CLIENT ALERT

Court to CFTC: Take No Action on PredictIt Event Contract No-Action Relief

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A federal court has enjoined the U.S. Commodity Futures Trading Commission from closing the PredictIt event contract market.[1] PredictIt is an online market that allows users to trade based on the anticipated outcome of political events. Staff of the CFTC granted a no-action letter to PredictIt in 2014, stating that staff would not recommend an enforcement action against PredictIt. Staff rescinded that relief in 2022, prompting users of the market to challenge that rescission. Although the court's decision only temporarily enjoins the CFTC from shuttering PredictIt while the matter pends before the U.S. District Court for the Western District of Texas, the decision is significant for its finding that both the issuance and revocation of an agency's staff no-action relief may constitute a "final agency action;" a view that is contrary to that of other federal circuit courts.

Given that many agencies beyond the CFTC use staff no-action relief to address specific issues, the Fifth Circuit decision has the potential to impact no-action relief generally, rather than just the CFTC's use of no-action relief. Agencies oftentimes rely upon the no-action relief process as an informal mechanism to address complicated regulatory issues in an expedited manner relative to using an agency order or rulemaking. To the extent the Fifth Circuit's reasoning holds, and the withdrawal of staff no-action relief is found to constitute final agency action, one potential by-product may be that no-action relief becomes rarer and will take longer to obtain, as agencies consider the possibility of increased judicial examination.

[1] *Clarke et al. v. CFTC*, No. 22-51124 (5th Cir. July 21, 2023) (hereinafter "**Order**").

With the issuance of the preliminary injunction, PredictIt may continue operations, pending the outcome of the district court action. This decision creates a circuit split concerning whether agency staff no-action relief is reviewable in court. Prior to this decision, the Second, Third, and Seventh Circuits had found that staff no-action relief did not constitute final agency action, meaning that a staff decision to grant, modify, or withdraw no-action relief was not eligible for judicial review under the Administrative Procedure Act ("**APA**"). With its decision in *Clarke et al.*, the Fifth Circuit has created a split on the finality of staff no-action relief.

Factual Background and Procedural History

The PredictIt market "was conceived as a data-gathering tool for academic researchers . . . . allow[ing] people to make small investments based on predicting political events, like future elections or the passage of federal legislation."[2] These small investments took the form of "event contracts" available to trade on the market. Offering these types of contracts would normally require registration with the CFTC as a designated contract market ("**DCM**"). In 2014, the CFTC issued a no-action letter to the Victoria University of Wellington in New Zealand (the "**University**") allowing it to operate PredictIt without registering as a DCM.[3] In 2022, after almost eight years of operation, the CFTC's Division of Market Oversight ("**DMO**") revoked the no-action letter and directed PredictIt to cease operations by February 15, 2023.[4] The revocation letter alleged that PredictIt had violated the terms of the 2014 no-action letter, but did not identify specific violations.

Following this revocation, the Users, a group comprised of market operators, traders, and academics who all used PredictIt, filed suit against the CFTC and requested a preliminary injunction. The Users claimed that the rescission of the no-action letter was made in an arbitrary and capricious manner and constituted the withdrawal of a license without the necessary procedural steps.[5]

As the February 15 deadline for closing PredictIt approached without a ruling from the district court, the Users filed a motion for injunction pending appeal with the Fifth Circuit. The court heard arguments in February 2023 and less than a month after arguments, in March 2023, DMO issued a new letter that (i) withdrew the original rescission of the 2014 no-action letter and (ii) "determined as a preliminary matter that [the 2014 letter was] void and should be withdrawn."[6] The new letter provided some explanation for revoking the no-action letter and gave the University an opportunity to respond. The CFTC then moved to dismiss Users' appeal, claiming it was moot, and the Users cross-moved for sanctions. A Fifth Circuit panel denied both motions, and issued an order declaring that the CFTC was "ENJOINED from closing the

2 Order at 2.

3 CFTC Letter No 14-130 (Oct. 29, 2014). Pursuant to the initial no-action relief, the University was not required to register as a designated contract market ("**DCM**"), swap execution facility ("**SEF**"), or a foreign board of trade ("**FBOT**").

4 CFTC Letter No. 22-08 (Aug. 4, 2022). Willkie discussed the no-action letter revocation in another alert, available here.

5 Order at 4.

6 CFTC Letter No. 23-03 (Mar. 2, 2023).

PredictIt Market or otherwise prohibiting or deterring the trading of Market contracts until 60 days after a final judgment in this matter."[7]

The Fifth Circuit Decision

In the Order, the court granted a preliminary injunction, halting the revocation of PredictIt's no-action relief and allowing the market to continue its operations. But what is most notable about this decision is not the court's issuance of the injunction, but rather how the court decided two threshold issues concerning the revocation.[8] First, the court found that the withdrawal of no-action relief constitutes a final agency action. And second, the court determined that the Users' lawsuit was not moot despite the updated March 2023 letter. The court's decision to classify the withdrawal of no-action relief as a final agency action is particularly significant as the finding is contrary to other circuits' holdings.

The Withdrawal of the No-Action Letter Was a "Final Agency Action"

The court considered whether the withdrawal of no-action relief constituted a final agency action. The court determined that the withdrawal of the no-action letter constituted "agency action" under the APA because the University had initially sought no-action relief as a "green light" to operate the event contract market.[9] The court found that the no-action letter constituted a "form of permission" that the court considered a "license" under the APA. Because the no-action letter constituted a "license" within the meaning of the APA, the court concluded its withdrawal was an "agency action" eligible for judicial review.[10]

The court found the withdrawal of the letter was "final" because it was unappealable and subjected impacted parties to potential enforcement proceedings. The court noted that once DMO staff decided to withdraw the letter, there was no opportunity for further appeal within the agency. Additionally, the court explained that CFTC regulations provide that beneficiaries "may rely" on no-action letters.[11] The court found that this language undermines the contention that the CFTC is in no way bound through no-action letters.[12]

The dissent rejected the finding that the no-action letter was a final agency action, pointing out that under the CFTC's regulations, no-action letters are "informal and advisory" in nature and do not "mark the consummation of [the CFTC's]

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7 Order at 5–6.

8 The court also considered whether the decision to withdraw no-action relief was committed to agency discretion and if the Users had standing to bring their action. Order at 12–15. This alert will not discuss the court's findings on those issues.

9 Order at 8.

10 Order at 9.

11 Order at 10; *see* 17 C.F.R. § 140.99(a)(2).

12 Order at 11, n.6.

decision making."[13] The dissent explained that the no-action letter process is not intended to extend rights to a party, but instead express a division's intent not to recommend an enforcement action. The dissent expressly rejected the idea that the "absence of a recommendation to prosecute [like in no-action relief] equates to formal consent."[14] The dissent also cited to case law from three other circuits that addressed no-action relief revocation. These examples, none of which concerns the CFTC, all held that no-action letters are non-binding and devoid of legal authority.[15] The dissent also made the point that neither the opinion nor the concurrence cite to a case holding that no-action relief constitutes a final agency action.

The March 2023 Letter Did Not Moot the Case

The court considered whether the Users' appeal was moot in light of the issuance of the DMO's March 2023 letter. The CFTC argued that the March letter replaced the initial withdrawal of no-action relief and provided the DMO's rationale for revocation. Additionally, the CFTC argued that the new letter provided the University with an opportunity to "submit any objections" regarding the revocation.[16] The court rejected those arguments, finding that "[p]ost-filing events do not moot a case '[a]s long as the parties still have a concrete interest in the outcome of the litigation.'"[17] The court also emphasized that the fact that the University "can try to change the DMO's mind does not change the fact that the DMO has declared the no-action letter 'void.'"[18]

Next Steps

With the preliminary injunction, PredictIt can continue to operate while waiting for the district court decision. The case returns to the district court, which has not yet ruled on the initial complaint asking the court to "hold unlawful and set aside" the revocation of the no-action letter as arbitrary and capricious.[19] The CFTC has also filed a motion to transfer venue to the District of Columbia. Although it is yet to be seen how the district court will examine the revocation of no-action relief under an arbitrary and capriciousness standard, this is likely not the final time the issue will appear before a court, especially now that the Fifth Circuit has created a split with other federal circuit courts.

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13 Order at 24.

14 Order at 25.

15 *Trinity Wall St. v. Wal-Mart Stores, Inc.*, 792 F.3d 323, 331 (3d Cir. 2015); *Board of Trade of City of Chicago v. SEC*, 883 F.2d 525, 530 (7th Cir. 1989); *New York City Emps.' Ret. Sys. v. SEC*, 45 F.3d 7, 12 (2d Cir. 1995).

16 Order at 11.

17 Order at 6.

18 Order at 7.

19 Brief for Petitioner at 7, *Clarke et al., v. CFTC*, Case No. 1:22-cv-00909 (W.D. Tex. Sept. 9, 2022).

If you have any questions regarding this client alert, please contact one of the authors, any member of our CFTC team listed below, or the Willkie attorney with whom you regularly work.

Willkie has a dedicated team of attorneys with extensive knowledge and experience in all aspects of the Commodity Exchange Act and the CFTC regulatory regime. We would be pleased to assist on your matters.

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