

SUBMISSION COVER SHEET

Exchange Identifier Code (optional) #04-30

Date April 8, 2004

ORGANIZATION

Chicago Mercantile Exchange Inc.

FILING AS A:

DCM

DCO

DTEF

TYPE OF FILING

• **Rule Amendments**

Self-Certification Under Reg. 40.6(a) or 41.24

Commission Approval Requested Under Reg. 40.5 or 40.4 (a)

Notification of Rule Amendment Under Reg. 40.6(c)

Non-Material Agricultural Rule Change Determination Under Reg. 40.4(b)

• **New Products**

Self-Certification Under Reg. 40.2 or 41.23

Commission Approval Requested Under Reg. 40.3

RULE NUMBERS

Live Cattle Futures Rule 10103.A.

DESCRIPTION (Rule Amendments Only)

Change in USDA report used for premiums and discounts



30 South Wacker Drive
Chicago, IL 60606-7499
www.cme.com

April 8, 2004

Ms. Jean A. Webb
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington DC 20581

Re: Section 5c(c)2 and Regulation 40.5 Submission. Request for Commission Rule Approval of Amendments to Live Cattle Futures Rule 10103.A. CME Submission #04-30.

Dear Ms. Webb:

- 1. Request for Commission Rule Approval.** The Chicago Mercantile Exchange ("CME" or "Exchange") hereby requests Commission approval of amendments to Live Cattle Futures Rule 10103.A. These amendments change the USDA report used as the source of market-based value differentials for delivered cattle that differ from the par specifications for quality grade, yield grade, and carcass weight.
- 2. Text of Proposed Amendments.** The text of the proposed amendments are shown below with additions underlined:

10103.A. Sources and Calculation of Adjustment Factors

Quality grade adjustments for all delivery units will make use of the live weight equivalent of the Choice-Select boxed beef spread calculated from information reported by USDA (in \$/cwt.) for the day of tender in the National Daily Boxed Beef Cutout and Boxed Beef Cuts report. This is referred to hereafter as the Live Equivalent Choice-Select Spread (LECSS) and is computed by subtracting the "Select Boxed Beef Cut-Out Value" from the "Choice Boxed Beef Cut-Out Value" and multiplying that result by 0.0063. Boxed Beef Cut-Out Values from the 600/750 pound category are used for live-graded delivery units with an average live weight less than 1,190 pounds and for carcass-graded delivery units with an average carcass weight less than 750 pounds. Boxed Beef Cut-Out Values from the 750/900 pound category are used for live-graded delivery units

with an average live weight greater than or equal to 1,190 pounds and for carcass-graded delivery units with an average carcass weight greater than or equal to 750 pounds.

The USDA By-Product Drop Value report for the day of tender shall serve as the source of information for calculating the condemned liver factor used in carcass-graded deliveries. The condemned liver factor shall equal the reported liver value (in \$/cwt.) multiplied by -0.01.

In addition, quality grade, yield grade and carcass weight adjustments will make use of factors calculated from values reported by USDA (in \$/cwt.) in the [~~National Weekly Direct Slaughter Cattle – Premiums and Discounts~~]5-Area Weekly Weighted Average Direct Slaughter Cattle – Premiums and Discounts report. The Prime, Standard, Yield Grade 1, Yield Grade 2, Yield Grade 4, Yield Grade 5, 550-600 lbs. 900-950 lbs. and 950-1000 lbs. factors are calculated by multiplying the reported simple average for the corresponding category by 0.0063. If a quality grade or yield grade is broken into subcategories on this report, then the factor for that quality or yield grade shall be the simple average of all reported averages for the subcategories in that category multiplied by 0.0063. The most recently issued report with respect to the day a Certificate is tendered shall be used to calculate the factors for that delivery unit. When a Certificate is tendered on the same day that a new report is issued, that new report shall be used in factor calculation regardless of the time of day that the report is released.

(Remainder of Rule 10103.A. unchanged)

3. **Effective Date and Rule Promulgating Authority.** These amendments were approved by the Board of Directors of the Chicago Mercantile Exchange at its Regular Meeting on Wednesday, April 7, 2004, under the authority granted by CME Rule 230.j. These amendments will apply to the October 2004 and subsequent contract months upon Commission approval and notification of market participants.
4. **Operation, Purpose & Effect.** The Live Cattle futures contract currently uses USDA's "National Weekly Direct Cattle – Premiums and Discounts" report as the source of market-based value differentials for delivered cattle that differ from the par specifications for quality grade, yield grade, and carcass weight (Exhibit 1). The use of this report first applied to the June 1998 contract month, which was listed for trading in May 1997.

In December 2002, CME's Ad Hoc Live Cattle Advisory Group made a formal request to USDA to create a new report that 1) includes only cattle slaughtered in the 5-area price reporting region that corresponds to CME's live cattle delivery area, and 2) uses weighted averages instead of simple averages to correct for different sizes of packing plants. Because the national report includes data from locations far removed from the CME delivery area, reported values may differ substantially from actual values in the delivery area due to local supply-demand conditions and other factors. Furthermore, because the national report uses a

simple average, each observation for a given attribute has an equal impact on the reported average. As a result, individual observations based on a small number of animals may artificially skew the reported average.

In response to this request, USDA published the first “5-Area Weekly Weighted Average Direct Slaughter Cattle – Premiums and Discounts” report in October 2003 (Exhibit 2). The Exchange believes this new report is less subject to artificial distortions and presents a more representative view of premiums and discounts in the CME Live Cattle delivery area, for the reasons cited above. As part of this Submission, files containing data from both USDA reports will be provided electronically to Commission staff.

The Exchange believes it is important to implement these changes on certain of the existing contract months so that the benefits of this new report can be realized as soon as possible. It is important to note that these premiums and discounts do not have any impact on the par value of the contract, and affect only those market participants who make and take delivery. In addition, no cattle will have been placed on feed at the time of this submission that would be available for delivery in October 2004. For all of these reasons, the Exchange believes that implementing these changes on the October 2004 contract month will be market-neutral.

5. **Opposing Views.** The Exchange is not aware of any opposing views to these amendments. On January 30, 2004, CME staff presented a recommendation to adopt this new report was presented to the National Cattlemen’s Beef Association (NCBA) Live Cattle Marketing Committee. This recommendation is consistent with NCBA Policies M 1.22 and M 2.6, and there were no objections from those in attendance (Exhibit 3). On March 2, 2004, the same recommendation was discussed with CME’s Ad Hoc Live Cattle Advisory Group, again with no objections.
6. **Necessary Amendments or Interpretations to the Act or Regulations.** The Exchange is not aware that any such amendments or interpretations are needed to accommodate these proposed amendments.

If you have any questions regarding this submission, please contact Mr. Paul Peterson at (312) 930-4587 or via e-mail at ppeterso@cme.com . Please refer to CME Submission #04-30 in all correspondence regarding this matter.

Sincerely,



Ms. Jean A. Webb
Amendments to Live Cattle Rule 10103.A.
April 8, 2004

EXHIBIT 1

LM_CT155

St. Joseph, MO Mon Apr 05, 2004 USDA Market News Service

NATIONAL WEEKLY DIRECT SLAUGHTER CATTLE - PREMIUMS AND DISCOUNTS

For the Week of: 4/5/2004

Value Adjustments

	Range	Simple Avg.	Change
Quality:			
Prime	0.00 - 27.00	7.73	(0.81)
Choice	0.00 - 0.00	0.00	0.00
Select	(15.00)- (6.00)	(13.50)	(2.50)
Standard	(35.00)- (9.00)	(21.10)	(1.70)
Ave Choice or Better	0.00 - 13.75	3.46	0.05
Dairy - Type	(8.00)- 0.00	(0.82)	(0.02)
Bullock/Stag	(40.00)- (15.00)	(25.00)	2.00
Hardbone	(35.00)- (20.00)	(26.70)	(0.14)
Dark Cutter	(40.00)- (15.00)	(28.23)	1.31
Over 30 months of age	(35.00)- 0.00	(8.85)	1.61

*Cutability Yield Grade, Fat/Inches

1.0-2.0 < .10"	0.00 - 8.00	2.83	(0.26)
2.0-2.5 < .20"	0.00 - 5.00	1.63	(0.14)
2.5-3.0 < .40"	0.00 - 5.00	1.21	0.12
3.0-3.5 < .60"	(1.00)- 0.00	(0.08)	0.02
3.5-4.0 < .80"	(1.00)- 0.00	(0.08)	0.02
4.0-5.0 < 1.2"	(20.00)- (8.00)	(13.50)	0.14
5.0/up > 1.2"	(25.00)- (10.00)	(18.31)	0.27

Weight:

400-500 lbs	(40.00)- (5.00)	(22.00)	1.09
500-550 lbs	(30.00)- 0.00	(15.33)	0.49
550-600 lbs	(15.00)- 0.00	(2.92)	(0.17)
600-900 lbs	0.00 - 0.00	0.00	0.00
900-950 lbs	(5.00)- 0.00	(0.58)	0.06
950-1000 lbs	(18.00)- 0.00	(7.75)	0.70
over 1000 lbs	(30.00)- (10.00)	(18.18)	1.37
Hide Brand Location	0.00 - 0.00	0.00	0.00

Based on individual packer's quality, cutability, and weight buying programs. Values reflect adjustments to base prices, dollars per cwt., on a carcass basis.

* If yield grades are not available, yield differentials may be based on fat at 12th rib using a constant of average ribeye area and muscling for carcass weight and KPH. Superior or inferior muscling may adjust lean yield.

Source: USDA Market News Service, St. Joseph, MO
 816-238-0678 email: stjoe.lgmn@usda.gov
 www.ams.usda.gov/mnreports/lm_ct155.txt

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Ms. Jean A. Webb
Amendments to Live Cattle Rule 10103.A.
April 8, 2004

EXHIBIT 2

LM_CT169

St. Joseph, MO

Mon Apr 05, 2004

USDA Market News Service

5-AREA WEEKLY WTD AVERAGE DIRECT SLAUGHTER CATTLE - PREMIUMS AND DISCOUNTS

For the Week of: 4/5/2004

Value Adjustments

	Range	Wtd Avg	Change
Quality:			
Prime	3.00 - 27.00	15.24	(0.29)
Choice	0.00 - 0.00	0.00	0.00
Select	(15.00)- (6.00)	(11.47)	(1.52)
Standard	(35.00)- (9.00)	(21.43)	(3.54)
Ave Choice or Better	0.00 - 3.50	1.61	0.00
Dairy - Type	0.00 - 0.00	0.00	0.00
Bullock/Stag	(40.00)- (25.00)	(34.27)	0.00
Hardbone	(35.00)- (20.00)	(28.72)	(0.62)
Dark Cutter	(40.00)- (30.00)	(33.81)	(0.04)
Over 30 months of age	(35.00)- 0.00	(7.16)	1.38
*Cutability Yield Grade, Fat/Inches			
1.0-2.0 < .10"	0.00 - 8.00	3.95	0.00
2.0-2.5 < .20"	0.00 - 3.00	2.01	0.00
2.5-3.0 < .40"	0.00 - 2.50	1.95	0.86
3.0-3.5 < .60"	(1.00)- 0.00	(0.19)	0.00
3.5-4.0 < .80"	(1.00)- 0.00	(0.19)	0.00
4.0-5.0 < 1.2"	(20.00)- (8.00)	(17.53)	0.00
5.0/up > 1.2"	(25.00)- (13.00)	(22.92)	0.00
Weight:			
400-500 lbs	(40.00)- (14.00)	(24.49)	1.72
500-550 lbs	(30.00)- (12.00)	(22.43)	1.72
550-600 lbs	(7.00)- 0.00	(0.79)	0.00
600-900 lbs	0.00 - 0.00	0.00	0.00
900-950 lbs	(2.00)- 0.00	(0.01)	0.00
950-1000 lbs	(10.00)- 0.00	(3.71)	3.44
over 1000 lbs	(25.00)- (10.00)	(18.19)	5.16
Hide Brand Location	0.00 - 0.00	0.00	0.00

Based on individual packer's quality, cutability, and weight buying programs. Values reflect adjustments to base prices, dollars per cwt., on a carcass basis.

Weighted average price is calculated on individual packer slaughter volume of packers represented in the 5 state area.

* If yield grades are not available, yield differentials may be based on fat at 12th rib using a constant of average ribeye area and muscling for carcass weight and KPH. Superior or inferior muscling may adjust lean yield.

Source: USDA Market News Service, St. Joseph, MO
 816-238-0678 email: stjoe.lgmn@usda.gov
www.ams.usda.gov/mnreports/LM_CT169.txt

0950C

Ms. Jean A. Webb
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April 8, 2004

EXHIBIT 3

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FARM POLICY

GOVERNMENT AFFAIRS CENTER
NATIONAL CATTLEMEN'S BEEF ASSOCIATION



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APPROVAL AND PROMULGATION OF AIR QUALITY IMPLEMENTATION PLANS; NORTH DAKOTA; STATE IMPLEMENTATION P

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CATTLE

M 1.22 2003 CME CONTRACT CHANGES

11/24/2003

MARKETING

Gregg Doud

FARM POLICY

Chief Economist

gdoud@beef.org

FEDERAL LANDS

FOOD SAFETY AND

HEALTH

WHEREAS, current contract specifications of Chicago Mercantile Exchange's (CME) Live Cattle Futures Contract do not accurately reflect the consistent and decade-long increase in average fed cattle weights, and

FOREIGN TRADE

NATURAL

WHEREAS, the Live Cattle Futures Contract specifications do not reflect the natural variability in cattle weights relative to average fed cattle weights, and

RESOURCES AND

ENVIRONMENT

OTHER

WHEREAS, the Live Cattle Futures Contract specifications do not accurately reflect the current beef packer buying practices of discounting only extremely light or heavy cattle, and

TAX AND CREDIT

WHEREAS, the Live Cattle Futures Contract specifications do not treat live and carcass deliveries on an equal and consistent basis, and

WHEREAS, the Live Cattle Futures Contract specifications force cattle producers to excessively sort cattle that are delivered on a live basis, and

WHEREAS, the Live Cattle Futures Contract has not reduced the volatility of the fed cattle basis, and

WHEREAS, the Live Cattle Futures Contract specifications have not enabled the convergence of the cash and futures markets at expiration, and

WHEREAS, the Live Cattle Futures Contract has greatly limited the deliverable supply of cattle;

THEREFORE BE IT RESOLVED that NCBA requests Chicago Mercantile Exchange to make the following changes to the current contract specifications of their Live Cattle Futures Contract:

- 1) Increase the upside weight specifications for carcass deliveries from 900 pounds to 950 pounds and for live animal deliveries from 1400 to 1450 pounds.
- 2) Eliminate the 100 pound delivery discount, while

POLICY HOME
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POLICY INDEX

>M 2.2 1999 CME PROPOSAL

>M 2.3 2001 EASTERN CORN BELT DELIVERY POINT

>M 2.4 2001 FUTURES TRADING

>M 2.5 2001 CROSS HEDGING

>M 2.7 2002 FUTURES CONTRACT MODIFICATIONS

>M 2.8 1999 LIVE CATTLE FUTURES/DELIVERY WEIGHT SPECIFICATIONS

>M 2.9 2003 LIVE CATTLE FUTURES CONTRACT

- maintaining the current rules eliminating from delivery those animals weighing 200 pounds over or under the average weight of the delivery load.
- 3) Change the currently used United States Department of Agriculture premium/discount grids to trade volume weighted grids of premiums and discounts reflective of the average grid in use within the geographical delivery area.
 - 4) To lessen the stress on the livestock, allow the scheduling of live deliveries throughout the day similar to the manner carcass deliveries can now be scheduled.
 - 5) Change the par delivery unit from the currently only steers to steers and heifers.
 - 6) Certify Greeley, Colorado as a delivery point.

explore

FARM POLICY

GOVERNMENT AFFAIRS CENTER
NATIONAL CATTLEMEN'S BEEF ASSOCIATION



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LIVE CATTLE MARKETING

CATTLE HEALTH

CATTLE

M 2.6 2002 LIVE CATTLE CONTRACT

11/24/2003

MARKETING

Gregg Doud
Chief Economist
gdoud@beef.org

FARM POLICY

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FOOD SAFETY AND

WHEREAS, the Chicago Mercantile Exchange has proposed to change the premium/discount structure of the Live Cattle Contract based on USDA's weekly National Premiums and Discounts for Slaughter Steers and Heifers report, and

HEALTH

FOREIGN TRADE

NATURAL

WHEREAS, the Premiums and Discounts report provides little historical data, does not reflect actual market offerings due to "packer intent," and does not include weighted averages based on number of cattle reported,

RESOURCES AND

ENVIRONMENT

>M 1.1 2002 LIVE CATTLE
MARKETING
OPPORTUNITIES

OTHER

THEREFORE BE IT RESOLVED, NCBA recommends the following changes to the CME proposal:

TAX AND CREDIT

1. Heifers allowed for delivery.
2. Spot month position limits remain at current levels.
3. Premiums and Discounts report should be based on weighted averages and actual market transactions.
4. Changing the actual average hot carcass yield for carcasses-graded deliveries to 62.5% from 63%.
5. Extending the number of trading days in the month.