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Division of
Market Oversight

August 13, 2010

Kathleen M. Cronin, Esq.
General Counsel and Corporate Secretary
Chicago Mercantile Exchange, Inc.
The Board of Trade of the City of Chicago, Inc.
New York Mercantile Exchange, Inc.
Commodity Exchange, Inc.
20 South Wacker Drive
Chicago, Illinois 60606

Re: The Board of Trade of the City of Chicago, Inc.
Market Regulation Advisory Notice RA0907-1

Dear Ms. Cronin:

The Chicago Board of Trade's ("CBOT") self-certified Market Regulation Advisory Notice RA 0907-1, issued on October 19, 2009, states that CBOT rules do not permit the execution of Exchange of Futures for Futures trades ("EFFs") and that CBOT does not permit contingent or transitory Exchanges for Related Positions ("EFRPs").[1] The Advisory Notice was issued subsequent to the Commission's approval of a rule submitted by ELX Futures L.P. ("ELX")[2] permitting market participants to negotiate privately two discrete but integrally-related transactions that result in establishing futures positions on ELX while concurrently liquidating futures positions on another designated contract market ("DCM") that lists "look-alike" contracts or, conversely, establishing positions on another DCM to replace identical positions liquidated on ELX.

The Advisory Notice informed market participants that EFFs are impermissible under CBOT Rule 538 and that the Rule, by its terms, permits only Exchange for Physicals ("EFPs"), Exchange for Risk ("EFRs") and Exchange of Options for Options ("EOOs"). Subsequent to

[1] On June 9, 2010, CME Group self-certified Market Regulation Advisory Notice RA1006-5, which extends the provisions of its earlier notice to all CME Group exchanges and, in FAQ Q2 appended to the Advisory reiterates that Rule 538 "does not allow for the execution of EFF transactions on any CME Group exchange. Therefore, in no case can a futures contract be used as the related position component of an EFRP transaction."

[2] Letter dated October 5, 2009 from David Stawick, Secretary of the Commission, to Neal Wolkoff, Chief Executive Officer, ELX Futures L.P., with notification of the Commission's approval of ELX Rule IV-5(a)(iv) and (v).

CBOT's filing of its Advisory Notice, the Division of Market Oversight, pursuant to Commission Regulations 38.5(b) and (c), requested that CBOT respond in writing to several specific questions associated with the Advisory Notice.[3] After considering CBOT's responses[4] as well as the relevant CBOT rules (including its advisories and interpretations), the submissions received from ELX, and other records related to this matter, staff advised CBOT of its conclusion that CBOT has mischaracterized: (i) EFF trades and matched block trades that are executed to enable inter-exchange transfers of futures positions as categorically wash or fictitious trades prohibited by the CEA; and (ii) matched block trades as impermissible contingent and transitory trades. Staff further noted that CBOT's interpretation of its rules respecting EFFs and matched block trades cannot be justified by the Commission's regulatory precedents. In light of those conclusions, staff requested that CBOT provide a written statement, together with supporting data, information and documents, further addressing the concerns expressed in its October 30 letter.[5] CBOT submitted their responses in their letter, dated February 8, 2010.

On August 13, 2010, the Commission advised CBOT that it fully supports staff's conclusion that ELX's EFFs, when used solely to liquidate and establish "look-alike" futures positions on different DCMs, are not wash or fictitious sales prohibited by the CEA. The Commission concluded further that neither Core Principle 9 nor Commission Regulation 1.38 prohibits or mandates a DCM's acceptance of: (i) EFF trades; or (ii) matched block trades used to transfer positions from one exchange to another exchange with a different clearing house. Finally, the Commission advised CBOT that it has directed staff to separately undertake a thorough analysis of the Core Principle 18 claims that have been made in connection with this matter.

In light of the Commission's directive, and pursuant to Commission Regulations 1.31 and 38.5(b) and (c), staff requests that CBOT provide a written statement, together with supporting data, information and documents, addressing the following:

1. Please identify each legal, economic and business rationale for prohibiting EFFs. Please include a detailed explanation for your assertion that: (a) permitting EFFs would enable ELX to free ride on CBOT's investments in exchange facilities, clearing facilities, or product development; and (b)CBOT's EFF prohibition contributes to inter-exchange competition.

2. Please identify each legal, economic and business rationale for permitting EFPs, EFRs and EOOs. Please include a detailed description of the mechanics involved in the various forms of EFRPs permitted under CBOT Rule 538 and how they may be materially distinguishable from those associated with EFFs.

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[3] Letter dated October 30, 2009 from David P. Van Wagner, Chief Counsel for CFTC's Division of Market Oversight, to Kathleen Cronin, General Counsel and Corporate Secretary for the CME Group, Inc.

[4] Letter from Kathleen Cronin to Steven Schoenfeld, Director of CFTC's Division of Market Oversight, dated November 16, 2009.

[5] Letter dated January 22, 2010 from Richard A. Shilts, Acting Director of DMO to Kathleen Cronin.

3. In its February 8, 2010 letter to Commission staff, CBOT stated:

    A. [A]lthough we respond to ELX's allegations in more detail below in your response to the specific questions posed by the commission, we note that ELX can compete effectively without a CFTC order forcing CBOT and CME clearing to close out open positions without any legitimate trade. ELX has established open interest, a relatively tight bid/offer spread and depth at the inside market. Any person or entity holding CBOT positions can liquidate its CBOT positions and establish ELX positions using the respective electronic systems of each market. In addition, since most of the open interest is in the front month, it rolls each quarter, and parties are free to roll their positions from CBOT to ELX by means of legitimate transactions.

    B. CBOT is not unreasonably restraining trade in violation of Core Principle 18 by refusing to structure its rules in the way that will best facilitate the transfer of its open book of business to OCC in order to assist ELX in its efforts to acquire a greater market share of Treasury futures contracts.

    Please identify each basis for the foregoing contentions. Please provide empirical evidence supporting the various assertions made in this statement.

4. Please explain the basis for setting CBOT's minimum block trading sizes respecting Treasuries. For each of the last 12 months, please identify: (i) the percentage of CBOT contracts traded in block trades and permissible EFRPs; and (ii) the percentage of CBOT contracts traded in lots at or above ELX's minimum block trading size.

5. Please identify an appropriate maximum percentage of block trades and permissible EFRPs that CBOT believes avoids material risk to the liquidity and price discovery functions of its centralized Treasuries market, and explain how that figure was reached.

6. Please identify each potential impact of EFF transactions on CBOT's centralized trading respecting Treasuries, including the impact on trading volume, liquidity and the price discovery function of such markets. In your answer, please address separately the potential impact of EFFs that result in a net move of a customer's open interest from CBOT to another DCM, of EFFs that result in a net move of a customer's open interest from another DCM to CBOT, and those that result in no net move of open interest.

7. Describe with specificity how permitting EFFs would undermine any of: (a) the purposes of the CEA; or (b) CBOT's rules. With respect to CBOT's rules, please identify in your answer each specific rule affected and the date each such rule was adopted. Please also include a description of the purpose and function of each affected rule.

8. Describe each step that CME/CBOT would need to take in order to permit and implement EFF transactions, including the anticipated mechanics and reporting requirements to clearinghouses.

9. Please identify each distinction between ELX's EFF rule and NYMEX's Basis Trade Facility.

10. Provide CBOT's projection of likely volume of EFFs if CBOT were required to permit them as another EFRP. If you expect the likely volume to be materially different from, or similar to, other EFRPs, explain in detail the basis for your expectation.

11. Please produce all documents (beginning July 2009) discussing potential customer demand for EFFs, including the results of any surveys, outreach, or other information available to CBOT. Please include any information concerning the customers most likely to use EFFs.[6]

12. Provide in an itemized form the fee(s) and any other revenues that CME group recognizes each time a permissible EFRP is transacted, including both the clearing and execution fees. If CME believes the fees or revenues from EFFs could differ materially from those for other EFRPs in the event it were required to accept them, please identify and explain the expected difference.

Please include in your response any and all empirical evidence.

Please send your written statement within 30 days from the date of this letter to the undersigned at the address above.

Sincerely,

Richard A. Shilts
Acting Director

[6] For purposes of this question, the term "documents" means all computer files and written, recorded, and graphic materials of every kind in the possession, custody or control of CBOT. The term "documents" includes, without limitation, electronic mail messages, electronic correspondence and drafts of documents.