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September 11, 2007

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RE: Regulation 40.6 Submission. Certification of Amendments to CME Live Cattle Futures Rules 10101. SCOPE OF CHAPTER, 10103.B.4.a. Par Delivery Unit, 10103.B.4.b. Weight Deviations, 10103.B.5.a. Time for Inspection, 10103.B.6. Delivery Invoice, 10103.B.7. Cost of Inspection, Weighing and Storage, 10103.C.1. Conditions, 10103.C.3. Seller's Duties, 10103.C.5.a. Par Delivery Unit, 10103.C.5.d. Yield Grade Deviations, 10103.C.5.e. Quality Grade Deviations, 10103.C.5.f. Quantity Deviations, 10103.C.5.g. Other Deviations, 10103.C.6.a. Time for Inspection, 10103.C.6.b. Grading and Determining Yield, 10103.C.7. Delivery Notice, 10103.C.8. Cost of Inspection, Weighing, and Transportation, 10103.C.9. Penalties, 10104.A. Tendering a Certificate, 10104.D. Retender, 10104.E. Reclaim, and INTERPRETATIONS & SPECIAL NOTICES RELATING TO CHAPTER 101 CME Submission #07-74.

Dear Mr. Stawick:

On August 27, 2007, Chicago Mercantile Exchange Inc. ("CME" or "Exchange") approved amendments to CME Live Cattle Futures Rules 10101. SCOPE OF CHAPTER, 10103.B.4.a. Par Delivery Unit, 10103.B.4.b. Weight Deviations, 10103.B.5.a. Time for Inspection, 10103.B.6. Delivery Invoice, 10103.B.7. Cost of Inspection, Weighing and Storage, 10103.C.1. Conditions, 10103.C.3. Seller's Duties, 10103.C.5.a. Par Delivery Unit, 10103.C.5.d. Yield Grade Deviations, 10103.C.5.e. Quality Grade Deviations, 10103.C.5.f. Quantity Deviations, 10103.C.5.g. Other Deviations, 10103.C.6.a. Time for Inspection, 10103.C.6.b. Grading and Determining Yield, 10103.C.7. Delivery Notice, 10103.C.8. Cost of Inspection, Weighing, and Transportation, 10103.C.9. Penalties, 10104.A. Tendering a Certificate, 10104.D. Retender, 10104.E. Reclaim, and INTERPRETATIONS & SPECIAL NOTICES RELATING TO CHAPTER 101.

These amendments will be effective with the October 2008 and subsequent contract months, which will be listed for trading at the start of business on Monday, September 17, 2007. It should be noted that the Exchange temporarily postponed the listing of these contract months pending consideration of these rule amendments, and notified the Commission of this postponement in CME Submission #07-34 dated May 1, 2007.

The amendments are presented below, with additions underlined and deletions bracketed and overstruck.

## Chapter 101 Live Cattle Futures

### 10100. SCOPE OF CHAPTER

This chapter is limited in application to futures trading of live beef cattle. The procedures for trading, clearing, [~~inspection~~] grading, delivery and settlement, and any other matters not specifically covered herein shall be governed by the rules of the Exchange.

### 10103. SETTLEMENT PROCEDURES

#### 10103.B. Live Graded Deliveries

##### 4. Par Delivery and Substitutions.

- a. Par Delivery Unit. A par delivery unit is 40,000 pounds of USDA estimated Yield Grade 3, 55% Choice, 45% Select quality grade live steers, [~~averaging between 1,100 pounds and 1,425 pounds with no individual steer weighing more than 100 pounds above or below the average weight for the unit. No~~] with no individual animal weighing less than 1,050 pounds or more than 1,475 pounds [shall be] deliverable at par.

Par delivery units shall have an estimated average hot yield of 63%.

All cattle contained in a delivery unit shall be healthy. No c[G]attle which are unmerchantable, such as crippled, sick, obviously damaged or bruised, or which for any reason do not appear to be in satisfactory condition to withstand shipment by [~~rail or~~] truck shall be [~~excluded~~] deliverable. No cattle showing a predominance of dairy breeding or showing a prominent hump on the forepart of the body shall be deliverable. Such determinations shall be made by the grader and shall be binding on all parties.

- b. Weight Deviations. Steers weighing less than 1,050 pounds or more than 1,550 pounds shall not be deliverable. Steers weighing more than 1,475 pounds but less than or equal to 1,550 pounds shall be deliverable at an adjustment equal to the 950-1000 lbs Factor described in Rule 10103.A., multiplied by the average live weight of the delivery unit. [from 100 to 200 pounds over or under the average weight of the steers in the delivery unit shall be deliverable at a discount of 3¢ per pound, provided that no individual animal weighing less than 1,050 pounds or more than 1,475 pounds shall be deliverable. For purposes of computing such discount, the weight of the over or under weight animals shall be considered the same as the average weight per head of the delivered unit. Steers weighing more than 200 pounds over or under the average weight of the load are not acceptable.] The judgment of the grader as to the number of such overweight or underweight cattle in the delivery unit shall be final and shall be so certified on the grading certificate.

##### 5. Procedures and Standards for Grading, Estimating Yield and Weighing.

- a. Time for [~~inspection~~] Grading. To be eligible for delivery, cattle must be confined in a secured pen at an approved [delivery] livestock yard[s] prior to 9:00 a.m. local time on the day of delivery. [~~inspection~~] Grading and weighing shall be done on the day of delivery unless more deliveries are indicated than can be conveniently [~~inspected~~] graded and weighed on the intended delivery day. In such case the President may

allow [~~inspections~~] grading and weighing after 2:00 p.m. local time on the day preceding delivery. The buyer must be notified within an hour after the cattle are in his holding pen that the delivery intended for him for the following day has been [~~inspected~~] graded, weighed and sealed in his holding pen.

6. Delivery Invoice.

After grading and weighing, the USDA shall notify the Exchange of the results, from which the Exchange shall promptly prepare its Delivery Invoice incorporating the pen number, number of head, net weight, quality grade, estimated average hot yield, estimated yield grade, date of receipt of cattle and date of USDA [~~inspection~~] grading. The Delivery Invoice shall be promptly delivered to the buyer and seller. Upon receipt, the USDA Livestock Acceptance Certificate shall be forwarded to the clearing member representing the buyer.

7. Cost of [~~Inspection,~~] Grading and Weighing [~~and Storage~~]

All yardage costs, including driving of livestock, feeding, bedding, weighing, insurance and any other required services up to and including weighing shall be borne by the seller in accordance with the published rates as set forth in the tariff of the livestock yard. The seller shall also bear the costs of grading and documentation, which will be established annually by the Exchange.

Any charges accruing after delivery by seller to the buyer's holding pen shall be borne by the buyer.

**10103.C. Carcass Graded Deliveries**

1. Conditions.

A buyer assigned a Certificate of Delivery may call for delivery of the cattle to an approved slaughter plant corresponding to the stockyards designated in the Certificate, or to any other approved slaughter plant within 150 miles of the feedlot from which the cattle originate. For the purposes of Chapter 101, a feedlot shall be defined as any location where cattle are confined to a pen and provided access to feed and water including, but not limited to, commercial feeding operations, farmer feeding operations and stockyards.

Final grading will reflect actual carcass results. If the buyer elects carcass grading, slaughter shall not occur prior to the second business day following the buyer's notification of the CME Clearing House. The Clearing House must be notified by 10:00 a.m. on the second business day prior to the day of slaughter of the buyer's election of carcass grading, [~~and~~] the approved slaughter plant[.] and slaughter day, and whether the buyer consents to a Large Lot Delivery Unit if elected by the seller under Rule 10103.C.5.f.

Upon arrival at the slaughter plant, cattle must be allowed access to water.

3. Seller's Duties.

On the second business day prior to the day of slaughter, the Clearing House will notify the seller of the buyer's election of carcass grading, the approved slaughter plant selected by the buyer, [~~and~~] the day of slaughter selected by the buyer and representatives of the approved slaughter plant, and whether the buyer consents to a Large Lot Delivery Unit if elected by the seller under Rule 10103.C.5.f. The seller shall be responsible for contacting representatives of the slaughter plant to coordinate arrival time and time of slaughter. The cattle shall be scheduled to arrive between 6:00 a.m. and 6:00 p.m. local time on the day of slaughter. The seller shall be responsible for transportation to the slaughter plant. The seller shall notify the Clearing House of the agreed upon arrival time by 3:00 p.m. on the second business day prior to slaughter.

5. Par Delivery and Substitutions.

a. Par Delivery Unit. A par delivery unit, shipped to an approved slaughter plant designated by the buyer, shall be 40,000 pounds of live steers which produce Yield Grade 3, 55% Choice, 45% Select grade steer carcass beef, with no individual carcass weighing less than 600 pounds or more than 900 pounds.

Par delivery units shall have an actual average hot yield of 63%.

All cattle contained in a delivery unit shall be healthy. Cattle which are unmerchantable, such as crippled, sick, obviously damaged or bruised, or which for any reason do not appear to be in satisfactory condition to enter normal fresh meat marketing channels shall be excluded. No cattle showing a predominance of dairy breeding or showing a prominent hump on the forepart of the body shall be deliverable.

For carcass graded deliveries only, a "prominent hump on the forepart of the body" shall be defined as a hump on a live animal which, when measured on the resulting carcass, is expected to exceed 2 inches in height when measured from a line formed by the extension of the top line (including the fat) and measuring the lean muscle (excluding the fat) perpendicular to that line in the center of the hump. Any animal(s) with a hump estimated to exceed 2 inches when measured in this manner shall be excluded from the delivery unit. If the delivered live weight falls below the 5% tolerance as specified in Rule 10103.C.5.f., the seller is responsible for replacing the removed animal(s) until the minimum live weight is achieved.

Such determination shall be made by USDA personnel and shall be binding on all parties. All resulting carcasses must be merchantable. Carcasses which are not suitable to enter normal fresh meat marketing channels will be excluded from the delivery unit.

- d. Yield Grade Deviations. Yield grade 3 carcasses are deliverable at par. Each carcass with a yield grade of 1, 2, 4 or 5 shall receive a per pound adjustment equal to the corresponding factor described in Rule 10103.A. Per animal yield grade adjustments shall be calculated by multiplying the per pound adjustment by the average live weight of the delivery unit. ~~[Notwithstanding the above, if the cattle are slaughtered in a plant where normal use of "hot fat trimming" makes yield grade determination impossible, all carcasses will be considered to be par with respect to yield grade.]~~
- e. Quality Grade Deviations. Delivery units resulting in 55% USDA Choice grade carcasses and 45% USDA Select grade carcasses are deliverable at par. All grad[e]able carcasses in a delivery unit shall receive a quality grade adjustment computed from the factors described in ~~[Section]~~ Rule 10103.A. The Live Equivalent Choice-Select Spread (LECSS) and other factors are defined in ~~[Section]~~ Rule 10103.A. Per pound quality grade adjustments shall be as follows:

USDA Prime:	+0.45 x LECSS + Prime factor
USDA Choice:	+0.45 x LECSS
USDA Select:	-0.55 x LECSS
USDA Standard:	+0.45 x LECSS + Standard factor
Below USDA Standard:	+0.45 x LECSS + Standard factor + sub-Standard factor

Carcasses deemed ungrad[e]able with respect to quality grade by the USDA shall receive a per pound quality grade discount equal to 25% of the settlement price. The per animal quality grade adjustment shall be calculated by multiplying the per pound quality grade adjustment by the average live weight of the delivery unit.

- f. Quantity Deviations. Variations in quantity of a delivery unit not in excess of 5% of 40,000 pounds of live weight at the approved slaughter plant shall be permitted at the time of delivery, with appropriate adjustment to reflect delivered weight but with no further penalty.

The seller shall be responsible for sorting the cattle into deliverable units prior to arrival at the slaughter plant, with each unit weighing between 38,000 pounds and 42,000 pounds and meeting the other specifications of the contract, except for Large Lot Delivery Units as described in the following paragraph. Any cattle delivered to a slaughter plant in excess of 42,000 pounds, or which do not otherwise meet the specifications of the contract, shall not be considered part of the delivery unit, and the seller shall be responsible for merchandising those additional and/or undeliverable cattle.

Delivery cattle from Certificates of Intent that were tendered to the same delivery

point on the same date by one seller and are subsequently assigned to a single buyer may be grouped together for processing at the slaughter plant if both the buyer and seller consent. These Large Lot Delivery Units may not exceed a size of ten contracts. The par delivered live weight of Large Lot Delivery Units shall be 40,000 pounds times the number of contracts included in the Large Lot Delivery Unit. A 5% variance in this par delivered weight shall be allowed without penalty. For Large Lot Delivery Units only, the seller shall be relieved of the requirement that cattle be sorted into units weighing between 38,000 and 42,000 pounds prior to arrival at the slaughter plant.

- g. Other Deviations. If one or more of the carcasses is condemned or is unacceptable for entry into normal fresh marketing channels (for reasons such as measles), than each such carcass shall not be considered as part of the delivery unit. If a carcass is removed from the delivery unit for reasons stated above, the total carcass weight will reflect only those carcasses acceptable for delivery, and the total delivered live-weight shall be reduced by the average live weight times the number of carcasses removed. In the event that the total live weight falls below the 5% tolerance as specified in Rule 10103.C.5.f. as a result of the condemnation, ~~[the seller is responsible for replacing the removed carcass(es) by purchasing a steer carcass(es) from the approved slaughter facility. The live weight equivalent of such replacement carcass(es), calculated on the basis of the weight of the replacement carcass(es) divided by 63%, shall be added to the delivered live weight.~~

~~Alternatively, in the absence of contrary instructions delivered to the Clearing House at the time of tender by the clearing member representing the seller,] for each removed carcass an amount equal to either 1) the par value of a steer at the average live weight per head of the delivery unit, or 2) the average dollar value of the remaining carcasses in the delivery unit, whichever is greater, shall be credited to the buyer.~~

Excess trimming required due to injection site abscesses or other carcass defects will reduce the total delivered carcass weight, and the resulting hot yield.

Liver condemnations in excess of 20% are the liability of the seller. To determine the maximum number of allowable liver condemnations in a par delivery unit, the number of head in the delivery unit shall be multiplied by 0.20 and the result rounded to the nearest integer. For each liver in excess of the maximum allowable, a discount equal to the condemned liver factor (described in Rule 10103.A.) multiplied by the average live weight of the delivery unit shall be applied.

If, after title to the delivery unit has passed from the seller to the buyer, an animal is condemned or otherwise becomes unacceptable for slaughter due to reasons clearly beyond the control of the seller (e.g., a broken leg caused by a fall after the pen has been sealed), that animal shall be removed from the delivery unit. An amount equal to either 1) the par value of a steer at the average live weight per head of the delivery unit, or 2) the average dollar value of the remaining animals in the delivery unit, whichever is greater, shall be credited to the seller.

If, after title to the delivery unit has passed from the seller to the buyer, a carcass is condemned, heavily trimmed, or altered in any manner such that the value of the carcass is adversely affected due to reasons clearly beyond the control of the seller (e.g., a carcass that falls off the chain or rail and onto the floor), that carcass shall be removed from the delivery unit. An amount equal to either 1) the par value of a steer at the average live weight per head of the delivery unit, or 2) the average dollar value of the remaining carcasses in the delivery unit, whichever is greater, shall be credited to the seller.

If, after title to the delivery unit has passed from the seller to the buyer, any carcass data required to perform the delivery calculations cannot be obtained for one or more carcasses due to reasons clearly beyond the control of the seller (e.g., the approved slaughter facility fails to hold carcasses for regrade), each such carcass shall be deemed Choice when the final quality grading results cannot be obtained; Yield

Grade 3 when the actual yield grade results cannot be obtained; 63% or the average hot yield of the remaining carcasses in the delivery unit, whichever is greater, when the actual hot yield cannot be obtained.

6. Procedures and Standards for Grading, Determining Yield and Weighing.
  - a. Time for Arrival and Visual Inspection. Cattle shall arrive at the time agreed upon by the seller and the approved slaughter plant. Weighing and visual inspection of the cattle by USDA Meat Grading Service Personnel to ensure general conformance with the contract shall be done at the time of delivery. After completion of weighing and visual inspection, cattle will be placed in a holding pen as a unit prior to slaughter. Identity of the delivery unit shall be maintained in a manner satisfactory to the USDA Meat Grader, and shall include sealing the holding pen with a numbered seal, and recording the seal number and the plant-assigned sequential lot number of the delivery unit.
  - b. Grading and Determining Yield. [~~Carcasses must receive final grade within three business days of slaughter.~~] Approved slaughter plants normally grading after one business day must hold carcasses falling in the top third of [~~the Select grade~~] any quality grade except Prime for re-grading two business days after slaughter. Approved slaughter plants normally grading after two business days may hold carcasses falling in the top third of [~~the Select grade~~] any quality grade except Prime for re-grading three business days after slaughter. Final grade and yield results must be completed within three business days of slaughter.
7. Delivery Notice.

Final grading results must be completed within three business days after the day of slaughter. The USDA Meat Grader shall notify the Exchange of the results, from which the Exchange shall promptly prepare its Delivery Invoice incorporating the lot number, number of head, net live weight, quality grade, actual average hot yield, yield grade, date of delivery to the slaughter plant, and date of final USDA [~~inspection~~] grading. The Delivery Invoice shall be promptly delivered to the buyer and seller. Upon receipt, the USDA Carcass Grading Results Certificate shall be forwarded to the clearing member representing the buyer.
8. Cost of [~~inspection~~] Grading, Weighing, [~~Storage~~] and Transportation.

Death loss, feed and yardage, and all other costs are the responsibility of the seller until the cattle are delivered to the slaughter plant selected by the buyer. The buyer will be assessed a standard freight rate per mile for each additional mile the cattle are hauled over and above the distance between the feedlot and the stockyards to which the seller originally tendered the cattle, and this freight assessment will be paid to the seller. The standard freight rate per mile will be established annually by the Exchange. The seller shall be responsible for the cost of visual inspection and weighing upon arrival at the slaughter plant. Any additional costs of carcass grading shall be borne by the buyer.
9. Penalties.

If the seller fails to present the required quantity of deliverable cattle to the slaughter plant on the date and time specified by the buyer, the [~~penalties shall be \$.005~~] seller shall be penalized \$0.015 per pound each business day, payable to the Exchange, [~~that a load of cattle is presented but fails to pass visual inspection~~] until proper delivery is made. [~~However, for each business day that the seller fails to present a load of cattle the USDA Meat Grader can visually inspect (according to the provisions of Rule 10103.C.6.a.) the penalty shall be \$.015 per pound.~~]

10104. **PROCEDURES FOR TENDER, DEMAND, RETENDER, RECLAIM, AND ASSIGNMENT OF CERTIFICATES OF DELIVERY**

**10104.A. Tendering a Certificate**

A clearing member representing a short may present a Certificate of Delivery (on a form prescribed by the Clearing House) to the Clearing House no later than 4:30 p.m. on any business day except that Certificates may not be tendered:

1. On or before the first Friday of the contract month;
2. After the third business day after expiration.

A Certificate of Delivery is a commitment to deliver cattle conforming with contract specifications at the delivery point designated in the Certificate, or at a corresponding approved slaughter plant selected by the buyer, if the Certificate is not reclaimed.

A Certificate tendered before the termination of trading requires delivery on the sixth business day that is also a delivery day following the tender of that Certificate, if the buyer elects live grading. If the buyer elects carcass grading, the Certificate requires delivery at the option of the buyer on any day the slaughter plant is in operation between the third business day and the sixth business day, inclusive, following tender of that Certificate.

A Certificate tendered on or after the day trading terminates requires delivery on the fourth business day that is also a delivery day following the tender of that Certificate, if the buyer elects live grading. If the buyer elects carcass grading, the Certificate requires delivery at the option of the buyer on the third business day or fourth business day following tender of that Certificate, or on an intervening day that the slaughter plant is in operation.

A Certificate must include the name, location, business address, and telephone number of the feedlot from which the cattle originate. A Certificate must also include: (1) the distance between the feedlot and the stockyards to which the cattle are tendered for delivery; (2) the distance between the feedlot and the approved slaughter plants corresponding to the stockyards to which the cattle are tendered for delivery; and (3) any other approved slaughter plants within 150 miles of the feedlot and the distances to such approved slaughter plants.

The seller is responsible for determining, in advance of tendering a Certificate, if the delivery point stockyards will be able to accommodate a live-graded delivery on the sixth business day following the day of tender (fourth business day following the day of tender if tender is on or after the last trading day) should the buyer request one. If the buyer requests a live-graded delivery which the stockyards is unable to accommodate, then this will be deemed a failure by the seller to present a load of cattle for USDA grading under Rule 10103.B.8. In addition, the Exchange may prohibit deliveries on certain days for certain locations at which it deems deliveries would not be feasible due to auctions or other activities.

#### **10104.D. Retender**

A clearing member representing a long that is assigned a Certificate may retender that Certificate. The following rules govern retender:

4. A long assigned a Certificate must establish a short position in the delivery month and notify the Clearing House of retender by 4:30 p.m. on the business day following assignment. The short position may be established for the purpose of retendering without regard to the provisions of Rule [848] 562.

#### **10104.E. Reclaim**

A clearing member representing a short that has tendered a Certificate may reclaim that Certificate upon the first or second retender if there is no Demand Notice issued for that Certificate.

The reclaiming short must have established a long position in the contract month and must issue a Reclaim Notice (on a form prescribed by the Clearing House) to the Clearing House by 5:00 p.m. on the day the Certificate is retendered. The long position may be established for the purpose of reclaiming without regard to the provisions of Rule [848] 562.

### **[INTERPRETATIONS & SPECIAL NOTICES RELATING TO CHAPTER 101]**

#### **INTERPRETATION OF RULE 10104.A.—TENDERING A CERTIFICATE**

~~The seller is responsible for determining, in advance of tendering a Certificate, if the delivery point stockyards will be able to accommodate a live-graded delivery on the sixth business day following the day of tender (fourth business day following the day of tender if tender is on or after the last trading day) should the buyer request one. If the buyer requests a live-graded delivery which the stockyards is unable to accommodate, then this will be deemed a failure by the seller to present a~~

~~load of cattle for USDA inspection under Rule 10104.B.8. In addition, the Exchange may prohibit deliveries on certain days for certain locations at which it deems deliveries would not be feasible due to auctions or other activities.~~

~~If the buyer elects carcass grading, slaughter shall not occur prior to the second business day following the buyer's notification of the CME Clearing House. The buyer shall notify the Clearing House of the approved slaughter facility and slaughter day no later than 10:00 a.m. Chicago time, at least two business days prior to the slaughter day.~~

#### **INTERPRETATION OF RULE 10103.C.5.a.—PAR DELIVERY UNIT**

~~For carcass graded deliveries only, a "prominent hump on the forepart of the body" shall be defined as a hump on a live animal which, when measured on the resulting carcass, is expected to exceed 2 inches in height when measured from a line formed by the extension of the top line (including the fat) and measuring the lean muscle (excluding the fat) perpendicular to that line in the center of the hump.~~

~~Any animal(s) with a hump estimated to exceed 2 inches when measured in this manner shall be excluded from the delivery unit. If the delivered live weight falls below the 5% tolerance as specified in Rule 10103.C.5.f., the seller is responsible for replacing the removed animal(s) until the minimum live weight is achieved.~~

#### **INTERPRETATION OF RULE 10103.C.5.g.—OTHER DEVIATIONS**

~~The seller shall be responsible for sorting the cattle into deliverable units prior to arrival at the approved slaughter facility, with each unit weighing between 38,000 pounds and 42,000 pounds and meeting the other specifications of the contract, except for Large Lot Delivery Units as described in the Interpretation of Rule 10103.C.6.a. Any cattle delivered to an approved slaughter facility in excess of 42,000 pounds, or which do not otherwise meet the specifications of the contract, shall not be considered part of the delivery unit, and the seller shall be responsible for merchandising those additional and/or undeliverable cattle.~~

~~If, after title to the delivery unit has passed from the seller to the buyer, an animal is condemned or otherwise becomes unacceptable for slaughter due to reasons clearly beyond the control of the seller (e.g., a broken leg caused by a fall after the pen has been sealed), that animal shall be removed from the delivery unit. An amount equal to either 1) the par value of a steer at the average live weight per head of the delivery unit, or 2) the average dollar value of the remaining animals in the delivery unit, whichever is greater, shall be credited to the seller.~~

~~If, after title to the delivery unit has passed from the seller to the buyer, a carcass is condemned, heavily trimmed, or altered in any manner such that the value of the carcass is adversely affected due to reasons clearly beyond the control of the seller (e.g., a carcass that falls off the chain or rail and onto the floor), that carcass shall be removed from the delivery unit. An amount equal to either 1) the par value of a steer at the average live weight per head of the delivery unit, or 2) the average dollar value of the remaining carcasses in the delivery unit, whichever is greater, shall be credited to the seller.~~

~~If, after title to the delivery unit has passed from the seller to the buyer, any carcass data required to perform the delivery calculations cannot be obtained for one or more carcasses due to reasons clearly beyond the control of the seller (e.g., the approved slaughter facility fails to hold carcasses for regrade), each such carcass shall be deemed Choice when the final quality grading results cannot be obtained; Yield Grade 3 when the actual yield grade results cannot be obtained; 63% of the average hot yield of the remaining carcasses in the delivery unit, whichever is greater, when the actual hot yield cannot be obtained.~~

#### **INTERPRETATION OF FEEDLOT FOR LIVE CATTLE**

~~For the purposes of Chapter 101, a feedlot shall be defined as any location where cattle are confined to a pen and provided access to feed and water including, but not limited to, commercial feeding operations, farmer feeding operations and stockyards.~~

#### **INTERPRETATION OF RULE 10103.C.6.a—TIME FOR ARRIVAL AND VISUAL INSPECTION**

~~Delivery cattle from Certificates of Intent that were tendered to the same delivery point on the same~~



~~date by one seller and are subsequently assigned to a single buyer may be grouped together for processing at the slaughter facility if both the buyer and seller consent. These Large Lot Delivery Units may not exceed a size of ten contracts. The par delivered live weight of Large Lot Delivery Units shall be 40,000 pounds times the number of contracts included in the Large Lot Delivery Unit. In accordance with Rule 10103.C.5.f, a 5% variance in this par delivered weight shall be allowed without penalty.~~

~~For Large Lot Delivery Units only, the seller shall be relieved of the requirement (expressed in the interpretation of Rule 10103.C.5.g) that cattle be sorted into units weighing between 38,000 and 42,000 pounds prior to arrival at the approved slaughter facility.]~~

### **Discussion of Amendments**

The changes presented above reflect the Exchange's ongoing commitment, begun in CME Submission #07-39 dated May 17, 2007, to relieve market congestion by permitting the delivery of heavier cattle in live graded deliveries and eliminating long-standing inconsistencies between live graded and carcass graded deliveries. It was stated in that submission that "...the Exchange is actively pursuing other contract changes, which will be applied to newly listed contract months, to further increase deliverable supplies and prevent a recurrence of these problems." The amendments presented here, effective with the October 2008 contract month, are the latest efforts in that process.

#### **Weight-Related Changes to Rules 10103.B.4.a. and 10103.B.4.b.**

The current live graded delivery process imposes four sets of potentially conflicting weight requirements. One set of specifications requires the average weight of the delivery unit to be between 1,100 pounds and 1,350 pounds (between 1,100 pounds and 1,425 pounds beginning December 2007). Any delivery unit averaging less than 1,100 pounds or more than 1,350 pounds (less than 1,100 pounds or more than 1,425 pounds beginning December 2007) is not deliverable under any circumstances.

A second set of specifications requires the weights of the individual animals to be within  $\pm 100$  pounds of the average weight of the delivery unit for delivery at par, and within  $\pm 101$ -200 pounds of the average weight of the delivery unit for delivery at a 3-cent discount. Any individual animal weighing more than 200 pounds above or below the average weight of the delivery unit is not deliverable under any circumstances.

The third set of specifications requires the weights of the individual animals to be no less than 1,050 pounds and no greater than 1,400 pounds (no greater than 1,475 pounds beginning December 2007). The fourth set of specifications requires the delivery unit to weigh between 38,000 pounds and 42,000 pounds.

Failure to satisfy one or more of these four interrelated sets of specifications causes the delivery to fail. A brief example demonstrates how these weight requirements, even using the heavier weights that will become effective with the December 2007 contract month, can interfere with the delivery process and restrict the ability to make delivery.

*Suppose that a delivery unit has 30 animals with a total weight of 42,000 pounds and an average weight of 1,400 pounds, which is well within the allowable range of 1,100 pounds and 1,425 pounds. This delivery unit contains one animal that weighs 1,500 pounds, one that weighs 1,490 pounds, and one that weighs 1,480 pounds; all the others weigh 1,390 pounds. Even though the 1,500 pound animal is within 100 pounds of the average weight of the delivery unit and should be deliverable at par, the fact that it weighs more than 1,475 pounds means that it is not eligible for delivery and must be removed from the delivery unit.*

*Removing the 1,500 pound individual results in a delivery unit of 29 animals with a total weight of 40,500 pounds and an average weight of 1,396 pounds. Once again, the 1,490 pound animal is within 100 pounds of the average weight of the delivery unit and should be deliverable at par, but*

*because it weighs more than 1,475 pounds it is not eligible for delivery and must be removed from the delivery unit.*

*Removing the 1,490 pound individual results in a delivery unit of 28 animals with a total weight of 39,010 pounds and an average weight of 1,393 pounds. Yet again, the 1,480 pound animal is within 100 pounds of the average weight of the delivery unit and should be deliverable at par, but because it weighs more than 1,475 pounds it is not eligible for delivery and must be removed from the delivery unit.*

*Removing the 1,480 pound individual results in a delivery unit of 27 animals with an average weight of 1,390 pounds and should be deliverable at par. In addition, all of the individual animals now weigh less than 1,475 pounds. However, the total weight of the delivery unit is now only 37,530 pounds, which is less than the 38,000-pound minimum, so the entire load is rejected and the delivery fails.*

As this example shows, coordinating four different sets of weight requirements can be extremely difficult, and these operational hurdles likely discourage deliveries even when market conditions make delivery economically feasible. In effect, the delivery process is similar to solving a set of simultaneous equations. In addition, the final outcome is highly sensitive to which animals are sorted off during the delivery process, and it can be shown that the same set of animals can become deliverable or undeliverable depending on which individuals, and in what order those individuals, are sorted off from the delivery unit.

Consequently, the current live graded delivery requirements may result in additional handling of the animals, even if they have been properly sorted prior to arrival at the delivery point. This additional handling often leads to delays in completing the delivery process and increases the risk of injury to the animals. Furthermore, the complexity of meeting these multiple weight requirements requires delivering shorts to ship additional animals to the delivery point, and then transport the rejected and/or extra animals back to the feedlot once the delivery is completed, all of which imposes additional costs in the form of freight and shrink.

While CME's current live graded delivery procedures may have reflected cash market cattle marketing practices at some time in the past, they do not represent how cattle in the cash market are bought and sold today. In contrast, CME's carcass graded delivery procedures are consistent with current cash market practices, and those carcass specifications should serve as the template for reconfiguring the live graded delivery specifications. Therefore, beginning with the October 2008 contract month, CME is eliminating all requirements pertaining to the average weight of the delivery unit, as well as all requirements pertaining to the range of weights around that average weight. Only individual weights will be considered upon implementation of these amendments. At the same time, CME also is eliminating the 3-cent discount for cattle weighing  $\pm 101$ -200 pounds of the average weight of the delivery unit.

In addition, CME is making additional changes to the individual weight specifications, including a further increase in the maximum deliverable weight. As noted earlier, beginning with the December 2007 contract month the maximum individual live weight will increase to 1,475 pounds at par, which is equivalent to 950 pounds on a carcass basis. With these latest amendments, effective with the October 2008 contract month, individual animals weighing more than 1,475 pounds but less than or equal to 1,550 pounds (equivalent to 950-1000 pounds on a carcass basis) will be deliverable on a live graded basis, at the same market-based discount used for 950-1000 carcasses in carcass graded deliveries. These changes will make the weight requirements for live graded and carcass graded deliveries seamless for cattle weighing between 1,050 pounds and 1,550 pounds, will permit the delivery of the same animals in either live graded or carcass graded deliveries, and will result in identical outcomes under both delivery methods for the same grading results.

To determine the impact on deliverable supplies of this latest weight increase, we have reviewed CME carcass graded deliveries beginning December 2003. It should be noted that there was no distinction between carcasses weighing 950-1000 pounds and those weighing more than 1000 pounds in CME carcass graded deliveries prior to December 2003, so the necessary data are not available to conduct this analysis for earlier delivery periods.

For all delivery periods from December 2003 through June 2007, there were 404 carcass graded deliveries involving 12,858 head. Of the resulting 12,858 carcasses, 337 carcasses (2.62%) weighed 950-1000 pounds; only 56 carcasses (0.44%) weighed more than 1,000 pounds. However, these data understate the impact on deliverable supplies and the ability and willingness of delivering shorts to make delivery, due to the elimination of the weight-related bottlenecks and penalties described above.

In designing these changes, the Exchange has worked closely with the USDA-AMS Livestock & Grain Market News Branch so that live graded deliveries can be completed in a timely and efficient fashion, without compromising the grading results that determine the final value of the delivered animals. CME is confident that these changes will streamline the live graded delivery process, but will closely monitor the results in October 2008 and subsequent delivery periods to see if any modifications are needed.

### Other Changes

In addition to the amendments discussed in the previous section, the Exchange is taking this opportunity to eliminate obsolete and/or inconsistent rule language, incorporate all Interpretations into the corresponding rules, and further align the carcass graded and live graded delivery provisions. These changes are self-explanatory and can be summarized as follows:

#### Obsolete/Inconsistent Rule Language

- Change "inspection" to "grading" to more accurately reflect the procedures used in the Live Cattle delivery process (Rules 10100, 10103.B.5.a., 10103.B.6., 10103.B.7., 10103.C.7., 10103.C.8.)
- Eliminate the reference to shipment of live cattle by "rail" in live graded deliveries and make the corresponding live and carcass language consistent (Rule 10103.B.4.a.)
- Make consistent use of the term "approved livestock yards" in live graded deliveries (Rule 10103.B.5.a.)
- Standardize use of the terms "approved slaughter plant" and "slaughter plant" (Rules 10103.C.5.f., 10103.C.6.a., 10103.C.6.b.)
- Eliminate the provisions for "hot fat trimming" in carcass graded deliveries (Rule 10103.C.5.d.)
- Correct the spellings of "gradable" and "ungradable" (Rule 10103.C.5.e.)
- Replace the word "Section" with "Rule" (Rule 10103.C.5.e.)
- Eliminate the provisions that allow the purchase of replacement carcasses in carcass graded deliveries (Rule 10103.C.5.g.)
- Clarify the title and make consistent use of the term "visual inspection" to describe the examination process performed at the time of unloading in carcass graded deliveries (Rule 10103.C.6.a.)
- Clarify the procedure used by USDA for re-grading of carcasses in carcass graded deliveries and eliminate redundant language so that carcasses in the top third of any quality grade except Prime are eligible for regrade (Rule 10103.C.6.b.)
- Eliminate the references to "storage" in the delivery process (Rules 10103.B.7., 10103.C.8.)
- Change "Rule 818" to "Rule 562" to reflect revised rule numbers (Rules 10103.D., 10103.E.)

#### Interpretations

- Move the first paragraph of "Interpretation of Rule 10104.A – Tendering a Certificate" to the end of Rule 10104.A.
- Move the second paragraph of "Interpretation of Rule 10104.A – Tendering a Certificate" to the middle of Rule 10103.C.1., with corresponding language in Rule 10103.C.3.
- Move "Interpretation of Rule 10103.C.5.a. – Par Delivery Unit" to the end of Rule 10103.C.5.a.
- Move the first paragraph of "Interpretation of Rule 10103.C.5.g. – Other Deviations" to the end of Rule 10103.C.5.f.

- Move the second, third, and fourth paragraphs of "Interpretation of Rule 10103.C.5.g. – Other Deviations" to the end of Rule 10103.C.5.g.
- Move "Interpretation of Feedlot for Live Cattle" to the middle of Rule 10103.C.1.
- Move "Interpretation of Rule 10103.C.6.a. – Time for Arrival and Visual Inspection" to the end of Rule 10103.C.5.f.

Carcass Graded Deliveries

- Make the language and penalties for failure to deliver in carcass graded deliveries consistent with those used in live graded deliveries (Rule 10103.C.9.)
- Clarify the deadlines for the receiving long in a carcass graded delivery to accept or reject Large Lot Delivery (Rules 10103.C.1.) and for the Clearing House to notify the delivering short (Rule 10103.C.3.)

Concluding Comments

The Exchange believes that these actions demonstrate its continuing commitment to protecting the integrity of its contracts and meeting its obligations under the Core Principles. In particular, Core Principle #3 requires Designated Contract Markets to list "only contracts that are not readily susceptible to manipulation" and Guideline #1 requires, for contracts involving physical delivery, that "the terms and conditions, as a whole, result in a deliverable supply such that the contract will not be conducive to price manipulation or distortion and that the deliverable supply reasonably can be expected to be available to short traders and salable by long traders at its market value in normal cash marketing channels."

The Exchange believes these amendments reflect the best interests of the broad spectrum of market participants, and are in keeping with CME's responsibilities as a Designated Contract Market to maintain fair, efficient, and orderly markets, so that the Live Cattle contract continues to perform its vital price discovery and risk management functions.

The Exchange certifies that this action complies with the Commodity Exchange Act and the regulations thereunder.

If you have any questions regarding this submission, please contact Paul Peterson at (312) 930-4587 or via e-mail at paul.peterson@cmegroup.com or myself. Please refer to CME Submission #07-74 in all correspondence regarding this matter.

Sincerely,

/s/ Stephen M. Szarmack  
Director and Associate General Counsel