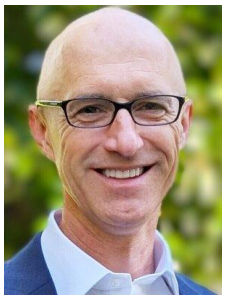
Should Prediction Markets Allow Trading On Nonpublic Info?

By **Jan Jindra and Angela Golemac** (February 19, 2026)



Jan Jindra

Angela Golemac

Prediction market platforms, such as Polymarket and Kalshi, allow participants to trade on the likelihood of events related to elections, geopolitics, corporate gatherings and cultural outcomes.

Polymarket, which purports to be the world's largest prediction market, has drawn particular attention following a wager on the U.S. capture of Venezuelan President Nicolás Maduro in January, in which an unknown trader reportedly earned roughly $400,000 after placing large bets just hours before the military operation became public.

The timing and concentration of these trades have fueled speculation that participants with access to private information may be profiting in prediction markets.

Following this and similar incidents, prediction markets have become a subject of considerable interest to the media, regulators and policymakers.[1] In particular, recent trading activity has raised questions about whether some participants may be engaging in trading that is based on material nonpublic information or information that has not been publicly disclosed and that would reasonably be expected to influence market prices if it were known.

Prediction market platforms operate under the U.S. Commodity Futures Trading Commission's jurisdiction, but within an evolving regulatory framework. The CFTC prohibits trading on MNPI in futures and swaps markets, particularly under Section 6(c)(1) of the Commodity Exchange Act and Regulation Rule 180.1.[2] However, there is some ongoing uncertainty about how existing derivatives and anti-fraud rules, written for traditional markets, apply to event-based contracts.

Reflecting the uncertainty surrounding the regulatory framework for prediction markets, on Jan. 20, CFTC Chair Michael Selig announced a review of the agency's rules to assess whether the current regulatory framework adequately addresses emerging markets such as prediction market platforms.[3]

Advocates of a laissez-faire approach to prediction markets argue that these markets aggregate dispersed information more effectively than polls or expert forecasts, in part because trading by better-informed participants can rapidly move prices toward accurate outcomes. Others, however, worry that unclear rules governing informed trading in prediction markets — and lax enforcement of those rules — invite manipulation, unfairness and the misuse of insider information, eroding institutional trust.

In this article, we review economic arguments and consider their implications for and against allowing informed trading on the prediction markets. We also discuss recent developments in the regulatory environment of prediction markets.

Recent Instances of Unusual Trading Concerns on Polymarket

In early January, an anonymous trader, new to Polymarket, earned nearly $400,000 by

placing a series of trades betting that Maduro would lose power.[4] The account placed the largest trade just minutes before a secret U.S. military operation became public.

At the time of the largest trade, the market implied only an 8% probability of Maduro's ouster. After the news broke, prices surged. Market observers flagged the activity as suspicious, noting the absence of public signals that could plausibly justify such confidence, as well as the timing and concentration of bets using a new account.[5]

A similar pattern of trading was also observed leading up to announcements of the 2025 Nobel Peace Prize and Google's Year in Search 2025 rankings.

María Corina Machado, a leader of the opposition to Maduro, was not viewed as a leading contender for the Nobel Peace Prize on Polymarket until the evening before the announcement.[6] During a 90-minute period, trading activity increased the event contract price sharply, implying that the probability of her winning rose from 3.6% to more than 70%.[7]

Comparable concerns arose when a trader reportedly earned nearly $1 million on Polymarket by correctly predicting outcomes in markets tied to Google's Year in Search 2025 rankings, with unusually accurate bets on niche outcomes and a 22-for-23 success rate.[8]

These examples are not isolated. Together, they suggest a recurring pattern in prediction markets tied to sensitive or hard-to-forecast events. Prices abruptly move shortly before public announcements that disclose new and unexpected information. These movements are driven by a small number of unusually large high-conviction trades that do not appear to be explained by chance in the mix of public information.

While the risk of trading based on MNPI exists across prediction market platforms, Polymarket may present a greater opportunity for such trading due to less strict identity verification and the difficulty of tracing trades to specific individuals.[9] For example, Kalshi, another prediction market, more expressly forbids trading on MNPI and supports developing regulations limiting such trading. However, it remains unclear whether self-monitoring alone can reliably detect and deter informed trading in practice.[10]

Current Regulatory Oversight of Prediction Markets

Governments have historically restricted corporate insider trading to preserve confidence in markets and public institutions.[11] Trading by corporate insiders raises concerns about fairness and fiduciary duty, while trading by public officials on classified or confidential information raises additional concerns about corruption and abuse of power.

Prediction markets fall under the oversight of the CFTC because event contracts are treated as derivatives.[12] Investigating and ultimately proving the misuse of MNPI information in court, however, is resource-intensive. As a result, some observers have questioned whether effective enforcement may be constrained by the CFTC's comparatively limited staffing and resources compared to agencies such as the U.S. Securities and Exchange Commission and the U.S. Department of Justice.[13] It is possible that regulators may rely on interagency coordination, with agencies collaborating and sharing expertise in enforcing rules curbing trading on MNPI.

While the CFTC has jurisdiction over event contracts, it has not finalized clear rules defining which event contract categories may be offered on prediction markets. In 2024, the CFTC

proposed, but did not finalize, rules clarifying the definition of gaming as it pertains to event contracts.[14] That proposal would have classified many contracts tied to elections, sports and awards as impermissible if offered on a regulated U.S. exchange, effectively limiting the ability of prediction market platforms to operate within the CFTC's framework.[15]

However, on Jan. 20, as part of his "Future-Proof" initiative, Selig announced that existing derivatives regulations were designed for traditional futures markets and do not adequately address newer products such as prediction markets.[16] Selig has called for modernized, tailored rules that would provide greater regulatory clarity while allowing prediction markets to develop domestically without relying on ad hoc enforcement.

Regulatory uncertainty is further compounded by jurisdictional tension between federal derivatives oversight and state gambling laws, as state regulators have increasingly challenged prediction market contracts tied to sports and other events as unlicensed wagers.[17]

Legislative responses have also emerged. In response to trading on MNPI concerns in prediction markets, Rep. Ritchie Torres, D-N.Y., introduced the Public Integrity in Financial Prediction Markets Act.[18] The bill would prohibit federal elected officials, political appointees, executive branch employees and congressional staff from trading prediction market contracts tied to government policy, government action or political outcomes when they possess, or could reasonably obtain, MNPI through their official duties.[19]

MNPI Improvements in Market Efficiency

Proponents of the laissez-faire approach to trading based on MNPI argue that it can improve the informational content of prices.[20] When traders possess MNPI about a future event and trade on it, their trades push prices toward the "true value." Other market participants observe these price movements and update their beliefs even without knowing the source of the information. As a result, prices may incorporate relevant information more quickly — i.e., ahead of the disclosure of the MNPI — than they otherwise would.[21]

One line of economic research on prediction markets builds on this intuition, emphasizing that speculative markets are particularly effective at aggregating dispersed, tacit information because they reward accuracy.[22] Accordingly, prices move because participants with better information are willing to put money at risk. In that sense, informed trading is the very mechanism by which prediction markets work.

Under this framework, prediction markets can outperform traditional forecasting institutions precisely because they induce self-selection. Better-informed participants trade more aggressively and move prices toward the correct outcome, while excluding informed traders risks degrading the accuracy of prices.

This argument is broadly anchored in the seminal economic research by economists Sanford Grossman and Joseph Stiglitz, who model securities markets in which prices reflect a weighted aggregation of private signals held by informed traders.[23] In their framework, markets become informative precisely because some participants invest in acquiring information and trade on it. Excluding informed traders (i.e., traders who invest in obtaining information) slows price discovery and reduces price accuracy.

This is consistent with the findings of some empirical studies of publicly traded equities, which show that insider trading is linked to rapid price adjustments and accelerated price discovery.[24] This would suggest that informed trading can play a meaningful role in

incorporating information into prices.

Other research, however, reaches more mixed conclusions. One study finds that informed trading does not consistently move prices in the correct direction or lead to immediate price adjustment.[25] In some instances, prices show little reaction or even move opposite to what the insider information would predict, particularly when traders use strategies that obscure their trading intent.

Cross-country evidence further complicates the interpretation of insider trading's economic effects.

Studies comparing markets with different levels of enforcement find that stronger enforcement of insider trading laws reduces insider trading ahead of earnings announcements and shifts price discovery toward public disclosures.[26] In those markets, stock prices react more clearly and strongly when earnings are released, consistent with improved price efficiency.

These findings suggest that while informed trading can accelerate price discovery under some conditions, allowing insiders to freely exploit informational advantages may ultimately lead to noisier prices and less informative markets.

MNPI And Undermined Trust and Market Participation

While price accuracy is an important function of the market, it is not its only economic objective. Well-functioning markets, including prediction markets, require participation, liquidity and trust in the integrity of the market to function effectively. Some potential problems with pervasive informed trading include putting the market at risk and creating a moral hazard in which informed traders may influence the timing of disclosure or the underlying event itself.

Under the Grossman-Stiglitz framework, if prices become too informative because there are too many informed traders, the uninformed traders' rational response is not to participate. Faced with the prospect of systematically trading against better-informed counterparts, uninformed participants withdraw, causing liquidity to decline, bid-ask spreads to widen, and markets to become fragile. In the extreme, this dynamic can lead to market breakdown. Even proponents of informed trading acknowledge that prediction markets face a fundamental trade-off between attracting broad participation and achieving highly accurate prices.[27]

Pervasive trading based on MNPI also raises concerns beyond adverse selection. When traders can profit from MNPI, they may have incentives to influence the timing, content or disclosure of information, or even the underlying events themselves. Informed traders could delay or accelerate announcements, shape messaging or expend effort to affect outcomes in ways that make their positions profitable. These incentives create a moral hazard that is particularly acute in markets tied to policy decisions or real-world events.

If uninformed participants perceive that outcomes are routinely influenced or decided by those with privileged information, they may reasonably conclude that the market is unfair or stacked against them. Participation then declines not because prices are inaccurate, but because traders no longer trust the process by which prices are formed. Although prices may be accurate at isolated moments, repeated episodes of apparent trading on MNPI can erode confidence over time, ultimately leading to declining participation and market failure.

From an economic perspective, the regulatory and legislative initiatives concerning prediction market platforms do not appear to be aimed at eliminating informed trading altogether. Rather, they reflect a recognition that the misuse of certain forms of information for trading purposes could be socially costly. Markets function because participants believe that rules are enforced and no group of traders can consistently extract rents at others' expense. If such beliefs are diminished, the existence of the markets is put at risk.

For prediction markets, whose value depends almost entirely on voluntary participation and trust, this dynamic is especially important. In addition, trading by public officials on classified information can generate negative externalities by undermining trust in public institutions, imposing costs that extend well beyond the markets themselves.

Jan Jindra, Ph.D., is a principal at the Brattle Group Inc. He previously served as an assistant director at the U.S. Securities and Exchange Commission.

Angela Golemac, Ph.D., is an associate at the Brattle Group.

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