

Prediction Markets: Emerging Compliance Considerations for Regulated Advisers

Understanding Prediction Markets

The rapid growth of prediction market platforms presents new compliance considerations for Registered Investment Advisers (“RIAs”) and other regulated financial firms. Platforms such as Kalshi and Polymarket allow participants to trade binary “yes/no” contracts tied to the outcome of events such as, but not limited to, corporate transactions, regulatory approvals, political outcomes, sporting events, and economic developments (“event contracts”). By aggregating market participants’ views, platforms generate real-time implied probabilities of a future event occurring.

These markets function as exchange-traded venues for speculation on future events. The Commodity Futures Trading Commission (“CFTC”) regulates such platforms as event contracts are generally treated as commodity derivative instruments rather than securities. Their increasing popularity raises important governance and compliance considerations for regulated firms whose employees participate in these markets.

Compliance and Enforcement Risks

Compliance Officers should consider assessing the risks that employee participation in prediction markets may pose. On February 5, 2026, Manhattan U.S. Attorney Jay Clayton emphasized this point during remarks at the Securities Enforcement Forum in New York, noting that: “A prediction market doesn’t insulate you from fraud.” This statement underscores that trading activity on prediction markets may raise serious regulatory concerns, particularly where material non-public information (“MNPI”), fraud, or fiduciary duties are implicated.

The CFTC maintains anti-fraud authority under Section 6(c)(1) of the Commodity Exchange Act and Regulation 180.1, which prohibit trading based on MNPI obtained through fraud, deception, or in breach of a pre-existing duty, such as an employee’s obligations to their employer. In addition, several ongoing legal challenges question whether certain event contracts should be classified as derivatives, or potentially as forms of unlicensed gambling.

Recent high-profile trades on prediction market platforms have raised concerns that insider or confidential information may influence trading outcomes. In February 2026, Kalshi announced that it had fined and suspended an employee of the popular YouTube personality “MrBeast”, after the employee was found to have traded approximately \$4,000 on prediction markets related to MrBeast’s videos, with “near perfect trading success”, allegedly due to his insider knowledge of MrBeast’s video content. Kalshi also reported their findings and actions to the CFTC, which issued an advisory notice on the case on February 25th.

These developments have heightened scrutiny around the risks associated with unsupervised participation in prediction markets by employees, especially in regulated firms.

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Key Regulatory Risks for Investment Advisers

Prediction markets can create several potential regulatory risks for regulated firms, particularly when contracts reference single-company outcomes such as IPO timing, mergers and acquisitions, financings, or regulatory approvals.

KEY RISK AREAS INCLUDE:

- **INSIDER TRADING AND “SHADOW TRADING” RISK**
Employees with access to MNPI through board seats, corporate access, expert networks, research, or transaction activity could engage in insider and/or shadow trading through event contracts.
- **CONFLICTS OF INTEREST AND FRONT-RUNNING**
Trading event contracts tied to portfolio companies, pending deals, or advisory engagements could create potential conflicts of interest and raise fiduciary duty concerns.
- **CIRCUMVENTION OF TRADING RESTRICTIONS**
Prediction market contracts could provide a mechanism for gaining economic exposure to companies during blackout periods, such as Regulation M restricted periods, or issuers on firm restricted lists.
- **SUPERVISORY AND AML RISKS**
Some platforms permit funding or settlement through crypto-linked mechanisms, which could create AML, recordkeeping, or supervisory gaps if employee accounts are not disclosed.
- **EMPLOYEE CONDUCT RISK**
Significant personal trading losses or excessive trading activity could raise employee conduct or financial disclosure concerns.

Practical Governance and Policy Considerations

Chief Compliance Officers should evaluate whether prediction market activity should be addressed within existing compliance frameworks. Enhanced governance measures may include:

- Reviewing the firm’s investment strategy and potential MNPI exposure and incorporating prediction market activity into the firm’s risk assessment(s).
- Updating personal trading policies to address prediction market trading with additional requirements including, but not limited to:
 - Requiring pre-clearance for event contract trades (consider scope – e.g. just business-related event contracts);
 - Requiring account disclosure and transaction reporting for prediction market trading activity; or
 - Prohibiting certain prediction market trading activity altogether.

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- Enhancing insider trading policies to clarify that MNPI restrictions extend to event contract trading and are not limited to securities transactions.
- Applying restricted list controls to event contract trades.
- Incorporating prediction market activity into quarterly and annual employee certifications.
- Providing annual compliance training that addresses prediction markets, the legal, regulatory, and reputational risks they present.

CCOs should consider taking a risk-based approach to predictive market trading and associated compliance controls based on the firm's investment strategy, risk tolerance, operational capabilities, governance oversight, and exposure to MNPI.

Optima's Recommendation

As prediction markets and the associated legal/regulatory framework continue to evolve, regulated financial institutions should proactively assess the associated legal, regulatory, and reputational risks, and implement proportionate controls (governance, documentation, training, and oversight). This will help to position firms effectively as the regulatory landscape surrounding prediction markets evolves.

About Optima Partners

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