Care to Predict What Happens? Kentucky's New Prediction Markets Tax

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In the recently concluded 2026 Regular Session of Kentucky's General Assembly, there was significant activity concerning prediction markets like Kalshi and Polymarket, all with potential serious economic impact. Specifically, House Bills 757, 869 and 904 all addressed prediction market contracts in one way or another.

Via essentially a double-barrel blast against prediction markets, Kentucky has enacted what is, at its end, a 14.25% transactional-based excise tax on prediction market contracts. But in doing so, it has not "legalized" nor "regulated" this space. Or has it?

Kentucky now finds itself at the center of the battle over prediction markets in the United States. Kentucky state officials have pursued aggressive enforcement actions against prediction market platforms, and the Commodity Futures Trading Commission (CFTC) has brought its own federal litigation aimed at curbing the state's reach.[1]

Background on the Economic Impact of Sports Betting

The Supreme Court's 2018 ruling in *Murphy v. National Collegiate Athletic Association* effectively allowed states to legalize sports betting and nullified a 1992 federal law — the Professional and Amateur Sports Protection Act (PASPA).[2] The Court held that PASPA violated the Tenth Amendment's anticommandeering doctrine. Instead of passing a federal law that bans gambling, the PASPA singled out states by prohibiting states from authorizing gambling on sports.

Since the Court's ruling in *Murphy*, 39 states and Washington D.C. have legalized some form of sports betting, and the sports betting industry has boomed across the country. In 2018, American sports bettors collectively wagered $6.61 billion. In 2025, Americans

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wagered $164 billion — a dramatic 2,381% increase.[3]

Kentucky legalized sports betting in March 2023 when Governor Andy Beshear signed House Bill 551 into law, making Kentucky the 37th state to permit regulated sports wagering. Kentucky has deep roots in wagering culture stretching back nearly 150 years, anchored by the Kentucky Derby at Churchill Downs. First run in 1875, the Kentucky Derby is the oldest continuously held major sporting event in the United States. Formal betting on early Derby Days involved auction pools, pari-mutuel wagering, and bookmaking. In 2026, wagering from all sources on the Derby Day racing card totaled $340 million.[4] However, with the widespread popularity of mobile betting apps, Kentuckians can now wager far beyond "the most exciting two minutes in sports."[5]

Prediction Markets are Not Sports Betting Markets

Prediction contract markets are not sports betting markets. Typically, prediction market platforms operate by allowing users to buy and sell event contracts. An event contract allows people to speculate on the outcome of a specific event and pays its face value if the event happens and $0 if it does not. For example, a contract priced at $0.60 suggests a 60% probability, as perceived by those trading, of an event occurring before the contract's expiration. Additionally, option contracts allow a user to trade in and out of positions, unlike typical sports bets. A user could, for example, put in $50 that President Trump will sanction a certain country, and sell the position for a profit if current prediction market prices are better. In this way, option contracts operate similarly to certain stock trades.

While some sports-related prediction contracts are within the activity on these platforms, users can also invest in a variety of political and cultural events, including predicting the winner of the 2026 Nobel Peace Prize, the winner of Love Island USA Season Eight, or who Spotify's Top Global Artist 2026 will be.

Because prediction markets are framed, correctly, as federally regulated event contracts and not state-regulated gambling,

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prediction markets are regulated by the CFTC as a Designated Contract Market.

Kentucky has spent decades building a regulated gambling model around horse racing, which holds great economic and cultural significance for the Commonwealth. While traditional horse wagering and sports betting are legal under Kentucky state law and regulated by the Kentucky Horse Racing and Gaming Commission (KHRGC), because prediction markets reflect probability and allow traders to enter and exit positions before an event concludes, the prediction market industry asserts that the model more closely resembles traditional financial exchanges. Others argue that because some of the underlying assets of many prediction market contracts are sporting events, they are subject to regulation by the gaming authorities.

Regardless, the Commonwealth will need to sort out its approach quickly. As sports betting has grown in popularity, so has its revenue. While the Commonwealth initially anticipated online sports wagering excise taxes would create $23 million in annual revenue, tax revenue has doubled those initial estimates, with Kentucky collecting over $46 million in 2025.[6]

A review of the 2026 legislation suggests that Kentucky lawmakers appear to have viewed prediction markets as a fast-emerging substitute or competitor for regulated sports wagering, horse racing wagering, and fantasy contests. The legislative record, such that it is, reflects concern, appropriately, that Kentucky may be limited in directly regulating prediction markets because of federal law, but that the state can still regulate Kentucky licensees, impose taxes, and prevent state-licensed gaming participants from affiliating with prediction market reforms. By passing House Bills 757, 869, and 904, Kentucky's General Assembly effectively targets prediction markets as a new form of event-based wagering that could compete with, or route around, Kentucky's regulated sports betting, horse racing, fantasy contest, and charitable gaming systems.

Kentucky House Bill 757: The Prediction Market Operator Excise Tax

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The tax created by HB 757 is, on its face, extremely broad. The bill set the prediction market operator excise tax at 14.25% of "transaction fees."

It is written to capture any prediction contract purchased within the state border of Kentucky, **but**, as written, it also subjects to tax any prediction contract involving a Kentucky resident occurring anywhere — no border limitation language was enacted addressing transactions involving Kentucky residents.

This provision alone raises significant jurisdictional and constitutional issues, particularly under the dormant Commerce Clause, given that prediction contracts purchased by, for example, a Kentucky resident while traveling in California would be subject to this tax as well. So, not only is Kentucky the first state in the country [7] to tax prediction market contracts, but the tax as presently written is virtually unprecedented in its grasp concerning out-of-state transactions involving a Kentucky resident, raising substantial questions about whether it impermissibly burdens interstate commerce.

The best indication that the Legislature sees the different industries as one is shown by rate. The 14.25% tax rate on prediction market contracts is equivalent to that which is levied upon sports betting transactions in Kentucky; however, the "tax base" is somewhat different in specificity. The tax is imposed on the "transaction fees" of a "Prediction Market Operator," and is not subject to any further deduction nor offset. "Transaction fee" is both the fee charges to complete a contract transaction and the amount paid by a consumer to purchase a contract. And, by creating a monthly tax compliance structure akin to sales and use tax, HB 757 also seeks to impose personal liability on the market platform operator, which is defined as a "Prediction Market Operator."

Excepted from being subjected to the 14.25% transaction tax are any contract of sale of a commodity or an option thereon, including any swap or derivative transaction based on agricultural commodities, with specific reference made to the Federal Commodity Exchange Act. Further, note that a prediction market may include a board of trade designated as a contract market by the CFTC.

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Personal liability, like sales and use taxes and other excise taxes imposed by Kentucky, is imposed and that liability specifically attaches to corporate officer-type positions, with such liability being personal and individual liability, both joint and several, for the transaction tax. However, there is no personal or individual liability for the tax if the involved person had "no authority to collect, truthfully account for, or pay over any tax at any time the taxes imposed become or became due."[8] Also, note the use of the word "collect," suggesting that the Kentucky Legislature believes that a Prediction Market Operator may collect such taxes from the parties to the contract, in the manner of a "trust fund" tax type structure, assuming the contract is subject to tax by Kentucky to begin with. That is a wholly different concern.

Kentucky House Bill 904: The Gaming Bill

Another large piece of legislation which worked through the General Assembly involved prediction markets and other independent gaming-related changes. HB 904, dubbed the "Wagering Consumer Protection Act," in sum bars any business regulated by the Kentucky Horse Racing and Gaming Corporation from engaging, directly or indirectly through other entities, in prediction market-related transactions. HB 904 also changed the minimum age for legal sports betting in Kentucky from 18 years to 21 years of age and banned proposition bets against individual college athletes competing for Kentucky teams. For example, a sportsbook could not offer a bet like "Will XXX, star player for the Kentucky Wildcats, score over 20 points tonight?"

HB 904 aimed to bring multiple forms of gaming under a more unified regulatory system overseen by the KHRGC. Prediction markets are federally enforced and HB 904 purports to act as a firewall to preserve authority for the KHRGC or the Kentucky Department of Revenue to regulate prediction market conduct or activity in Kentucky in accordance with applicable federal law. However, as laws and attitudes surrounding prediction markets have developed rapidly since the *Murphy* decision and America's newfound love for prediction market websites and apps, this language left room for litigation regarding the constitutionality of HB

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904.

Kentucky House Bill 869: The Tax Cleanup Bill

As is not uncommon in Kentucky legislation, there was some drama associated with HB 757. It passed overwhelmingly in the Kentucky House of Representatives and Senate, but Governor Andy Beshear vetoed several of its provisions. When the General Assembly returned after a break but prior to adjourning for this Session, the HB 757 veto was overridden by the House and the Senate, again, overwhelmingly.

HB 757 carries an effective date of January 1, 2027. HB 757, as initially passed, contained the following language: "It is the purpose and intent of the General Assembly to levy taxes on persons engaged in the operations of a Prediction Market. It is not the intent of the General Assembly to legalize these activities." But when the General Assembly returned after its short break and again before it adjourned, it enacted HB 869, a sort of tax cleanup bill with a multitude of various tax-related provisions addressed therein. Kentucky's prediction market tax was amended by HB 869, and the above-quoted text as to purpose and intent was specifically stricken by the General Assembly in HB 869. No public dialogue as to the reason has been located.

HB 869 revised the "firewall" approach by amending HB 904 to address contracts with entities offering sports events contracts or sports prediction markets and authorized administrative action by the KHRGC. Effectively, the bill tightened enforcement and focused the restriction on sports-related prediction market contracts.

Prediction Markets in Kentucky Moving Forward

With roughly three months before its January 1, 2027, effective date, it will be quite interesting to see how the industry and other state and federal regulators react to this new frontier of taxation. Litigation has commenced, with lawsuits advancing various claims already filed by the industry, the Kentucky Attorney General, and the CFTC. A growing number of states have begun acting related to prediction markets, including Illinois, Tennessee, North Carolina,

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Michigan, Ohio, and New Jersey. Kentucky is at the forefront.

Our state and local tax team will be watching intently to see how Kentucky's predictions market tax plays out in practicality and whether other states follow suit with similar legislation. You can find those future updates on our Tax Law Defined® Blog.

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[1] *Commonwealth v. KalshiEX LLC, et al.*, No. 26-CI-00689 (Ky. Cir. Ct. June 17, 2026); *Commonwealth v. QCX LLC, et al.*, No. 26-CI-00696 (Ky. Cir. Ct. June 17, 2026); *Coalition for Fair Markets v. Commonwealth, et al.*, No. 26-CI-00667 (Ky. Cir. Ct. June 12, 2026).

[2] *Murphy v. Nat'l Collegiate Athletic Ass'n*, 584 U.S. 453, 454 (2018).

[3] Aleksandra Dimitrova, How Much Money Do Americans Spend on Sports Betting, PlayersTime (Feb. 28, 2026) https://www.playerstime.com/reports/how-much-money-do-americans-spend-on-sports-betting/.

[4] Alexis Cubit, Kentucky Derby 2026 Payouts as Churchill Downs Sees Drops in Wagering, Courier Journal (May 3, 2026), https://www.courier-journal.com/story/sports/horses/kentucky-derby/2026/05/03/golden-tempo-kentucky-derby-betting-payouts-run-for-the-roses-odds-churchill-downs-gambling-records/89106648007/.

[5] *See* Racing at Churchill Downs, Churchill Downs, https://www.churchilldowns.com/racing/ (last visited Aug. 14, 2026).

[6] Complaint ¶ 39–40, *Commonwealth of Kentucky v. QCX LLC, et al.*, 26-CI-00696 (Ky. Cir. Ct. June 17, 2026); Sports Betting Tax Revenue Surges 382% as States Expand Legal Markets, Courier Journal (Dec. 10, 2025 at 02:23 PM EST), https://www.wkyt.com/2025/12/10/sports-betting-tax-revenue-surges-382-states-expand-legal-markets/; Eric Ramsey, US Sports

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Betting Revenue & Handle, Legal Sports Report (Mar. 27, 2026), https://www.legalsportsreport.com/sports-betting-states/revenue/.

[7] Since Kentucky's Tax was enacted, the states of North Carolina and Illinois have followed in taxing these contracts.

[8] Ky. Rev. Stat. § 138.507(6).

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