SPORTS EVENT CONTRACTS:
NO DICE UNLESS THERE IS AN ECONOMIC PURPOSE AND
THE EXCHANGE IS OPEN TO THE PUBLIC

STATEMENT OF COMMISSIONER DAN M. BERKOVITZ

RELATED TO REVIEW OF ERISX CERTIFICATION
OF NFL FUTURES CONTRACTS

APRIL 7, 2021

Executive Summary*: The Commission should permit a designated contract market ("DCM") to list contracts on sporting events that are designed to hedge the risks of commercial activity related to those events, including legalized sports bookmaking. However, the proposal (withdrawn) by Eris Exchange ("ErisX") to list contracts based on the outcome of football games was deficient because: (1) ErisX did not provide sufficient evidence of hedging utility; and (2) ErisX's proposed exclusion of the general public from trading the contract on the DCM would violate DCM Core Principles and CFTC regulations regarding impartial access (Core Principle 2) and antitrust considerations (Core Principle 19). A DCM cannot exclude retail participants. Core Principle 2 prohibits a DCM from imposing discriminatory access criteria on the basis of net worth, as ErisX has proposed. Core Principle 19 requires a DCM to not impose any material anticompetitive burden on trading. ErisX's proposed sporting event contracts are functionally identical to the sports bets offered by bookmakers to the general public, and are designed so that sports bookmakers may use the exchange to hedge the risks arising from selling those contracts to the public. It would be anticompetitive to allow bookmakers to trade these contracts on the exchange so they can sell them to the public at casinos, racetracks, and other betting establishments, while at the same time*

prohibiting the public from obtaining those contracts through open, transparent, competitive trading on the exchange. Although contracts involving gaming should be permitted to be traded on a DCM if they have an economic purpose, which may include hedging by sports bookmakers, gaming contracts without any such economic purpose should not be permitted on a DCM.

I. The ErisX Petition.

On December 15, 2020, the CFTC received a self-certification filed by ErisX under Regulation 40.2 for the listing of three financially settled contracts that it called "RSBIX NFL Futures Contracts" ("NFL Contracts").[1] The ErisX certification included the following assertions:

The contracts are futures contracts. According to ErisX, "[t]he proposed Contracts will be structured as a futures contract for each sports event outcome."[2]

The contracts mirror common sports bets. ErisX's certification stated that the NFL Contracts "will be listed for individual sporting events, and will include contracts based on the

[1] ErisX, CFTC Regulation 40.2(a) Certification (Dec. 14, 2020) ("ErisX Certification"), available at https://www.cftc.gov/sites/default/files/filings/ptc/20/12/ptc121520erisdcmdcm005.pdf. Regulation 40.2 permits a DCM to file a certification that a product to be listed for trading by the DCM complies with all of the requirements of the Commodity Exchange Act ("CEA") and CFTC regulations. At the outset of the 90-day review, the CFTC requested, and received, public comment on several questions related to gaming and the NFL Contracts. *See* CFTC, Questions on the Eris Exchange, LLC ("ErisX") RSBIX NFL Futures Contracts for Public Comment, available at https://www.cftc.gov/sites/default/files/filings/documents/2020/orgdcmerisquestionsre201223.pdf.

[2] ErisX Certification at 10. The NFL Contracts are more akin to binary options.

moneyline,[3] the point spread,[4] and the total points for each game."[5] ErisX's description of the NFL Contracts employs the same terminology and indicates that the contracts would function in the same manner as the moneyline, point spread, and total points sports bets offered by sports bookmakers to the general public.[6]

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[3] An ErisX moneyline contract "settles based upon the outright winner of a game. . . . The buyer of a Contract (long position) would take the position that the away team will win the game, and the seller of a Contract (short position) would take the position that the home team will win the game." The buyer posts the purchase price of the contract to the exchange, and the seller posts the sale price to the exchange. If the away team wins, the buyer of the contract receives both the purchase and sale price that was posted to the exchange, and the seller of the contract receives nothing. If the home team wins (away team loses), the buyer receives nothing and the seller receives both the purchase and sale price that was posted to the exchange. If the game results in a tie, each member's collateral is returned. ErisX Certification at 4.

[4] An ErisX point spread contract "settle[s] based upon the winner of a game after taking into account the away team's total points as adjusted by the point spread." Both the buyer and seller of the contract deposit the price of the contract to the exchange. If the buyer is correct, and the away team's adjusted points are higher than the home team's actual points, then the buyer receives its deposit plus the deposit of the seller, and the seller loses its deposit and receives nothing—or vice versa if the seller is correct. Here, too, each party to the option either receives a payout or nothing, depending on the occurrence or non-occurrence of the specified event. If the two scores after point spread are equal and thus resulting in a tie, the contract price deposited is returned to both the buyer and the seller. *Id*. at 4-5.

[5] An ErisX over/under contract "settle[s] based upon the total points scored by each team in a game, and whether the point total was over or under a predetermined point threshold (the 'over/under value')." Both the buyer and seller pay the contract price to the exchange. If the total points scored by both teams exceed the over/under value, the buyer receives its deposit and the contract price deposited by the seller, and the seller loses its deposit and receives nothing—or vice versa if the total points are less than the over/under value. If the final total points were equal to the over/under value of the contract, the contract price deposited is returned to both the buyer and seller. *Id*. at 5.

[6] *See, e.g.*, American Gaming Association ("AGA"), *The Basics of Sports Betting* (describing moneyline, point spread, and over/under), available at https://www.americangaming.org/wp-content/uploads/2020/03/AGA_Basics-of-Sports-Betting.pdf; Swain Scheps, *Sports betting for dummies*, at 43-58 (describing moneyline, point spread and over/under bets); Safest Betting Sites, Your Guide to the Safest Betting Sites, NFL Betting, Pro Football Bet Types, available at https://www.safestbettingsites.com/nfl-betting#football-bet-types ("The point spread is synonymous with the NFL, and by far the most utilized form of football wagering strategy."); Jason Radowitz, *How Does Sports Betting Work? Doc's Sports Provides the Answers* Doc's Sports Service (Aug. 3, 2020) ("Moneyline bets take some stress away. With a moneyline bet, you only need your team to win the game and don't need to worry about how much they do it by. We've all been there where we've taken a team to win by 7.5 and then a team wins by just seven. Those are the worst bad breaks and losing bets possible and not fun to endure. After the game, you'll then wish you had been on the moneyline instead. Those absolutely sting."); *see also* Robert Schmidt and Benjamin Bain, *There's a Plan to Bring Sports Gambling to the Futures Market*, Bloomberg Businessweek (Feb. 3, 2021) ("In its application, ErisX is seeking approval for three different types of contracts on NFL games, each mirroring a common type of bet. One is based on the so-called moneyline, a wager on the outright winner of the game. Another

Hedging utility. According to ErisX, the NFL Contracts would "permit Licensed Sportsbooks to manage commercial risk by hedging their exposure [to imbalances in their books]," and are "tailored to address the unique risks of Licensed Sportsbooks."[7] ErisX claimed that contracts with alternative specifications "would create a disparity between the commercial risks faced by Licensed Sportsbooks and the hedge used to mitigate the commercial risk."[8] ErisX also asserted that the NFL Contracts could be used by vendors and stadium owners to hedge their commercial risks that depend on attendance at football games because teams that win more games have better attendance and are more likely to make the playoffs and host additional games.

Compliance with DCM Core Principles. The ErisX Certification included explanations of how it believed the NFL Contracts complied with the relevant DCM core principles and CFTC regulations.

Exclusion of retail customers. ErisX proposed to limit trading in the NFL Contracts to "eligible contract participants ("ECPs") that fall into one of the following categories: (1) commercial market participants seeking to hedge their cash market exposure; or (2) designated market makers."[9] These limitations "mean that retail (non-ECP) persons and persons seeking to

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contract takes into account the point spread for the favored team. And the third is on the "over-under," or total points scored."). These types of bets are offered for a variety of sporting events, including professional football, baseball, basketball, and hockey, and for intercollegiate athletic events too. Wikipedia, *Sports betting* (explaining moneyline, point spread, and over/under bets), available at https://en.wikipedia.org/wiki/Sports_betting.

[7] ErisX Certification at 6.

[8] *Id*.

[9] *Id*. at 1.

profit based upon the outcome of particular sporting events will not be eligible to trade the Contracts."[10]

On December 23, 2020, the CFTC informed ErisX that it had determined that the NFL Contracts "may involve, relate to, or reference . . . gaming" under CFTC Regulation 40.11. The CFTC requested that ErisX suspend any listing and trading of the contracts during the pendency of a 90-day review period beginning on that date.[11] The CFTC sought public comments on a number of questions related to the certification, and received 25 comment letters in response.[12] On March 22, 2021, one day before the expiration of the 90-day review period, ErisX withdrew its certification.

ErisX officials have been quoted as stating that they may re-file another certification.[13] In light of the public comments received on the initial filing, and the potential for a subsequent

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[10] *Id*. at 4. For a natural person to qualify as an ECP, they must have invested on a discretionary basis in excess of $10 million in the aggregate, or $5 million if the transaction is for risk management purposes. For entities, the definition of ECP includes financial institutions, insurance companies, commodity pools with greater than $5 million in assets, employee benefit plans, governmental entities, SEC-registered broker/dealers, futures commission merchants, floor brokers, floor traders, and investment advisers. CEA §1a(18); 7 U.S.C. §1a(18).

[11] Letter from Christopher J. Kirkpatrick, Secretary of the Commission, CFTC, to Mr. Thomas Chippas, Chief Executive Officer, ErisX (Dec. 23, 2020), available at https://www.cftc.gov/sites/default/files/filings/documents/2020/orgdcmerissignedletter201223.pdf.

[12] Fifteen comment letters supported the listing of the contracts, seven opposed the listing of the contracts, and three letters neither supported nor opposed the listing of the contracts. Comments for Industry Filing 20-004, available at https://comments.cftc.gov/PublicComments/CommentList.aspx?id=5203.

[13] Alexander Osipovich and Dave Michaels, Wall Street Journal, NFL Futures Plan Withdrawn as Regulator Prepared to Reject It (Mar. 23, 2021), available at https://www.wsj.com/articles/nfl-futures-plan-withdrawn-by-exchange-as-regulator-prepared-to-spike-it-11616521600?st=4woyq3k67shbwg6&reflink=article_email_share&mg=prod/com-wsj.

filing, I believe that it may be helpful to provide my views on the now-withdrawn ErisX certification and some of the issues it presented.[14]

II. Standard of Review.

As enacted by Congress in the Dodd-Frank Act, CEA Section 5c(C)(5)(C) ("the CEA gaming provision") prohibits the listing of agreements, contracts, transactions or swaps in an excluded commodity[15] that involve (i) activity that is unlawful under any federal or state law, (ii) terrorism, (iii) assassination, (iv) war, or (vi) gaming, *if* the Commission determines such agreements, contracts, or transactions are "contrary to the public interest."[16] The CEA gaming provision thus requires a two-part test for the Commission to prohibit a contract that involves gaming. First, the Commission must find that a contract "involves" gaming. Second, it must determine that the contract involving gaming is "contrary to the public interest."

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[14] The views expressed in this document are solely my own and do not reflect the views of the agency, any other Commissioner, or CFTC employee.

[15] The category of "excluded commodity" includes financial measures, such as interest rates, currency rates, and economic and commercial indexes, and events associated with financial, commercial, or economic consequences. CEA §1a(19)(iv); 7 U.S.C. §1a(19)(iv). ErisX's self-certification described various financial, commercial, or economic consequences arising from the outcomes of football games. Although at first glance it may appear odd that a football game or the outcome of a football game could be considered a commodity, such a result is consistent with the broad definitions in the CEA of "commodity" and "excluded commodity." As one appellate court observed, "literally anything other than onions [can] become a 'commodity' and thereby subject to CFTC regulation simply by its futures being traded on some exchange." *Bd. of Trade of City of Chicago v. SEC*, 677 F.2d 1137, 1142 (7th Cir. 1982), *vacated as moot, SEC v. Bd. of Trade of City of Chicago*, 459 U.S. 1026 (1982). *See also CFTC v. My Big Coin Pay, Inc.*, 334 F. Supp. 3d 492, 497 ("[A]n expansive definition of commodity reasonably assures that the CEA's regulatory scheme and enforcement provisions will comprehensively protect and police the markets."); Paul Architzel, *Event Markets Evolve: legal certainty needed, Futures Industry* (March/April 2006) ("A broad interpretation of 'excluded commodity' might include betting transactions on sporting and other events."), available at https://secure.fia.org/downloads/fimag/2006/marapr06/mar-apr_eventmarkets.pdf. The nomenclature is an anachronism; the regulatory exclusions for various types of swap transactions involving these financial commodities that had been enacted as part of the Commodity Futures Modernization Act of 2000 ("CFMA") were generally repealed in the Dodd-Frank Act.

[16] CEA §5c(C)(5)(C) also authorizes the Commission to prohibit by rule or regulation other "similar activity" that the Commission determines, by rule or regulation, to be contrary to the public interest.

The Commission has interpreted the "public interest" test in the CEA gaming provision as a restoration of the "economic purpose" test that was eliminated in the Commodity Futures Modernization Act of 2000 ("CFMA").[17] The referenced economic purpose test included a requirement that an application for the listing of a contract demonstrate that the contract "reasonably can be expected to be, or has been, used for hedging and/or price basing on more than an occasional basis."[18] The Commission also has concluded it has "discretion to consider other factors in addition to the economic purpose test in determining whether an event contract is contrary to the public interest."[19]

During the Senate's consideration of the CEA gaming provision, Senator Lincoln, then-Chair of the Senate Committee on Agriculture, Nutrition and Forestry, stated that this provision was intended to enable the CFTC to prohibit the trading of derivative contracts based on sporting events:

> Mrs. Feinstein: . . . Will the CFTC have the power to determine that a contract is a gaming contract if the predominant use of the contract is speculative as opposed to hedging or economic use?
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> Mrs. Lincoln: That is our intent. The Commission needs the power to, and should, prevent derivatives contracts that are contrary to the public interest because they exist predominantly to enable gambling through supposed event contracts. It would be quite easy to construct an "event contract" around sporting events such as the Super Bowl, the Kentucky Derby, and

[17] In the Commission's 2012 NADEX Order, which prohibited the listing or trading of political event contracts, the Commission determined 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 [CFMA]." *See* In the Matter of the 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, Order Prohibiting the Listing or Trading of Political Event Contracts, at 3, available at https://www.cftc.gov/PressRoom/PressReleases/6224-12 ("NADEX Order").

[18] Economic and Public Interest Requirements for Contract Market Designation, Final Rulemaking, 64 Fed. Reg. 29217, 29222 (June 1, 1999).

[19] NADEX Order, at 4.

> Masters Golf Tournament. These types of contracts would not serve any real commercial purpose. Rather, they would be used solely for gambling.[20]

In 2011, the Commission promulgated Regulation 40.11 to implement the CEA gaming provision.[21] Regulation 40.11(a) prohibits the listing of an agreement, contract, or transaction "that involves, relates to, or references terrorism, assassination, war, gaming, or an activity that is unlawful under any State of Federal law . . . ."[22] Regulation 40.11(c) provides for a 90-day review period for any such contract that the Commission determines may involve gaming or any of the other activities referenced in Regulation 40.11(a).

During the 40.11 rulemaking comment period, the Commission was urged to further define the term "gaming" to avoid market uncertainty as to the scope of the prohibition.[23] In the final rulemaking, the Commission stated it "agrees that the term 'gaming' requires further clarification and that the term is not susceptible to easy definition."[24] The Commission declined, however, to provide such further definition, stating instead that it would "consider individual product submissions on a case-by-case basis."[25] The ErisX certification presented such a product for the Commission's consideration.

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[20] 156 Cong. Rec. S5906-07 (July 15, 2010) (statements of Sen. Diane Feinstein and Sen. Blanche Lincoln), available at https://www.congress.gov/111/crec/2010/07/15/CREC-2010-07-15-senate.pdf.

[21] Provision Common to Registered Entities, 76 Fed. Reg. 44776, 44786 (July 27, 2011) ("[The Commission notes] that its prohibition of certain 'gaming' contracts is consistent with Congress's intent to 'prevent gambling through the futures markets' and to 'protect the public interest from gaming and other event contracts.'" (internal footnote omitted)).

[22] 17 C.F.R. 40.11(a)(1).

[23] 76 Fed. Reg. at 44785.

[24] *Id*.

[25] *Id*. *See, e.g.*, *SEC v. Chenery Corp.*, 332 U.S. 194, 202-3 (1947) (an administrative agency may choose to consider and resolve issues on a case-by-case basis rather than through rulemaking).

With respect to product certifications submitted under Regulation 40.2 that may involve gaming, the Commission also reviews the certifications under the same standards that apply to all other product certifications submitted under Regulation 40.2. These include whether the proposed product complies with "applicable provisions of the Act, including core principles, and the Commission's regulations thereunder."[26]

III. Review of the NFL Contracts.

A. The NFL Contracts involve gaming.

Football is a game. Betting on the outcome of games is "gaming." The American Gaming Association ("AGA") website provides a one-page summary of the business of sports betting. Under the heading "The Basics of Sports Betting," this AGA document identifies and explains key sports betting terms and concepts, including descriptions of the moneyline, point spread, and over/under bets.

The NFL Contracts are identified by the same labels and structured to match the basic types of sports bets described by the AGA. The asserted economic purpose of the NFL Contracts—to enable sports bookmakers to hedge their gaming contracts with the public—does not undermine the conclusion that the NFL Contracts involve gaming. To the contrary, it supports this conclusion: a contract that is structured identically to gaming contracts, labelled with the same terms as gaming contracts, and designed with a purpose to hedge gaming contracts "involves" gaming.[27]

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[26] 17 C.F.R. §40.2 (a).

[27] *See* Merriam-Webster, Definition of "Involve" ("to relate closely: CONNECT"), available at https://www.merriam-webster.com/dictionary/involve; *see also* Matt Levine, You Can't Trade Football Futures, available at https://www.bloomberg.com/opinion/articles/2021-03-24/nfl-futures-betting-you-can-t-trade-on-pro-football-odds ("It is clever to argue 'no no no, this is not a *gaming* contract, this is a contract to *hedge gaming risk*,' and I applaud the ingenuity, but of course it didn't work.").

B. Hedging utility.

The Commission has interpreted the public interest test in the CEA gaming provision to encompass the economic purpose test that the CFMA deleted from the CEA. Notably, however, the CEA gaming provision does not *require* the Commission to prohibit contracts involving gaming or to prohibit a contract simply because it involves gaming; it provides the Commission with the *discretion* to prohibit them. In my view, the Commission should recognize the significant growth of sports betting as a legalized activity in recent years with significant underlying commercial activity. The Commission should permit a DCM to list contracts involving sports events where a DCM demonstrates that such contracts have an economic purpose and hedging utility related to such commercial activity.

In 2010, at the time the CEA gaming provision was enacted as part of the Dodd-Frank Act, sports betting was generally illegal in the United States, including under prohibitions on state-authorized sports betting in the Professional and Amateur Sports Protection Act ("PASPA"). Sports betting was permitted only in Nevada casinos and three states hosted sports lotteries or permitted sports pools.[28] In light of the widespread illegality of sports betting at the time, it is not surprising that sports betting contracts were held out in legislative discussions as a prime example of event contracts that would not have a legitimate economic purpose. [29]

The sports betting landscape today, however, is dramatically different from when Congress enacted the gaming provision and the Commission promulgated Regulation 40.11. In

[28] *Murphy v. NCAA*, 138 S. Ct. 1461, 1471 (2018).

[29] Neither ErisX nor any other applicant could have met this standard prior to *Murphy v. NCAA* and the subsequent legalization of sports betting in the states, since at such time there would not have been any legal economic risks to hedge.

the three years since the Supreme Court's 2018 decision invalidating PASPA,[30] sports betting in the U.S. has expanded rapidly, both geographically and in the total dollar amount of betting annually. Half of the states and the District of Columbia have legalized sports betting, and more are considering whether to do so.[31] Morningstar projects that in 2024, the aggregate amount of legal sports betting in the U.S. will reach $81 billion.[32]

Because in many states sports betting is now legal under both state and federal law, it would not be "contrary to the public interest" for the Commission to permit the listing of sports event contracts if an exchange can demonstrate that the contracts will be used to hedge commercial risks arising from lawful commercial activity related to sports betting.[33] In my view, however, ErisX did not provide sufficient evidence that the NFL Contracts would provide an effective and more-than-occasionally-used hedging mechanism for licensed sportsbooks, vendors, or stadium owners. Among other issues, for example, the AGA, which represents licensed sportsbooks, cast doubt upon the utility of the contracts, stating that the proposed contracts "pose complex legal and policy questions," and informing the Commission that "some AGA members also believe these proposed contracts will have limited utility for their individual

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[30] *Murphy*, 138 S. Ct. at 1461 (2018).

[31] These activities were permitted to continue under PASPA. *Id.* at 1471. As of March 10, 2021, sports betting is legal and operational in 20 states and the District of Columbia, and legal but not yet operational in five states. *See* American Gaming Association, *Interactive Map: Sports Betting in the U.S.*, available at https://www.americangaming.org/research/state-gaming-map/.

[32] Dan Wasiolek, *U.S. Sports Betting Worth a Wager for Investors*, Morningstar (Oct. 9, 2020), available at https://www.morningstar.com/articles/1003994/us-sports-betting-worth-a-wager-for-investors.

[33] In reviewing contracts designed to hedge economic risks arising from gaming activities that are lawful under federal and state law, such as sports betting, the Commission should be wary of using "other factors in addition to the economic purpose test" to second-guess state and federal legislatures regarding the costs and benefits or legislative decisions to permit the underlying gaming activity. On the other hand, it may be appropriate to consider such "other factors" for contracts involving gaming activities that are not permitted under state or federal law, as the Commission did in the NADEX Order with respect to political event contracts.

operations."[34] Further, ErisX provided no evidence to support its claim that the NFL Contracts could be used to hedge the non-gaming economic consequences arising from the outcomes of NFL games, such as changes in revenue for in-stadium and other vendors.

If ErisX or any other applicant can demonstrate that sports event contracts such as the NFL Contracts can be used for an economic purpose other than for gaming itself, meaning they reasonably can be expected to be used for hedging and/or price basing on more than an occasional basis, then in my view it would not be contrary to the public interest to permit their listing. To date, however, there has been no such demonstration.

C. Violations of Core Principles.

Even if a proposed contract passes muster under Regulation 40.11, it also must satisfy all the other requirements of Regulation 40.2, including compliance with the CEA core principles and CFTC regulations. In my view, contracts that exclude retail participation on a DCM, such as the NFL Contracts, do not satisfy these requirements.

Excluding retail customers from trading the NFL Contracts would violate DCM Core Principle 2 (impartial access) and Core Principle 19 (antitrust considerations). To the best of my knowledge, no DCM has ever prevented—and the CFTC has never previously permitted a DCM to prevent—retail customers from trading a contract competitively on a DCM.

[34] AGA Comment Letter at 2, available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=64800&SearchText=.

1. Core Principle 2 (impartial access).

DCM Core Principle 2 requires a DCM to "enforce compliance with the rules of the contract market, including [] access requirements . . . ."[35] In connection with Core Principle 2, CFTC Regulation 38.151 states:

> A designated contract market must provide its members, persons with trading privileges, and independent software vendors with **impartial access** to its markets and services, including:
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> (1) Access criteria that are **impartial**, transparent, and applied in a **non-discriminatory** manner . . .[36]

In the preamble to the final rule implementing Regulation 38.151, the Commission made clear its interpretation of Core Principle 2 as requiring DCMs to provide impartial, non-discriminatory access. The Commission concluded that "impartial access rules are necessary in order to prevent the use of discriminatory access requirements as a competitive tool against certain participants."[37] The Commission stated that such impartial access "will likely enhance the DCM's liquidity and the overall transparency of the swaps and futures markets."[38] The Commission emphasized that access criteria should be based only "on the financial and operational soundness of a participant, and not on factors that could bar access and result in discriminatory access or act as a barrier to entry."[39] In the notice of proposed rulemaking, the Commission specifically rejected as discriminatory any access criteria based on a person's net worth (e.g., ECP status): "The Commission believes that the requirement to provide impartial

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[35] CEA §5(d)(2), 7 U.S.C. §7(d)(2).

[36] 17 C.F.R. §38.151 (emphasis added).

[37] Core Principles and Other Requirements for Designated Contract Markets; Final Rule, 77 Fed. Reg. 366612, 36625 (June 19, 2012).

[38] *Id*.

[39] *Id*.

access requires DCMs to avoid the creation of exclusive membership standards that focus on high net worth."[40]

ErisX proposed to limit trading in the NFL Contracts to ECPs that are either (i) licensed sportsbooks, vendors, or stadium owners, or (ii) designated market makers. Under ErisX rules, a market maker must (a) meet ErisX's definition of a Professional Trading Firm; and (b) enter into a market making agreement with ErisX. According to ErisX, "[t]he foregoing limitations on eligible participants mean that retail (non-ECP) persons and persons seeking to profit based on the outcome of particular sporting events will not be eligible to trade the Contracts."[41]

ErisX's exclusion of individuals who are not ECPs is the very kind of discrimination based on net worth that the Commission has prohibited. It is blatantly discriminatory to bar retail customers with less than $10 million in discretionary investments from access to the DCM. None of ErisX's proposed access criteria relate to the permissible factors of financial or operational soundness. Moreover, if ErisX applied its access criteria in a truly non-discriminatory manner, all other persons "seeking to profit based on the outcome of sporting events"—a category that includes licensed sportsbooks, in-stadium and other vendors, and stadium owners—also would not be able to trade the contracts, and there would be nobody left to trade.

2. Core Principle 19 (antitrust considerations).

Core Principle 19 states:

> (19) ANTITRUST CONSIDERATIONS.—Unless necessary or appropriate to achieve the purposes of this Act, the board of trade shall not—

[40] Core Principles and Other Requirements for Designated Contract Markets; Proposed Rule, 75 Fed. Reg. 80572, 80578, n.51 (Dec. 22, 2010).

[41] ErisX Certification at 4.

> (A) adopt any rule or taking [sic] any action that results in any unreasonable restraint of trade; or
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> (B) impose any material anticompetitive burden on trading on the contract market.[42]

In addition to a DCM's antitrust obligations under Core Principle 19, the CEA imposes an obligation upon the Commission to foster competition. CEA Section 15 requires that in issuing any order or approving any rule or regulation of a contract market, the Commission must "take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the objectives of the [CEA]."[43] The Commission therefore has an obligation to ensure that the terms of contracts listed on exchanges do not impermissibly restrict competition.

The sports betting market as envisioned by ErisX would be anticompetitive—it would protect the bookmakers from competition by members of the public and non-market making ECPs. The market structure that would have resulted from ErisX's proposal would be one where sports bookmakers could trade amongst themselves to swap their risks and together balance their books, while preserving their exclusive ability to provide sports event contracts to the public.[44]

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[42] CEA §5(d)(19), 7 U.S.C. §7(d)(19). CFTC Regulation 38.1000 reflects the statutory language in Core Principle 9. 17 C.F.R. §38.500.

[43] 7 U.S.C. §19(b).

[44] ErisX represents that sportsbooks "seek to operate a balanced book," but limitations on bookmaking to in-state residents create "a geographic bias that favors a particular outcome." In other words, most people bet on the home team, and this makes it difficult for the bookmakers in a particular state to operate a balanced book. "For example, if the majority of customers for a Licensed Sportsbook in New Jersey are New York Giants fans who desire to place wagers backing the Giants, this will create risk imbalance." ErisX states that the NFL Contracts will permit a bookmaker in one region to offset an imbalance in its book with a bookmaker in another region who may have an imbalance in the opposite direction. Letter from Mr. Thomas Chippas, ErisX, to CFTC, Re: Commodity Futures Trading Commission Rule 40.11 Review of Proposed RSBIX NFL Futures Contracts, Dec. 29, 2020, available at https://comments.cftc.gov/PublicComments/CommentList.aspx?id=5203&ctl00_ctl00_cphContentMain_MainContent_gvCommentListChangePage=1.

Members of the public would be prohibited from accessing the DCM to either post or accept bids or offers from other market participants. The proposed restrictions on participation in the trading of the NFL Contracts thus would protect sports bookmakers from competition from retail traders and non-market making ECPs; retail customers would be required to obtain their sports betting contracts from bookmakers.

Prohibiting retail customers from accessing sports bet contracts offered on a DCM would harm the public. On a DCM, retail participants would benefit from exchange-based prices that would more accurately reflect the market's assessment of the probability of an event, rather than the odds dictated to the customer by a bookmaker.[45] On the DCM, members of the public could make or take bids or offers placed by other market participants—including the bookmakers, market-makers, and other members of the public—rather than be consigned to take-it-or-leave-it odds offered by bookmakers. The price discovery process on the exchange would be transparent, in contrast to the opaque price-setting process of a bookmaker or casino. The bid/ask spread on the exchange likely would be smaller than the commission or "vig" charged by the bookmakers.[46] The two-tier market structure that ErisX's proposal would create—a non-public

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[45] See, e.g., Ed Miller and Matthew Davidow, The Logic of Sports Betting 64 (Ed Miller 2019) ("The vast majority of lines get set through price discovery at a small handful of market making books. The retail books then use these lines to price their markets. Even if public action on one side or another of these markets is lopsided, the retail books stay firm with their prices so as not to offer arbitrage opportunities with market makers."). *See also* Steven D. Levitt, *Why Are Gambling Markets Organised So Differently From Financial Markets*, The Economic Journal, at 223-246 (Apr. 2004) ("[T]he bookmakers are able to set prices in order to exploit their greater talent, and apparently yielding greater profits than could be obtained if the bookmakers acted like traditional market makers and attempted to equilibrate supply and demand, avoiding taking large stakes in the outcomes of games.").

[46] *See, e.g., Sports betting for dummies*, at 18:

> On average, a bookmaker keeps 1 cent for every 22 cents wagered; a 4.5 percent commission. If you were to make your coin flip bet at a bookmaker, the terms would be altered slightly to your distinct disadvantage. You still lose $1 on tails, but when heads comes up, you'd only profit 96-ish cents. Even if the coin is fair, the game is tilted against you. It's a mathematical certainty that if you played forever, you'd give all your money to the bookmaker.

exchange designed to solely support the business of the dealers who would then have the exclusive ability to offer the same contracts at a mark-up to the public off-exchange—has been rejected in CFTC-regulated swaps markets[47] and is contrary to the public interest.[48]

The economic purpose test in the CEA gaming provision does not require that all market participants have an economic purpose in trading the contract—just that the contract "can be expected to be, or has been, used for hedging and/or price basing on more than an occasional basis." CFTC markets are composed of both hedgers and speculators. Once hedgers are permitted in a market, speculators must be permitted as well. Speculators have a variety of

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For the twelve-month period ending January 31, 2021, sports bookmakers in Nevada enjoyed a 7.42% winning percentage in football games. Nevada Gaming Control Board, Gaming Revenue Report, at 1 (Jan. 2021), available at https://gaming.nv.gov/modules/showdocument.aspx?documentid=17538.

[47] ErisX's NFL Contracts would create the type of bifurcated dealer-to-dealer and dealer-to-customer market structure for sports events contracts that the Commission has recently sought to prevent in the swaps market. The Commission recently restricted the practice of post-trade name give-up ("PTNGU") on swap execution facilities. *See* Post-Trade Name Give-up on Swap Execution Facilities, 85 Fed. Reg. 44693 (July 24, 2020). The use of PTNGU by swap dealers has perpetuated a bifurcated swap market, where swap dealers respond to requests-for-quotes from the "buy-side" in one market and then trade with each other on a swap execution facility in exchange-style trading to hedge those risks. In this structure, non-dealers must ask dealers for quotes for swaps, and unless they sacrifice their anonymity (and provide competitively disadvantageous position information to their counterparties) they cannot participate with the dealers or other buy-side market participants in exchange-style trading for those same swaps. One of the purposes of the Commission's prohibition on PTNGU is "promoting fair competition among market participants, including through impartial access to a SEF's trading platform." Joint Statement of Chairman Heath P. Tarbert, Commissioner Rostin Benham, and Commissioner Dan M. Berkovitz in Support of Final Rule Restricting Post-Trade Name Give Up, available at https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertbehnamberkovitzjointstatement062520.

[48] In this structure bookmakers would be operating what essentially would be "bucket shops" for the contracts traded on the exchange. *See, e.g.*, Edwin Lefèvre, *Reminiscences of a Stock Operator*, at 16 (Wiley, 1994) ("You know how they traded in bucket shops. You gave your money to a clerk and told him what you wished to buy or sell. He looked at the tape or the quotation board and took the price from there—the last one of course. . . [T]he bucket shop would deduct both buying and selling commissions and if you bought a stock at 20 the ticket would read 20 ¼. You thus had only ¾ of a point's run for your money."). Bucket shops have been prohibited from taking quotes from commodity futures exchanges since the early 20th century. *See, e.g., Board of Trade of City of Chicago v. Christie Grain & Stock Co.*, 198 U.S. 236, 245 (1905) ("The telegraph companies all receive the quotations under a contract not to furnish them to any bucket shop or place where they are used as a basis for bets or illegal contracts."). *Christie* is often cited as establishing the economic purpose test for distinguishing between lawful hedging or speculation and gambling.

motivations, and neither the exchanges nor the CFTC has ever sought to limit speculation in DCM contracts based upon the net worth of a speculator, or to probe into the motives of speculators—other than to prohibit fraud or manipulation.[49]

The contracts proposed by ErisX would be a no-lose situation for the bookmakers, and a no-win situation for the public.[50] ErisX's proposed restrictions are both anticompetitive and harmful to retail market participants.[51]

IV. Contracts involving gaming without an economic purpose should not be permitted on a DCM

As described above, if sports event contracts involving gaming are found to have an economic purpose, they should be permitted to be listed on a DCM and retail customers cannot

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[49] In any commodity market, speculators have a wide variety of motivations, some of which are not discernible from gambling. *See, e.g.*, Thomas Hieronymus, *Economics of Futures Trading*, at 242 (Commodity Research Bureau, 1971) (identifying motives for retail commodity speculation as "to increase a relatively unimportant amount of money into an important amount," "supplementing income and gaining a return on capital," the "stimulation of the game," and that "some people receive a masochistic pleasure from losing." Hieronymus describes the reaction of one "chronic loser" who explained that he continued to trade because "he could afford it and enjoyed speculation in the same way that his friends enjoyed an occasional trip to Las Vegas even though they knew they didn't really have much of a chance of winning.").

[50] Some may object that permitting retail customers to trade the NFL Contracts on a DCM would in effect permit sports betting in states where it currently is prohibited. In my view, however, the exclusion of retail customers on the DCM is not an acceptable alternative.

[51] *See also* Competition, Concentration, and Cartels in the Swaps Market, Remarks of Commissioner Dan M. Berkovitz at the Commodity Markets Council State of the Industry 2019 (Jan. 27, 2019), available at http://www.commoditymkts.org/wp-content/uploads/2019/02/2019-01-27-Berkovitz-FINAL-Statement-CMC-Competition-Cartels-sent-to-CMC.pdf:

> I will conclude by recalling that at the dawn of the industrial age, the great industrialists claimed that dealer cartels and restraints on the forces of free market competition would enable them to both earn predictable profits and provide great benefits to the general public. For well over a century, we have consistently rejected this approach, as expressed through our antitrust laws and economic policies, and instead favored a free market approach of economic liberty, freedom to trade, and competition. Congress affirmed this fundamental economic policy for derivative markets in both the Commodity Exchange Act and the Dodd-Frank Act.

be prohibited from trading those contracts. In my view, however, based upon the gaming provision and the general purposes of the CEA, it would be contrary to the public interest to permit the listing of contracts involving gaming that do not have an economic purpose.

In Section 3(a) of the CEA, Congress finds that the transactions subject to the CEA "are affected with a national public interest by providing a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair and financially secure trading facilities."[52] In Section 3(b) Congress declares that the purpose of the Act is to further these interests "through a system of effective self-regulation of trading facilities, clearing systems, market participants and market professionals under the oversight of the Commission."[53] The CFTC describes its mission as to "promote the integrity, resilience, and vibrancy of the U.S. derivatives markets through sound regulation."[54]

Contracts or transactions involving gaming that do not have any of the purposes described in CEA Section 3(a)—managing price risks or price-basing—are not the types of contracts contemplated by Congress to be within the public interests served by the CEA or the functions of the facilities regulated by the CFTC.[55] It would be contrary to the public interests

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[52] 7 U.S.C. §5.

[53] *Id*.

[54] CFTC Mission Statement, available at https://www.cftc.gov/About/AboutTheCommission.

[55] *Compare, e.g., Sports Betting for dummies*, at 1 ("Sports betting is *fun*. Not just game-of-Parcheesi-fun or go-to-the-moves fun. I'm talking about genuine *exhilaration*. Betting takes what you already love about sports to the next level. . . When you win a bet that all of your friends said you were crazy to make, it's a flavor of elation you won't soon forget.") *with Bd. of Trade of City of Chicago v. Christie Grain & Stock Co*., 198 U.S. 236, 249 (1905) ("[Plaintiff's exchange is] a great market, where, through its eighteen hundred members, is transacted a large part of the grain and provision business of the world. . . Speculation of this kind by competent men is the self-adjustment of society to the probable. Its value is well known as a means of avoiding or mitigating catastrophes, equalizing prices, and providing for periods of want.").

identified in the CEA to permit the use of CFTC-licensed facilities solely for non-economic purposes.

V. Conclusion.

If sporting event contracts with an economic purpose, such as hedging, are allowed to be traded on a DCM, the general public must be able to access and trade those contracts on the exchange. The public cannot be barred from trading a contract listed on a DCM. However, gaming contracts without any economic purpose should not be permitted on a DCM.