

Comments may also be submitted by facsimile at (301)427-2521, provided the facsimile is confirmed by hard copy submitted by mail and postmarked no later than the closing date of the comment period.

Comments may also be submitted by e-mail. The mailbox address for providing e-mail comments is [NMFS.Pr1Comments@noaa.gov](mailto:NMFS.Pr1Comments@noaa.gov). Include in the subject line of the e-mail comment the following document identifier: File No. 731-1774.

**FOR FURTHER INFORMATION CONTACT:** Jennifer Skidmore or Carrie Hubbard, (301)713-2289.

**SUPPLEMENTARY INFORMATION:** The subject amendment to Permit No. 540-1811, issued on March 31, 2006, and most recently amended on June 16, 2006, is requested under the authority of the Marine Mammal Protection Act of 1972, as amended (MMPA; 16 U.S.C. 1361 *et seq.*), the Regulations Governing the Taking and Importing of Marine Mammals (50 CFR part 216), the Endangered Species Act of 1973, as amended (ESA; 16 U.S.C. 1531 *et seq.*), and the Regulations Governing the Taking, Importing, and Exporting of Endangered and Threatened Species (50 CFR 222-226).

Permit No. 540-1811, issued to John Calambokidis, currently authorizes aerial and vessel surveys, photo-identification, behavioral observations, tagging (using suction-cup attached tags), biopsy, video and acoustic recording, and incidental harassment of all species of odontocetes and baleen whales in the North Pacific Ocean. The purpose of the modification is to enhance the examination of movements (for stock structure assessment) and habitat use of: blue (*Balaenoptera musculus*), fin (*B. physalus*), sei (*B. borealis*), gray (*Eschrichtius robustus*), sperm (*Physeter macrocephalus*), Bryde's (*B. edeni*), humpback (*Megaptera novaeangliae*) and minke (*B. acutorostrata*) whales, Mesoplodon beaked whales (*Mesoplodon* spp), Cuvier's (*Ziphius cavirostris*) and Baird's (*Berardius bairdii*) beaked whales, and bottlenose (*Tursiops truncatus*) and Risso's (*Grampus griseus*) dolphins via dart tagging. For each species, an addition of 20 takes by dart tagging are requested, with the exception of sei whales, where only 5 takes are requested. Additionally, an increase in the number of biopsy and suction-cup tagging takes (between 10 - 40 takes) for several cetacean species (fin, sperm, and short-finned pilot whales (*Globicephala macrorhynchus*) and Baird's, Cuvier's, and Mesoplodon beaked whales) are being requested in

order to better increase understanding of stock structure and behavior. Takes by Level B harassment (e.g., incidental harassment of non-target animals) are already authorized under Permit No. 540-1811 and no additional Level B harassment takes are requested. Dart tagging will occur concurrently with already permitted activities (i.e., vessel surveys, photo-identification, suction-cup tagging etc), primarily in Californian waters, though some species may be tagged opportunistically elsewhere where activities are authorized (i.e., U.S. and international waters of the Pacific including Alaska, Washington, Oregon, and other U.S. territories). The amended permit, if issued, would be valid until the permit expires on April 14, 2011.

Concurrent with the publication of this notice in the **Federal Register**, NMFS is forwarding copies of this application to the Marine Mammal Commission and its Committee of Scientific Advisors.

Documents may be reviewed in the following locations:

Permits, Conservation and Education Division, Office of Protected Resources, NMFS, 1315 East-West Highway, Room 13705, Silver Spring, MD 20910; phone (301)713-2289; fax (301)427-2521;

Northwest Region, NMFS, 7600 Sand Point Way NE, BIN C15700, Bldg. 1, Seattle, WA 98115-0700; phone (206)526-6150; fax (206)526-6426;

Alaska Region, NMFS, P.O. Box 21668, Juneau, AK 99802-1668; phone (907)586-7221; fax (907)586-7249; and

Southwest Region, NMFS, 501 West Ocean Blvd., Suite 4200, Long Beach, CA 90802-4213; phone (562)980-4001; fax (562)980-4018.

Dated: May 1, 2008.

**P. Michael Payne,**

Chief, Permits, Conservation and Education Division, Office of Protected Resources, National Marine Fisheries Service.

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## COMMODITY FUTURES TRADING COMMISSION

### Concept Release on the Appropriate Regulatory Treatment of Event Contracts

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Request for Public Comment.

**SUMMARY:** The Commodity Futures Trading Commission (Commission or CFTC) is soliciting comment on the appropriate regulatory treatment of financial agreements offered by markets

commonly referred to as event, prediction, or information markets.<sup>1</sup> For ease of reference and to avoid classification issues, these financial agreements are referred to herein as event contracts. In general, event contracts are neither dependent on, nor do they necessarily relate to, market prices or broad-based measures of economic or commercial activity.<sup>2</sup> Rather, event contracts may be based on eventualities and measures as varied as the world's population in the year 2050, the results of political elections, or the outcome of particular entertainment events.<sup>3</sup> The Commission's staff has received a substantial number of requests for guidance on the propriety of trading various event contracts under the regulatory rubric of the Commodity Exchange Act (CEA or Act). Given the substantive and practical concerns that may arise from applying federal regulation to event contracts and markets, the Commission believes that it is appropriate to solicit and consider the public's comments in advance of issuing any definitive guidance.

**DATES:** Comments must be received by July 7, 2008.

**ADDRESSES:** Comments should be sent to the Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581, Attention: Office of the Secretariat. Comments may be sent by facsimile to 202.418.5521, or by e-mail to [secretary@cftc.gov](mailto:secretary@cftc.gov). Reference should be made to the "Concept Release on the Appropriate Regulatory Treatment of Event Contracts." Comments may also be submitted through the Federal eRulemaking Portal at <http://www.regulations.gov>.

**FOR FURTHER INFORMATION CONTACT:** Bruce Fekrat, Special Counsel, Office of the Director (telephone 202.418.5578, e-mail [bfekrat@cftc.gov](mailto:bfekrat@cftc.gov)), Division of

<sup>1</sup> See Michael Gorham, *Event Markets Campaign for Respect*, Futures Industry Magazine (Jan./Feb. 2004); Justin Wolfers and Eric W. Zitzewitz, *Prediction Markets*, 18 J. Econ. Persp. 107 (Spring 2004); Robert W. Hahn and Paul C. Tetlock, *Using Information Markets to Improve Public Decision Making*, AEI-Brookings Joint Center for Regulatory Studies Working Paper 04-18 (March 2005); Hal R. Varian, *Can Markets Be Used to Help People Make Nonmarket Decisions?*, The New York Times (May 8, 2003).

<sup>2</sup> The term event contract is not intended to encompass contracts that generate trading prices that predictably correlate with market prices or broad-based measures of economic or commercial activity, or contracts which substantially replicate other commodity derivatives contracts, such as binary options on exchange rates or the price of crude oil. The aforementioned contracts are unambiguously subject to CFTC regulation.

<sup>3</sup> See, e.g., Retired claims list at the Foresight Exchange, available at <http://www.ideosphere.com/fx-bin/ListClaims>.

Market Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

#### SUPPLEMENTARY INFORMATION:

### I. Introduction

#### A. Purpose of the Release

Since 2005, the Commission's staff has received a substantial number of requests for guidance on the propriety of offering and trading financial agreements that may primarily function as information aggregation vehicles. These event contracts generally take the form of financial agreements linked to eventualities or measures that neither derive from, nor correlate with, market prices or broad economic or commercial measures. Event contracts have been based on a wide variety of interests including the results of presidential elections, the accomplishment of certain scientific advances, world population levels, the adoption of particular pieces of legislation, the outcome of corporate product sales, the declaration of war and the length of celebrity marriages. In response to the various requests for guidance, and to promote regulatory certainty, the Commission has commenced a comprehensive review of the Act's applicability to event contracts and markets. To further its review, the Commission is issuing this release to solicit the expertise of interested persons, including CFTC-registered markets, exempt markets, over-the-counter derivatives dealers, capital market participants, legal practitioners, state and federal regulatory authorities, academicians and research institutions with respect to the practical and regulatory issues relevant to regulating event contracts and markets.

Broadly speaking, the Commission must determine:

1. Whether event contracts are within the Commission's jurisdiction and if so, why (or why not)?
2. If event contracts are within the Commission's jurisdiction, should there be exemptions or exclusions applied to them and if so, why (or why not)?
3. How should the Commission address the potential gaming aspects of some event contracts and the possible pre-emption of state gaming laws?

The Commission urges interested persons to provide detailed and comprehensive comments that will assist the Commission in conducting its review and analysis of the Commission's regulatory purview over event contracts, the interests that may appropriately underlie Commission-regulated transactions, and the

appropriate regulatory treatment of markets that may offer event contracts.

#### B. CFTC Experience With Event Contracts

The Iowa Electronic Markets (IEM), an electronic trading facility that functions as an experimental and academic program, is one of the better known and oft discussed real-money event markets currently in operation.<sup>4</sup> The IEM operates in part pursuant to a 1993 no-action letter issued by Commission staff which, without asserting jurisdiction or describing the potential parameters of the Commission's regulatory purview over the market, allows the IEM to list various event contracts subject to certain conditions and limitations for covered contracts.<sup>5</sup>

The IEM continues to be most recognized for its presidential election contracts. The IEM offers a vote share contract and a winner-take-all contract for the 2008 U.S. presidential election cycle. Its vote share contract is ultimately associated with the candidates that will be nominated by each party. Each vote share contract has a maximum value of \$1 and a contract payout that is directly based on the percentage of the popular vote received by each of the two major party candidates. For instance, a contract for a candidate who receives 40% of the popular votes cast for both candidates will be worth \$.40 at settlement.

In contrast, the IEM's 2008 presidential election winner-take-all contract will have a value of either \$1 or \$0 at settlement. The IEM's winner-take-all-contract is also associated with a specific candidate, but instead of having a payout that is tied to a particular percentage of the popular vote received by each candidate, the contract will distribute a fixed payout of \$1 to its holder if and only if the candidate referenced by the contract receives a greater percentage of the popular vote cast. Although the IEM's

<sup>4</sup> The IEM is run by the University of Iowa Departments of Accounting and Economics and the University's College of Business Administration.

<sup>5</sup> CFTC Staff Letter No. 93-66 [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,785 (June 18, 1993). This no-action letter superseded the operative terms of a more limited letter issued to the IEM in 1992. The 1993 letter's relief extends to IEM contracts based on political elections, economic indicators, and certain currency exchange rates. The letter requires that the IEM limit access to any one submarket to between 1,000 and 2,000 traders. The letter also sets the maximum amount that any single participant can risk in any one submarket at five hundred dollars. The letter makes clear that relief is premised on, among other factors, the IEM's representations concerning the market's specific manner of operation and academic purpose, and the assurance that the IEM will not receive any profit or other form of compensation from its activities.

presidential election contracts are imperfect vehicles for the discovery of information, there is some consensus on the question of whether the IEM's contracts can function capably as predictive tools.<sup>6</sup> Indeed, trading data generated by some IEM presidential election contracts arguably have produced better predictive indicators than data obtained from professional polling organizations.<sup>7</sup>

### II. Commodity Options and Futures and the Attributes of Event Contracts

The Commission, with some exceptions, has exclusive jurisdiction over two relevant types of derivative instruments—commodity options and commodity futures contracts. Section 4c(b) of the Act gives the Commission plenary jurisdiction over commodity options, and provides that “[n]o person shall \* \* \* enter into \* \* \* any transaction involving any commodity regulated under this Act which is of the character of, or is commonly known to the trade as, an option \* \* \* contrary to any rule, regulation or order of the Commission[.]” Section 2(a)(1)(A) of the Act provides that the Commission shall have exclusive jurisdiction with respect to accounts, agreements, and transactions (including options) involving contracts of sale of a commodity for future delivery. Event contracts, depending on their underlying interests, can be designed to exhibit the attributes of either options or futures contracts.

A significant number of event contracts are structured as all-or-nothing binary transactions commonly described as binary options.<sup>8</sup> Binary event contracts typically pay out a fixed amount when an outcome either occurs or does not occur. The trading of such contracts can facilitate the discovery of information by assigning probabilities, through market-derived prices, to discrete eventualities. For example, a binary contract based on whether a particular person will run for the presidency in 2012, can pay a fixed \$100 to its buyer if and only if that individual runs for the presidency in 2012. If the contract's traders believe that the likelihood of the individual's candidacy in 2012 is around 17 percent, the price of the contract will be around

<sup>6</sup> See, e.g., Michael Abramowicz, *Information Markets, Administrative Decision Making, and Predictive Cost-Benefit Analysis*, 71 U. Chi. L. Rev. 933, 950 (2004).

<sup>7</sup> See Cass R. Sunstein, *Group Judgments: Statistical Means, Deliberation, and Information Markets*, 80 N.Y.U. L. Rev. 962, 1029-31 (June 2005).

<sup>8</sup> See, e.g., Intrade Prediction Markets, Current Events Contracts at <http://www.intrade.com/jsp/intrade/contractSearch/>.

\$17, and will approximate the market's consensus expectation of the individual's candidacy.

In addition to binary event transactions, the term event contract has also been used to identify transactions, based on interests other than market prices, which resemble futures contracts. For instance, these types of event contracts can price consensus estimates of moving values, such as the number of hours the average U.S. resident spends in traffic or the share of votes that a particular candidate for political office may receive. Unlike binary transactions, and similar to any commodity futures contract, this type of contract creates continuous and ongoing obligations that are linked to moving measures or levels, as opposed to being dependent on the outcome of a single discrete occurrence.

### III. The Commission's Regulatory Purview

As discussed above, with some limited exceptions, the regulatory purview of the Act extends to and includes transactions that are either structured as options or futures when such transactions involve interests that constitute commodities under the Act. Section 1a(4) of the Act defines commodity in two distinct ways. First, Section 1a(4) specifically enumerates certain articles or goods as commodities.<sup>9</sup> Second, Section 1a(4) defines the term commodity as including those articles or goods, and services, rights or interests, "in which contracts for future delivery are presently or in the future dealt in." Therefore, an underlying interest that is not enumerated in Section 1a(4) may be a statutory commodity under the Act if it reasonably can underlie a futures contract on a forward looking basis.<sup>10</sup>

In addition to Section 1a(4), Section 1a(13) of the Act identifies certain interests as excluded commodities and thereby gives further shape to the statutory definition of commodity.<sup>11</sup>

<sup>9</sup> 7 U.S.C. 1a(4). Section 1a(4) of the Act enumerates the following commodities: wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, *Solanum tuberosum* (Irish potatoes), wool, wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil, and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans, soybean meal, livestock, livestock products, and frozen concentrated orange juice.

<sup>10</sup> See *United States v. Valencia*, No. H-03-024, 2003 WL 23174749 at \*8 (S.D. Tex Aug. 25, 2003) (noting that the determination of whether West Coast natural gas is "a commodity in which contracts for future delivery are presently or in the future dealt in," is a fact question, and that "there is no evidence that West Coast gas could not in the future be traded on a futures exchange.")

<sup>11</sup> 7 U.S.C. 1a(13). Section 1a(13) of the Act provides that:

The Section 1a(13) definition of excluded commodity is composed of four subsections. The third subsection defines the term to include any economic or commercial index that is based on prices, rates, values, or levels not within the control of any party to the relevant contract. The fourth subsection of Section 1a(13) provides that an excluded commodity includes an occurrence, extent of an occurrence, or contingency associated with a financial or economic consequence that is not within the control of the parties to the relevant transaction.

For the purpose of discussion and analysis, the types of event contracts that Commission staff has reviewed can be categorized, albeit imperfectly, as contracts that are based on narrow commercial measures and events, contracts based on certain environmental measures and events, and contracts based upon general measures and events. Narrow commercial measures quantify and reflect the rate, value, or level of particularized commercial activity, such as a specific farmer's crop yield. Narrow commercial events, on the other hand, are events that might, in and of themselves, have commercial implications, such as changes in corporate officers or corporate asset purchases.

Environmental measures can be characterized as quantifications of weather phenomena, such as the volatility of precipitation or temperature levels, that do not predictably correlate to commodity market prices or other measures of broad economic or commercial activity. By comparison, environmental events can include the formation of a specific type of storm, within an identifiable geographic region, the likelihood of which will not

The term "excluded commodity" means—

(i) an interest rate, exchange rate, currency, security, security index, credit risk or measure, debt or equity instrument, index or measure of inflation, or other macroeconomic index or measure;

(ii) any other rate, differential, index, or measure of economic or commercial risk, return, or value that is—

(I) not based in substantial part on the value of a narrow group of commodities not described in clause (i); or

(II) based solely on one or more commodities that have no cash market;

(iii) any economic or commercial index based on prices, rates, values, or levels that are not within the control of any party to the relevant contract, agreement, or transaction; or

(iv) an occurrence, extent of an occurrence, or contingency (other than a change in the price, rate, value, or level of a commodity not described in clause (i)) that is—

(I) beyond the control of the parties to the relevant contract, agreement, or transaction; and

(II) associated with a financial, commercial, or economic consequence.

predictably correlate to commodity market prices or measures of broad economic or commercial activity.

General measures can be described as measures that are not commercial or environmental measures. As such, general measures do not quantify the rate, value, or level of any commercial or environmental activity and can, for example, include the number of hours that U.S. residents spend in traffic annually or the vote-share of a particular presidential candidate. Similarly, general events, such as whether a Constitutional amendment will be adopted or whether two celebrities will decide to marry, can be described as events that do not reflect the occurrence of any commercial or environmental event. The category of general measures and events can be further divided into a multitude of subcategories, such as political or entertainment measures or events.

Since 1992, Commission-regulated exchanges have listed for trading a variety of commodity futures and options contracts with payout terms based on interests other than price-based interests. These contracts involve interests as diverse as regional insured property losses, the count of bankruptcies, temperature volatilities, corporate mergers, and corporate credit events.<sup>12</sup> While not strictly price-based, the interests underlying these contracts have been viewed by Commission staff as having generally-accepted and predictable financial, commercial or economic consequences. In other words, unlike the interests that event contracts cover, these underlying interests have been viewed as measures and occurrences that reasonably could be expected to correlate to market prices or other broad-based commercial or economic measures or activities.

### IV. Further Statutory Background

Federal regulations were initially applied to commodity derivatives trading in 1921.<sup>13</sup> At that time, Congress

<sup>12</sup> For example, the Chicago Board of Trade's catastrophe single event insurance option contracts (which are no longer listed) paid out a fixed amount if and only if insured property damage exceeded \$10 billion for a specific region during a specified interval of time.

<sup>13</sup> See, e.g., *Hearing on Futures Trading Before the House Committee on Agriculture*, 66th Cong., 3rd Sess. 1043 (1921); *Hearings on H.R. 5676 Before the Senate Committee on Agriculture and Forestry*, 67th Cong., 1st Sess. 452 (1921); *Hearings on Futures Trading Before the House Committee on Agriculture*, 67th Cong., 1st Sess. 7-9 (1921); 61 Cong. Rec. 4761 (1921) (remarks of Senator Capper, the sponsor of the Senate bill which became the Futures Trading Act of 1921 (later restyled as the Grain Futures Act of 1922 when found to be unconstitutional for its use of taxation to penalize off-exchange futures trading)).

acknowledged that commodity futures markets could benefit commerce by facilitating the hedging of commercial risks and the discovery of reliable commodity prices.<sup>14</sup> The Grain Futures Act of 1922, the forerunner to the CEA, consequently was enacted to promote the financial vitality of futures trading by limiting price manipulations and other disturbances that were prevalent at the time and widely perceived to result from excessive speculation.<sup>15</sup>

In identifying the national public interests that render federal regulation necessary, the Act focuses on the commercial benefits that well-functioning derivatives markets can provide by broadly expressing their critical functions. Customarily, hedging and price basing have been identified as two critical functions of the commodity derivatives markets.<sup>16</sup> For instance, Section 3 of the Act, as amended by the Commodity Futures Modernization Act of 2000 (CFMA),<sup>17</sup> finds that transactions subject to the CEA are affected with the national public interest because they provide a means for “managing and assuming price risks.” Section 3 of the Act also identifies price discovery and price dissemination as separate public interests warranting Federal regulation.<sup>18</sup>

<sup>14</sup> See S. Rep. No. 871 (August 23, 1922). The Congressional record is replete with discussion of the commercial importance of commodity futures trading. The record suggests that commercial interests must be able to look to properly functioning commodity futures markets for market information and products that facilitate the making of marketing, financing, and distribution decisions. S. Rep. No. 93–1131, at 12 (1974). The Congressional record also indicates that an initial purpose behind regulating commodity futures trading was to secure fair and orderly markets for producers and other commercial participants who used the markets for price basing and hedging. *Hearings on S. 2485, S. 2578, S. 2837 and H.R. 1311 before the Senate Committee on Agriculture and Forestry*, 93d Cong., 2d Sess. at 234 (1974); see also 80 Cong. Rec. 10739 (April 11, 1974).

<sup>15</sup> E.g., 61 Cong. Rec. 4761–4763 (1921) (remarks of Senator Capper); 61 Cong. Rec. 1379 (1921) (remarks of Rep. Bland); 61 Cong. Rec. 1313–1314 (remarks of Rep. Tincher, the sponsor of the House bill which became the 1921 Act); 61 Cong. Rec. 1376 (1921) (remarks of Rep. Gensman).

<sup>16</sup> Hedging occurs when positions acquired are economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise. See, e.g., 17 CFR 1.3(z) (definition of bona fide hedging). Price basing, a function of price discovery and dissemination, can occur when commercial entities enter into transactions in a particular commodity based upon commodity futures prices for that or a related commodity, oftentimes at a differential.

<sup>17</sup> Appendix E, section 108, Pub. L. 106–554, 114 Stat. 2763.

<sup>18</sup> The hedging and price basing purposes of commodity futures trading are emphasized in other provisions of the Act as well. See, e.g., 7 U.S.C. 6a, 6b, and 6c. As a matter of background, the provision in the Grain Futures Act that was the forerunner of current CEA Section 3 provided that:

Although repealed by the CFMA, former Section 5(g)<sup>19</sup> of the Act may be relevant to analyzing the findings and purposes discussed in Section 3 of the Act. Former Section 5(g) provided that the Commission could not designate a board of trade as a contract market unless the board of trade demonstrated that transactions for future delivery in the commodity for which designation as a contract market was sought “will not be contrary to the public interest.”<sup>20</sup> The public interest test of Section 5(g) included an “economic purpose” test, subject to a final test of the public interest.<sup>21</sup> The economic purpose test applied under former Section 5(g) was used to prohibit the trading of certain contracts. Notably, the economic purpose test regarding contracts appropriate for trading on a futures exchange was not necessarily congruent

Transactions in grain involving the sale thereof for future delivery as commonly conducted on boards of trade and known as “futures” are affected with a national public interest; that such transactions are carried on in large volume by the public generally and by persons engaged in the business of buying and selling grain and the products and by-products thereof in interstate commerce; that the prices involved in such transactions are generally quoted and disseminated throughout the United States and in foreign countries as a basis for determining the prices to the producer and the consumer of grain and the products and by-products thereof and to facilitate the movements thereof in interstate commerce; that such transactions are utilized by shippers, dealers, millers, and others engaged in handling grain and the products and by-products thereof in interstate commerce as a means of hedging themselves against possible loss through fluctuations in price; that the transactions and prices of grain on such boards of trade are susceptible to speculation, manipulation, or control, which are detrimental to the producer or the consumer and the persons handling grain and products and by-products thereof in interstate commerce, and that such fluctuations in prices are an obstruction to and a burden upon interstate commerce in grain and the products and by-products thereof and render regulation imperative for the protection of such commerce and the national public interest therein.

Grain Futures Act, ch. 369, 42 Stat. 998 (Sept. 21, 1922). In 1936, Congress restyled the Grain Futures Act as the Commodity Exchange Act and amended this provision to substitute the word “commodity” for “grain.” Pub. L. 74–675, section 2, 49 Stat. 1491 (June 15, 1936).

<sup>19</sup> 7 U.S.C. 7(g), as amended by the Commodity Futures Trading Commission Act of 1974, Pub. L. 93–463, 88 Stat. 1389 (1974). In 1992, Section 5(g) was redesignated Section 5(7) of the Act. See *Futures Trading Practices Act of 1992*, Pub. L. 102–546, 106 Stat. 3590 (1992). The CFMA repealed all of former Section 5 of the Act, including Section 5(g) (redesignated as Section 5(7)), and replaced it with current Section 5. Section 5 was radically restructured by the CFMA to provide for designation criteria and core principles with which a DCM must comply. Appendix E of Pub. L. 106–554, 114 Stat. 2763 (2000).

<sup>20</sup> The House Committee on Agriculture stressed that contracts that could be expected to be used almost entirely for speculation would be against the public interest. H.R. Rep. No. 975, 93 Cong., 2d Sess. 29 (1974).

<sup>21</sup> See H.R. Rep. No. 1383, 93d Cong., 2d Sess. 36 (1974).

with the scope of the Commission’s jurisdiction. Accordingly, while futures contracts that failed the economic purpose test were prohibited from trading on futures exchanges and thus illegal because of the on-exchange trading requirement, they (and any instrument with identical terms) remained futures contracts, fully subject to the Commission’s jurisdiction.

By enacting the CFMA, Congress sought “to promote innovation for futures and derivatives and to reduce systemic risk by enhancing legal certainty in the markets for certain futures and derivatives transactions[.]”<sup>22</sup> As demonstrated by the IEM, innovative event markets have the capacity to facilitate the discovery of information, and thereby provide potential benefits to the public. Subject to certain exceptions, Section 4(c)(1) of the Act gives the Commission the authority to “promote responsible economic or financial innovation and fair competition” by exempting any transaction or class of transactions from any of the provisions of the Act, including the requirement that they trade on Commission-regulated markets, where the Commission determines that such action would be consistent with the public interest. Pursuant to Section 4(c), Congress gave to “the Commission a means of providing certainty and stability to existing and emerging markets so that financial innovation and market development can proceed in an effective and competitive manner.”<sup>23</sup> Under Section 4(c), the Commission has the discretion to grant an exemption to certain classes of transactions without having to make a determination that such transactions are subject to the Act in the first instance.<sup>24</sup> Notably, the Commission can use its Section 4(c)

<sup>22</sup> House Report No. 106–711(III) September 6, 2000.

<sup>23</sup> House Conference Report 102–978, 1992 U.S.C.C.A.N. 3179, 3213.

<sup>24</sup> With respect to the exercise of this discretion, the House-Senate Conference Committee responsible for the review of Section 4(c) stated that:

The Conferees do not intend that the exercise of exemptive authority by the Commission would require any determination beforehand that the agreement, instrument, or transaction for which an exemption is sought is subject to the Act. Rather, this provision provides flexibility for the Commission to provide legal certainty to novel instruments where the determination as to jurisdiction is not straightforward. Rather than making a finding as to whether a product is or is not a futures contract, the Commission in appropriate cases may proceed directly to issuing an exemption.

Conf. Report at 3214–3215. Although Section 4(c) only speaks to futures contracts, Section 4c(b) of the Act, the Commission’s plenary authority to regulate transactions that involve commodity options, provides the Commission with comparable exemptive authority for options.

exemptive authority not only on a case-by-case, or product-by-product basis, but may also use the authority to establish a set of regulatory provisions applicable to a defined class of products.

## V. Issues for Comment

### A. Request for Comment

The following questions consider the Commission's regulatory purview over event contracts, the interests that may appropriately underlie Commission-regulated transactions, and the appropriate regulatory treatment of event contracts. The Commission encourages comments on the specific questions posed, as well as the broad range of issues raised in this concept release. In providing comments, please describe your relevant experience and discuss in detail the facts and legal provisions that support your conclusions. Furthermore, please consider the Commission's mandate to protect commodity futures and options markets and customers, and ensure the integrity of the commodity derivatives marketplace, as well as the expected effects of any Commission action on competition, efficiency, innovation and the financial integrity of transactions. Any recommendation with respect to the regulatory treatment of event contracts and markets should be consistent with and supported by the Act, practical, and amenable to effective and efficient implementation.

### B. Public Interest

1. What public interests are served by event contracts that are designed and will principally be traded for information aggregation purposes and not for commercial risk management or pricing purposes?

2. How are these interests consistent with the public interest goals embodied in the Act?

3. What calculations, analyses, variables, and factors could be used to objectively determine the social value of information to the general public that may be discovered through trading in event contracts? Should this be a factor in determining whether the Commission plays a role in regulating these markets?

### C. Jurisdictional Determinations

4. What characteristics or traits are common to or should be used to identify event contracts and event markets?

5. How do these characteristics and traits differ from those of commodity futures and options contracts that customarily have been regulated by the Commission? How are they similar?

6. Are there criteria based on the provisions of the Act that could be used

to make jurisdictional determinations with respect to event contracts and markets?

7. Given the purposes and history of the Act, would it be appropriate for the Commission to apply a test premised on commercial risk management or pricing functions to demarcate the Commission's jurisdiction over particular contracts? If so, what factors could be used to make such a determination?

8. Given the purposes and history of the Act, would it be appropriate for the Commission to apply any test premised on the economic purpose of certain types of transactions to demarcate the Commission's jurisdiction over particular contracts? If so, what factors could be used to make such a determination?

9. What calculations, analyses, variables and factors would be appropriate in determining whether the impact of an occurrence or contingency will result in a financial, commercial or economic consequence that is identified in Section 1a(13) of the Act?

10. What calculations, analyses, variables, and factors would be appropriate in determining whether an economic or commercial index that is based on prices, rates, values, or levels should or should not qualify as an excluded commodity under Section 1a(13) of the Act?

11. What identifiable factors, statutorily based or otherwise, limit the events and measures that may underlie event contracts when such contracts are treated as Commission-regulated transactions?

12. What objective and readily identifiable factors, statutorily based or otherwise, could be used to distinguish event contracts that could appropriately be traded under Commission oversight from transactions that may be viewed as the functional equivalent of gambling?

13. The Commission notes that Section 12(e) of the Act generally provides that the CEA supersedes and preempts other laws, including state and local gaming and bucket shop laws, with respect to transactions executed on or subject to the rules of a Commission-regulated market, or with respect to transactions exempted from the Act pursuant to the Commission's exemptive authority under Section 4(c) of the Act. What are the implications of possibly preempting state gaming laws with respect to event contracts and markets that are treated as Commission-regulated or exempted transactions?

14. Should certain underlying events or measures—such as those based on assassinations or terrorist activities—be prohibited altogether due to the social

perception and impact of such events? What statutory or other legal basis would support this treatment?

15. Are there event contracts, such as political event contracts, that should be prohibited from trading under the Act, or that deserve separate treatment or consideration, due to the nature and importance of their outcomes? What statutory or other legal basis would support this treatment?

### D. Legal Implementation

16. Is it appropriate for the Commission to direct certain or all event contracts onto markets that are regulated differently from and perhaps less stringently than DCMs? For example, it may be warranted or necessary to treat event markets that aggregate information solely for academic or research purposes, event markets set-up for internal corporate purposes, or event markets that offer exceedingly low notional value contracts to traders differently than markets that possess the attributes of traditional DCMs.

17. Is it appropriate for the Commission to use the Section 4(c) exemptive authority of the Act for implementing a regulatory scheme for event contracts and markets? In this regard, the Commission notes that it has the discretion to grant an exemption under Section 4(c) to certain classes of transactions without having to make a determination as to whether such transactions are subject to the Act in the first instance.

18. Is the issuance of staff no-action relief, such as the relief issued to the IEM, an appropriate or preferable means for establishing regulatory certainty for event contracts and markets? Is a policy statement appropriate or preferable?

19. What are the benefits and drawbacks of permitting certain event markets to operate pursuant to Commission established conditions that are similar to the conditions under which the IEM operates?

### E. Market Participants

20. Would it be appropriate to allow market participants, and in particular, retail customers, to trade on Commission-regulated event markets with the knowledge that the Commission may not be able to effectively monitor the measures or events that underlie certain event contracts?

21. What unique protections and prophylactic measures are appropriate or necessary for the protection of retail users of event contracts and markets?

22. What are the implications of permitting the intermediation of event

contracts, including intermediation on behalf of retail market participants, both with respect to trade execution and clearing?

23. Are there any types of trader or intermediary conduct, peculiar to event contracts and markets, that should be prohibited or monitored closely by regulators?

24. What other factors could impact the Commission's ability, given its limited resources, to properly oversee or monitor trading in event contracts?

Issued in Washington, DC, on May 1, 2008 by the Commission.

**David A. Stawick,**

*Secretary of the Commission.*

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## DEPARTMENT OF DEFENSE

### Office of the Secretary

[Transmittal Nos. 08-49]

#### 36(b)(1) Arms Sales Notification

**AGENCY:** Department of Defense, Defense Security Cooperation Agency.

**ACTION:** Notice.

**SUMMARY:** The Department of Defense is publishing the unclassified text of a section 36(b)(1) arms sales notification. This is published to fulfill the requirements of section 155 of Public Law 104-164 dated 21 July 1996.

**FOR FURTHER INFORMATION CONTACT:** Ms. B. English, DSCAIDBO/CFM, (703) 601-3740.

The following is a copy of a letter to the Speaker of the House of Representatives, Transmittals 08-49 with attached transmittal, policy justification, and Sensitivity of Technology.

Dated: April 29, 2008.

**Patricia L. Toppings,**

*OSD Federal Register Liaison Officer,  
Department of Defense.*