager” and “bet”, the act of taking a position on the aggregate election results across all states is not similar to the state law definitions of the terms “wager” or “bet” given the lack of an aleatory element. The precise test for when a contract involves “wagering” or “betting” vary from state to state, but the principles discussed herein apply generally across the various states.

As cited in the Nadex Order, for example, under Wisconsin law, a “bet” is defined to mean “a bargain in which the parties agree that, dependent upon chance even though accompanied by some skill, one stands to win or lose something of value specified in the agreement,” but excludes any “*bona fide* business transactions which are valid under the law of contracts”.²¹ A Wisconsin court, when finding that a pyramid scheme does not fall within the exception, reasoned that the pyramid club at issue had no element of a “*bona fide* business purpose”.²²

To the contrary, as discussed earlier, the Proposed Event Contract serves the *bona fide* business purpose of risk hedging, in the same way as insurance contracts do. Though one can argue that taking a position on the aggregate election result (and thus outcome of the Proposed Event Contract) depends upon chance to a limited extent, this fact on its own does not mean that taking a position on the Proposed Event Contract is analogous to betting, as every derivatives contract necessarily involves an element of chance. This position was clearly articulated by an Illinois court when it decided which test to adopt for determining whether a contest is “one of skill or chance” under state law.²³ Having considered the “any chance test”, which would find a contest to be “gambling” if it involved any chance whatsoever, the Illinois court rejected

¹⁹ S.C. Code Ann. § 16-19-90 (“Any person who shall make any bet or wager of money ... upon any election in this State shall be guilty of a misdemeanor”).

²⁰ *Id.*

²¹ Wis. Stat. Ann. § 945.01(1).

²² See *State v. Dahlk*, 330 N.W.2d 611, 618 (Wis. App. 1983).

²³ See *Dew-Becker v. Wu*, 178 N.E.3d 1034, 1140 (Ill. 2020), reh’g denied (Sept. 28, 2020).



this standard, finding instead that the “any chance test” results in “essentially no test at all, as every contest involves some degree of chance.”²⁴

As discussed above, in the case of the Proposed Event Contract, chance will not be the dominant factor in determining a participant’s economic exposure, which, instead, will be driven primarily by the research performed. In addition, where the opportunity for *bona fide* risk hedging is present and contracts trade on an organized and regulated market, the activity should not be considered illegal gambling, wagering or betting under state law. Though states have an interest in prohibiting these illegal activities, which are different from economic hedging activities, the Proposed Event Contract, like other event contracts, should be considered legal hedging activities. Any concerns that states might have with respect to the Proposed Event Contract are further mitigated by the fact that the Proposed Event Contract will be listed and traded on a federally regulated platform.

III. The Proposed Event Contract should not be considered contrary to the public interest

The CFTC stated in the Nadex Order 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 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 Commodity Futures Modernization Act of 2000. The restored economic purpose test calls for an evaluation of an event contract’s utility for hedging and price basing purposes. As discussed above, the Proposed Event Contract serves the economic hedging purposes. Additionally, we are aware of the extensive research that has been performed and presented to the Commission as to the hedging and price basing functions that could be served by the Proposed Event Contract.²⁵

Although the CFTC noted in the Nadex Order that it has the discretion to consider other factors in addition to the economic purpose test in determining whether an event contract is contrary to the public interest, the CFTC concluded that the political event contracts considered in the Nadex Order could potentially be used in ways that would have an adverse effect on the integrity of elections, for example by creating monetary incentives to vote for particular candidates even when such a vote may be contrary to the voter’s political views of such candidates.

While it is theoretically possible that mis-incentives could arise as a result of event contracts relating to particular elections, the underlying question of the Proposed Event Contract is about the cumulative results of hundreds of separate elections through States and electoral districts in the United States. The combined outcome of multiple, geographically dispersed elections does not present the potential risk of manipulation that is at least potentially present in a contract relating to a single, small-scale, local election with the expected margin of victory within relatively few voters.

Considering the various public policy considerations that have been advocated in other public comment letters, we would like to briefly add two considerations below.

Times Have Changed

²⁴ *Id.*

²⁵ See, e.g., Joseph A. Grundfest, Comment for Industry Filing 22-002 (Comment No: 69695) (September 15, 2022), available at <https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69695&SearchText=>.



Society has changed significantly in the ten years since the Nadex Order was released. We now live in a truly digital age. The largest global technology companies (often referred to as “BigTech”) harvest vast amounts of data from their platforms to generate advanced insights into various areas of importance, including the likelihood of various election outcomes, in a data-driven economy. Meanwhile, the explosive growth of election-related trading on illegal or unregulated platforms over the past decade demonstrates the strong interest that the public has in election-related contracts and the economic needs that these contracts fill. Kalshi allows businesses and individuals to access a regulated platform responsive to their needs and interests. The public interest would be served, not harmed, by the approval of the Proposed Event Contract on a regulated U.S.-based market.

Comparison to Unregulated Alternatives

There are currently two pure prediction markets operating in the United States under Staff no-action positions, IEM and PredictIt.²⁶ In addition, a number of decentralized prediction market platforms are also available to U.S. residents. There are also offshore platforms that combine traditional sports wagering with contracts involving politics and other world events that can potentially be accessed by U.S. persons through the use of a “virtual private network”. None of these platforms are required to comply with the CFTC regulations intended to protect market participants from manipulative or fraudulent activity nor are they required to have the types of checks and mechanisms needed to fight market manipulation, preserve market integrity, and protect retail participants that the Kalshi Platform implements.

As a fully regulated and demonstrably compliant marketplace, Kalshi will take direct responsibility for protecting the integrity of the Kalshi Platform and the welfare of the predominantly retail traders (including small business owners) that are expected to participate. Moreover, all contract positions on the Kalshi Platform are limited and required to be fully cash collateralized – leverage and margin are not permitted. These measures will help protect smaller traders against significant unexpected losses.

The inclusion of the Proposed Event Contract on the Kalshi Platform under the Commission’s oversight would greatly enhance the integrity of the election contract trading market in the United States and would protect all those who trade in it. Kalshi, along with each other CFTC-regulated contract market, must comply with the Core Principles delineated in the CEA and Commission’s Regulations. At a high level, the Core Principles are designed to ensure market integrity and protect traders from fraud and abuse. Having election contracts under the Commission’s purview would replace the current scene of susceptible, manipulatable markets with the strength and integrity of an Exchange overseen by a federal regulator.

IV. Conclusion

The Proposed Event Contract serves a clear economic purpose that meets both the hedging and the price-basing needs of traders with a commercial interest in the aggregate outcome of the U.S. midterm elections. The economic benefits of the Proposed Event Contract will be greatly enhanced if it is permitted to trade on the Kalshi Platform, a designated contract market supervised by the Commission.

²⁶ The Commission’s recent withdrawal of “no-action” relief previously granted to PredictIt has allowed PredictIt to continue to operate its election trading platform through the upcoming elections cycle. See Withdrawal of CFTC Letter No. 14-130, CFTCLTR No. 22-08.



Moreover, to the extent that the common law-based “Dominant Factor Test” is applied to the Proposed Event Contract, the outcome of traders in this contract will not be derived primarily from luck or chance.

Based on the underlying extrinsic economic utility of the Proposed Event Contract to be available on the Kalshi Platform, the regulatory oversight the Kalshi DCM will be subject to, we do not believe that the Proposed Event Contract should be treated as involving “gaming” or against laws, or otherwise against public interest and should be approved by the Commission.

Sincerely,

CohenWilson LLP d/b/a DLx Law

A handwritten signature in black ink that reads "Lewis Rinaudo Cohen".

Lewis Rinaudo Cohen
Co-Founder