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HEDGESTREET SATISFACTION OF DESIGNATION CRITERIA WITH CONTRACT MARKET IN LISTING *i*HEDGELETS AND, IN CONNECTION WITH THOSE PRODUCTS, PERMITTING INTERMEDIATION AND TRADING ON MARGIN

Contract Market Criteria For Designation	Current Compliance (HedgeStreet has amended the rule numbers in this section to reflect the current version of the rules)	HedgeStreet's Proposed Additional Compliance
<p>Designation Criterion 1 <i>In General</i> – “To be designated as a contract market, the board of trade shall demonstrate to the Commission that the board of trade meets the criteria specified in this subsection.”</p>	<p>HedgeStreet's submissions dated December 19, 2003 through February 3, 2004, include, among other things, the HedgeStreet Contract Market Application, Rulebook, Agreement Framework between HedgeStreet and onExchange, Master Agreement for <i>i</i>Map Services between HedgeStreet and USinternetworking, HedgeStreet Membership/Account Application, Regulatory Chart, HedgeStreet/NFA Regulatory Services Agreement (“RSA”) and documents relating to the trading system.</p>	<p>In order to introduce intermediation on HedgeStreet and to list <i>i</i>Hedgelet Contracts that may be traded in a manner other than full collateralization prior to order execution, HedgeStreet has entered into agreements with both The Clearing Corporation (“CCorp”) and National Futures Association (“NFA”).</p>
<p>Designation Criterion 2 <i>Prevention of Market Manipulation</i> – “The board of trade shall have the capacity to prevent market manipulation through market surveillance, compliance, and enforcement practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions.”</p>	<p>Rule 5.13(d) specifically bars price manipulation. Rule 5.13(i) specifically bars any activity that affects the integrity of the market or its underlying systems. HedgeStreet has an agreement with NFA to assist it in carrying out various self-regulatory responsibilities with respect to market surveillance. (<i>See</i> HedgeStreet/NFA RSA) In addition, HedgeStreet has provided a statement of the requirements for the positions within its compliance department and has hired a compliance director who meets those requirements.</p>	<p>HedgeStreet has entered into a revised Regulatory Services Agreement (“Amended RSA”) with NFA so that NFA will conduct trade practice, market and financial surveillance services of <i>i</i>Hedgelets and CCorp members.</p> <p>The NFA has established procedures designed to reveal various trading abuses, including attempts to manipulate futures prices. The HedgeStreet Compliance staff will monitor overall activity in each market on a real-time basis and will oversee NFA's surveillance activities. NFA would provide HedgeStreet with data regarding positions of large traders, futures and cash prices. NFA together with the HedgeStreet Compliance staff, will monitor trading to prevent manipulation, price distortion, and disruption of the cash settlement process.</p> <p>As with the current system, the system that shall be used for <i>i</i>Hedgelets will automatically create a full and accurate record of all entries into the system, including all bids, offers and orders, and all matched transactions, allowing for a comprehensive audit trail.</p>

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<p>Designation Criterion 3 Fair and Equitable Trading – “The board of trade shall establish and enforce trading rules to ensure fair and equitable trading through the facilities of the contract market, and [sic] the capacity to detect, investigate, and discipline any person that violates the rules. The rules may authorize – (A) transfer trades or office trades; (B) an exchange of futures – (i) futures in connection with a cash commodity transaction; (ii) futures for cash commodities; or (iii) futures for swaps; or (C) a futures commission merchant, acting as principle or agent, to enter into or confirm the execution of a contract for the purchase or sale of a commodity for future delivery if the contract is reported, recorded or cleared in accordance with the rules of the contract market or a derivatives clearing organization”</p>	<p>Rule 5.13(b) prohibits entering into any trade that has been directly or indirectly pre-arranged. Rule 5.13(c) prohibits entering into any trade that does not result in a change in beneficial ownership, that is designed to unnaturally inflate trading volume, that in any way attempts to circumvent the Market's order processing, trade ordering, and trade execution systems, or otherwise to circumvent exposure of the order to open and competitive bidding on the Market, or that has some other illegitimate purpose. Rule 5.13(l) prohibits engaging in activity that would violate the CEA or the Commission's Regulations.</p>	<p>In order n order to list iHedgelets, which may be executed through intermediaries, HedgeStreet has drafted Rule 3.3((g) (requires only those Clearing Members properly registered under the Act to be permitted to conduct futures-related business); 3.3(i) (requires Clearing Members to use due diligence in receiving and handling orders from Customers); 3.3(j) (requires Clearing Member to provide written confirmations to all Customers) 3.3(k) (requires priority for Customer orders); Rule 5.13 (authorizes block trades); 5.14 (authorizes transfer trades); 5.15 (authorizes cross trades); 5.16(authorizes give-ups)</p> <p>Clearing Members and their customers may enter into off-exchange block, cross and transfer transactions with iHedgelets as long as such off-exchange transactions are executed in accordance with HedgeStreet's block trading, cross trade and transfer trade rules. HedgeStreet Rule 5.13 (Block Trading), 5.14 (Transfer Trades) and 5.15 (Cross Trades) respectively. Therefore, HedgeStreet has added following rules; (Rule 5.22(a)) in order to accommodate block trading and cross trades on HedgeStreet (prohibiting Clearing Members from accepting any orders or attempting to enter a transaction on the market which is not competitively executed on the Market except in Compliance with the Rules governing off-exchange transactions); (Rule 5.22(f)) in order to accommodate transfer trades on HedgeStreet (prohibiting all Members from agreeing to transfer or from transferring the benefit of any position in any iHedgelet Contract to another person other than through a transaction executed through the Market, except in accordance with HedgeStreet Rules.)</p> <p>HedgeStreet entered into an Amended RSA with NFA so that NFA will conduct trade practice and market surveillance functions of iHedgelets and Clearing Members. The NFA has established procedures designed to reveal various trading abuses, including attempts to manipulate futures prices. The HedgeStreet Compliance staff will monitor overall activity in each market on a real-time basis and will oversee NFA's surveillance activities. The NFA will provide HedgeStreet with data regarding positions of large traders, futures and cash prices. NFA together with the HedgeStreet Compliance staff, will monitor trading to prevent manipulation, price distortion, and disruption of the cash settlement process.</p>

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<p>Designation Criterion 4 Trade Execution Facility –“The board of trade shall (A) establish and enforce rules defining, or specifications detailing, the manner of operation of the trade execution facility maintained by the board of trade, including rules or specifications describing the operation of any electronic matching platform; and (B) demonstrate that the trade execution facility operates in accordance with the rules or specifications.”</p>	<p>Rule 5.8; Application, Appendix D – Licensing and Support Agreement with ONXBOT, dated August 7, 2003; Application, Appendix F – Hosting Agreement with USI, dated November 6, 2003; ONXBOT responses to CFTC Technical Review of Electronic Trading Systems, dated October 11, 2000; ONXBOT response to CFTC request for current technical information, dated August 18, 2003, including ONXBOT ECS Release Notes dated July 2003; ONXBOT ECS Administrator’s Guide.</p>	<p>In order to accommodate the trading of <i>iHedgelets</i>, HedgeStreet has added Rules 5.3 (Trading <i>iHedgelets</i>); and amended Rules 5.5 (Order Entry); 5.11 (Acceptable Orders) to the <i>iMarket</i> rulebook.</p> <p>Orders in <i>iHedgelets</i> will be executed in accordance with a price-time priority algorithm meaning that the best bid or offer will have priority over all other bids or offers, and bids or offers entered at the same price will be executed in the order they were received by the system. All limit orders entered into the system would identify quantity and price. Orders would be filled and executed in the sequence in which they were received on an “or better” basis. As such, limit orders would be recorded and logged into the server as they were received and would be assigned order entry times to a precision of no worse than to the nearest one second</p>

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<p>Designation Criterion 5 <i>Financial Integrity of Transactions</i> – “The board of trade shall establish and enforce rules and procedures for ensuring the financial integrity of transactions entered into by or through the facilities of the contract market, including the clearance and settlement of the transactions with a derivatives clearing organization.”</p>	<p>Application. HedgeStreet does not credit a contract bundle to the account of any member until the member had paid for the contract bundle in full in immediately available funds. HedgeStreet ensures the movement of funds from accounts as appropriate. All member funds are kept in appropriately titled customer segregated accounts.</p>	<p>HedgeStreet has entered into an agreement with CCorp to provide clearing and settlement of <i>iHedgelets</i> for HedgeStreet. All Hedgelet transactions will continue to be fully collateralised. Because CCorp will be the counterparty to every <i>iHedgelet</i> trade, the financial integrity of those contracts will be dependent on CCorp’s creditworthiness. As the Commission knows CCorp guarantee is backed by risk margin deposits, by its clearing fund, and by the Commission’s ongoing regulatory oversight.</p> <p>HedgeStreet also has entered into an Amended RSA with NFA to address relevant surveillance issues relating to intermediation and to provide a regular analysis of the financial status of CCorp members. HedgeStreet will rely on CCorp as well to monitor the financial status of CCorp Members.</p> <p>HedgeStreet Rule 3.1(d) states that HedgeStreet may in its sole discretion, approve, deny or condition any Clearing Member application as HedgeStreet deems necessary or appropriate. In addition, HedgeStreet Rule 3.3(a) states that if a Member fails to satisfy any Member Obligations, HedgeStreet may revoke or suspend any member privileges in full or in part. HedgeStreet Rule 3.3(h) requires Clearing Members to provide financial statements to HedgeStreet. HedgeStreet Rule 9.5 authorizes HedgeStreet to impose one or more various penalties including full or partial suspension of membership status or privileges as well as full or partial revocation of membership privileges. In addition HedgeStreet Rule 9.7 authorizes HedgeStreet to limit the activities of a Non-Member by suspending or denying access to the market.</p> <p>HedgeStreet Rule 3.1(a)(ix) requires FCM applicants to provide a letter acknowledge the segregation of Customer funds. HedgeStreet Rule 3.3(f) requires each applicant for Clearing membership on HedgeStreet to have adequate financial resources and credit, and that each Clearing Members maintains at all times their financial resources at or in excess of the amount prescribed by HedgeStreet from time to time in its capacity as a Clearing Member. All Clearing Members that are FCMs must comply with the financial requirements set forth by the Commission.. HedgeStreet Rule 3.3(p) allows Clearing Members to invest Customer funds as long as such funds are invested pursuant to Commission Regulation 1.25.</p> <p>CCorp Rule 203 states that the failure of any clearing member to comply with CCorp Rules and By laws, including any financial standards applicable to membership, may subject a clearing member to a suspension or revocation of clearing privileges. Pursuant to this rule, CCorp also may; (a) impose additional capital, margin or other requirements upon the clearing member; (b) allow such clearing member to submit trades solely for the members own account; (c) allow such clearing member to submit trades for liquidation only; (d) limit or restrict the type of contracts that may be cleared by such member in any of its accounts with CCorp; or (e) limit or restrict the number of contracts that are permitted to be maintained by such member in any of its accounts</p>

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<p>Designation Criterion 6 <i>Disciplinary Procedures</i> – “The board of trade shall establish and enforce disciplinary procedures that authorize the board of trade to discipline, suspend, or expel members or market participants that violate the rules of the board of trade, or similar methods for performing the same functions, including delegation of the functions to third parties.”</p>	<p>Rulebook Chapter 9 (Rule Enforcement) includes rules and procedures relating to rule enforcement, including summary and non-summary disciplinary actions; Application, pp. 25-32 (Compliance and Rule Enforcement).</p>	<p>In order to list <i>iHedgelets</i>, which may be executed through intermediaries, HedgeStreet has drafted Rule 9.7 (Actions Respecting Non-Members) which shall apply to all Customers of Clearing Members.</p>
<p>Designation Criterion 7 <i>Public Access</i> – “The board of trade shall provide the public with access to the rules, regulations, and contract specifications of the board of trade.”</p>	<p>Application, p. 25. HedgeStreet posts all rules and contract specifications on its web site.</p>	<p>HedgeStreet does not believe any changes to its rules or procedures are necessary as a result of the introduction of <i>iHedgelets</i> and intermediation.</p>
<p>Designation Criterion 8 <i>Ability to Obtain Information</i> – “The board of trade shall establish and enforce rules that will allow the board of trade to obtain any necessary information to perform any of the functions described in this subsection, including the capacity to carry out such international information-sharing agreements as the Commission may require.”</p>	<p>Rules 3.1, 3.2 and 9.1; Application pp 5 & 6. Membership Account Application (Appendix B); Regulatory Chart (Appendix C).</p>	<p>HedgeStreet will require Clearing applicants to complete a membership application. HedgeStreet will maintain these applications which Members must update pursuant to Rule 3.3(a). In order to list <i>iHedgelets</i>, which may be executed through intermediation, HedgeStreet has drafted Rule 3.3(d) (requiring Members to notify HedgeStreet of certain disciplinary history); 3.3(e) (requiring Members to supervise employee activities or agents relating to transactions effected on HedgeStreet); 3.3(f) (requiring Clearing Members to maintain certain financial requirements), 3.3(q) (requiring that Clearing Members comply with Commission recordkeeping requirements).</p>