



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
Telephone: (202) 418-5260
Facsimile: (202) 418-5527
www.cftc.gov

Division of
Market Oversight

October 30, 2009

Kathleen Cronin
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, IL 60606

RE: The Board of Trade of the City of Chicago, Inc. ("CBOT") Market Regulation
Advisory Notice RA0907-1

Dear Ms. Cronin:

On October 19, 2009, CBOT issued Market Regulation Advisory Notice RA0907-1 ("Advisory Notice") stating, among other things, that CBOT rules do not permit the execution of Exchange of Futures for Futures ("EFF") transactions and that CBOT does not permit contingent or transitory Exchanges for Related Positions ("EFRPs"). The Advisory Notice was issued subsequent to the Commodity Futures Trading Commission ("Commission") approving an EFF rule submitted by ELX Futures L.P. ("ELX"). That rule allows market participants to privately negotiate 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 identical contracts, or conversely, establishing positions on another DCM to replace identical positions liquidated on ELX.

The Advisory Notice identifies EFFs as impermissible under CBOT Rule 538. Additionally, the Advisory Notice points out that the Rule allows parties to privately negotiate a number of EFRP transactions with similar financial outcomes. Specifically, CBOT Rule 538 allows parties to privately negotiate Exchange for Physical ("EFP") transactions, Exchange for Risk ("EFR") transactions, and Exchange of Options for Options ("EOO") transactions. As the CBOT allows certain similar transaction as EFRPs and not others, the Division of Market Oversight ("DMO") has certain questions concerning CBOT's prohibition of EFFs under the EFRP rule.

Therefore, pursuant to Commission Regulations 38.5(b) and 38.5(c), DMO requests a written statement, together with supporting data, information and documents that:

1. Provide a rationale (legal and economic) for not allowing EFFs while allowing EFPs, EFRs, and EOOs.

2. Demonstrate how the Advisory Notice and Rule 538 comply with Core Principle 18 (Antitrust Considerations);

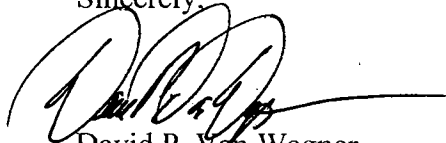
3. Respond to the assertion in the attached October 20, 2009 letter from ELX Futures LP (“ELX letter”) that CBOT’s self certification of the Advisory Notice amounts to a “false certification” as that term is used in Regulation 40.6(b);

4. Respond to the assertion in the ELX letter that CME Group Designated Contract Markets have “in a number of markets, and for many years, accepted transitory trades”; and,

5. Address why, despite the statement in CME Group Market Advisory Notice RA0901-5 that the four CME Group exchanges are adopting harmonized rule language with respect to Rule 538, the CBOT Advisory Notice prohibits EFFs while EFFs are permitted on COMEX.

Please send your written statement within two weeks from the date of this letter to Steven Schoenfeld, Division Director, at the address above. If you have any questions about this matter, please feel free to call me at 202-418-5481 or Rick Shilts, Deputy Director for Market & Product Review, at 202-418-5275.

Sincerely,

A handwritten signature in black ink, appearing to read 'David P. Van Wagner', with a long horizontal flourish extending to the right.

David P. Van Wagner
Chief Counsel

Attachment:
ELX Letter



Neal L. Wolkoff
Chief Executive Officer
ELX Futures L.P.
www.elxfutures.com

T. 212 294 8056
F. 212 294 8058

110 East 59th Street
New York, NY 10022
nwolkoff@elxfutures.com

October 20, 2009

Mr. David Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Dear Mr. Stawick:

ELX Futures, L.P. ("ELX") respectfully submits this request, pursuant to Commission Reg. 40.6(b), 17 CFR 40.6(b), to the Commodity Futures Trading Commission (the "Commission") to stay the self-certified Advisory Notice filed by the CME Group's ("CME")¹ subsidiary CBOT on October 16, 2009 (CBOT RA0907-1), hereinafter referred to as the "Rule Interpretation." The request for the Commission to stay the effectiveness of such self-certified Rule Interpretation is based on (1) the factual errors contained in the certification, which render the certification a "false certification" as that term is used in 40.6(b); and (2) because implementation of the Rule Interpretation will violate Core Principle 18 (Antitrust Considerations), Section 5(d)18 of the Commodity Exchange Act (the "Act"), 7 USC Section 7(d)18.

The Commission may hold hearings to determine whether a false certification has been filed, and may direct the modification of CME Rule 538 to remove any antitrust taint or ambiguity created by the erroneous Rule Interpretation, pursuant to Section 8a(7) of the Act, 7 USC Section 12a(7).

The Rule Interpretation sets forth the purported right of the CME and its CBOT subsidiary to subject the CME's clearing members to rule enforcement actions should they offer for clearing to the CME's clearinghouse Exchange of Futures for Futures ("EFF") trades that are executed and submitted in accordance with a duly approved rule by the Commission.

¹ Inasmuch as the direct threat of disciplinary action for submitting an EFF trade to the CME clearinghouse is on the CME's clearing members, we will ignore the substantive role of the CBOT and treat that captive organization as the issuer of the Rule Interpretation in name only.

ELX maintains that once the Commission has approved a rule, an exchange using its rule enforcement powers as a self-regulatory organization ("SRO") does not have the authority to say that it will deny use of the rule by intended beneficiaries without first seeking reconsideration from the Commission.

In light of the Commission's rule approval, in which the Commission concluded as part of its statutory consideration that ELX Rule IV-15 did not violate the Act, users of the rule, and ELX Futures, L.P. ("ELX"), are entitled to the legal certainty that Commission approval brings. Section 5c(c)(3) of the Act, 7 USC Section 7a-2(c)(3), which deals with rule approval standards, states that, "the Commission shall approve any such ... new rule, or rule amendment unless the Commission finds that the ... new rule or rule amendment would violate this Act." Conversely, by approving a rule submitted for prior approval, and reviewing the rule for 45 or 90 days, as the case was with ELX's EFF Rule, the Commission did not find that the Rule violated the Act.

Inasmuch as ELX submitted the EFF rule for Commission approval, which was granted, CME does not now have a basis to contend that the EFF rule violates regulatory concerns or the public interest. Those concerns have been vetted and found lacking in merit by the Commission. If CME believes the Commission made an error, rather than seeking to impose its own independent view on whether the EFF rule should be permitted to apply then CME should ask the Commission for reconsideration rather than unilaterally taking its own action to chill the market's use of the approved rule.

In its Rule Interpretation, CME contends that it does not accept "contingent or transitory EFRPs," and then characterizes the EFF as a transitory and contingent trade. In addition, CME references its Rule 538 and states that the EFF Rule is outside the coverage of the Rule. On both claims the CME is inaccurate. By certifying incorrect information in its filing, the Commission has clear grounds for staying the self-certification. Further, an understanding of accurate information pertaining to the matters at hand should result in the Commission ultimately denying CME's Rule Interpretation in its entirety unless it is first withdrawn.

As to its first claim about not accepting transitory trades, CME has in a number of markets, and for many years, accepted transitory trades (we will not seek to draw a distinction between transitory and contingent trades, and instead treat them interchangeably). Transitory trades are the basis for every, or nearly every, trade in the Clearport service. Transitory trades are accepted for EFRPs in the FX market; in energy; in metals; and under a recent Advisory Notice, in agricultural markets.

In its Advisory Notice dated October 2, 2009, (CME Group RA0910-5) CME proposes for its CBOT affiliate a transitory EFRP (see Q&A #9) in its agricultural products:

Q9: Can two EFRPs be utilized to facilitate inventory financing in CBOT agricultural commodities?

A9: The following transaction is permitted provided that it is entered into for

the purpose of obtaining inventory financing for an agricultural commodity. A participant may purchase the agricultural commodity and sell the equivalent quantity of futures contracts to a counterparty through the execution of an EFP and may grant to the counterparty the non-transferable right to effect a second EFP on some date certain in the future which will have the effect of reversing the original EFP.

On October 2 the Advisory proposed a trade where Party A sells to Party B on Day 1 and agrees to buy the same contracts back from Party B on Day 3, which is most definitely a contingent trade. Yet, the certification dated October 16 claims that no such trades are allowed.

Transitory trades satisfy Rule 538 (see below for the discussion of the CME's recent rule "harmonization" effort) in many different markets, and they (assuming the EFF is one) cannot reasonably be considered a rule violation - an offense to the public interest - when it comes to U.S. treasury futures, one of the few markets in which the CME has faced direct competition over the last dozen years.

In addition to the inaccuracy that CME does not accept transitory trades, the EFF is factually not a transitory trade. The EFF consists of a trade where A sells an ELX OTC Future to B and A buys an OTC CME future from B. A transitory trade involves the rapid or prearranged purchase and sale of the same contracts between parties. Here, the parties are exchanging different contracts, i.e. CME and ELX OTC futures, and thus the EFF trade as proposed by ELX and approved by the Commission is not transitory or contingent.

As to the second claim, that the EFF falls outside of Rule 538, CME omits important facts in its certification which render the certification materially inaccurate. These facts are as follows:

1. On October 2, CME released Advisory RA0910-5, which sought the "harmonization" of EFRP rules across the several markets controlled under the CME umbrella. Within the harmonized rules were two NYMEX Rules dealing with EFFs between cash settled e-minis in natural gas and crude and their larger, physically settled brethren contracts. (see Footnote 2). While the Advisory eliminated NYMEX Chapter 6, it was silent about the status of these EFF rules, and did not explicitly prohibit EFFs in the amended Rule 538. The CME now asks the market to believe that "harmonization" does not mean that various markets would live under the same rule interpretations. Instead, the CME claims that "harmonization" means essentially that it can impose whatever interpretation it wants in any given market to suit its interests.
2. Although the Rule Interpretation cites the Rule language, it fails to cite the explanatory questions and answers that come after the rule language and that were made part of the Advisory RA0910-5. These questions and answers were made part of the certification that accompanied the October 2 Advisory, and are part of the rule submission. In the very first question, the CME poses the relevant question:

Q1: What are EFRP transactions?

A1: EFRP is an acronym for Exchange for Related Positions. Exchange for Physical ("EFP"), Exchange for Risk ("EFR") and Exchange of Options for Options ("EOO") transactions are collectively known as EFRP transactions. ...

An EFR transaction is a privately negotiated and simultaneous exchange of a futures position for a corresponding **OTC swap or other OTC derivative** in the same or a related instrument (emphasis added).

An exchange of an OTC future in the EFF Rule can be reasonably interpreted as an "OTC swap or other OTC derivative." This is certainly the case where the CME has two existing rules allowing EFFs², which have to be assumed to be carried over into the new "harmonized" regime.

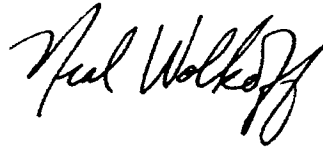
CME's Rule Interpretation has no factual or regulatory basis, and is clearly oriented toward avoiding a business challenge from a new market trading competitive products.

Most troubling, the Rule Interpretation threatens firms using ELX Rule IV-15 with the rule enforcement powers that CME was given to protect the public interest. ELX is the fourth futures exchange in 11 years to try to compete with U.S. Treasury futures traded on the CME and its predecessor CBT. ELX, however, is the first to grab consistent market share, and attract a customer base beyond the initial investors. Absent a regulatory purpose to use rule enforcement powers, the threatened use of such is in violation of Core Principle 18, and has chilled the market into not using a valid rule, thus sparing CME from legitimate market competition that would further the public interest and benefit investors.

² Prior to the Issuance of CME Advisory Notice RA0910-5, which sought the "harmonization of EFRP Rules across markets, and was made effective October 5, 2009, the NYMEX rulebook contained EFF Rules for natural gas and crude markets:: Rule 6.21B Exchange of NYMEX Futures, Section B. Exchange of NYMEX Cash Settled "Penultimate Big" Futures for, or in Connection with, NYMEX "Physical" Futures Transactions

Thank you for your consideration.

Sincerely,

A handwritten signature in black ink, appearing to read "Neal Wolkoff". The signature is written in a cursive style with a large, stylized initial "N".

Neal L. Wolkoff

cc: Cyrus Amir-Moki, Esq., Counsel to the Chairman