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Chicago Board of Trade

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Senior Vice President/Government Relations

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COMMODITY FUTURES
TRADING COMMISSION
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Ms. Jean Webb
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

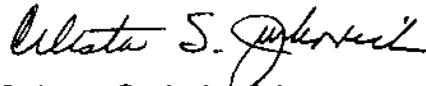
Re: Cantor Financial Futures Exchange Meeting

Dear Ms. Webb:

Attached in the Chicago Board of Trade's request to appear, statement of interest and abstract of comments for the public meeting which the CFTC is convening on Tuesday, August 11, 1998 regarding its consideration of the application of Cantor Financial Futures Exchange to be designated as a contract market in the trading of government securities futures contracts.

If the CBOT is invited to appear, I will supply you with the names of the individuals who will participate.

Sincerely,



Celesta S. Jurkovich



**BOARD OF TRADE OF THE CITY OF CHICAGO
STATEMENT OF INTEREST, QUALIFICATIONS AND ABSTRACT OF
COMMENTS
FOR THE PUBLIC MEETING BEFORE THE COMMODITY FUTURES TRADING
COMMISSION ON THE DE NOVO APPLICATION FOR CONTRACT MARKET
DESIGNATION
FILED BY THE CANTOR FINANCIAL FUTURES EXCHANGE**

I. Statement of Interest

The Board of Trade of the City of Chicago ("CBOT®" or "Exchange") is pleased to submit this Statement of Interest, Qualifications and Abstract of Comments to the Commodity Futures Trading Commission ("CFTC" or "Commission") in connection with the Commission's scheduled August 11, 1998, public meeting on the application for contract market designation submitted by the Cantor Financial Futures Exchange, Inc. ("Cantor Exchange"). The Cantor Exchange is being formed pursuant to a joint venture between the New York Cotton Exchange ("NYCE") and the Cantor Group.¹

The CBOT wishes to appear in opposition to the Cantor Exchange application at the public meeting. We have a strong interest in ensuring that all contract markets are held to the same legal standards, consistently applied. The CBOT has filed four comment letters on the Cantor Exchange application as additional information has become available and material terms of the proposal have changed since the Commission first published notice of the application in the Federal Register on February 3, 1998. (See CBOT letters dated April 3, April 27, June 30 and July 16, 1998, copies attached at Appendix A.) Those letters describe the many ways in which the application is materially incomplete and fails to comply with applicable legal requirements for contract market designation.

On July 23, 1998, the CBOT submitted a formal petition requesting the Commission alternatively to (1) suspend consideration of the Cantor Exchange application as materially incomplete until the Cantor Exchange and its sponsors correct all deficiencies in the record; (2) if the foregoing request is denied, hold a formal hearing "on the record" to gather additional information on the Cantor

¹ The term "Cantor Group" is used to refer generically to Cantor Fitzgerald, L.P. and related companies under its common control. These related entities include four subsidiaries of Cantor Fitzgerald, L.P. which have roles in the proposed venture. The Cantor Group, however, is not part of the ownership structure of the Cantor Exchange, even though it will control the exchange through appointing 8 of 13 members on the Cantor Exchange board and will operate the exchange. The Cantor Group will also control all floor brokerage trade execution on the exchange.

Exchange to fill the many gaps in the record; and (3) if the foregoing requests are denied, conduct a public hearing on the application to allow for public dialogue on the plethora of legal and policy issues that exist. On August 3, 1998, the Commission published notice in the Federal Register that it would hold a public meeting on the Cantor Exchange application approximately one week later on August 11, 1998. The Commission gave interested parties until August 6, 1998 to advise the Commission of their intention to participate in the public meeting.

However, on August 5, 1998, the Cantor Exchange submitted additional rule changes which further change the work-in-progress application. As we have documented in our comment letters, the Cantor Exchange's previous submissions have provided confusing and often contradictory explanations on many material points, and are missing critical information on many others. There is little time before the public meeting on August 11 to determine whether the Cantor Exchange's newest submission supplies answers or, as with the past submissions, raises more questions.

We reiterate the need for a complete application to be presented to the public in order to have meaningful analysis and comment. If the Commission decides to proceed with the public meeting notwithstanding the Cantor Exchange's submission of additional materials at this late date, the Commission should attempt through the meeting to establish a common factual understanding on the Cantor Exchange proposal on which all parties could base an informed legal analysis. Once the Commission has received a complete application, it should reopen the public comment process, with a notice that provides a comprehensive description of the proposal, including identification of special issues the public should address, based on the Commission staff's synthesis and legal analysis of the application materials.

Further public comment is needed for another reason. The Commission's Federal Register notices on the application mask the many legal and policy issues that exist and have prevented meaningful public scrutiny. In this vein, the Commission's public statements foster the mistaken impression that the Cantor Exchange is an electronic exchange,² even though its members cannot directly execute trades through interactive computer terminals and must rely on the intermediation of floor brokers (the Terminal Operators) who (it appears) *are not members* of the exchange. These Terminal Operators, *200 to 300 in number*, will operate in a closed, back room trading environment where they will be free to have extensive communication with customers and one another and will have considerable leeway in executing orders.

² For example, anyone visiting the Commission's Website for information on contract applications pending before the Commission will receive an explanation that the Cantor Exchange is "a new exchange which plans to conduct trading electronically in affiliation with the NYCE." This is the same type of description offered on the same page to describe FutureCom, which unlike the Cantor Exchange, is structured as an electronic exchange. <http://www.cftc.gov/dea/pending/newcontr.htm>. A print out of the Website page is attached as Appendix B.

Until yesterday, there was no hint of the rules of conduct that will govern the Terminal Operators.³ It is still a mystery how those rules will be enforced and by whom. What is also known is that the Cantor Exchange will foster non-competitive, exclusionary trading practices; allow non-members to execute orders and allow the Cantor Group to enjoy a floor brokerage monopoly and fixed brokerage commission rates.

One area of persistent confusion is whether the persons who are solely responsible for executing orders on the Cantor Exchange -- the Terminal Operators -- are members of the Cantor Exchange, subject to the Cantor Exchange's self-regulatory jurisdiction as such. This is an important legal question, one that goes to the very heart of the model of exchange self-regulation embodied in the CEA, which is premised upon *exchange jurisdiction over and surveillance of members* to protect customers and market integrity. This is why Section 4(a)(2) of the Commodity Exchange Act requires futures contracts to be traded "by or through a member of such contract market" [CEA §4(a)(2)]. If the Floor Broker/Terminal Operators are not members of the Cantor Exchange, as we believe is intended, then the Cantor Exchange would violate this basic tenet of futures regulation and circumvent numerous other legal requirements. Moreover, CFTC rules would prohibit their registration as floor brokers.⁴ If, on the other hand, the Floor Broker/Terminal Operators are members, other legal deficiencies follow, *such as the absence of defined enforcement procedures for disciplining Floor Broker/Terminal Operators.*⁵

³ In the August 5 submission, the applicant now for the first time is proposing a new Rule 712-A, "Conduct of Terminal Operators," which sets out certain trade practice requirements.

⁴ Earlier this week, we asked NFA if it could provide any clarification on how the NFA could process the Terminal Operators' floor broker applications in light of existing CFTC rules which require that the Terminal Operators be members of the new exchange (*i.e.*, be granted "trading privileges" on the new exchange). NFA has raised this matter with Commission staff. We have been advised that Commission staff has adopted an interpretation for NFA, but asked NFA not to disclose that interpretation. The applicant's August 5 submission reveals that it plans to circumvent CFTC requirements by deeming Terminal Operators to have "trading privileges" but solely for purposes of the CFTC's floor broker registration requirements.

⁵ Even if the Cantor Exchange were to ask the Commission to waive the member trading requirement pursuant to its exemptive authority, which the applicant has not, we question how such waiver and the consequent avoidance of meaningful accountability of the Floor Broker/Terminal Operators could ever meet the CEA's public interest requirement for exemptive relief. See CEA §4(c).

In short, it is impossible to complete a legal analysis of the Cantor Exchange proposal without an answer to the question of whether or not the Floor Broker/Terminal Operators are members of the Cantor Exchange, yet over six months after the Commission first published notice of the Cantor Exchange application, this basic issue is still not clearly answered. ***Given the central importance of this issue to a legal analysis of the application, the Commission should clarify whether the Floor Broker/Terminal Operators are members of the Cantor Exchange, with all the attendant obligations that implies for both the Cantor Exchange and the Terminal Operators, and should allow further public comment once that issue is resolved and the application is finally complete.***

II. Qualifications

The CBOT, established in 1848, has extensive experience in all facets of exchange operations, including self-regulation and compliance with federal statutory requirements. Today, the CBOT is a CFTC-designated contract market in over 25 futures and options on futures contracts, including Treasury Bond, Ten-Year Note, Five-Year Note and Two-Year Note Futures contracts, which the Cantor Exchange is proposing to replicate. Currently, the CBOT offers these contracts through competitive open outcry trading on the exchange floor during daytime trading sessions and electronic trading on the Project A System 15 hours a day. Later this year, pending membership and regulatory approval, trading hours on this electronic system will expand to include U.S. business hours.

The CBOT has extensive experience protecting the integrity of our markets through highly effective compliance and disciplinary programs. The Exchange's Office of Investigations and Audits ("OIA") has primary responsibility for administering these programs, with a full time staff of over 100 employees in five regulatory areas. OIA uses sophisticated computer programs to analyze the CBOT's audit trail data for potential trading abuses.

III. Abstract of Comments

The CBOT will address the more egregious legal flaws and deficiencies of the application which we have identified in our letters dated April 3, April 27, June 30 and July 16, 1998, copies of which are attached. In particular, we will address deficiencies relating to (1) fitness standards for exchange governing boards, (2) non-competitive trading, including through the EFP mechanism (the Cantor Exchange does not prohibit transitory EFPs), (3) impermissible execution monopoly and price fixing of floor brokerage commissions, (4) trade execution by or through members of a contract market, and (5) Cantor Exchange rules for Floor Broker/Terminal Operators. Each of these deficiencies, taken individually or in combination, would support a finding by the

Commission that the Cantor Exchange application is "contrary to the public interest" and should be disapproved. CEA § 5(7).

Additionally, the Commission staff has expressed concerns about the adequacy of the NYCE's compliance program. Given these findings, NYCE's ability to assume the added responsibility of overseeing activities on the new Cantor Exchange markets, which will operate in fundamentally different ways than the NYCE markets with which the NYCE compliance staff is familiar, is subject to serious question. These concerns are all the more acute in light of the CFTC Division of Trading and Markets' findings in its July 28, 1998 Rule Enforcement Review of the NYCE that the NYCE's "Compliance staff has lost a number of investigators, *which has diminished the Exchange's ability to perform its self-regulatory responsibilities.*" (Page 4; emphasis added.) The Division further stated that its concerns with NYCE's compliance staffing level "are amplified by the possibility that the Exchange will have to assume compliance responsibilities for the proposed Cantor Financial Futures Exchange." (Page 8, fn 9) The Division has recommended that the NYCE hire additional Compliance investigators, and instructed the NYCE to report back on its hiring plans, along with its plans for merging its compliance department with the CSCE's, within 60 days of the report. A copy of this Rule Enforcement Review is attached as Appendix C.