Division of Legislative Services
RESEARCH REPORT

Prediction Markets:
Legal and Policy Landscape

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Overview

Prediction markets are often mistaken for being relatively new gambling or trading instruments. However, prediction markets have existed since the early twentieth century, when market prices on elections were printed daily in newspapers such as the *New York Times*[1]. Election betting was used to predict the outcomes of an election during a time when other forecasting tools, such as scientific polling, were not yet available. Additionally, the lack of telecommunication mediums like the internet prevented mass participation in the market. Yet despite this limitation, the capacity of betting markets to aggregate information proved to be a much better predictive forecasting instrument than other information available during early twentieth century.

By 1988, in an effort to offer better forecasts on elections than traditional polls, three economists from the University of Iowa began development of the first live-prediction market in the U.S., the Iowa Electronic Market (IEM). In its early stage, the IEM was limited to only faculty and students at the University of Iowa, comprising of only 200 total participants. In its first live market, the IEM successfully predicted the 1988 Presidential election winner with an accuracy much better than other traditional polls. To further increase the pool of participants, the IEM received approval from the **Commodities Futures Trading Commission** (CFTC), a federal agency, for its operation as a non-profit academic research tool, exempting the IEM from regulation under CFTC and opening participation to non-university affiliates[2]. The success of the IEM would later inspire early efforts to create new prediction markets, including the Pentagon-sponsored exchange, the Policy Analysis Market[3], which would have enabled participants to trade bets on geopolitical events such as coups, terrorist attacks, or regime changes. A majority of these endeavors, however, were shut down due to violations of federal regulations or practices deemed unethical.

Nonetheless, by 2004 the CFTC approved Hedge Street Inc.[4] as the first **designated contract market** (DCM), which is a market that offers binary contracts or a type of financial derivative. This opened the doors for the commercialization of prediction markets, departing from its origins as a non-profit academic endeavor.

Today, Kalshi and Polymarket, the biggest prediction market platforms, allow for users to place bets on a variety of outcomes such as weather, elections, geopolitical events, and sports. The two platforms have only been public for less than five years and are on pace to reach an estimated trading volume of $1 trillion by 2030. While the CFTC has designated both platforms as DCMs, the platforms' involvement in sports betting and lack of regulation into insider trading, as well as their facilitation of "unethical" trading contracts, have drawn strong opposition by state regulators. States contend that sports betting as facilitated by prediction market platforms fall under the definition of sports gambling and therefore are subject to state regulations. Prediction markets and the CFTC argue that sports betting is a type of financial derivative and falls under CFTC jurisdiction.

[1] *New York Times*, "Election Betting Slow In Wall St." Sep. 28, 1924
[2] CFTC, 1993
[3] The Policy Analysis Market, Robin Hanson
[4] Now known as crypto.com

How Prediction Markets Work

Pricing

Prediction markets, like Kalshi and Polymarket, are platforms where participants are able to buy binary contracts or financial contracts where payout is dependent on a yes or no proposition. Each event that a participant places their bet on pays out if that event occurs, and its price reflects the market's estimated probability of that event. For example, a contract priced at ±$0.35 means that the market predicts a 35% chance of the event occurring or not occurring. Participants can buy multiple contracts (100 contracts would cost $35.00) and depending on the occurrence of that event, participants can realize a profit or a loss. All contracts settle at $1 if the event occurs or $0 if the event does not occur.

Resolution and Settlement

In the example above (not calculating commission fees), buying 100 contracts for the market price of $0.35 would provide a payout of $100 ($65 profit) if the event occurred or -$35.00 loss if the event did not occur. The resolution or settlement of a contract under prediction markets is slightly different than some financial derivatives which are resolved based on observable prices[5]. Prediction markets settle their contracts based on events, the definitions of which can be ambiguous and the sources for verifying the occurrence of that event can be contested. Therefore, in every binary contract hosted by prediction market platforms, the definition for the event must be defined as well as the conditions that would resolve the event and the source to verify the occurrence of the event. While this process creates immediate settlement in predicating sporting events due to the easily and trusted verifiability of a sporting event, political events are more complex to verify. For example, a contract on if a presidential candidate *wins* an election but lacks in defining if winning means "winning the popular vote" or "winning the electoral vote."

Figure 1. Example of a Prediction Market Contract.

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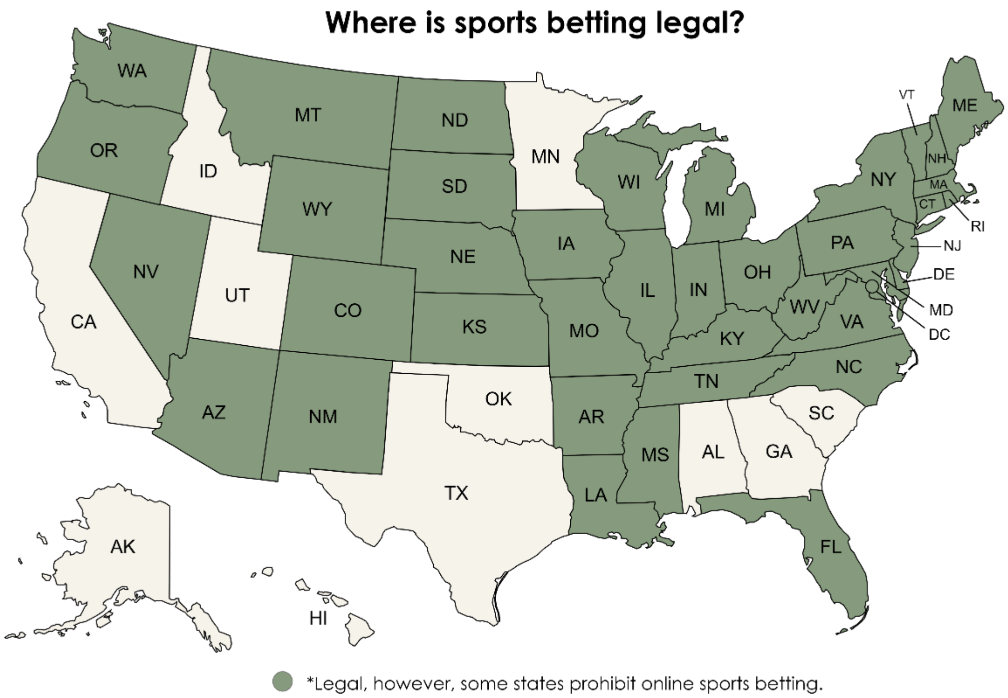
[5] Stock prices, gold prices, interest rates

Prediction Markets and Sports Betting

Prediction markets have been in operation relatively uncontested. The contracts offered in prediction markets have been defined by the CFTC as a form of financial instruments. However, with the growing popularity of sports betting and the legalization of the activity by 40 states, prediction market platforms recently [began offering sports-event contracts](). To the 11 states where sports betting is illegal, and some states where it is legal, sports betting contracts offered through prediction market platforms are indistinguishable from traditional sports betting and therefore fall under their regulatory authority. The CFTC and prediction market platforms, however, argue that the sports betting contracts offered under prediction markets are different operationally and legally.



This difference in legal interpretation has resulted in a series of legal battels regarding prediction markets, with states suing prediction market platforms for violating state gambling laws and the CFTC challenging state efforts to ban or restrict prediction markets. To better understand the legal landscape surrounding this issue, this section briefly examines how prediction markets operate and how they compare with conventional sports betting markets.

Operation and Procedures: Prediction Markets & Traditional Sportsbook

The Opponent

The overarching difference between prediction markets and gambling is in who the "opponent" is. In prediction markets, the "opponent(s)" are the participants within that market. This structure functions in much the same way as future markets are structured, which require two participants on opposite sides of the market. Meanwhile, in gambling, particularly sports betting, participants compete against the "house" or the platform facilitating the wagers.

Revenue Generation

In prediction markets like Kalshi or Polymarket, revenue is mainly generated from transaction fees, and bid-ask spread fee or the fractional difference between the buy and sell contract price. In sports betting, however, revenue is generated by the "house" or the sportsbook baking a margin into the odds. This is often termed as the "vig." Because sportsbooks act as the house and take opposite sides of a wager, this model, unlike the prediction market business model, exposes sportsbooks to financial risk.

Regulatory Structures and Oversight

Currently, sports betting, the wagering on the outcome of a sporting event, is legal in at least 39 states (33 of which allow for online sports betting) and illegal in 11 states. Sports betting is also directly regulated under state law and is a source of revenue for many states. Prediction markets, conversely, are DCMs that facilitate the trade of financial derivatives and are regulated under the exclusive jurisdiction of the CFTC.

Financial Derivatives

The structural differences between prediction markets and sportsbooks have become central to ongoing regulatory debate. However, at the core of the legal dispute is whether prediction markets offering sports betting should be classified as a form of financial instrument such as a financial derivative or gambling. To examine this legal dispute in greater detail, this section provides an overview of how financial derivatives operate as a form of financial instrument.

In broad terms, financial derivatives are contracts between two parties. The value of the contract is derived from the price of an asset which fluctuates based on the real market value of that asset. There are four types of financial derivatives, and each type functions as a tool to **hedge risk** or to **speculate** on the value of an underlying asset. The four types of financial derivatives include options, futures, forwards, and swaps. For purposes of brevity and relevance to the specific subject of this report, this report will highlight only futures and swaps.

Futures are a type of financial derivative where two parties enter a contract to buy or sell an asset at a future date. For example, if an investor wanted to purchase gold without owning the physical gold and the investor wanted to protect his investment from fluctuations in the price of gold, the investor could enter into a futures contract with a gold dealer and buy gold at a fixed price in the future. Depending on how the value of gold changes in the future, the investor or gold dealer could increase or lose in their investment.

Swaps are a type of financial derivative where two parties, mostly investors and large corporations, enter a contract to exchange or swap a scheme of payments into another one of a different nature. For example, assume an individual entered into a financial contract with a variable rate loan. This means that the interest rate of that loan varies and fluctuates which can place that individual at a financial risk. To mitigate risk and uncertainty, entering into a swap contract can allow that individual to swap their variable rate to a fixed rate.

Legal Disputes

The legal dispute surrounding prediction markets and sportsbooks arise because at the surface, prediction markets and sportsbooks betting involves consumers taking positions on future outcomes. In both prediction markets and sportsbooks betting, the consumers are betting on an unknown event. However, Kalshi and other prediction market operators argue that the *economic and financial consequence* underlying sports-event contracts they host are what makes them different from recreational sports betting.

CFTC and Prediction Market Operators Arguments

The CFTC and developers of prediction market platforms raise two points in defense that sports-event contracts are not a form a gambling. The first point raised is that prediction market operators offer a type of financial derivative, which is evident by the economic and financial consequences underlying a sporting event. Secondly, financial derivatives are a form of financial instrument that is subject to regulation under the **Commodity Exchange Act**[6] (CEA) which falls under the jurisdiction[7] of the CFTC.

> ***Swap***: *any agreement, contract, or transaction ... that provides for any purchase, sale, payment, or delivery … that is dependent on the occurrence, nonoccurrence, or the extent of the occurrence of an event or contingency associated with a* ***potential financial, economic, or commercial consequence.***

In a recent case, *Kalshiex, LLC v. Flaherty*, the United States Court of Appeals for the Third Circuit[8] granted Kalshi a preliminary injunction preventing New Jersey from enforcing a state law against its sports-related event contracts. The Court held that sports betting contracts offered by a prediction market operator, Kalshi, are swaps and that New Jersey's gambling laws are preempted from regulating federally licensed DCMs.

The Court reasoned that the outcome of a sports event is associated with a~~,~~ "potential financial, economic, or commercial consequence," for stakeholders like sponsors and advertisers. The Court stated that the outcome of sporting events can essentially affect the revenues, valuations, and commercial decisions of broadcasters, sponsors, advertisers, and teams. This, according to the Court, is no different than how financial markets operate, which are associated with uncertain events that have a "potential financial, economic, or commercial consequence."

This argument forms the basis of the prediction market position that sporting-event contracts should be viewed as financial instruments linked to events that have financial, economic, or commercial consequences rather than recreational wagers. Additionally, in defining that sports-event contracts are swaps, prediction market operators are able to invoke the preemption rule.

States Arguments

States argue that sporting-event contracts constitute sports wagering and are therefore subject to the regulatory authority of the state and not the CFTC. In defining sports-event contracts as a form of gambling, states contest that such activity is explicitly prohibited by the CEA. States point to the process in which DCMs are able to certify their contracts and the type of prohibited activities outlined in the CEA as reasons to conclude that prediction market operators are in violation of state and federal law.

To provide context, the types of event contract wagers that DCMs can offer are numerous and require approval from the CFTC. However, there is also a process for DCMs to self-certify their event contract. Previously from 1974 to 2000, prediction market operators were required to seek pre-approval from the CFTC before they can offer event contracts. However, in 2000 Congress amended the CEA through the Dodds-Frank Act, and allowed

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6 7 USC § 1a(47)(A)
7 (C)7 USCS § 7a-2
8 Kalshiex, LLC v. Flaherty, 172 F.4th 220

prediction market operators to self-certify that their event contracts complied with the statute and CFTC's regulations. In 2010, Congress amended the CEA by enacting a "special rule" that granted authorization to the CFTC to review, and prohibit, specific types of event contracts if, based on its evaluation, the contracts are not aligned with the "public interest." The specified types of event contracts that are prohibited are the following:

(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.

Furthermore, states raise the issue that prediction market operators host contracts that go against the "public interest[9]," and are susceptible to insider trading. At the time of the publication of this report, at least 19 federal lawsuits have been filed and are currently at various stages.

In the first case filed against prediction market operators, in September 2025, *Commonwealth v. KalshiEX LLC*, the Superior Court of Massachusetts granted a preliminary injunction banning Kalshi from offering sports contracts in the state. The Court reasoned that although Kalshi is a DCM and offers derivative contracts, the sport-event contracts they offer cover outcomes such as over-under bets, game winners, and point spreads which resemble traditional sports betting and are recreational in nature. However, an appeals court granted Kalshi an emergency stay, effectively putting the ban on hold. This has driven at least 37 states to file an amicus brief in support of Massachusetts lawsuit against Kalshi.

In another case, *KalshiEX LLC. v. Martin*, the United States District Court for the District of Maryland denied Kalshi's motion for a preliminary injunction. The Court ruled that Kalshi failed to provide evidence showcasing that the CEA preempts state gaming laws when sports wagers are made on platforms like Kalshi. The Court reasoned that Congress lacked a "clear and manifest purpose" to preempt state gambling laws when enacting the CEA. Kalshi in response is currently appealing the decision in the United States Fourth Circuit Court of Appeals.

States' Legislative Approaches to Prediction Markets

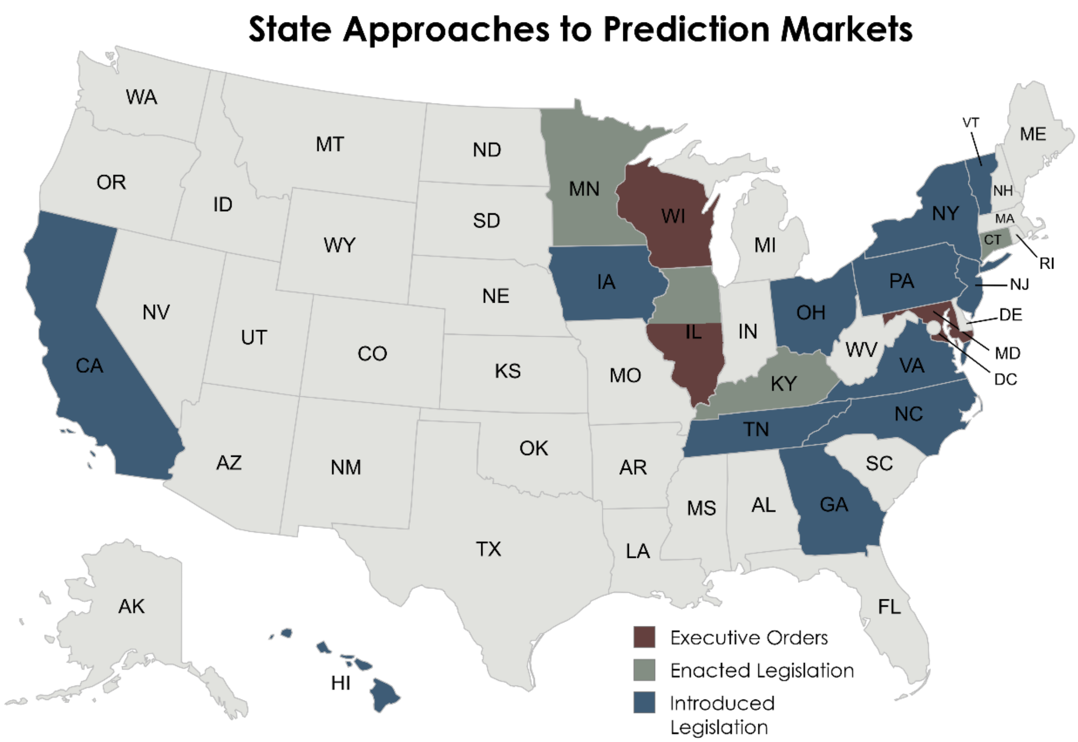
At the time of the publication of this report, 18 states have introduced at least 35 legislative measures pertaining to prediction markets. This is despite the litigation pending across the country. Four states, Kentucky[10], Connecticut[11], Minnesota[12], and Illinois,[13] remain the only states where any bills have been enacted. Other states including Illinois, Maryland, and Wisconsin signed executive orders effectively prohibiting state employees, appointees, or all employees of the executive branch from engaging in financial

[9] The public interest is an integral part of the CEA which grants the Commission authority to prohibit prediction markets from listing trades of event contracts that it determines are contrary to the public interest. 7 U.S. Code § 7a-2
[10] HB 757, HB 904
[11] HB 5229
[12] SB 3432
[13] SB 3019

transactions on prediction markets using nonpublic government information. In analyzing all 35 bills that have been introduced or enacted, we identified that the approaches states are taking fall along a regulatory spectrum from least restrictive to highly restrictive frameworks. In light of this, the legislation highlighted below is in order of least restrictive to highly restrictive legislative approaches.

Studies of Prediction Markets

Two states introduced measures that focused on directing state agencies to conduct studies on the effects of prediction markets.



*__Illinois__ also enacted legislation relating to prediction markets.

Connecticut. In 2026, HB 5229 was enacted which directed the Commissioner of Consumer Protections and other state agencies to conduct a study concerning the effects of prediction market platforms on residents of the state including to persons under the age of 21 and other concerns.

Virginia introduced HB 271 and SB 195 directing the Virginia Gaming Commission (Commission) to conduct a study evaluating the legal, economic, technological, and public-policy implications of prediction markets. The legislation requires the Commission to complete the study by October 2029.

Youth Protections and Advertising Restrictions

California, Connecticut, Georgia, Illinois, New York have introduced legislation that prohibit prediction market platforms from allowing use by or advertising to consumers under the age of 21.

Insider Information Safeguards

California and New York introduced legislation to prohibit state employees from participating in prediction market contracts if they come into possession of nonpublic information that is related to the contract they are participating into.

Licensing and Taxes

Five states have introduced legislation aimed at providing oversight of prediction market operators and levying an excise tax similar to taxes levied to gambling.

New Jersey introduced S4447 requiring prediction market operators to disclose how event contracts outcomes are determined and requires operators to implement measures to detect and prevent any fraudulent or manipulative conduct by consumers and requires operators to report the fraud to the Attorney General. Additionally, the bill requires prediction market operators to obtain a "athletic event market operator" license and partner with a sports wagering licensee to facilitate sports or horse racing betting. The legislation also imposes a 10% surcharge on prediction market revenues and prohibits public officials, candidates, and campaign staff from participating in political prediction markets.

Pennsylvania introduced HB 2497 which broadly defines event contracts and explicitly classifies exchanging, "wagers, over-under bets, moneylines, pools, and straight bets," as forms of "event outcome prediction wagering." Furthermore, the bill requires prediction markets to apply for a license with a fee of $1 million and imposes a 20% tax on gross event outcome prediction wagering revenue, or the total money received by a prediction operator from contracts. Additionally, the bill would require a 2% tax on the operators' daily gross revenue.

Kentucky enacted HB 757 which imposes a first in the nation excise tax on prediction market operators at a rate of 14.25% of the transactional fee that operators generate from consumers. The bill is currently being litigated by a coalition of prediction market operators.

Illinois enacted SB 3019 (budget bill) which amended the Sports Wagering Act by creating a new definition of "exchange wagers." This effectively places "agreements, contracts, transactions, and swaps" under the definition of "sports wagering." Additionally, the bill imposes a transaction tax equal to 1.75% on each exchange wager and is set to increase after the first five million exchange wagers to 3.5%.

Iowa introduced SF 2470 requiring prediction market operators to apply for a $10 million permit and imposes a 20% tax on the adjusted revenues received each calendar year by a prediction market operator from any event contract originating in the state. Additionally, the bill applies retroactively to tax years beginning on or after January 1, 2026.

Prohibition of Prediction Markets

Kentucky enacted HB 904 prohibiting racetracks or racing associations from participating in prediction market or contracting with providers that offer event-contracts. Additionally, the bill changed the minimum age for legal sports betting in Kentucky from 18 years to 21 years.

Minnesota. In 2026, Minnesota became the first state to enact legislation banning prediction market operators that facilitate or promote contracts on elections, sports, wars, disasters, and other activities. The same bill, SF 3432, made it a felony to operate or advertise prediction market contracts in the state. This law, however, was recently blocked by federal judge.

Hawaii introduced HB 2198 to place prediction market event contracts under the definition of gambling, effectively prohibiting the operation of prediction markets in the state. Similarly, North Carolina and Vermont have introduced legislation that prohibit prediction markets.

Delaware and Sports Betting

Although Delaware's Constitution permits a range of legalized gambling[14], the legalization of sports wagering followed a different path. In 1992, Congress enacted the Professional and Amateur Sports Protection Act (PASPA) which prohibited any new form of sports betting by any state or governmental entity. While the PASPA did not directly prohibit sports wagering in the United States, it limited new forms of sports betting and provided a number of exemptions for states which had existing sports wagering schemes legal under state law. Delaware, which operated a professional football betting game in the 1970s (Scorecard), was one of three states, alongside Oregon and Montana, that received a limited grandfather exemptions under the PASPA, while Neveda was the only state that retained full sports betting operations.

With Neveda having a near monopoly over sports betting, Delaware and the two other states often sought to expand their sports betting operations but were met with legal challenges by the federal government. These challenges continued until the U.S. Supreme Court's decision in *Murphy v. National Collegiate Athletic Association*, in which the Supreme Court held that the PASPA violated the anticommandeering doctrine embodied in the Tenth Amendment. By striking the PASPA in its entirety, the Court returned the authority of regulating sports wagering to individual states. Within weeks of the Courts decision, Delaware was the first state to expand sports wagering beyond the narrow NFL parlay that had existed under the PASPA.

Currently, the Delaware Lottery, a division of the Department of Finance, oversees the operations and promulgation of rules relating to various gambling games including sports betting. Additionally, under Delaware Code, the Director of the Delaware Lottery is required to report and certify to the State Treasurer the total lottery revenues that the state receives. According to Delaware Lottery, revenue generated from Delaware Lottery is the 5th largest source of revenue for the state.

[14] Section 17 of Article II of the Delaware Constitution

Figure 2. Source [Delaware Lottery]

Recommended Policy Approaches

In light of Delaware's history with sports betting, the Delaware General Assembly could take four policy approaches with regards to prediction markets and sports-event contracts. The recommendations are organized in order of feasibility and restrictiveness, with Recommendation 4 being the least feasible and most restrictive policy approach.

Recommendation 1: The Delaware legislature could take a neutral position and refrain from passing legislation until ongoing litigation and federal regulatory developments provide more clarity on the issue of prediction markets and sports-event contracts. While this approach could prolong regulatory uncertainty, and place Delaware's sportsbooks at a competitive disadvantage, it avoids passing legislation that could be litigated and therefore risk costly litigation and waste legislative and regulatory resources.

Recommendation 2: The Delaware legislature could carefully evaluate and direct the Delaware Secretary of Finance to study prediction markets and sports-event contracts. The study could examine the legal landscape surrounding state regulation of prediction markets, legal interpretations of cases relating to prediction markets, revenue losses or gains from prediction markets, and the impact of prediction markets on Delawareans.

Recommendation 3: The Delaware legislature could introduce legislation that seeks to mitigate the risk of insider trading within prediction markets by prohibiting state employees from participating in prediction market contracts using nonpublic information.

Recommendation 4: The Delaware legislature could require prediction market operators to meet state licensing, transparency, responsible gaming, and consumer protection standards comparable to traditional sportsbooks. This policy approach, however, is likely to face legal challenges and should therefore be crafted to withstand potential litigation.