

May 18, 2005

Ms. Jean A. Webb
Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, D.C. 20581

Reference File #2553.01
Rule Certification

OFFICE OF THE SECRETARIAT

2005 MAY 19 AM 7: 50

RECEIVED
C.F.T.C.

Dear Ms. Webb:

Pursuant to Commission Regulation 40.6(a), the Chicago Board of Trade (CBOT[®]) hereby submits the following:

- **Clarification, via the attached Notice, concerning margin treatment afforded to members pursuant to CBOT Regulation 431.01.**

The Exchange intends to issue the referenced Notice one day after the Commission's receipt of this filing.

There were no opposing views concerning this Notice.

The CBOT certifies that the provisions of this Notice comply with the Commodity Exchange Act and the rules thereunder.

Sincerely,

Paul J. Draths
Vice President and Secretary

B051705

May 19, 2005

Notice

RE: Clarification to Regulations 431.01 & 431.06 Margins – Non-Clearing Members

The Financial Compliance Committee would like to clarify the margin treatment afforded members, specifically with regard to the following regulation:

Regulation 431.01 Margins – Non-Clearing Members: A non-clearing member who makes his own futures trades or who on the Floor gives his orders for futures trades which are exclusively for his account shall be subject solely to the provisions of this Regulation. All futures transactions in such account shall be margined to the market.

The Committee is clarifying that:

- 1) **Lessees (where the clearing firm has NOT indemnified the lessor):** At the discretion of the clearing member firm, these accounts may be margined to the market in accordance with Regulation 431.01. However, clearing firm must follow prudent risk management procedures for members' accounts as described below.
- 2) **Lessees (where the clearing firm HAS indemnified the lessor):** Clearing member firms routinely indemnify the lessor in the case of losses by the lessee; in such cases clearing member firms are not able to rely on the membership as collateral. Therefore, clearing member firms must margin indemnified lessees in accordance with Regulation 431.02.
- 3) **Proprietary Accounts:** Regulation 431.01 applies only to those trades made for an individual's own account including both floor and electronic trades. This regulation does **not** apply to proprietary accounts of member firms.
- 4) **Options:** Regulation 431.01 applies only to futures transactions. According to Regulation 431.06 if the account has any options positions the entire portfolio of positions are subject to margin as calculated using SPAN. The firm may open a second trading account that holds only futures positions and separately margin the futures account on a mark to market basis.

The Committee also would like to stress that Regulation 431.01 does not obviate the need for prudent risk management policies. At a minimum, the Committee expects that members' accounts that are marked to the market be monitored for the "risk" of the account (SPAN should be used to measure the account's overall risk), and if an account does not maintain collateral that is greater than the risk presented by the account, the Committee expects that the firm is taking appropriate measures. These measures include: 1) calling for additional collateral; and/or 2) reducing the account's risk through liquidation or the addition of risk reducing positions. In calculating the level of collateral in the account, the firm may consider the account's Net Liquidating Equity, the market value of securities (less SEC haircuts), plus 50% of the current

bid price of owned memberships, 50% of the value of leased memberships may also be used only in instances where the clearing member firm has *not* indemnified the lessor. For all accounts where the member does not maintain collateral that is greater than the risk presented by the account, the clearing member firm must take the appropriate capital charge.

This notice is meant to give clearing member firms clarity regarding member margin treatment, where over the years contradictory interpretations and practices may have evolved. The Financial Compliance Committee recognizes that procedures referenced herein may contradict the current margin procedures of some clearing member firms. Therefore, the Committee is allowing accounts that are not currently in compliance with the above-referenced procedures 60 days (i.e., until the close of business July 18, 2005) in which to comply. Accounts currently in compliance must continue as such throughout this 60 day period.

This notice supersedes any prior written or verbal interpretations with respect to these matters. Any question regarding the treatment of member margins should be directed to Barbara Lorenzen at (312) 435-3683 or Lori Gialessas at (312) 435-7171.

* SPAN is a trademark of Chicago Mercantile Exchange Inc. ("CME"). CME assumes no liability in connection with the use of SPAN by any person or entity.