

Tab 14



LONDON METAL EXCHANGE

From the Company Secretary's Office

To: All members
Date: 24 November 1994
Subject: Rule Change: Net Worth Requirement for Categories 1, 2, 3 and 4

At a Meeting of the Board of Directors held on 9 November 1994, it was resolved that pursuant to Regulation 1 Part 2 Membership Enforcement and Discipline of the Rules the net worth requirement of Members be amended with effect from 1 April 1995, as follows:-

Category	Present Net Worth Requirement *	Net Worth Requirement * 1 April 1995	Relevant Part 2 Regulation
1. Ring Dealing Member	STG.2,00,000	STG.5,000,000	1.2.4
2. Associate Broker Clearing Member	STG.2,000,000	STG.5,000,000	1.3.1.3
3. Associate Trade Clearing Member	STG. 500,000	STG.2,500,000	1.3.1.3
4. Associate Broker Member	STG.1,000,000	STG.5,000,000	1.4.1.2

* Sterling or Sterling Equivalent.

The Board of Directors asks Members to not that, where possible, they should meet the new requirements as soon as possible before 1 April 1995 deadline.

N D Banks

cc. Board directors

Ref:94/436



LONDON METAL EXCHANGE

To: All Members, Warehouse Companies and their London Agents

Subject: LME WAREHOUSING PROCEDURES

The LME has revised its arrangements with warehouse companies for the storage of metals on LME Warrant.

Some of the revised arrangements impact on Members and their clients but they generally recognise existing practice and procedures as well as taking into account new developments in warehousing requirements in the last few years.

Members are asked to note that the annual pay up of rent is now obligatory and as soon as practicably possible a legend to that effect will appear on all new Warrants.

The obligation to pay rent annually at 31st March will also apply to all LME Warrants not bearing any such legend. Failure to pay rent on time will allow warehouse companies to exercise rights of recovery including interest charges before release of metal.

The delivery of Warrants through Clearing after 1st April in any year, for which rent is outstanding as at the previous 31st March, will be a breach of LME Rules and subject to disciplinary action with effect from 1st April 1996.

Members should also note that the warehouse companies are being reminded of their obligation to reject material and refuse to put metal on LME Warrant which does not meet the requirements of LME Contracts.

Because of difficulties that have emerged when warehouse companies seek to replace Warrants for legitimate reasons, such as corporate identity change, it will also be a breach of LME Rules if Warrant holders fail to co-operate with procedures laid down. Co-operation of Members in orderly replacement of Warrants when necessary, which in any case is in the interests of Members, is vital to the integrity of the Market. These procedures will take effect from 1 February 1996.

D. E. King

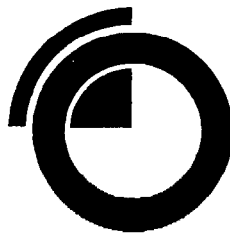
Ref: 96:019

Date: 11th January 1996

cc: Board of Directors

THE LONDON METAL EXCHANGE LIMITED, 56 LEADENHALL STREET, LONDON EC3A 2BJ
TELEPHONE: 44 (0)171 264 5555 TELEX: 8951367 FAX: 44 (0)171 680 0505

A COMPANY LIMITED BY GUARANTEE. REGISTERED IN ENGLAND No. 2128666. REGISTERED OFFICE: 56 LEADENHALL STREET, LONDON EC3A 2BJ



LONDON METAL EXCHANGE

From the Company Secretary's Office

To: All Members

Subject: Automatic Declaration of Certain In-the-Money Options

Pursuant to Notice 96:451 of 20th December 1996, wherein Members were advised that the Board of Directors at its Meeting on 13th December 1996 had resolved to adopt a recommendation by the Traded Options Committee for the automatic declaration of certain in-the-money Options, it has now been possible to accelerate the implementation date for this project and accordingly it is now intended that the procedures set out below will be implemented for the June 1997 declaration.

PROCEDURE

The procedure, which will apply initially to Exchange Options only (not Client Options), is as follows:-

1. At 17.00 hours on the Last Trading Day for the relevant (i.e. expiring) Exchange Option, the Executive will calculate the at-the-money Strike Price and the range of Exchange Options which will be automatically declared for each metal in each clearing currency as follows :-
 - a) The Futures price for the relevant Prompt Date (i.e. the third Wednesday) will be calculated in the normal way from the Closing Prices.
 - b) The Executive, in its absolute discretion, will identify the at-the-money Strike Price, as being the closest Strike Price to the Futures price for the relevant Prompt Date.
 - c) The Executive will identify the two Strike Price gradations either side of the identified at-the-money Strike Price.

In the event that the Futures price for the relevant Prompt Date is exactly mid-way between two Strike Prices, the at-the-money Strike Price will be established by rounding to the higher of the two Strike Prices.



- d) When the Closing Prices are published as provisional, a provisional at-the-money Strike Price will also be published and be subject to the same objection procedures as the Futures prices.
- e) Subject to any changes to the above as a result of changes to the Closing Prices or the at-the-money Strike Price pursuant to the objection procedure, the at-the-money Strike Price for each metal in each clearing currency will be published by the Exchange as final at the same time as the Futures valuations are published as being final at around 18.15 hours.

The Exchange will at the same time publish the range of Strike Prices which will be subject to automatic declaration, i.e. for Call Options, Strike Prices two Gradations or more below the at-the-money Strike Price and for Put Options those which are two Gradations or more above the at-the-money Strike Price.

- 2. An Exchange Call Option will be declared automatically if it is in-the-money with a Strike Price that is two Gradations, or more, below the at-the-money Strike Price.
- 3. An Exchange Put Option will be declared automatically if it is in-the-money with a Strike Price that is two Gradations, or more, above the at-the-money Strike Price.
- 4. All other Exchange Options will be subject to manual declaration by the Taker in accordance with the current procedures which are set out in Regulation 3 of Part 5A Options Regulations of the LME Rules.
- 5. Clearing Members will be able to access all of their Exchange Options subject to automatic declaration at LCH on the morning of the Last Declaration Day, prior to the time when the declarations become effective, through their LCH terminals.
- 6. In the event of an excessive overnight price movement for a particular metal, or for other reasons, Takers of Exchange Options will be able to reverse the automatic exercise of an Exchange Option by manual intervention prior to the time when declarations become effective. This process can be manually re-reversed if the Taker so desired, again via Members' LCH terminals.
- 7. All declaration times will continue to be as at present.



8. It is the Taker Members' responsibility to ensure that any Exchange Options which are in-the-money but not subject to automatic declaration are manually declared and that any Exchange Options which as a result of a large price movement are out-of-the-money, but are still subject to automatic declaration, are manually un-declared, via their LCH terminals.
9. In addition to the information available from the LME Matching and Clearing Systems, there will be a LMEVFS feed to quote vendors which will provide the at-the-money Strike Prices and the range of Strike Prices for which declaration will be automatic, together with the foreign exchange rates used for the three non-major clearing currencies.
10. As has already been set out in the first section of this Notice, the procedure does not include Client Options. However, Regulations 3.4 and 3.5 of Part 5A, Options Regulations do allow for the declaration between the parties to a Client Option to be in such a manner as has been agreed between them. It would, therefore, not be a breach of the LME Rules for Members to adopt the above procedures for the declaration of Client Options.

A handwritten signature in black ink, appearing to read 'N. D. Banks', with a long horizontal line extending to the right.

N. D. Banks

8th April 1997

Ref: 97:128

cc: Board of Directors



LONDON METAL EXCHANGE

From the Company Secretary's Office

To: All Members

Subject: Non-Market Price Transactions (NMPTs) - Standard Risk Disclosure

Pursuant to Notice 97:296 of 23rd September 1997, please find herewith the LME's Standard Risk Disclosure to be used in compliance with the terms of the above Notice.

Members are reminded that any alternate risk disclosure used must meet the standards set by the Standard Risk Disclosure.

STANDARD RISK DISCLOSURE STATEMENT FOR NMPTs

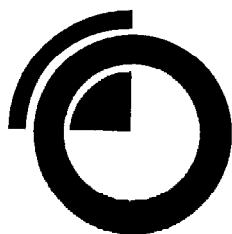
"The London Metal Exchange requires that before we enter into any transaction with you otherwise than at current market prices (termed "non-market price transactions" or "NMPTs"), we must draw your attention to the risks inherent in entering into such trades. NMPTs may have legitimate uses for some market participants. However, unless properly controlled it is possible that NMPTs may be used to defer accounting for losses or profits and thereby avoid their disclosure. Alternatively, the use of NMPTs could facilitate fraud or the concealment thereof. Unless the true market value of NMPTs is taken into account when considering the overall trading position, the apparent financial position may well be misleading. Accordingly it is the responsibility of market participants to ensure that all NMPTs have been properly authorised, reported, reviewed and accounted for."

N. D. Banks

6th October, 1997

Ref: 97:321

cc: Board of Directors



LONDON METAL EXCHANGE

To: All Ring Dealing Members

Subject: Access to Audio and Video Tapes

Ring Dealing Members will recall that on 26th June 1997, the LME introduced procedures for access to audio and video tapes, to be effective 1st October 1997.

After two months of operation, an internal review of the procedures has been undertaken and the Board of Directors at its Meeting on 10th December 1997 resolved to accept a recommendation to slightly amend those procedures in order to make them more efficient and convenient for both Ring Dealing Members and LME Executive staff.

The amended procedures, which also reflect the appointment of Mr. Alan Whiting as Executive Director: Regulation and Compliance, are effective immediately and a copy is enclosed for your information.

N. D. Banks
Director of Operations

Enc.

12th December 1997

Ref: 97:432

cc: Board of Directors
Ring Committee



CENTRALISED RECORDING OF ALL RING DEALING MEMBERS' TELEPHONE LINES ON THE TRADING FLOOR AND VIDEO SURVEILLANCE OF TRADING IN THE RING

Since the introduction on 1st October 1997 of the centralised recording of all Ring Dealing Members' telephone lines in the Ring Dealing Area of the Exchange and video recording of trading in the Ring, in the light of experience it is now appropriate to amend the Rules for access to, and retention of, the tapes as follows :-

A) RULES FOR ACCESS TO AUDIO TAPES

1. SECURITY

- 1.1 Audio tapes resulting from the compulsory recording of Ring Dealing Members' telephone lines on the Trading Floor will be the property of the Exchange.
- 1.2 The audio tapes will be kept in a secure environment in the basement of the Exchange premises for a period of approximately three months. After this duration the audio tapes will be kept off-site at a secure location to be determined by the LME Executive.
- 1.3 The audio tapes will be held by the Exchange for a total period of thirty months and then re-used, if appropriate.
- 1.4 The Executive will maintain a written record of all Ring Dealing Members' requests for access to audio tapes.
- 1.5 The Executive will maintain a written record of its authorisations of Ring Dealing Members' requests for access to audio tapes.
- 1.6 Ring Dealing Members will only be able to access audio tapes of their own telephone lines. They will be entitled to listen to the contents thereof with the use of headsets provided by the Executive in a secure room in the basement of the Exchange premises. Two booths will be provided for confidentiality.



2. ACCESS TO AUDIO TAPES OF RING DEALING MEMBERS' TELEPHONE LINES

- 2.1 An Authorised Dealer or senior member of a Ring Dealing Member's staff e.g. Compliance Officer, may require access to an audio tape of that Member's own telephone lines, by filling in an Audio Recording Access Request Form.
- 2.2 In normal circumstances the LME's Chief Executive or Executive Director for Regulation and Compliance (DRC), or any staff member of the LME Compliance or Market Operations Departments authorised by the Chief Executive or DRC, may listen to audio tapes of any Ring Dealing Members' telephone lines as part of the Exchange's monitoring and surveillance procedures, but only after the appropriate Ring Dealing Member has received written notification.
- 2.3 In the event that the DRC considers that to notify the Ring Dealing Member could prejudice the Exchange's ability to carry out its regulatory functions, the DRC may in writing authorise access to audio tapes by the LME Compliance Department without the Ring Dealing Member in question being notified. All appropriate written documentation will be maintained by the LME Compliance Department.
- 2.4 In the event that a third party such as a regulatory authority, a Client, or another Member requests access to an audio tape of a Ring Dealing Member's telephone lines, written authorisation will be required from the Chief Executive or Managing Director of the relevant Ring Dealing Member.
- 2.5 In the event that a relevant regulatory authority such as the SFA considers that to seek the Ring Dealing Member's permission and involvement could prejudice the regulatory authority's ability to carry out its regulatory functions and the DRC concurs, the DRC may in writing authorise access to audio tapes by the regulatory authority without advising the Ring Dealing Member in question. All appropriate written documentation regarding such third party access will be maintained by the DRC.
- 2.6 Subject to any legal constraints, for example a court order, where a Ring Dealing Member requires a copy of a recording of its telephone lines made by the Exchange, a copy of the relevant portion of the audio tape will be provided by the Executive.



- 2.7 The DRC may in writing authorise the making of a copy of a portion of audio tape of a Ring Dealing Member's telephone lines in the event he deems it necessary for the LME Compliance Department. He may also authorise in writing the making of a copy for and its provision to an appropriate regulatory authority such as the SFA to fulfil its relevant regulatory obligations.
- 2.8 In the event that a third party such as a regulatory authority, a Client, or another Member requests a copy of a recording of a Ring Dealing Member's telephone lines made by the Exchange, a copy of the relevant portion of the audio tape will be provided by the Executive subject to written authorisation by the Chief Executive or Managing Director of the relevant Ring Dealing Member.
- 2.9 In the event that a relevant regulatory authority such as the SFA considers that to seek the Ring Dealing Member's permission and involvement could prejudice the regulatory authority's ability to carry out its regulatory functions and the DRC concurs, the DRC may in writing authorise the making of a copy of the relevant portion of the audio tape of a Ring Dealing Member's telephone lines without advising the Ring Dealing Member in question.
- 2.10 The Board of Directors may amend the Rules for access to audio tapes of Ring Dealing Members' telephone lines as and when it deems appropriate.

3. ADVICE TO CLIENTS

- 3.1 There will be no warning tone to indicate that calls are being recorded from the Trading Floor. (This use by the LME of audio recording without the warning tone has been approved by the Office of Telecommunications.)
- 3.2 Ring Dealing Members must inform Clients that when conversing with their own staff by means of telephone communications on the Trading Floor, the conversation will be audio recorded. Ring Dealing Members may wish to include this information in their agreements with Clients using the following or similar wording :-

"The Ring Dealing Member wishes to draw to the attention of Clients that all telephone conversations to and from the LME Trading Floor are subject to audio recording by the Exchange. Such recording has been approved by OFTEL and will take place without the use of a warning tone."



4. AUDIO RECORDING PLAYBACK REQUESTS

- 4.1 The Ring Dealing Member must complete the Audio Recording Access Request Form in full stating the name of the Ring Dealing Member name of individual wishing to listen to the audio tape, handset (by colour), date and time of recording required, and signed by a senior manager from the Ring Dealing Member such as an Authorised Dealer or Compliance Officer.
- 4.2 When the relevant audio tape has been retrieved by a properly authorised IT Supervisor from the Executive on the instruction of the LME Market Operations Department or, where appropriate, the LME Compliance Department, the relevant Ring Dealing Member will be notified and a time will be arranged for the authorised person to access and listen to the audio tape.
- 4.3 When the person authorised by the Ring Dealing Member listens to the relevant audio tape in the designated secure room, an appointed member of the LME Market Operations Department or, where appropriate, the LME Compliance Department, and a properly authorised IT Supervisor from the Executive will be present.
- 4.4 In the event of third party access to an audio tape recording of a Ring Dealing Member's telephone lines being granted, subject to the procedures in Regulation 2, a senior person from the relevant Ring Dealing Member will be present with an appointed member of the LME Compliance Department and a properly authorised IT Supervisor from the Executive.
- 4.5 The LME Compliance Department will maintain a written record of every event of access being granted for a play back by a Ring Dealing Member and/or third party.

5. COSTS

- 5.1 The charges and costs for the installation and maintenance of a centralised voice recording system for the Trading Floor will be prescribed by the Board of Directors and may vary from time to time as it deems appropriate.
- 5.2 The charges and costs for each playback by a Ring Dealing Member and/or third party will be prescribed by the Executive and may vary from time to time as it deems appropriate.



6 LIABILITY

- 6.1 Members should note that the centralised voice recording services provided by the Exchange are subject to exclusion of liability as cited in Regulation 15 of Part 3 Trading Regulations :

" the Exchange shall not be liable to any Member or Client for loss (including any indirect or consequential loss including, without limitation, loss of profit), damage, injury, or delay, whether direct or indirect, arising from any of the circumstances or occurrences referred to in Regulation 15 of Part 3 Trading Regulations from any act or omission of the Exchange, its officers, employees, agents or representatives under the Rules or pursuant to the Exchange's obligations under statute or from any breach of contract by or any negligence howsoever arising of the Exchange, its officers, employees, agents or representatives."

B) RULES FOR ACCESS TO VIDEO TAPES

1. SECURITY

- 1.1 Video tapes resulting from the recording of Ring trading will be the property of the Exchange.
- 1.2 The video tapes will be kept in a secure environment in the basement of the Exchange premises for a period of approximately three months. After this duration the video tapes will be kept off-site at a secure location to be determined by the Executive.
- 1.3 The video tapes will be held by the Exchange for a total period of thirty months and then re-used, if appropriate.
- 1.4 The Executive will maintain a written record of all Ring Dealing Members' requests for access to video tapes.
- 1.5 The Executive will maintain a written record of its authorisations of Ring Dealing Members' requests for access to video tapes.
- 1.6 Ring Dealing Members will be able to access video tapes of trading activity in each section of the Ring relevant to their specific enquiry. They will be entitled to view the contents thereof with the use of television monitors provided by the



Executive in a secure room in the basement of the Exchange premises. Two booths will be provided for confidentiality.

2. ACCESS TO VIDEO TAPES OF RING TRADING

- 2.1 An Authorised Dealer or senior member of a Ring Dealing Member's staff e.g. Compliance Officer, may require access to a video tape of that Member's own trading activity, by filling in a Video Recording Access Request Form.
- 2.2 In normal circumstances the Chief Executive or DRC, or any staff member of the LME Compliance or Market Operations Departments authorised by the Chief Executive or DRC, may view a video tape of any Ring Dealing Members' trading activity as part of the Exchange's monitoring and surveillance procedures.
- 2.3 All appropriate written documentation will be maintained by the LME Market Operations Department or, where appropriate, the LME Compliance Department.
- 2.4 In the event that a third party such as a regulatory authority, a Client, or another Member requests access to a video tape of a Ring Dealing Member's trading activity, written authorisation will be required from the Chief Executive or Managing Director of the relevant Ring Dealing Member.
- 2.5 In the event that a relevant regulatory authority such as the SFA considers that to seek the Ring Dealing Member's permission and involvement could prejudice the regulatory authority's ability to carry out its regulatory functions and the DRC concurs, the DRC may in writing authorise access to video tapes by the regulatory authority without advising the Ring Dealing Member in question. All appropriate written documentation regarding such third party access will be maintained by the DRC.
- 2.6 Subject to any legal constraints, for example a court order, where a Ring Dealing Member requires a copy of a recording of its trading activity made by the Exchange, a copy of the relevant portion of the video tape will be provided by the Executive.
- 2.7 The DRC may in writing authorise the making of a copy of a portion of video tape of a Ring Dealing Member's trading activity in the event he deems it necessary for the LME Compliance Department. He may also authorise in writing the making of a copy for and its provision to an appropriate



regulatory authority such as the SFA to fulfil its relevant regulatory obligations.

- 2.8 In the event that a third party such as a regulatory authority, a Client, or another Member requests a copy of a recording of a Ring Dealing Member's trading activity made by the Exchange, a copy of the relevant portion of the video tape will be provided by the Executive subject to written authorisation by the Chief Executive or Managing Director of the relevant Ring Dealing Member.
- 2.9 In the event that a relevant regulatory authority such as the SFA considers that to seek the Ring Dealing Member's permission and involvement could prejudice the regulatory authority's ability to carry out its regulatory functions and the DRC concurs, the DRC may in writing authorise the making of a copy of the relevant portion of the video tape of a Ring Dealing Member's trading activity without advising the Ring Dealing Member in question.
- 2.10 The Board of Directors may amend the Rules for access to video tapes of Ring Dealing Members' trading activity as and when it deems appropriate.

3. VIDEO RECORDING PLAYBACK REQUESTS

- 3.1 The Ring Dealing Member must complete the Video Recording Access Request Form in full stating the name of the Ring Dealing Member name of individual wishing to view the video tape, date and time of recording required, and signed by a senior manager from the Ring Dealing Member such as an Authorised Dealer or Compliance Officer.
- 3.2 When the relevant video tape has been retrieved by a properly authorised IT Supervisor from the Executive on the instruction of the LME Market Operations Department or, where appropriate, the LME Compliance Department, the relevant Ring Dealing Member will be notified and a time will be arranged for the authorised person to access and view the video tape.
- 3.3 When the person authorised by the Ring Dealing Member views the relevant video tape in the designated secure room, an appointed member of the LME Market Operations Department or, where appropriate, the LME Compliance Department, and a properly authorised IT Supervisor from the Executive will be present.



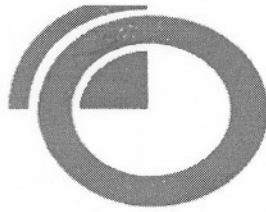
- 3.4 In the event of third party access to a video tape recording of a Ring Dealing Member's trading activity being granted, subject to the procedures in Regulation 2, a senior person from the relevant Ring Dealing Member will be present with an appointed member of the LME Compliance Department and a properly authorised IT Supervisor from the Executive.
- 3.5 The LME Compliance Department will maintain a written record of every event of access being granted for a playback by a Ring Dealing Member and/or third party.

4. COSTS

- 4.1 The charges and costs for the installation and maintenance of a video surveillance recording system for Ring trading will be prescribed by the Board of Directors and may vary from time to time as it deems appropriate.
- 4.2 The charges and costs for each playback by a Ring Dealing Member and/or third party will be prescribed by the Executive and may vary from time to time as it deems appropriate.

5. LIABILITY

- 5.1 Members should note that the video surveillance recording services provided by the Exchange are subject to exclusion of liability as cited in Regulation 15 of Part 3 Trading Regulations :
- " the Exchange shall not be liable to any Member or Client for loss (including any indirect or consequential loss including, without limitation, loss of profit), damage, injury, or delay, whether direct or indirect, arising from any of the circumstances or occurrences referred to in Regulation 15 of Part 3 Trading Regulations from any act or omission of the Exchange, its officers, employees, agents or representatives under the Rules or pursuant to the Exchange's obligations under statute or from any breach of contract by or any negligence howsoever arising of the Exchange, its officers, employees, agents or representatives."



LONDON METAL EXCHANGE

Executive Director: Regulation and Compliance

To: All Members
Subject: Reporting of Open interest on the LME
Ref: 98/090 : R006
Date: 12 March 1998

Introduction

1. Board Notice 97:226 of 5 July 1997 proposed changes to the current Open Interest Reporting. This Notice clarifies certain points relating to this proposal and provides a definition of "Market Open Interest". There are worked examples in the Appendices of how the new Market Open Interest is arrived at together with examples of how the current Exchange Open Interest is calculated.

Principle behind Open Interest

2. Daily Open Interest information is useful to participants and potential users of the Markets who use it as an indicative measure of the liquidity and depth of the Markets. Open Interest Figures should reflect the number of Contracts that will have to be taken to delivery or settled for each Futures or Options Contract for all Market Participants, including those at customer and affiliate levels. The fact that LME forward contracts can not be settled until the prompt date should not alter the fact that offsetting positions have the potential to reduce market exposure, and as such should reflect a reduction in Open Interest.

Changes to proposals in Board Notice 97:226

3. The reporting requirements outlined in Board Notice 97:226 have not changed. However, the method of calculating Open Interest (the Exchange's own calculation) has been amended. This is a result of comments received from Members and consultation with LCH. LCH figures included in Board Notice 97:226 are now excluded from the Market Open Interest calculation for two reasons. Firstly, to include them would have the effect of double counting Members' house positions. Secondly, LCH's role is to provide a "guarantee" to LME Clearing Members with the objective of reducing counterparty risks in the Market. To consider the Principal to Principal contracts between LCH and its

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LME-000953

Clearing Members (resulting from novation) as trading positions which could effect Open Interest would be misleading and misinterpret LCH's role in the Market.

Definition of the new Market Open Interest

4. Market Open Interest for a Contract is the total longs (or shorts but not both) of the sum of all Reporting Members' net longs and net shorts for each of the following categories:

- segregated customers
- non-segregated customers
- segregated affiliates
- non-segregated affiliates
- house or proprietary accounts

5. The LME will calculate the Market Open Interest daily for each Contract by Prompt dates (and by months, strikes, puts, calls for options) across all LME traded currencies. (Please refer to Appendix 1 to 5 for examples.) Open Interest reporting is planned to commence in June 1998. Market Open Interest figures will be published on the Vendor Feed System at the beginning of next year. The reason for the time gap is to ensure that the reporting process is running smoothly and that Members are able to report on time. During this period, the Compliance Department will also carry out data integrity checks.

Current Exchange Open Interest

6. The current method of calculating Open Interest is the net uncovered exposures of the LCH with all its Clearing Members for a particular contract. (Please refer to Appendix 6 for example) The current Open Interest figures will continue to be published alongside the new Market Open Interest to enable users of this information to make comparisons. Market Open Interest is likely to be significantly higher than the current Exchange Open Interest.

Method of Daily Reporting

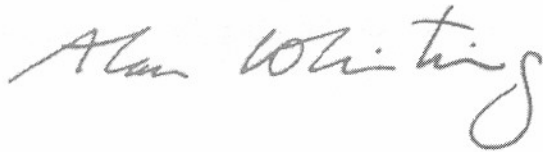
7. All Members are required to submit their Open Interest information electronically to the Exchange by 9.00 a.m. each day. Timeliness of reporting is critical since the Exchange requires the Members' reporting information in order to calculate the Markets' Open Interest Figures. Appendices 1-5 show how Members should calculate the information that has to be reported to the LME. Members should report information for

each contract across all LME traded currencies. Members will report five pairs of longs and shorts for each contract.

Queries

8. All queries relating to this Notice should be directed to Miss Odile de Puyfontaine on 0171-264-5511 or Mrs Joanna Stuart on 0171-264-1703 in the Compliance Department.

Questions relating to IT and the project schedule should be directed to Daniel Cohen, the Open Interest Project Manager at the Exchange on 0171-264- 5657.

A handwritten signature in cursive script that reads "Alan Whiting".

A. Whiting

cc: Board of Directors

**MEMBER 'A' COPPER FUTURES POSITIONS
ACROSS ALL LME TRADED CURRENCIES, PROMPT XXX FEBRUARY 1998
CLIENT'S POINT OF VIEW**

Member's In-house Calculations

Proprietary A/C	House A/C 1			Reported to LME
Long	50			0
Short	-150			-100
Net	-100			
Unseg Customers	Account 1	Account 2	Account 3	
Long	60	40	0	10
Short	-100	-30	-40	-80
Net	-40	10	-40	
Unseg Affiliates	Affiliate A/C 1	Affiliate A/C 2	Affiliate A/C 3	
Long	100	10	30	105
Short	-30	-5	0	0
Net	70	5	30	
Seg Customers	Account 4	Account 5	Account 6	
Long	20	0	40	40
Short	-60	-10	0	-50
Net	-40	-10	40	
Seg Affiliates	Affiliate A/C 4	Affiliate A/C 5		
Long	150	20		170
Short	0	0		0
Net	150	20		

Members report to the LME the sum of their net Longs and the sum of their net Shorts for each category of accounts. (The first prompt is TOM.)

**MEMBER 'B' COPPER FUTURES POSITIONS
ACROSS ALL LME TRADED CURRENCIES, PROMPT XXX FEBRUARY 1998
CLIENT'S POINT OF VIEW**

Member's In-house Calculations

Proprietary A/C	House A/C 2			Reported to LME
Long	+100			70
Short	-30			0
Net	70			
Unseg Customers	Account 7	Account 8	Account 9	
Long	+100	+60	+15	70
Short	-40	-50	-30	-15
Net	60	10	-15	
Unseg Affiliates	Affiliate A/C 6	Affiliate A/C 7	Affiliate A/C 8	
Long	+60	+70	+110	80
Short	-10	-40	-190	-80
Net	50	30	-80	
Seg Customers	Account 10	Account 11	Account 12	
Long	0	0	0	0
Short	-100	-130	-90	-320
Net	-100	-130	-90	
Seg Affiliates	Affiliate A/C 9	Affiliate A/C 10		
Long	+100	+90		100
Short	-70	-20		0
Net	30	70		

Members should supply the data as at their end of day processing

Members with multiple House sub-accounts should use their own judgement in deciding whether it is reasonable for them to be amalgamated.

MARKET OPEN INTEREST CALCULATION

IN A HYPOTHETICAL 2-MEMBER MARKET
COPPER ACROSS ALL LME TRADED CURRENCIES,
PROMPT XXX FEBRUARY 1998

LME's Calculations

Proprietary A/C	MEMBER A	MEMBER B	
Long	0	70	70
Short	-100	0	-100
Unseg Customers	MEMBER A	MEMBER B	
Long	10	70	80
Short	-80	-15	-95
Unseg Affiliates	MEMBER A	MEMBER B	
Long	105	80	185
Short	0	-80	-80
Seg Customers	MEMBER A	MEMBER B	
Long	40	0	40
Short	-50	-320	-370
Seg Affiliates	MEMBER A	MEMBER B	
Long	170	100	270
Short	0	0	0

The LME will combine all the reported **Net Longs** (80+185+40+270+70=645) and **Net Shorts** (95+80+370+100=645) for each Contract

Market Open Interest is either the sum of the net Longs or sum of the net Shorts which is 645.

MEMBER 'A' COPPER OPTIONS POSITIONS

ACROSS ALL LME TRADED CURRENCIES,
EXPIRY, XXX MARCH 1998 FOR 1800 STRIKE

Member's In-house Calculations

Proprietary	House A/C 1		Reported to LME
PUT			
Long	100		100
Short	0		0
Net	100		
CALL			
Long	150		100
Short	-50		0
Net	100		
Unseg Customers			
	Account 1	Account 2	
PUT			
Long	100	10	50
Short	-50	-75	-65
Net	50	-65	
CALL			
Long	100	50	120
Short	0	-30	0
Net	100	20	
Unseg Affiliates			
	Affiliate A/C 1	Affiliate A/C 2	
PUT			
Long	100	0	100
Short	0	0	0
Net	100	0	
CALL			
Long	200	100	230
Short	-50	-20	0
Net	150	80	
Seg Customers			
	Account 3	Account 4	
PUT			
Long	100	20	50
Short	-50	-60	-40
Net	50	-40	
CALL			
Long	200	0	200
Short	0	0	0
Net	200	0	
Seg Affiliates			
	Affiliate A/C 4		
PUT			
Long	100		80
Short	-20		0
Net	80		
CALL			
Long	150		150
Short	0		0
Net	150		

Members will be reporting their Option Open Interest per month across all LME traded currencies. Up to the first Wednesday, the first Open Interest will be the nearby month, e.g. up to the 04/03/98, the first Open Interest is for March 1998. Tapos Open Interest are reported separately in the same format

MEMBER 'B' COPPER OPTIONS POSITIONS

ACROSS ALL LME TRADED CURRENCIES,
EXPIRY XXX MARCH 1998 FOR 1800 STRIKE

Member's In-house Calculations

Proprietary	House A/C 2		Reported to LME
PUT			
Long	0		0
Short	-50		-50
Net	-50		
CALL			
Long	100		65
Short	35		0
Net	65		
Unseg Customers			
	Account 5	Account 6	
PUT			
Long	100	0	0
Short	-200	-100	-200
Net	-100	-100	
CALL			
Long	150	200	50
Short	-350	-150	-200
Net	-200	50	
Unseg Affiliates			
	Affiliate A/C 4	Affiliate A/C 5	
PUT			
Long	50	30	0
Short	-200	-50	-170
Net	-150	-20	
CALL			
Long	150	20	0
Short	-300	-250	-380
Net	-150	-230	
Seg Customers			
	Account 7	Account 8	
PUT			
Long	150	350	325
Short	-200	-25	-50
Net	-50	325	
CALL			
Long	50	200	100
Short	-250	-100	-200
Net	-200	100	
Seg Affiliate			
	Affiliate A/C 6	Affiliate A/C 7	
PUT			
Long	50	0	0
Short	-180	0	-130
Net	-130	0	
CALL			
Long	60	0	0
Short	-120	-175	-235
Net	-60	-175	

Members must report the March contract up to the first Wednesday, (i.e. report up to the 04/03/98), Tapos Open Interest are reported separately in the same format

MARKET OPEN INTEREST CALCULATION

IN A HYPOTHETICAL 2-MEMBER MARKET
COPPER ACROSS ALL LME TRADED CURRENCIES,
EXPIRY, XXX MARCH 1998 FOR 1800 STRIKE

LME's Calculations

Proprietary	Member A	Member B	
PUT			
Long	100	0	100
Short	0	-50	-50
CALL			
Long	100	65	165
Short	0	0	0
Unseg Customers			
	Member A	Member B	Net
PUT			
Long	50	0	50
Short	-65	-200	-265
CALL			
Long	120	50	170
Short	0	-200	-200
Unseg Affiliates			
	Member A	Member B	
PUT			
Long	100	0	100
Short	0	-170	-170
CALL			
Long	230	0	230
Short	0	-380	-380
Seg Customers			
	Member A	Member B	
PUT			
Long	50	325	375
Short	-40	-50	-90
CALL			
Long	200	100	300
Short	0	-200	-200
Seg Affiliates			
	Member A	Member B	
PUT			
Long	80	0	80
Short	0	-130	-130
CALL			
Long	150	0	150
Short	0	-235	-235

The LME will combine the Net Longs and Net Shorts for each category of accounts for each strike by Put and by Call, for all Members .

Put Open Interest is 705
(Longs are 50+100+375
+80+100+705)
or
(Shorts are 265
+170+90+130+50
+705)

Call Open Interest is 1015
(Longs are 170+
230+300+150
+165)
or
(Shorts are 200+
380+200+235)

CALCULATION OF CURRENT EXCHANGE OPEN INTEREST

(same hypothetical data as Appendix 1)

Member A	Long	Short	Net
House	50	-150	-100
Unseg Customers			
1	60	-100	-40
2	40	-30	10
3	0	-40	-40
Unseg Affiliates			
1	100	-30	+70
2	10	-5	+5
3	30	0	+30
Total			-65

Member B	Long	Short	Net
House	100	-30	70
Unseg Customers			
7	100	-40	60
8	60	-50	10
9	15	-30	-15
Unseg Affiliates			
6	60	-10	50
7	70	-40	30
8	110	-190	-80
Total			+125

Member A	Long	Short	Net
Seg Customers			
4	20	-60	-40
5	0	-10	-10
6	40	0	40
Seg Affiliates			
4	150	0	150
5	20	0	20
Total			+160

Member B	Long	Short	Net
Seg Customers			
10	0	-100	-100
11	0	-130	-130
12	0	-90	-90
Seg Affiliates			
9	100	-70	30
10	90	-20	70
Total			-220

(Current Exchange Open Interest derived from
LCH's net uncovered exposures to its clearing Members)

	Longs		Shorts
Member B / House	+125	Member A / House	-65
Member A / Seg	+160	Member B / Seg	-220
Total	+285	Total	-285

The current Exchange Open Interest is the sum of all the Longs (125+160=285) or the sum of all the Shorts (-65+-220=-285) derived from the net of the sub-accounts of each Clearing Member.

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MARKET ABERRATIONS: THE WAY FORWARD

1 INTRODUCTION

- 1.1 In March 1998, the London Metal Exchange published a consultation paper entitled "Solutions to Market Aberrations". The consultation paper was distributed to all LME members, LME approved warehouses, producers and users of the markets, regulatory bodies and representative associations.
- 1.2 The LME has been encouraged by the scale and quality of the responses to this, the first, substantive consultation document in the regulatory area. Comments on the many possibilities aired in the consultation paper have been diverse. Sometimes the responses have been differentiated between category of member and sometimes between members on the one hand and users and producers/fabricators on the other. This is not surprising in view of the differing objectives which participants expect from the markets. Views on electronic trading were particularly segregated. On many issues, however, there was a marked and welcome degree of agreement across the members and users of the Exchange on the way forward; particularly for example, in regard to the policy on market interventions. All responses are summarised in tabular form and anonymously in the annexes to this paper.
- 1.3 The March consultation document emphasised the importance of a comprehensive approach if we are to succeed in discouraging market aberrations. Transparency, information, surveillance and discipline all have important roles to play in addition to specific market intervention actions taken by the LME. The consultation document aired many suggestions of possible ways forward in all these areas. This current paper looks at each of the issues in the order in which they were raised in the consultation document. It
- i examines the responses received;
 - ii analyses the issues raised in the consultation paper in the light of the consultation; and
 - iii makes firm proposals for the way ahead.
- 1.4 We hope that the document sets out clearly the regulatory policies which the LME will be pursuing in these areas. In view of the great

diversity of views it is inevitable that the chosen ways ahead will not be the first choices of all market participants and users. But where this is the case, the document should at least fulfil its purpose of explaining in some detail the reasoning and rationale underlying the chosen way forward.

2 REQUIREMENTS TO REGISTER ALL LME CLIENT CONTRACTS

Responses

- 2.1 There was overall support, particularly from Ring Dealing Members, for all LME client contracts to be registered. The broad view was that the LME should enforce this requirement rigorously and that “look alike” contracts should either be banned or brought on-Exchange.

Analysis

- 2.2 There are several inter-related issues. From a semantical perspective, LME client contracts have to be registered, otherwise they are not LME client contracts: so to that extent all LME client contracts are already registered. This of course misses the real issue which is that customers may believe that they are receiving an LME client contract when they are not.
- 2.3 Compliance staff have noted many instances where members have purported, or are alleged to have purported, to have issued LME client contracts without registering them. This behaviour has the following unacceptable regulatory and other consequences:
- ◆ Clients will be misled to believe that they have an LME registered contract subject to the scrutiny and transparency of the LME, a Recognised Investment Exchange. This will breach FSA’s Principles and both SFA and LME rules.
 - ◆ Customers who want to transfer positions will be unable to do so because there are no existing positions on-Exchange to allow such a contract.
 - ◆ If a default occurs, the client may have less protection than he believes exists.
 - ◆ LME volume and open interest figures will be inaccurate.
 - ◆ Market and price transparency will be compromised.

- ◆ Other members will unwittingly be subsidising the member who does not register all the trades he should as the LME will be deprived of its fees.
- 2.4 Past discussion of this issue has also involved requirements in relation to “look-alike” contracts and the timing of bringing over-the-counter (OTC) contracts on-Exchange. Board notice 97: 290 dated 15 September 1997 directs members to bring an OTC contract on-Exchange at the earliest opportunity. It is not part of the LME’s role to require members to bring OTC contracts on-Exchange: it is for members to decide, in the light of their clients’ requirements, whether to transact particular trades on-Exchange or OTC. The rationale of Board notice 97:290 is that where members intend to bring OTC contracts on-Exchange, but the specifications of the LME contracts prevent this at the outset, such contracts should be brought on-Exchange, at the earliest opportunity to prevent bunching and distorting the market shortly before prompt. This would help to ensure an orderly market. In practice the guidance is difficult to enforce because of the problems of establishing intentions at the time of the OTC contract.
- 2.5 The LME Board has, in the past, looked at the use of so-called “look-alike” contracts and the rights of the Exchange over LME contract criteria and terms and conditions. There has been some broad sentiment among the membership that OTC contracts should not be able to use LME contract criteria and that “look-alike” contracts should be required to be registered.
- 2.6 The main mischief in this area, which the LME rules must address, is when clients are misled into believing, or simply wrongly believe, that they are receiving LME client contracts when they are not. True volumes are also hidden from the market. LME rules should not attempt to deter members from using OTC contracts. Moreover, when members do issue OTC contracts there may well be some benefit, both to the member and the client, in making the contract subject to the criteria and terms and conditions which would apply to LME contracts in so far as this can be done for non-Exchange contracts.
- 2.7 The overriding requirement must be that the client is in absolutely no doubt as to the status of the contract he is receiving. It is clear to the LME compliance department that end customers do, at times, believe they are receiving LME registered client contracts when they are not. LME rules permit only Category 1, 2 or 4 members to issue LME client contracts. Overseas affiliates of LME members who are not

members themselves cannot issue LME client contracts but can act as agents for Category 1, 2 or 4 members.

The Way Forward

- 2.8 Customers of LME members must be clear when a contract is an LME contract and whether, therefore, they are getting the benefits and protection that come with registration.
- 2.9 The LME rules will be amended to require members to state clearly and boldly on their LME client contracts and confirmations with customers “**THIS IS AN LME REGISTERED CLIENT CONTRACT**”, and to state clearly and boldly on their OTC client contracts and confirmations “**THIS IS NOT AN LME REGISTERED CLIENT CONTRACT**”.
- 2.10 Failure to register contracts which have been represented to a client as being client contracts will be a breach of the rules and will be treated as a serious disciplinary offence.
- 2.11 Subject to 2.8, 2.9 and 2.10, members will be permitted to make their OTC contracts subject to the same criteria and terms and conditions as LME contracts where appropriate.
- 2.12 The guidance requiring those OTC contracts which are intended to be brought on-Exchange to be brought on at the earliest opportunity, is required for sound regulatory reasons and to protect the client. To improve compliance with this requirement, members wishing to bring OTC contracts on-Exchange using historic prices will have to notify their intention to the LME at the time of the original OTC contract. OTC contracts will continue to be able to be brought on-Exchange later, but at current prices. The NMPT rules will be revised accordingly.
- 2.13 The LME will incorporate in its educational programmes and seminars units describing and explaining LME registered client contracts and the benefits and protection which these contracts confer on customers.

3 IMPROVING TRANSPARENCY OF CLIENT TRADES

Responses

- 3.1 There was overall support for the recommendations to the Board by the LME Executive to improve the transparency of client trades.

The Way Forward

- 3.2 In parallel with the developments proposed in paragraphs 2.8 to 2.13 above, the LME will improve the transparency of client trades through the introduction of a non-segregated client sub-account at the London Clearing House. This will enable identification of the direction of client trades and enable compliance staff to monitor and reconcile registered client contracts in order to help enforce the above Rule which will require all LME client contracts to be registered.

4 TIMELY ALLOCATION OF ALL TRADES

Responses

- 4.1 There was overall support for reducing the matching period for give-up transactions. Following the recommendations in the market Aberrations Consultation Document, new rules on the matching period were proposed in Board notice 98/091:R007 of 12 March 1998 and came into effect on 15 June 1998.
- 4.2 Many comments about the time allowed for matching client give-up transactions were received from Category 1 and 2 members who were concerned that they would be unable to meet the new requirements for reasons beyond their control.

Analysis

- 4.3 Many of the concerns arose from misunderstandings that give-up trades would automatically fail if they were not matched within the new reduced time limits. However, in line with the treatment of timed trades, members are able to apply for extension to the matching timetable for give-ups on Day 1, and in exceptional circumstances members can apply to the LME compliance department for authorisation to match beyond Day 2. All late matched give-up trades (ie outside the new time limits) will be closely monitored. Later this year, when the LME will introduce its new disciplinary system, late matches could be subject to a higher fee to give an additional incentive to prompt matching.

The Way Forward

- 4.4 Administrative notice 98/212:A206 was issued on 10 June 1998 clarifying in detail the new requirements on the time for matching of give-ups and transfers. These requirements for the matching of give-ups and transfers became effective on 15 June 1998. For completeness the administrative notice covered the time

requirements for the input of all trades into the LME matching system.

5 TRANSPARENCY OF INTER-OFFICE DEALING

Responses

- 5.1 Suggestions to improve the transparency of inter-office dealing, through measures such as the introduction of a third Ring early in the morning or an automated trading system for inter-office dealing or for traded options, found little support from the membership. There was greater support from the industry and other respondents, especially for automated trading, but even so opinion was far from overwhelming. There was broad acceptance that the LME should have a contingency plan to introduce automated trading in a timely fashion in anticipation of potential future demand; but that any system developed should not be introduced for the present.
- 5.2 Lack of enthusiasm for these suggestions had little to do with any lack of desire to improve the transparency of inter-office dealing; and stemmed more from the fundamental nature and wider consequences of these changes. The consensus on a third morning ring, for example, was that it would not generate much additional business but would increase costs significantly.

The Way Forward

- 5.3 After careful consideration and discussion with Ring Dealing Members, the suggestion of a third morning ring will not be pursued.
- 5.4 Experience in other markets has shown the importance of the LME being able to react quickly and to respond to rapid changes in market demand if it is to remain competitive. While there is no pressure from the markets or membership to move to electronic trading and the LME's system of open outcry continues to be highly efficient and cost competitive, the LME is reviewing all aspects of trading as part of its IT strategy project.

6 ASSOCIATE BROKER CLEARING MEMBERS (ABCMs) TO PROVIDE PRICE TRANSPARENCY FOR INTER-OFFICE DEALING

Responses

- 6.1 There was substantial support for the suggestion that ABCMs should be required to publish on a real time basis deals that have been traded inter-office or directly with clients at prices outside the

indicative spread on the Vendor Feed System. Some ABCMs were opposed.

Analysis

- 6.2 At present there are no mechanisms for traded prices to be published real time.
- 6.3 Transparency will be delivered so long as there is integrity in the quotes displayed on the Vendor Feed System and provided that there are sufficient contributors to the Vendor Feed System. These issues are discussed in more detail in section 8 below on the Vendor Feed System.

The Way Forward

- 6.4 One important element of delivering integrity in the quotes on the Vendor Feed System is to ensure that in normal market circumstances members are willing to trade at the prices which they quote. In future any trading outside the indicative spread quoted in the Vendor Feed System will be investigated by the compliance department. Surveillance will cover all categories of membership.
- 6.5 The enlarged and upgraded compliance department, together with the recently introduced IT systems and analytical tools will enable effective monitoring. Unjustified trading outside the indicative spread will be a disciplinary offence.

7 ASSOCIATE TRADE CLEARING MEMBERS (ATCMs) TO PROVIDE PRICE TRANSPARENCY FOR INTER-OFFICE DEALINGS

Responses

- 7.1 There was general support for requiring ATCMs to provide more information, although not from the one response received from a Category 3 Member. There was, nevertheless, some apprehension that reporting requirements which were too onerous could drive ATCMs to the OTC market.

Analysis

- 7.2 There is no rational reason why Associate Trade Clearing Members should not report, along with other categories of Clearing Members, those elements of trade and warrant information which are essential if the market is to be properly monitored. None of this information is published – for reasons of commercial confidentiality: it is made

available only to the compliance department of the LME. Transmission of this information would not be costly or onerous to Category 3 Members.

The Way Forward

- 7.3 ATCMs commenced reporting the new market Open Interest data to LME compliance in June 1998. Reporting of large positions and warrant holdings will be introduced after a period of consultation in the autumn.

8 THE VENDOR FEED SYSTEM

Responses

- 8.1 Respondents were supportive of the changes already introduced to enhance the information carried on the Vendor Feed System and to improve its accessibility and reliability.
- 8.2 Ring Dealing Members were unanimous that the Reuters “Ring=” page, which currently features both Ring Dealing and Associate Broker Clearing Members should be confined to Ring Dealing Members: ABCMs could have a separate page.
- 8.3 Category 1 and 2 members were also strongly, but not unanimously, of the view that prices on the Vendor Feed System should remain indicative and not firm quotes at which contributors could be compelled to trade.
- 8.4 All categories of member and the industry welcomed the suggestions to tighten up the obligations on contributors to the Vendor Feed System, including the imposition of penalties for those not fulfilling their obligations and thereby undermining the integrity of the indicative price quotes.
- 8.5 Many ABCMs wanted the opportunity to be able to contribute to the Vendor Feed System as market makers had been frustrated that their applications had been on hold for a considerable period of time while the whole Vendor Feed System was under review.

Analysis

- 8.6 Indicative price quotes on the Vendor Feed System are essential for price transparency and integrity of the inter-office market.
- 8.7 Transparency and integrity dictate that as many contributors as possible should contribute indicative price quotes subject only to their ability and willingness to comply fully with the accompanying

obligations. Indicative price quotes cannot therefore be confined to Ring Dealing Members. Not only would this reduce transparency and integrity, it would also be anti-competitive when prices in the inter-office market have no direct bearing on the obligations of Category 1 members as Ring Dealing Members as such. That said, the current title of the Reuters “Ring=” page is misleading in so far as it implies either that all the contributors are Ring Dealing Members or that the prices emanate directly from the ring.

- 8.8 There is a widespread belief that the current operation of the system leaves a good deal to be desired. Analysis of the data supports this belief. Many contributors, but not all, are not updating indicative prices regularly or are not prepared to trade reasonable quantities at the prices quoted.
- 8.9 It has been suggested that there should be an absolute obligation on contributors to trade given quantities at the prices quoted; that is, that quotes displayed on the LMEVFS should be firm quotes rather than indicative price quotes. Although this would have the advantages of openness and certainty for the customer, it is not a reasonable demand to place on contributors when markets can move quickly. The outcome of such an obligation would be likely to reduce transparency through a reduction in the number of contributors.
- 8.10 It is, however, essential that indicative prices quoted are meaningful. Customers and the market need to know that they can trade in reasonable volumes at or very close to the indicative prices quoted in normal market conditions. Regular updating of indicative prices should increase the willingness of contributors to trade at the prices indicated.
- 8.11 Yet experience indicates that a requirement to update input prices regularly of itself is unlikely to deliver the degree of transparency and integrity required. The current system relies on a system of financial incentives – payments – to contributors inputting prices. The larger the number of prices input, the larger the rebate. Apart from the fact that this financial incentives scheme is not delivering the desired results, there is something rather incongruous in paying incentives to deliver what in effect are obligations. Experience suggests that a system of clear obligations coupled with penalties if the obligations are not delivered would be far more effective. This could be coupled to a volume-related payment per contributor per metal to cover costs.

The Way Forward

- 8.12 The system of indicative price quotes transmitted on the Vendor Feed System will be modified substantially to provide greater transparency and integrity of the inter-office market:
- i Reuters and other service vendors will be encouraged to change the title of their “Ring=” page.
 - ii Both Ring Dealing and Associate Broker Clearing Members will be required to input into the Vendor Feed System in respect of every metal contract in which they actively trade.
 - iii There will be strict obligations on contributors. They will be required to update prices at least six times per day at meaningful intervals.
 - iv The prices input will remain indicative price quotes, but contributors must generally be prepared to trade reasonable volumes to market users at the indicative prices input, in normal market circumstances.
 - v During any particular five minute ring trading period, only LME executive personnel will be authorised to input data into the system. During kerb trading times, only LME executive personnel and Ring Dealing Members will be authorised to input into the system, because during such times “the market” is on the Exchange floor. At all other times, all Ring Dealing Members and Associate Broker Clearing Members who are contributors will be authorised to input into the system.
 - vi The LME compliance department will use the new Compliance Support System to compare indicative prices quoted by contributors with those at which they actually trade. Any material or consistent divergence between the two will be investigated and dealt with on a case by case basis.
 - vii The current system of financial incentives linked to the number of prices input will be replaced with a structure which combines a volume related payment per metal per contributor with automatic financial penalties for failing to input and update quotes regularly throughout the day. Further penalties will be imposed on contributors repeatedly refusing to trade in normal market circumstances at their indicative prices.

9 INFORMATION ON CONCENTRATION OF LARGE POSITIONS AND WARRANT HOLDINGS

Responses

- 9.1 The publishing of information on the concentration of large positions and warrant holdings produced divided views between the industry, which was strongly in favour, and members, who were largely against.
- 9.2 Members' main concern was that an obligation on these lines could drive business off-Exchange in an attempt to preserve commercial confidentiality. Although individual companies would not be named there was concern that coupled with information already in the market place, the new information could expose individual members unfairly to concerted market behaviour, even when the members were not in any way abusing their large positions. Drawing business to the OTC market would reduce transparency. Some members were also concerned about how warrant financing would be handled. They feared that publication of large warrant holdings by warrant financiers could mislead the market into believing that stocks might not be available and that prices would come under pressure.
- 9.3 The industry and others saw publication of information on large positions as an essential element of the LME's policy to deliver greater transparency to the users of the markets. If information on large positions, and their build-up over time, were available to the markets it would be more difficult for dominant position holders to abuse their dominant positions, market participants could develop and amend their trading strategies as they saw fit, there would be greater certainty in the markets and market aberrations would diminish.

Analysis

- 9.4 It is very difficult to argue on either logical or empirical grounds against publication of large positions, on an anonymous basis, for both warrants and trading. One of the essential criteria of a free, competitive market is that no one or group of participants can move the market to their particular advantage. Reliance solely on LME intervention to prevent abuse of dominant positions will inevitably be less than ideal; partly because even with good and timely regulatory information intervention will come when abuse has already taken place, and partly because intervention itself will bring uncertainty and discontinuity to the market.

- 9.5 Publication by the LME of large positions would need to be handled carefully by market users. It would be incumbent on them to analyse the data and to understand their limitations. For example, far from all dominant positions are abused, so there should be no automatic presumption that dominant positions would invariably result in a tightness of the market. Sometimes, dominant positions can result from the drawdown of stocks by others rather than by the build-up of stocks by the – now – large warrant holder. Second, it will not be possible to separate out warrant financing from the large position information. Warrant financing can encompass a wide variety of both arrangements and objectives. Under some arrangements, the warrants in practice are not readily available to the market: under other arrangements the financed warrants are available to be lent and dominant financing deals are potentially open to the same abuse as directly owned positions.
- 9.6 Third, because of the possibility of covert collusion between apparently unconnected parties, a lack of published dominant positions would be no guarantee that effective large positions did not exist. In publishing any large position information, the LME would automatically aggregate positions of clients across brokers, would treat companies within a group and its affiliates as one, and would treat a firm's client and house positions as one unless the firm could demonstrate to the compliance department of the LME that the positions were entirely independent. The LME would also aggregate positions where it had evidence that members were acting together, but experience indicates that it may take some time for that information to come to light, even to the compliance department. Failure to disclose connected holdings would be a serious disciplinary offence as, of course, would collusion to manipulate the market.

The Way Forward

- 9.7 The LME believes that users of the markets have a right to know if large positions are held in the market, although large position information will need to be interpreted by market users with care. If information is published regularly, the development of such positions should become more readily apparent and can be taken into account in determining trading strategies. Also, while the information would be anonymous, its availability would make it more difficult for those who might be tempted to abuse their dominant positions.
- 9.8 From the beginning of 1999, the Exchange will be publishing more meaningful open interest information, which will provide greater transparency to the markets.

- 9.9 In addition the LME will, as soon as practicable, publish information on large warrant and trading positions. The information will be anonymous and will show the number of large position holdings within given bands, for example between w and x per cent, y and z per cent etc. The information will be published daily but because of the time needed for reporting, collating and checking it will initially refer to positions held two days previously. To speed analysis of information, consideration will be given to the possibility of introducing standardised codings for clients across all members.
- 9.10 For warrant holdings, warrants will be expressed as a percentage of total LME warrants for each metal. For trading positions, both longs and shorts, the most appropriate denominator to indicate the degree of concentration will be market open interest. The published information will give the number of positions falling within certain percentage bands and for given periods, e.g. cash to 1 week prompts, 1 month to 3 month prompts etc.
- 9.11 The details of the proposals and the required rule changes will be subject to the LME's standard regulatory consultation procedures.

10 ACCESS TO OTC INFORMATION

Responses

- 10.1 Respondents gave broad support in principle to the proposals to require members to provide a degree of OTC information to the compliance department of the LME on an entirely confidential basis. There were, nevertheless, significant concerns expressed about breaching the confidentiality of customers and about the dangers and costs of over-regulation.

The Way Forward

- 10.2 In order to fulfil its responsibilities to deliver fair and proper official markets, the compliance department of the LME will need access, on a wholly confidential basis, to essential information on the OTC business of its members.
- 10.3 Previous proposals put forward in Consultation Document 97:405 issued on 27 November 1997 will need to be reviewed regarding their practicality. The executive intend to publish new proposals in a separate consultation document to be issued in the autumn.

11 ACCESS TO WAREHOUSE INFORMATION

Responses

- 11.1 There was overwhelming support, from all categories of membership, warehouses and the industry, for the proposals that the LME compliance department should have access on request to more detailed information relating to LME warrants. Respondents emphasised that this information, as was proposed, should be available only to the LME compliance department, because of its highly confidential nature. There was slight concern that if the information required was too intensive and excessive, holders could be encouraged to move stocks off warrant.
- 11.2 Respondents took the opportunity to raise several other Warehousing issues which could have a significant effect on the fairness and transparency of the markets. In particular serious concern was expressed about the independence of warehouses, relationships between warehouse companies and members which are potentially open to anti-competitive and market distorting behaviour, long term storage and incentives offered by warehouses which can restrict the availability in practice of LME stocks, perceived excessive charges levied by warehouse companies for taking stocks out and the speed with which stocks can be taken out of warehouses.

Analysis

- 11.3 Concerns about the relationship between warehouse companies and LME members and warehouse company practices were raised by the Securities and Investments Board in its review of the LME and the metals markets. Liquidity and availability of LME stocks are essential elements of a fair and transparent market.

The Way Forward

- 11.4 The LME is taking action on all the warehousing issues. On the provision of information, when SWORD is implemented in 1999 the information available on warrants will both be more comprehensive and readily accessible directly by the LME compliance department. We believe that SWORD will deliver most of the information needed from a regulatory viewpoint in relation to LME stocks.
- 11.5 In the meantime, LME warehouses will be required to divulge to the LME compliance department, on request, the identity of parties i) placing metal on LME warrant, ii) to whom warrants are issued, iii) cancelling LME warrants, and iv) to whom metal is released.

- 11.6 Warehouse Companies have been reminded through a recent notice of the requirement to cooperate with regulatory enquiries made by the LME compliance department.
- 11.7 All the other warehousing issues are in the process of being addressed by the LME. Board notice 98/213, A:207, W:033 issued on 11 June 1998, sets out the LME's proposed new policy on the establishment of 'Chinese Walls' between LME members and related warehouse companies. The purpose of the proposed requirements is to prevent the improper use and knowledge of information in one part of the group (the warehouse) reaching and being used by another part of the group (the LME member) and vice versa, so that all participants in the market are competing on equal terms. The proposed "Chinese Walls" policy is compatible with both competition law and normal practice in the UK's financial services regulatory structure.
- 11.8 On charges, practices and incentives, warehouse notices W:033 and W:038 issued on 5 June 1998 and 19 June 1998 respectively required all LME warehouse companies to inform the LME of their FOT charge currently levied and to give the LME three months notice of increases in the maximum FOT charge. The LME has now published current maximum FOT charges (notice 98/261:A252:W048). Notice W:038 also clarified the LME's policy on anti-competitive warehouse practices and inducements to attract stocks into warehouses. All inducements which are likely to lead to distortions in the free flow of LME warranted metal will be treated as exceptional in the terms of the warehouse contract and will constitute a serious disciplinary offence.
- 11.9 The Board's attention has been drawn to various comments and reports alleging payment of exceptional inducements, demand for a variety of substantial additional charges in addition to FOT charges and impediments to speedy physical redelivery out of warehouses. The Exchange is looking into this matter and is reviewing, as a matter of urgency, its contractual arrangements with warehouse companies to ensure that LME approved warehouse companies and their placing metal on warrant adhere to the spirit as well as the letter of the LME rules. The Board will give consideration to making changes to warehousing rules where considered appropriate in the light of this review.
- 11.10 The LME has started discussions with the UK's financial regulatory authorities concerning the measures the LME can take in relation to all warehouse charges pertaining to LME warranted stocks, with the aim of fostering competition and preventing anti-competitive

practices. These discussions will be extended in due course to the UK competition policy authorities and to the financial services and competition directorates of the European Commission and concerned authorities in other jurisdictions where appropriate.

12 REQUIREMENT OF PRODUCERS OF REGISTERED BRANDS TO BECOME LME MEMBERS

Responses

- 12.1 The majority view was that a requirement for producers of registered brands to be LME members was neither justifiable nor practical.

Analysis

- 12.2 LME markets need liquidity and it is clearly in the Exchange's and its users' interests to have as registered brands all the quality brands demanded by the markets' users. The Exchange has in the past registered brands without specific requests from producers.
- 12.3 Moreover, there is little if any regulatory justification to require producers' membership. Any control which the LME needs to exert, it can do so through its ability to register, monitor and delist brands. In fact some producers choose to become Associate Trade Members (Category 5). They join voluntarily to gain access to information and to make a useful contribution to the development of the Exchange.

The Way Forward

- 12.4 As now, producers of registered brands should continue to be encouraged to become Category 5 members and to participate fully in the development of the Exchange. But, as now, membership should not be a requirement for the registering of producers' brands.

13 SPECIFIC MARKET INTERVENTION POLICIES

Responses

- 13.1 Virtually unanimous agreement that the markets could not be left to their own devices completely unfettered was qualified by a warning about the dangers of the markets becoming over-regulated. This concern was shared as much by industrial users as by members and reflected apprehension over the cost and constraints of too intrusive regulation. While appropriate controls are necessary, frequent and excessive interventions would be damaging to the markets.
- 13.2 There was deep concern about the perceived asymmetrical treatment of positions by the Exchange. The Exchange was seen by some as

being concerned only by dominant long positions and with the protection of short sellers, while taking no action against abusive dominant short positions.

- 13.3 As to the form of intervention, the overwhelming assessment was strongly against any form of automatic backwardation limit. Interestingly, automatic limits were opposed by all sectors of the markets, members, users, and industry. They were also opposed by the financial services and competition regulatory authorities.
- 13.4 Respondents were equally united in their opposition to other suggested automatic interventions such as increased margins, progressive liquidation of large positions on nearby prompts and position limits.
- 13.5 With a small number of exceptions, where respondents were looking for a degree of certainty which they believed would flow from automatic backwardation limits, the consensus was strongly in favour of discretionary action by the Exchange to deal with any actual or attempted market manipulations. There was an expectation that with its enhanced resources and powers and on-going surveillance of the markets, there should in the future be less need for specific interventions and greater expertise in the Exchange to deal with any instances which did occur on a discretionary basis. Also underlying the preference for discretionary intervention was a desire to take stock of the large number of regulatory reforms and developments which have taken place on the LME over the last year or so. It was sensible to give them a chance to be put into practice and their effectiveness assessed before considering introduction of an additional layer of regulation and restrictions.
- 13.6 Finally, all sectors of the markets were looking for a higher level of transparency over the processes and procedures which the LME would employ in exercising its discretionary interventions. This included a strong request for explanations of interventions, both as to why they were necessary and the type and level of limit imposed.

Analysis

- 13.7 The overwhelming reason why there was little support for automatic backwardation limits was that in terminal forwards markets such as the LME, backwardations often arose naturally and not as the result of any form of market abuse. There are many situations where a backwardation in a metal reflects the natural state or sentiment of the market. A temporary backwardation in a metal can be caused by a strike at a producer, reaction to a regional economic crisis, natural disaster in a mining area or any other temporary (actual or perceived)

interruption to supply or increase in demand. Markets such as the LME are clearly open to backwardations driven by market fundamentals; and it is a vital role of the markets to provide liquidity, entice supply and satisfy demand in these situations. Automatic backwardation limits would interfere with the free interplay of demand and supply and undermine one of the main functions of markets.

- 13.8 The small minority of market users who favoured automatic backwardation limits were looking for certainty. Even automatic limits, however, would not deliver certainty. The Exchange could not condone manipulation of the markets even if this resulted in a backwardation lower than the set intervention limit; so the Exchange could still have to intervene on a discretionary basis.
- 13.9 The more sophisticated variants of automatic backwardation limits, such as limits triggered by the levels of absolute stocks, or stocks in relation to consumption, do not overcome the fundamental difficulties of automatic limits, would be difficult to administer and are themselves capable of being manipulated – for example through the manipulation of stocks.
- 13.10 One of the strongest arguments for automatic backwardation limits/intervention is the difficulty in analysing and assessing the reasons for and causes of the backwardation or unusual price movements. Despite increased resources and expertise, discretionary intervention may, inadvertently, be mistaken and inappropriate. Even when it is ‘correct’ it will always be contentious because there will always be parties who will consider themselves to have been financially disadvantaged by the intervention even though they were not involved in the manipulation. Automatic backwardation limits would undoubtedly give the Exchange an easier life, if only by preventing it being blamed or accused of favouring one side or the other. The easier life is, admittedly, always tempting; but to opt for automatic limits for these reasons would be an abrogation of the Exchange’s responsibilities.
- 13.11 Within a discretionary regime, however, it would be beneficial to both members and market users if the LME and the Special Committee gave guidance, over and above the general guidance given in the past, on the issues and criteria it would take into account in considering whether intervention would be necessary. Such guidance would be particularly helpful in relation to dominant positions. Experience shows that the vast majority of market aberrations which have resulted in specific regulatory interventions by the Special Committee have involved dominant positions.

- 13.12 Board notice 97:247, which was generally welcomed, set out the general principle that if someone has a dominant position in the stock, he incurs additional responsibilities to the market to avoid his inherent market power resulting in market abuse, and this may mean that while he has a dominant stock position he will no longer be able to undertake trading strategies that would be acceptable in other circumstances. In particular Board notice 97:247 laid down the principle that a dominant position holder would be abusing the market if it used its dominant position to require other market users to pay more to meet their needs than they would have had to pay had the market reflected the natural interplay of supply and demand without any participants having a dominant position. The problem is that while this concept is clear, its application involves considerable judgement. The outcome is that intervention to prevent abuse of dominant positions tends to satisfy neither the market users nor the dominant position holders. Market users criticise the lack of certainty and what they see – incorrectly – as arbitrariness; while the dominant position holders seek definitive guidance on what price they can charge.
- 13.13 Intervention is often also criticised for protecting the shorts and for taking no account of dominant short positions. It is perceived as being one-sided. This is not in fact the case; the Exchange is entirely neutral as between speculative purchasers and speculative short sellers. The purpose of Intervention is not to protect the shorts. It is to ensure a fair price by preventing abuse and maintaining a proper market. The one-sided perception arises partly because one of the effects of intervention is to limit the downside for the shorts. The downside for shorts should of course only be limited to protect them against the risk of market abuse by the longs. Where there are fundamental economic reasons for a backwardation, the shorts should have to pay the fair market price determined by natural demand and supply.
- 13.14 The one-sided perception also results from the lack of financial penalties on abusive shorts. While the Exchange does not seek to favour shorts, backwardation limits do penalise longs, whereas there is currently no equivalent financial penalty on the misuse of dominant short positions. Apart from disciplinary action, the most severe action which can be taken by the Exchange against market abuse by shorts is to require them to trade out of their positions.

The Way Forward

- 13.15 The Exchange, through the compliance department and the Special Committee, will continue to intervene on a discretionary basis, where

appropriate, to prevent abuse of dominant shorts and to limit backwardations resulting from market manipulation. With greater surveillance of the markets and concentration on prevention of misdeeds, the expectation is that the need for specific public interventions to limit unjustified backwardations and other abuses should diminish over time. Given the ingenuity of the human mind and behaviour, we are, nevertheless, unlikely to have seen the last.

13.16 It is not possible to be precise about the exact procedures to be followed in every single case because cases differ substantially one from another. But broadly, the procedures to be adhered to by Exchange will be as follows:

- i The LME compliance department closely monitors the markets on a daily basis using both public and confidential regulatory information available to it.
- ii It has internal market and analytical expertise within the compliance department, but will also regularly consult outside analysts, the industry and other knowledgeable parties when assessing market developments.
- iii If the compliance department's assessment is that the near term market is being distorted, it will discuss with the relevant member(s) and/or client(s) their trading and strategy underlying their trading at an early stage. The LME's rules impose obligations on those holding large positions, irrespective of whether they are long or short positions.
- iv If, following discussions between the compliance department and the member(s)/client(s), the compliance department is still of the view that the market is being distorted, the Executive Director: Regulation and Compliance will convene the Special Committee.
- v The Board has given general guidance to the Special Committee in respect of dealing with dominant positions on a discretionary basis (see 13.18 and 13.24 below). It further believes that it would be beneficial to all sectors of the market if this guidance is published.
- vi After consulting practitioner and industry expertise and conducting analysis as appropriate, the Special Committee – which is non-conflicted and has powers of action delegated by the LME Board – will determine whether action should be taken. The form of any intervention will be tailored to the specific circumstances of each case (see 13.17 below) and determined

by the committee's assessment of the nature of any threat to the fairness of the market.

vii Where appropriate, intervention decided on by the Special Committee will be announced (see 13.19 below).

13.17 Various forms of intervention are available to the Special Committee which include imposing backwardation limits on the market as a whole which can vary over time and between prompt dates and requiring a member(s) to trade out of proprietary or client positions. The appropriate action will depend on the circumstances of the case. The LME rules (Rule 14 of Part 3) allow the Special Committee to take any other measures which it deems to be appropriate to prevent abuse of the markets.

13.18 In the Board's view, it is desirable that there should be a financial deterrent readily available against the threat of manipulative behaviour by large speculative short position holders as well as long position holders. It is not possible to handle manipulative short positions by the same mechanism as for manipulative long positions, but the Board is asking the Special Committee, as one option to consider imposing penal margin requirements if there is a threat of manipulative behaviour by short position holders. Such margins would add particularly to the armoury of financial penalties against abuse of dominant short positions (see 13.14 above). Penal margins, for example, might be required to be paid in cash on which interest would not be paid, could be up to 150 percent of the initial contract value and might be required to be maintained for a period after the positions are closed out. Any penal margins should be publicised. The Special Committee is being asked to consider whether penal margins may be appropriate when market positions (in futures and options) held by a party – or group of parties acting in concert – either individually or in aggregate during the prompt month account for 50 percent of LME stocks. The objective of penal margins would not be to prevent the emergence of large positions which may be needed for genuine reasons, but to protect against their misuse to manipulate the market.

13.19 The Exchange's aim will be to be as transparent as possible and to announce its interventionary actions to the market. In some instances, however, total transparency will not be feasible; for example where members are required to reduce or trade out of a proprietary or client position. Where interventions are publicly visible, such as the imposition of backwardation limits, the announcement of the limit(s) will give an explanation of both why the limits were imposed and the level of the limit(s). The LME does not intend to

enter into covert arrangements with members or clients as to the prices or terms at which they can trade

- 13.20 The timing of the announcement of any backwardation limits or other interventions will be as soon as possible after the decision has been taken and immediately prior to the commencement of a ring. The announcement will simultaneously be disseminated widely to all the information services.
- 13.21 The LME Board believes that it will be helpful for it to make public its general approach to the protection of the market from abuse by holders of dominant positions. It will be beneficial to all sectors of the market to give general but practical guidance on how it would expect dominant position holders to behave in order to comply with the requirements of Board notice 97:247 and hence not to put themselves in the position of being accused of market abuse (see 13.11 and 13.12 above). The LME rules, rightly, do not prevent dominant positions. Any guidance and action must be focussed closely on preventing abuse.
- 13.22 Dominant long position holders would not be in breach of the LME rules and guidance in the Financial Service Authority's (FSA) proposed Code of Market Conduct if they did not charge other market users a higher price than they would have been able to charge without the dominant position. Any general guidance must therefore be related to the price charged by the dominant position holder. The Special Committee is more likely to consider intervention warranted, other things being equal, the more dominant the stock position and the larger the backwardation existing in the market.
- 13.23 Actual decisions on market abuse will be taken by the Special Committee, to which the Board has delegated its powers for this purpose. The Special Committee has full authority to take whatever action it considers appropriate in any particular circumstances, but it does so in the knowledge of the Board's view of appropriate general policy. Experience has shown that the LME needs to retain full discretion to act beyond its general guidance, in either direction, in special circumstances. But in the absence of special factors, the Special Committee would be guided by the Board's general policy as set out in 13.24 below. Compliance with the general policy would carry with it a presumption, again in the absence of special factors, that the dominant position holder was exercising its dominant position in conformity with the LME rules and was not abusing the market.

The Board's Policy Guidance

- 13.24 In the Board's view it is desirable, in order to reduce the risk of abuse by dominant long positions, that there should be a presumption that in the absence of special factors:
- i If at any time a member or client holds 50% or more of the warrants and/or cash today/cash positions in relation to stocks, he should be prepared to lend, if asked, at no more than a premium of $\frac{1}{2}\%$ of the cash price for a day. After five successive days, he should be prepared to lend, if asked, at no more than a premium of $\frac{1}{4}\%$ of the cash price for a day.
 - ii If at any time a member or client holds 80% or more of the warrants and/or cash today/cash positions in relation to stocks, he should be prepared to lend, if asked, at no more than a premium of $\frac{1}{4}\%$ of the cash price for a day. After five successive days, the maximum premium would fall to 0.15%.
 - iii If at any time a member or client holds 90% or more of the warrants and/or cash today/cash positions in relation to stocks, he should be prepared to lend, if asked, at no more than the cash price.
 - iv As with the publication of large position information, in determining the application of the guidelines, it would be appropriate for the LME to aggregate the positions of a client across all brokers in reaching its estimate of dominant positions. Likewise it would be appropriate to aggregate the positions of a member, its related group companies and its clients unless the firm could demonstrate that the positions were independent.
- 13.25 While there is an element of averaging in all broad guidance, the guidance set out above should benefit all segments of the market. It is aimed at preventing abuse of dominant positions, not at dominant positions themselves. Coupled with the information on large positions to be published daily (section 9 above), market users would be given greater certainty about market conditions in the face of dominant positions. The dominant position holders themselves would have the surety in normal circumstances that if they acted in accordance with the guidelines then further action would not be taken against them for market abuse. The guidelines will allow them to pursue their proper business, including investments in stock holding, without distorting the market and the official market prices on which so much metals business is referenced.

- 13.26 If, despite all the procedures and in addition the guidance relating to dominant position holders, abuse of the market takes place, disciplinary action will be pursued separately and vigorously.
- 13.27 Once the new procedures are in place, all the current general backwardation limits will be reconsidered and they will be withdrawn where appropriate.
- 13.28 The working and effectiveness of these procedures will be reviewed in the light of experience.

14 CONCLUSION

- 14.1 Revised or additional rules will be introduced where necessary to implement all the action points set out in this paper. Changes in the LME's regulatory rules and procedures will be subject to the standard consultation procedures.
- 14.2 All new procedures will be closely monitored to ensure that they are working effectively and efficiently.

ANNEX 1

ANNEX 2



LONDON METAL EXCHANGE

To: ALL MEMBERS, WAREHOUSE COMPANIES, LONDON
AGENTS AND OTHER RELEVANT PARTIES

Ref: **98/363, A:351, W:072**

Date: 13 October 1998

Subject: **MARKET ABERRATIONS: THE WAY FORWARD**

The attached document – Market Aberrations: The Way Forward – sets out the LME Board's comprehensive response to the many issues raised in the consultation paper – Solutions to Market Aberrations – circulated on 9 March 1998. The paper summarises, issue by issue, the responses and views of the respondents to the consultation exercise, analyses the various arguments and views advanced, and then details the Board's policy decisions and guidance to take matters forward. The Board's deliberations encompass all the areas raised in the consultation exercise – transparency, information, surveillance, discipline and specific market interventions.

The Board is extremely grateful to all those who responded to the consultation document. The responses were numerous and extremely valuable. They were all given careful consideration and have been instrumental in guiding the Board's deliberations. Summaries of the responses are given in the annexes to the paper.

Revised procedures or additional rules will be introduced over the coming months where necessary to implement all the action points set out in the document. Changes to the LME's regulatory rules and procedures will be subject to the standard consultation procedures and their effectiveness will be reviewed in the light of experience.

A handwritten signature in black ink, reading "Alan Whiting". The signature is written in a cursive, flowing style.

A WHITING

cc: Board of Directors

-----**From Executive Director: Regulation and Compliance**

To: ALL MEMBERS, WAREHOUSE COMPANIES AND THEIR
LONDON AGENTS

Ref: **98/362, A:350, R:020, W:071**

Date: 13 October 1998

Subject: **RULE ADDITION – RELATIONSHIP BETWEEN MEMBERS
AND WAREHOUSE COMPANIES: CONFIRMATION OF
NOTICE 98/213, A:207, W:033**

Introduction

Notice 98/213, A:207, W:033 set out proposals by the Board of Directors to introduce rules to require “chinese walls” between a member of the Exchange and a related warehouse company. The proposed provisions were designed to prevent the misuse of confidential and price sensitive information and to ensure that members and warehouse companies could compete with each other on equal terms. The proposals were subject to consultation.

Consultation

Of the responses to the consultation, all but one were supportive of the Board’s proposals. The one non-supportive respondent believed that members of the Exchange should not be allowed to own warehouses. Any rule which attempted to prevent members owning warehouses would, however, be in conflict with UK competition law and with the way potential conflicts of interest are addressed elsewhere in the UK’s financial regulatory structure.

Several respondents suggested, in order to prevent warehouse abuses with any party, that the proposals should be widened to include all commercial agreements/relationships between members and warehouse companies which fall short of ownership. The Board’s attention has been drawn to various comments and reports alleging payment of exceptional inducements, demand for a variety of substantial charges in addition to FOT charges and impediments to speedy physical re-delivery out of warehouses. The Exchange is looking into these matters and is reviewing, as a matter of urgency, its contractual arrangements with warehouse companies to ensure that LME approved warehouse companies and their placing metal on warrant

adhere to the spirit as well as the letter of the LME rules. The Board will give consideration to making changes to warehousing rules where considered appropriate in the light of this review. The specific issues relating to common ownership of members and warehouse companies need to be addressed separately through the introduction of “chinese walls” procedures.

On the details of the Board’s proposals, amendments have been introduced in two areas in the light of the consultation. Under section 2 of the proposals – Definitions – it has been made clear that ‘confidential information’ includes any information which a warehouse company acquires through its warehousing activities in respect of specific LME brands, ahead of general publication by the LME. This clarification is incorporated by a new 2iv of the new rule addition set out below. Second, Ci of the proposals has been amplified to require that where the personnel of the related warehouse company and the member occupy the same premises, security access systems must be installed to prevent unauthorised access by the related company’s personnel.

Rule Addition

The Board of Directors has approved the rule changes and guidance as set out below. The new procedures come into effect immediately.

1 Background

The review by the Financial Services Authority (formerly the Securities and Investments Board) of the LME and the metals markets raised aspects of the relationship between warehouse companies and members which are potentially open to anti-competitive and distorting behaviour.

Concern centred around the independence of members and warehouse companies from one another, the flow of information between them and the existence of systemic advantages which could restrict the ability of both members and warehouse companies to compete with each other on equal terms. The main areas of concern are:-

- i the possibility that a member might gain access to price and/or commercially sensitive information from a warehouse company;
- ii the possibility that a member could pass commercially sensitive information gained from having access to one warehouse company to another warehouse company;
- iii the ability of a member to advantage one warehouse company by offering warrants from a competing warehouse company to customers at a discount; and
- iv the effect of long term storage deals restricting the amount of LME stocks in circulation.

These issues are of most concern and give rise to serious potential conflicts of interest where a member and a warehouse company are both part of the same group.

In the light of both UK competition law and the dependence, throughout the UK's regulatory structure, on "chinese walls" to handle conflicts of interest, it is not open to the LME to prevent the common or related ownership of LME members and warehouse companies. This Notice, therefore, proposes provisions and procedures to establish and enforce strict "chinese walls" between a member and a related warehouse company. These provisions are designed to prevent the misuse of confidential and price sensitive information.

2 Definitions

For the purposes of this Notice:

"Confidential Information" means, in respect of a warehouse company's business, any of the following, ahead of general publication by the LME:

- i stock figures for LME deliverable metal;
- ii all information relating to proposed or actual shipments of LME deliverable metal to be made or received by that warehouse company (including, in respect of shipments to be made by that warehouse company, any information of a commercially sensitive nature given to that warehouse company by the shipper, his agent or the recipient of that shipment, such as the identity of the customer, customs information, etc);
- iii all information related to the issuance, holding and cancellation of LME warrants by that warehouse company; and
- iv any other information in relation to specific LME brands which a warehouse company acquires through its warehousing activities.

"Related warehouse company" means a warehouse company which is a subsidiary or holding company of a member, or a subsidiary or holding company of one of a member's subsidiaries or holding companies. The terms "holding company" and "subsidiary" have the meanings given to them in section 736 of the Companies Act 1985.

3 Members' and Warehouse Companies' Obligations

Under the terms of the Conditions and Obligatory Procedural Notes for warehouse companies, a warehouse company is prohibited from revealing Confidential Information to other entities. This prohibition is an important part of the Exchange's rules and practices designed to ensure the orderliness of its market.

A member which encouraged or facilitated a warehouse company to breach these prohibitions would itself be in breach of its obligation to observe high

standards of integrity and fair dealing and high standards of market conduct under Regulation 9.6 of Part 2 of the LME's Rules and Regulations.

Equally, a member which took advantage in its trading of Confidential Information would be in breach of Regulation 9.6.

4 Members and Related Warehouse Companies

The risk that Confidential Information may pass between a warehouse company and a member is increased if they are both companies in the same group. A member must not unfairly take advantage of its group relationship with a related warehouse company by utilising Confidential Information in a way which would jeopardise the proper functioning of the metals market, or breach any of the Financial Services Authority's Statements of Principle, with which all members must comply, along with the LME's own Rules and Regulations.

It is essential that personnel engaged in trading activities do not come into possession of any Confidential Information. The LME considers that members will only be able to satisfy this requirement if appropriate procedures exist within both the member and the related warehouse company. Within the member itself, this will require that all personnel engaged in trading activities are made aware of the confidentiality procedures adopted by the related warehouse company to comply with the requirements set out in 5 below, and advised that if they inadvertently come into possession of any Confidential Information they must not trade on the basis of the information. Strict procedures as set out below must be put in place within the member itself to ensure these provisions are complied with.

5 Procedures to be followed

In order to ensure that Confidential Information is properly protected where a member has a related warehouse company, the Exchange will expect the member and the related warehouse company to put in place procedures which satisfy the following requirements:

A "Need to Know" Principle

Access to Confidential Information must be given only to those personnel whose responsibilities could not be carried out without such access. The LME expects related warehouse companies to organise their affairs in such a way that this number is kept to a minimum. This should be the case both for personnel within the related warehouse company and within the related member. Normally, for the related member, and even then only in exceptional circumstances, such information will be confined to common directors.

B Physical Separation

- i All Confidential Information must be kept in a secure location to which only authorised personnel have access. Access to unauthorised personnel must be effectively restricted (i.e. by locked door, security card, signing in and out procedure etc.).
- ii All Confidential Information held within a computer system must be accessible only by authorised personnel and be protected by a password. Passwords should be changed at regular intervals.

C Separation of Personnel

- i Related warehouse company personnel should be physically separated from the personnel of the member. Where they occupy the same premises, security access systems must be installed to prevent unauthorised access.
- ii It is obviously essential that personnel with access to Confidential Information do not also carry out any functions for the member, although the LME acknowledges that for strategic reasons it may be necessary for an employee of the member or related warehouse company to be a director of both that related warehouse company and a member. In these circumstances strict procedures must be put in place regarding board meetings etc, to ensure that no Confidential Information is disclosed by that director to other personnel of that member.
- iii Both the member and the related warehouse company must maintain a contemporary record of personnel sitting on each side of the “chinese wall”.

D Employee Awareness

- i It is essential that related warehouse companies ensure that relevant personnel are familiar with the procedures adopted to comply with this Notice and abide by them. It must be impressed upon relevant personnel that their obligations apply both during and outside of office hours. Employees must be trained in the procedures adopted and reminded of their obligations on a periodic basis.
- ii Each employee who has access to Confidential Information should also be given a set of written procedures to follow.
- iii Relevant employees should sign acknowledgements that they understand and will adhere to the confidentiality procedures.
- iv Internal sanctions should be established for breach of the confidentiality procedures and strictly enforced. Depending on the nature of the breach, sanctions may range from written warnings to dismissal.

6 Senior Employee

Related warehouse companies will be expected to appoint a senior employee who will be responsible for ensuring that the confidentiality procedures adopted are effective and are followed. Members' own compliance officers will be responsible for ensuring that members adopt and follow fully compliant procedures. Ultimately however, the LME will look to directors of the member to put in place procedures designed to ensure compliance with the terms of this Notice.

7 Duty to Inform LME

A member which comes into possession of any Confidential Information, whether through an employee or any other related party such as a Non-Executive Director or consultant, and whether from a related warehouse company or otherwise (or which is otherwise aware of a breach of these procedures) must immediately inform the LME of that fact.

8 Discounted LME Warrants

A member with a related warehouse company which is operating a listed warehouse in a particular location may not sell or offer to sell LME warrants issued in respect of other listed warehouses in the same LME approved Location or within a 250 mile radius of the related warehouse company at a discount to the related warehouse company's LME warrants, unless it can demonstrate that it would have offered the same discount even if it did not have a related warehouse company. Subject to the above proviso, a member must not otherwise offer any incentive to customers to exchange or substitute LME warrants issued by a related warehouse company for LME warrants issued by any other warehouse company's listed warehouse in the same Location or within a 250 mile radius of the related warehouse company. Any member or warehouse company which is aware of any such sale or offer must immediately inform the LME of that fact.

9 Access to Warehouses

Personnel of a member with responsibilities for a related warehouse company may not inspect metal held on LME Warrant by that member at another warehouse.

10 LME Inspections

The LME intends to make periodic and thorough inspections of members' and related warehouse companies' procedures to ensure compliance with the provisions of this Notice. These inspections may be conducted by third party professionals appointed by the LME. The cost of these inspection visits and any subsequent action taken will be paid for by the relevant member.

11 Disciplinary Sanctions

Breach of these procedures by a member or a related warehouse company will be regarded as an act of misconduct and will result in disciplinary action and the imposition of a severe penalty.

12 Review Procedures

The new procedures will be strictly monitored and will be reviewed after one year to ensure that the new system is delivering fair and transparent trading relations and preventing the misuse of confidential and price sensitive information.

A WHITING

cc Board of Directors



LONDON METAL EXCHANGE

-----*From Executive Director: Regulation and Compliance*

To: ALL MEMBERS
Ref: 99/064 : A064
Date: 22 February 1999
Subject: **CONCENTRATION OF WARRANT HOLDINGS**

The Consultation period on the publication of the concentration of warrant holdings closed on 26 January 1999. The LME began publication of information on the concentration of warrant holdings on 22 February 1999. The publication of this data forms an integral part of the LME's strategy to enhance market transparency.

An example of the format of the published table as well as a greater explanation behind its formation can be found in the LME notice 98/447, A:434.

The LME will publish information on the warrant holdings two trade days in arrears at 10.30am on the 'Statistics' page at the LME's internet site (<http://www.lme.co.uk>).

Questions regarding warrant banding should be directed to Sarah Watts (telephone: 0171 264 5691, e-mail: sarah.watts@lme.co.uk).

A WHITING

cc: Board Directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 99/075 : A075
Date: 26 February 1999
Subject: **PUBLICATION OF LARGE FUTURES POSITIONS**

Introduction

Section 9 of the LME Board's paper "Market Aberrations – The Way Forward" circulated to members under cover of board notice 98/363 A:351, W:072 of 13 October 1998 announced the Board's intention to publish regular information on an anonymous basis on the holding of large trading positions.

2 The notice sets out the proposed details of the information and the format in which it is to be published. Concentration of futures positions will be published on the LME's website on the internet – www.lme.co.uk in spring 1999 following this consultation period. The data will also be distributed on the LME's market data services system when it commences operation in the summer of 1999.

3 Comments on the details of the proposals set out in this notice should be sent to Mrs Joanna Stuart, Head of Market Surveillance, by 14 April 1999.

Identification of Holdings

4 The LME's compliance department receives daily reports of members' proprietary and customers' large futures positions. The identities of those customer accounts are disclosed, on a confidential basis, to the LME compliance department. For the purpose of identifying large positions, the LME will automatically aggregate a member's holding with those companies in the same group. Equally, a client's positions held across more than one member will also be aggregated automatically. These automatic aggregations will be based on accounts and grouping information supplied by member firms.

5 Where the LME compliance department believes that it is appropriate and meaningful, it will also aggregate positions which are not subject to automatic aggregation described in paragraph 4 above. For example, a member's proprietary positions will be aggregated with those of one or more of its customers if the LME compliance department believes that there is a



common purpose. In all such cases, LME compliance will inform the member affected.

6 Additionally, a new report will be published alongside the concentration of warrant holdings report which is currently available on the Internet. This will provide transparency to the markets on any large warrant and net (longs and shorts) cash today/cash positions which could potentially trigger the lending thresholds set by the Board’s policy guidance on market interventions. These are set out in Section 13.24 of the LME Board’s paper “Market Aberrations – The Way Forward”.

Content and Format of the Published Information

7 The information will be published daily, two days after the date on which the published holdings were held. The two day delay is currently required to allow members to report their positions and the LME to aggregate and check the data. Daily production will show the build up of large positions.

8 The proposed format of the concentration of warrant and long positions information (using a hypothetical example) is set out in the following table:

Large LME Warrant Holdings + Cash Today + Cash positions held on x.x.1999

Warrant & Cash Today & Cash/ Total Stocks	Alu	Copper	Zinc	Nickel	Lead	Tin	Alloy	Silver
30 - <40%	1	2	0	0	0	1	0	0
40 - <50%	1	0	0	1	0	0	0	0
50 - <80%	0	0	0	0	0	0	1	1
80 - <90%	0	0	0	0	1	0	0	0
>90%	0	0	1	0	0	0	0	0

9 The proposed format of the concentration of futures positions information (using a hypothetical example) is set out in the following table. The disclosure will cover the nearby three third Wednesdays. Dominant futures holdings will be disclosed based on the percentage of market open interest held by any one party or group. There will be one table showing the longs and shorts separately for each metal. If there are marked changes in liquidity for the nearby three second Wednesdays as a result of the proposed Index contract, the LME will consider, at a later date after conducting internal analysis, whether it is appropriate to include the three second Wednesdays as well.



Large LME Futures positions on x.x.1999

xx/xx/1999

Copper	LONG	17-Feb	17-Mar	21-Apr
5 - <10 %		1	2	1
10 - <20 %				
20 - <30 %		1	1	
30 - <40 %				
> 40 %				

	SHORT	17-Feb	17-Mar	21-Apr
5 - < 10 %			1	
10 - < 20 %				1
20 - < 30 %				
30 - < 40 %		1		
> 40 %				

Footnotes:

- i The figures show LME concentration of futures positions in terms of percentage holdings of market open interest two business days ago. The positions indicated in this table may no longer be held.
- ii The large positions indicated can be held by individual members, individual clients, linked group companies or can be the combined holding of members and/or clients where the LME compliance department believes there is a common purpose in, or a common effect produced by, those holdings.
- iii The information contained in this table relates only to LME registered contracts.
- iv This information needs to be interpreted carefully. There should be no automatic presumption that dominant positions will invariably result in a tightness of the market. Equally, because of the possibility of covert collusion between apparently unconnected parties, lack of published dominant positions is not a guarantee that effective large positions do not exist.
- v The market open interest information for other prompt dates are available on the Internet on page <http://www.lme.co.uk/cgi-bin/oicqi>. This could provide helpful information on the depth and liquidity of markets on other contracts.

A WHITING

cc: Board Directors

-----*From Executive Director: Regulation and Compliance*

To: ALL MEMBERS

Ref: 99/256 : A251 : R016

Date: 18 June 1999

Subject: **ACCESS TO OVER THE COUNTER (OTC) INFORMATION
IMPACTING THE OFFICIAL LME MARKETS**

Introduction

The LME issued consultation document 99/019 : A019 on 13 January 1999 setting out revised proposals on access to over-the-counter (OTC) information. A total of 19 responses were received: 7 were from ring dealing members, 11 from associate broker clearing members and one from a non-member trade association. A summary of the responses, on an anonymous basis, is attached.

Summary of Responses

2 All respondents were opposed to routine daily reporting of large OTC positions but a majority supported the LME compliance department having access to OTC information for the ad-hoc purpose of identification or resolution of an undesirable market situation. Respondents were, however, concerned as to how the LME could compel members' affiliates to provide OTC information given that its jurisdiction extends solely to members. Some questions were also raised concerning client confidentiality.

3 The main concerns raised by the proposals set out in 99/019 : A019 can be summarised as follows:

- Potential regulatory overlap with the FSA as far as monitoring of OTC transactions is concerned
- The lack of a clear definition of "OTC" for the purpose of routine daily reporting

- Possible breach of client confidentiality requirements
- Cost of implementation of the necessary IT changes
- Lack of LME jurisdiction to require access to OTC information of members' affiliates
- Potential unfairness if members are penalised as a result of non co-operation by its customers or affiliates

The way forward

4 The LME Board has considered the responses to the consultation document 99/019 : A019 and has weighed members' concerns alongside the LME's minimum needs for access to OTC information to enable it to fulfil its statutory duty to maintain fair and proper official markets.

5 The Board is persuaded by some of the concerns raised, particularly in relation to the routine daily reporting of large OTC positions. Routine daily large OTC position reporting would enable the LME to fulfil its statutory duties, but the Board has concluded that the cost would be disproportionate to the regulatory needs and that the LME's regulatory requirements can be met through more directed access to OTC information on a case by case basis. For a large proportion of the membership substantial IT systems changes would need to be introduced and substantial costs incurred to provide regular OTC information. Moreover, routine daily reporting of large OTC positions would require IT systems changes which could not be introduced for a considerable period of time in view of year 2000 considerations.

6 The Board recognises that over the last year and a half it has introduced significant measures which have delivered increased transparency to the markets. These measures include publication, on an anonymous basis, of dominant warrant holdings, tom and cash positions, nearby futures positions and the introduction of a new method for determining market open interest. The Board wishes to assess the impact of these new transparency measures before contemplating imposing any new regular reporting requirements on members. The expectation is that compliance with the new rules and procedures covering LME access to certain OTC information (see paragraph 7 below) on an ad hoc basis and in specific circumstances should allow

the exchange to fulfil its regulatory responsibilities and obviate the need for regular OTC reporting.

7 As explained in notice 99/019 : A019 and as clearly demonstrated by the Sumitomo affair, off-exchange positions can influence the official market, particularly where the off-exchange positions are hedged or backed onto the LME. To comply with its statutory duty to ensure a proper on-exchange market, there are occasions when the LME needs to have access to information about particular OTC positions of members and their affiliates in order to explain on-exchange positions. Customers, for example, may enter into OTC positions with members' affiliates and members' affiliates may then hedge or back these positions on-exchange. At times of market disorder, it is essential for the LME to be able to identify any parties attempting, directly or indirectly to manipulate the market and or holding large positions. The most likely route for manipulation is indirectly through off-exchange positions. By spreading off-exchange positions between LME members, effective dominant positions can arise unbeknown to the exchange and indeed, to the members. Sumitomo is the most prominent, but far from the only, case in point.

8 Ad hoc access to specific off-exchange position information in clearly prescribed circumstances will not be unduly burdensome. The revisions to rule 9 of part 2 of the LME rulebook limit the circumstances in which OTC information is to be supplied to those occasions when the LME has reasonable cause to suspect the existence, or the development or likely development of an undesirable situation or an undesirable or improper trading practice which, in its opinion, has affected or is likely to affect one of its markets. This formulation is taken from rule 14 of part 3 of the LME rulebook which deals with the powers of the Special Committee in emergency situations.

9 In practice this means that on the specific occasions when the LME compliance department will be asking members and their affiliates for off-exchange position information, the information requested will be very tightly delineated. Information requests will not be open-ended. Normally the LME will be able to point to specific on-exchange positions at the member firm with a request to confirm whether or not there are off-exchange positions which underlie the on-exchange positions, together with the identify of the client undertaking the off-exchange business with the member or affiliate.

10 Provision of such OTC information on an ad hoc basis will be confidential to the LME's compliance department, as is the case with

the on-exchange regulatory information. It will not involve changes in any way to members' accounting, management information or IT systems. Where members prefer, information relating to positions held by members' affiliates can be required by the LME directly from the affiliate and supplied to the LME directly by the affiliate. Members, however, may need to enter into arrangements with their affiliates which enable them to comply with the amended rule 9 of part 2 in so far as it relates to affiliates' OTC information. In addition, in order to ensure that client confidentiality requirements do not prevent members from complying with their duties to disclose OTC information in accordance with revised rule 9, members may need to amend their customer agreements to provide for appropriate regulatory disclosures to the LME compliance department. This should not create any problems. As mentioned in notice 99/019 : A019, many members already willingly supply relevant OTC information on request from the LME and clauses in client agreements normally allow for information to be supplied on request to the regulatory authorities. The amended rule 9 of part 2 makes explicit the LME's powers to obtain certain information in relation to members' OTC business in defined circumstances and the LME is the regulatory body responsible under UK law for regulating conduct on its markets.

11 Failure to provide the relevant OTC information requested would open the member to disciplinary action and other action available to the LME; for example directions to a member to trade out of client contract positions and/or exchange contract positions under rule 14.1 of part 3 of the LME's rules and regulations.

12 Implementation date for the new rule 9.1.3 of part 2 of the LME rulebook will be 1 September 1999 to allow members to revise arrangements/contract terms where necessary.

13 The current rule 9.1.2 of part 2 of the LME rule book will therefore be replaced with a new 9.1.2 and new 9.1.3 as follows:

9.1.2 such further information in relation to commercial matters as may be required by the Chief Executive or those empowered by him generally or in any specific case; and

9.1.3 such further information in relation to regulatory and compliance matters as may be required by the Executive Director: Regulation and Compliance or those empowered by him generally or in any specific case. Where the Executive Director: Regulation and Compliance or those

empowered by him have cause to suspect the existence or to anticipate the development or likely development of an undesirable situation or undesirable or improper trading practice, the information which may be required shall include information relating to the over-the-counter business of a member or any of its affiliates in metals, including any index thereon, traded on the exchange.

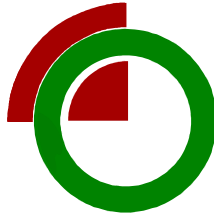
14 Notice 99/019 : A019 also proposed a pre-notification system if members wished to bring OTC contracts on-exchange using historic prices. The purpose of the proposal was to increase compliance with the guidance to bring such contracts on-exchange at the earliest opportunity in order to prevent bunching and distorting the market shortly before prompt.

15 Few representations were received on this proposal. Nevertheless, on further review, the LME believes the proposal would be costly in systems terms for both members and the exchange and believes that the same objective can be achieved more simply and at lower cost. Under the revised proposal, OTC contracts could be brought on-exchange at historic prices only if the contract is brought on-exchange at least a given period (such as three months) ahead of the prompt date. Any OTC contracts brought on-exchange closer to the prompt date than the prescribed period would be required to be brought on-exchange at current prices.

16 A further short consultation document will be issued in the coming week, describing this proposal in detail.

A WHITING

cc Board of directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: RING DEALING MEMBERS
ASSOCIATE BROKER CLEARING MEMBERS

Ref: 99/324 : A313 : R025

Date: 22 July 1999

Subject: **LME VENDOR FEED SYSTEM - CONFIRMATION OF NOTICE
99/146 : A144 : R11**

BACKGROUND

LME notice 99/146 : A144 : R11, issued on 20 April 1999, published the LME board's policy on vendor feed price quotations. The notice also consulted on proposed amendments to regulation 4.1 of part 3, trading regulations, of the LME's rules and regulations and on proposed terms and conditions for contributors to the vendor feed system. There were seven responses to consultation document. At its meeting on 21 July 1999, having taken into account representations during the consultation process, the board confirmed the arrangements for the vendor feed system as set out below.

POLICY - VENDOR FEED PRICE QUOTATIONS

Paragraph 3 of the LME board's policy on vendor feed price quotations states that contributors must generally be prepared to trade reasonable volumes with users of the market at the indicative prices input, in normal market circumstances. In view of the representations received and for the avoidance of doubt, the board wishes to clarify that the term "users of the market" does not include LME members. As set out in the policy document, the LME will monitor compliance with this obligation by comparing a contributor's quoted indicative prices with those prices at which the contributor actually traded. A copy of the board's policy is attached.

REGULATION 4.1 OF PART 3, TRADING REGULATIONS

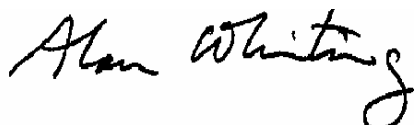
There is no change to the proposed amendments to regulation 4.1 of part 3, trading regulations, of the LME's rules and regulations. A copy of regulation 4.1 as amended is attached and shall come into force with immediate effect.

TERMS AND CONDITIONS

The proposed terms and conditions for contributors to the vendor feed system have been amended by the insertion of a new clause 5.3 and the deletion of former sub clause 5.4(d). These amendments do not materially change the effect of the terms and conditions.

Members currently contributing prices to the vendor feed system are, with effect from Monday 2 August 1999, deemed to be notified under regulation 4.1.3 of part 3 of the LME's rules and regulations in respect of each metal for which they currently contribute prices. This will bring the new system into force on that date. Those members' current vendor feed system agreements with the Exchange will be superseded on that date by the attached terms and conditions.

Those wishing to discuss arrangements for contributing to the vendor feed system should contact Mr John Vincent at the LME.

A handwritten signature in cursive script that reads "Alan Whiting".

A WHITING

cc: Board directors

VENDOR FEED SYSTEM
AMENDED
REGULATION 4, PRICE INFORMATION,
OF
PART 3, TRADING REGULATIONS

- 4.1 For the purpose of disseminating information as to prices obtaining at any time during business hours of any Business Day:-
- 4.1.1 the Exchange shall, during Ring and kerb trading, input current prices for all types of contract traded in the ring to the Exchange's price-reporting service;
- 4.1.2 subject to 4.1.3 below, each Ring Dealing and Associate Broker Clearing Member shall input into the Exchange's price-reporting service indicative current bid and offer prices and, in respect of Carries, price spreads, for all types of Contract;
- 4.1.3 a Member shall only be obliged to comply with 4.1.2 above if the Exchange has served a notice on it specifying the type or types of Contract, if any, in respect of which it must input prices;
- 4.1.4 the Exchange shall serve a notice under 4.1.3 above on a Ring Dealing or Associate Broker Clearing Member if that Member satisfies the criteria published by the Exchange from time to time;
- 4.1.5 the Exchange may serve a notice under 4.1.3 above on a Ring Dealing or Associate Broker Clearing Member if that Member requests it, and the Exchange considers it appropriate or desirable, to do so;
- 4.1.6 the Exchange may serve a withdrawal notice in respect of any type or types of Contract whereupon the Member served with the withdrawal notice shall not input prices in respect of the type or types of Contract specified in that withdrawal notice;
- 4.1.7 a Member served with a notice under 4.1.3 above must comply with any guidance issued by the Exchange and must abide by the terms and conditions for the Exchange's price-reporting service, as amended from time to time.
- 4.2 [no change]
- 4.3 [no change]

POLICY

VENDOR FEED PRICE QUOTATIONS

The following sets out the LME board's policy for the interpretation of the VFS rules set out in the market aberrations paper.

1. Both ring dealing and associate broker clearing members will be required to input into the vendor feed system in respect of every LME futures contract type in which they trade actively.

Inputs will be required for each futures contract type in which the member's active trading accounts for 1.5% or more of the total volume traded in respect of that contract type. The Executive will calculate the market shares on a rolling three monthly basis and update the list of required contributors at the beginning of each calendar quarter for the ensuing quarter.

2. Contributors will be required to update the prices for the futures contract types they quote at least six times per day at meaningful intervals.

This means that new inputs should be made throughout the trading day, whether or not prices have moved. Where prices are highly volatile inputs should be more frequent. On the introduction of the revised disciplinary system, failure to input and update quotes reasonably throughout the day will attract automatic financial penalties.

3. Contributors must generally be prepared to trade reasonable volumes with users of the market at the indicative prices input, in normal market circumstances. Any material or consistent divergences between the indicative prices quoted by contributors and those at which they actually trade will be investigated and dealt with on a case by case basis. Penalties will be imposed on contributors repeatedly refusing to trade in normal market circumstances at their indicative prices.

The LME compliance department will use the compliance support system to compare indicative prices quoted by contributors, and those at which they actually trade.

A high standard of accuracy in inputting prices will naturally be expected, but errors will doubtless creep in from time to time. Those will normally be picked up through the executive's checking procedures. Contributors whose inputs are repeatedly and regularly inaccurate will be fined. It is difficult to specify too precisely what would be classed as repeatedly inaccurate, but, as an indication, at least 90% of the input prices should be accurate.

The emphasis in the compliance department's monitoring is on 'reasonable volumes' in 'normal market circumstances', on 'material and consistent divergences', and on 'repeatedly refusing to trade'. All contributors will be expected to keep to the spirit of any guidelines, rather than any precise yardsticks.

Where prices are highly volatile and the market is moving rapidly actual prices may run ahead of the broker's ability to input the latest quotes. Such occurrences will, however, be rare.

Inputting errors aside, there will sometimes be valid reasons for the prices of actual trades with users of the market to diverge from indicative screen prices. The broker may have concerns about the motivations and/or creditworthiness of the counterparty, or might believe that the tonnage requested would move the price. In such circumstances the compliance department would be understanding, unless there were a repeated pattern of such excuses.

LONDON METAL EXCHANGE

VENDOR FEED SYSTEM

TERMS AND CONDITIONS

1. The following terms and conditions apply to all LME members for the time being subject to a notification under rule 4.1.3 of part 3, trading regulations, of the LME's rules and regulations.

2. In these terms and conditions the following words and expressions shall have the following meanings:

Contributor A Ring Dealing Member or an Associate Broker Clearing Member who has been notified by the LME under rule 4.1.3 of the Rules.

Far Forward Contract A Contract with a Prompt Date of more than three months as specified in the Schedule.

Information Indicative price quotes for Contracts as specified in paragraph 3.7 below and the Schedule.

LME The London Metal Exchange Limited

Nearby Contract A Contract with a Prompt Date of up to and including three months as specified in the Schedule.

Reuters Reuters Limited

Rules The rules and regulations of the LME as amended from time to time and including, for the avoidance of doubt, any guidance to those rules and regulations issued by the LME.

Schedule The schedule to these terms and conditions.

System The LME's price reporting service, currently known as the LME Vendor Feed System established by the LME in conjunction with Reuters, including any amended or replacement system established by the LME, either by itself or in conjunction with any other party.

Words and expressions defined in the Rules shall have the same meaning in these terms and conditions. Words importing the singular shall, where the

context permits, include the plural and vice versa. Words importing persons shall, where the context permits or requires, include partnerships and corporations.

3. Inputting Information

- 3.1 A Contributor shall input Information into the System by means of a Reuters terminal, or such other contributor facility designated by the LME on not less than three months' written notice.
- 3.2 A Contributor shall input Information in respect of Nearby Contracts manually and without the use of electronic aids or computer driven spreadsheets. In particular, information denominated in sterling must not be input by automatic means on a change in exchange rates.
- 3.3 A Contributor may use computer-driven spreadsheets to assist in the contribution of Information in respect of Far Forward Contracts provided that the systems used are manually operated and result in the generation of prices that reflect real price movements. Spreadsheets must not be externally triggered on a timed basis or as a result of a change in another Member's quoted prices.
- 3.4 A Contributor must not input Information in respect of a particular type of Contract during the Ring-trading period for that type of Contract and an Associate Broker Clearing Member must not input Information during kerb-trading periods.
- 3.5 A Contributor must not abuse the System by entering excessive volumes of Information in a continuous or concentrated manner.
- 3.6 A Contributor must obtain the written consent of the LME, such consent not to be unreasonably withheld, prior to changing its method or systems for inputting Information and must liaise with the LME when implementing any new or revised systems or method of inputting.
- 3.7 Information in respect of each type of Contract:-
 - a) must be input in bid/ask format;
 - b) must quote prices for Nearby Contracts;
 - c) must only be quoted in US dollars except that Information in respect of three month outright and cash to three month spreads for copper and lead Contracts may be quoted in sterling;
 - d) may quote prices in respect of Far Forward Contracts; and
 - e) must not quote prices or include other information which does not comply with any of (a) to (d) above.
- 3.8 For so long as a Contributor is obliged to input Information into the System it shall maintain a subscription to Reuters, or any other method of data

collection for the System designated under paragraph 3.1 above, to enable it to input Information.

- 3.9 Each Contributor undertakes that any person inputting information into the System on its behalf has its proper authority to do so and has been given adequate training.
- 3.10 A Contributor may use an agent to perform its obligations to input Information but will be responsible for the actions of that agent as if they were the actions of the Contributor.

4. Payment

- 4.1 The LME shall pay Contributors a fee for inputting Information into the System.
- 4.2 The LME shall prepare annual audited accounts for the System for the purpose, inter alia, of establishing the net operating profit of the System.
- 4.3 Subject paragraph 4.5 below, the LME shall set aside an amount of the net annual operating profit of the System for the payment of fees to Contributors to the System during that year, such amount to be at the absolute discretion of the board of directors of the LME.
- 4.4 The LME shall calculate a fee payment for each Contributor based on the volume of Information input by that Contributor during the year. In calculating a Contributor's fee payment the LME may take into account whether or not the volume of Information input by that Contributor was above or below the average for all Contributors during that period.
- 4.5 The LME may, from the income of the System for any one year, make provisions for deficits from previous years and provisions for developments to the System, such provisions to be at the absolute discretion of the board of directors of the LME.

5. Licence

- 5.1 In consideration for the payment to be made under paragraph 4 above, each Contributor grants to the LME the following rights in and licences over the Information input into the System:
 - a) To supply the Information to third parties by means of the System;
 - b) To use the Information in hard or soft copy form for its own purposes or for submission to other exchanges or regulatory bodies in such manner (and at such times) as the LME thinks fit;

- c) To consolidate the Information with Information input by one or more other Contributors (or otherwise);
 - d) To use or license others to use any of the information in a consolidated form with other information obtained or generated by the LME.
- 5.2 All other rights, including copyright, in the Information input into the System by a Contributor shall remain the property of that Contributor. However, each Contributor acknowledges that any information derived from the consolidated Information input by more than one Contributor, is the copyright and intellectual property of the LME.
- 5.3 Each Contributor acknowledges that copyright in Information input into the System by another Contributor is the property of that other Contributor. Each Contributor acknowledges that copyright in information generated or disseminated by the LME (such as, but not limited to, the LME's Official Prices, Unofficial Closing Prices, Closing Prices, Ring and kerb prices, official high and low prices, stock reports, volume reports and market-open-interest reports) is the property of the LME.
- 5.4 Should the LME use Information input into the System by any Contributor other than in a form consolidated with Information input by one or more other contributors, it will, if so requested in writing, identify Information input by a Contributor as having been input by that Contributor.
- 5.5 In consideration for the payments to be made under paragraph 4 above, each Contributor undertakes that Information which it has input into the System, or any information which conforms with the Information it is obliged to input into the System, shall not be publicised or made available to third parties by electronic means unless:
- a) it is the same as Information input into the System by that Contributor,
 - b) it is disseminated no sooner than it is input into the System, and
 - c) access to it is made available only to a known, closed user group.

6. Liability

- 6.1 The LME shall not be liable for any loss or damage arising from:
- a) any faults or delays in the System,
 - b) any inaccuracies or omissions in the Information displayed by the System,
or
 - c) any breakdown in links between a Contributor and the System.
- 6.2 Contributors undertake that Information input into the System shall not comprise administrative messages, defamatory or advertising material or any information the dissemination of which is contrary to the law or any of the Rules.

7. Termination

In the event that any Contributor is no longer obliged to input Information into the System, any rights or obligations in respect of the System accrued to that date shall continue.

**SCHEDULE
TO
LME VENDOR FEED SYSTEM
TERMS AND CONDITIONS**

1. INDICATIVE FUTURE PRICES, NEARBY CONTRACTS

Contributors inputting Information in respect of a Contract type must input a bid/ask price for each of the following Contracts:

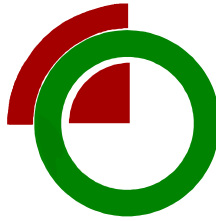
Three month outright
Cash to three months spread
First nearby month to three months spread
Second nearby month to three months spread
Third nearby month to three months spread

2. INDICATIVE FUTURE PRICES, FAR FORWARD CONTRACTS.

Contributors inputting Information in respect of any Contract type may, with the written agreement of the LME, input a bid/ask price for the following Contracts:

For copper, aluminium, zinc, nickel and silver: spreads from three months to 27 months.

For lead, tin and aluminium alloy: spreads from three months to 15 months.
[For the LME: outright values from three months to 12 months.]



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS

Ref: 99/326 : A315 : R027

Date: 22 July 1999

Subject: **TIMING OF TRADES BETWEEN RING DEALING MEMBERS
AND OTHER COUNTERPARTIES/CUSTOMERS**

Introduction

The recently completed cycle of member visits noted significant problems in compliance with board notice 91:234 LME Matching System-Use of Ring and Kerb Trade Time Indicators. These problems related to the misuse of mnemonics and the incorrect recording of exception times.

Rules

In order to achieve consistency amongst ring dealing members (RDMs) and to better reflect market practice it is proposed that two new time codes 'C' and 'D' be introduced to allow RDMs to demonstrate that the price achieved on a trade occurred during a particular market session. The 'C' and 'D' codes are to be used for trades between an RDM and any counterparty (other than another RDM) and will apply to trades executed in any geographical location. The responsibility will be placed on the RDM to demonstrate that the executed price was achieved during the implied market session. Trades between RDMs during ring and kerb sessions will continue to be matched using the appropriate 'R' and 'K' time codes. Trades outside of the appropriate market floor sessions are still designated 'timed' trades and must be recorded in the RDM's records and entered in to the LMEMS as such.

Interim



These proposals have been discussed and agreed with RDMs but they have indicated that they will not be able to introduce system changes to implement the new time codes until Q1 2000. In the interim therefore, members may use the 'C' and 'D' codes on their manual records (ie blotters, tickets etc.) but should enter the corresponding time of trade as detailed on the attached schedule, into the LMEMS.

Guidance

We have drafted guidance addressing certain forms of trade where it may be unclear in which market session the trade took place. Members' comments on the appropriateness of the guidance as well as the other matters addressed in this notice are sought.

Effective date

The interim measure will be effective from the date of this notice. The LME expects to implement system changes in the LMEMS by March 2000 and members should be in a position to comply with this rule by that date. Comments on the guidance and other matters should be sent to Liam McCarthy by 3 September 1999.

A WHITING

cc: Board directors



SCHEDULE OF RING AND KERB TRADE TIMES

Trades with RDM's	with	Trades with Non-RDM's	Time to be entered in LMEMS
R 1		C 1	Silver 11:44 Alloy 11:49 Tin 11:54 Aluminium 11:59 Copper 12:04 Lead 12:09 Zinc 12:14 Nickel 12:19
R 2		C 2	Copper 12:34 Alloy 12:39 Tin 12:44 Lead 12:49 Zinc 12:54 Aluminium 12:59 Nickel 13:04 Silver 13:09
R 3		C 3	Alloy 15:14 Silver 15:19 Lead 15:24 Zinc 15:29 Copper 15:34 Aluminium 15:39 Tin 15:44 Nickel 15:49
R 4		C 4	Silver 15:59 Lead 16:04 Zinc 16:09 Copper 16:14 Aluminium 16:19 Tin 16:24 Nickel 16:29 Alloy 16:34
K 1		D 1	13:29
K 2		D2	Alloy/Silver 16:44 Tin/Lead 16:49 Zinc/Nickel 16:54 Aluminium 16:59 Copper 16:59



Guidance on potential problems regarding trade time recording

A number of ring dealing members (RDMs) have requested clarification of the time of trade that should be used if a trade is not finalised at its initial point of execution, but is delayed awaiting an adjustment to one or more of the trade components. Examples of this practice include:

- A client requests a date adjustment on an outright trade either at a specified level (i.e. currently away from market levels) or at a specified time (i.e. during a floor session). The date adjustment may refer to either an outright date or to a succession of outright dates (i.e. basis the 'average').
- A client requests that a trade is converted into an LME acceptable currency, either basis a specified FX fixing time, or at a specified FX level (again, currently away from market levels)
- A client requests a series of executions be amalgamated over the duration of a trade day or part thereof. This could apply to a number of trades executed at the same price level or to trades where the final price is an average of the component parts.

The time used for both the time of trade on the members source document (ticket, blotter etc.) and that subsequently entered in to the LMEMS requires clarification.

The LME's view is that the point at which all elements of the trade are finally determined is the most appropriate 'time of trade'. However, for audit trail purposes, it is recommended that all relevant details, including the execution time of the originating trade, are available if requested by the client, the LME compliance department or the FSA.

This process could lead to instances where an originating trade is executed outside of the LME floor sessions (i.e. a 'timed' trade) but the trade is then date and/or price adjusted basis a floor session. This would result in the final trade being eligible for an appropriate timing short code ('C' or 'D') for the purposes of entry in to the LMEMS.

Conversely, a trade transacted during a floor session but then price and/or date adjusted outside of the relevant floor session should be recorded as a 'timed' trade.

It is also possible for a trade to originate during a floor session and then be adjusted during a later floor session. In this case, the latter session



code should be used as time of trade. Similarly, a 'timed' trade could be adjusted outside of market sessions. Here, the latter execution time should be used as the effective time of trade.

For client trades executed during a ring session and then converted in to an LME accepted currency, provided that the FX conversion is transacted during the session, then the appropriate timing code ('C' or 'D') may be used for trade time recording. In instances where the client requests that the metal trade be converted to another LME accepted currency either:

at a later point during the same trading day either based upon the publication of an official FX conversion rate or at a given point in time

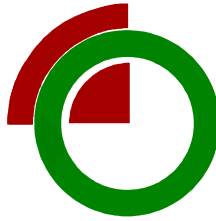
OR

at a specified FX conversion rate away from current FX market levels

then the trade must be recorded as a 'timed' trade using the time of the FX conversion, whether or not the appropriate market session is in progress at the time of the FX conversion.

This guidance applies to LME Exchange and Client Contracts, i.e. those eligible for matching or registration within the LMEMS.

Attention is drawn to board notice 98/212:A 206 which set out the timing requirements for registration of client trades. If an order to adjust a trade cannot be executed by the end of the original trade date, then the original trade details must be recorded in the LMEMS. In these circumstances the originating trade must be registered/matched using the original time of trade. If the adjustment is executed after the original trade date, members have the choice of either recording this as a correction to the original details (using the CR/CT mechanism) or, where appropriate, recording a carry trade to reflect the adjustment. For currency conversion trades post-trade date, members may use either the 'CX' trade type (when converting from one LME accepted currency to another) or the 'DE' trade type (when converting from an LME accepted currency into a non-accepted currency).



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 99/272 : A266
Date: 24 June 1999
Subject: **THE FUTURES BANDING REPORT AND WARRANT HOLDINGS, TOM AND CASH (WTC) REPORT**

The consultation period on the publication of the concentration of large futures positions closed on 14 April 1999. No significant issues were raised. The LME has now begun to publish information on concentration of large futures positions and dominant holdings of warrants, tom and cash (WTC) positions. The publication of this data forms an integral part of the LME's strategy to enhance market transparency.

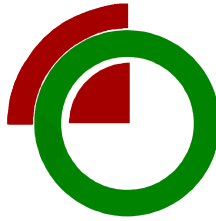
Examples of the WTC report and the futures banding report and detailed explanation of these reports can be found in the LME notice 99/075, A:075.

The LME will publish the reports two trade days in arrears at 10.30am on the 'Statistics' page at the LME's internet site (<http://www.lme.co.uk>) alongside the warrant banding reports which are currently published there.

Questions regarding the WTC and futures banding reports should be directed to the compliance department for the attention of Sarah Watts (telephone: 0171 264 5691, e-mail: sarah.watts@lme.co.uk) and Duncan Stewart (telephone: 0171 264 5693, e-mail: duncan.stewart@lme.co.uk) respectively.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 99/485 : A473 : R035
Date: 19 October 1999
Subject: **FINANCIAL RULES**

Introduction

Notice 99/315: A305 dated 21 July 1999 set out proposals for clarifying LME financial rules. The consultation has been completed and 2 written responses were received. Where appropriate substantive issues raised by the consultation have been reflected in the revised rules set out below. **These revised rules become effective from the date of this notice.**

The financial rules of the LME are set out in notice 94:436 and in Part 2 Membership Enforcement and Discipline of the LME rulebook. However, they do not address how to calculate net worth. The current practice has been to define net worth as shareholders equity. Normally, this does not include subordinated loans, as the LME rules are silent on this issue, although they have been allowed in exceptional circumstances.

While the SFA is the prudential regulator of LME members, the LME requires that all members of the Exchange are "Substantial" organisations. The levels of Net Worth Requirement set by the Board reflect this.

The LME ensures that members demonstrate their Net Worth Requirements by requiring the submission of annual financial statements.

It will be beneficial to members to have a standard and clear definition of net worth and a clear and consistent policy on the treatment of



subordinated loans. The proposals set out below would allow the use of subordinated loans to satisfy up to 50% of Net Worth Requirements. They follow the procedures adopted by the London Clearing House and thus will be familiar to members.

Rules

The following shall be added to Part 2 Membership, Enforcement and Discipline paragraph 1 of the LME rulebook.

The amount prescribed by the Board, from time to time, as the minimum Net Worth Requirement for each category of membership shall be met by permanent capital plus additional capital less disallowables.

- Permanent capital shall be issued and fully paid ordinary shares, issued and fully paid preference shares, share premium and other reserves not available for distribution. A deficit in reserves available for distribution will be deducted when calculating permanent capital.
- Additional capital shall be other equity reserves (distributable or otherwise) profit and loss reserves and subordinated loans.
- Disallowable items are intangible fixed assets such as goodwill, development costs etc, investments in subsidiaries and/or other group companies, shares in LCH and the value of exchange memberships.

Subordinated Loans

Subordinated loans will be accepted as satisfying in part LME Net Worth Requirements. Subordinated loans may not be used to meet more than 50% of a member's Net Worth Requirement. The LME requires prior notification of loans being repaid in order to be satisfied that the remaining capital is of a sufficient level to meet its Net Worth Requirements. Repayments without such notification accompanied by proposals, acceptable to the exchange, explaining how the Net Worth Requirements will be satisfied will be considered to be an act of misconduct.

Subordinated loans must be notified to the LME and be in a form that is acceptable to the LME. Subordinated loans executed by members that satisfy the SFA/FSA capital rules will satisfy the LME

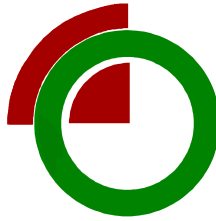


requirements. Such notification should be made to the regulation and compliance department of the LME.

Members are required to submit annual accounts to the Company Secretary of the LME in order to demonstrate compliance with the LME's Net Worth Requirements.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 99/486 : A474 : R036
Date: 19 October 1999
Subject: **REQUIREMENTS TO DISTINGUISH LME CLIENT
CONTRACTS FROM OTC CONTRACTS**

INTRODUCTION

Notice 99/262: A256 dated 22 June 1999 set out proposals for distinguishing LME client contracts from OTC contracts. The consultation has been completed and 3 written responses were received. Where appropriate substantive issues raised by the consultation have been reflected in the revised rules set out below.

Rule 2.2 of part 3, Trading Regulations, of the LME rules and regulations states that: -

All dealing by Members made subject to the Rules of the Exchange must be evidenced by an Exchange contract and/or Cross input into the Matching System and registered with the Clearing House.

This Rule is complemented by rule 1.6 of Part 4, Contract Regulations, which states that:-

A Member may not enter into a contract expressed to be “subject to the Rules and Regulations of the Exchange” or similar expression unless it is a Contract.

Rule 1.6 is designed to ensure that members’ clients can distinguish an LME Client Contract from an OTC “lookalike”.



Market Aberrations: The Way Forward, issued in October 1998, discussed the Exchange's concern that LME client contracts and OTC "lookalikes" were still not being clearly identified. That document stated that the LME rules would be amended to require members to state clearly and boldly on their LME client contracts "THIS IS AN LME REGISTERED CLIENT CONTRACT" and to state clearly and boldly on their OTC contracts "THIS IS NOT AN LME REGISTERED CLIENT CONTRACT".

RULE AMENDMENT

Rule 1.6 of part 4, Trading Regulations, of the LME rules and regulations is amended as follows:

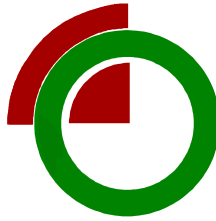
A Member may not enter into a contract expressed to be "subject to the Rules and Regulations of the Exchange" or similar expression unless it is a Contract. Written confirmation of a Client Contract must state clearly and in bold capitals the phrase "**THIS IS AN LME REGISTERED CLIENT CONTRACT**". Written confirmation of an over-the-counter contract in respect of LME-deliverable metal must state clearly and in bold capitals "**THIS IS NOT AN LME REGISTERED CLIENT CONTRACT**".

Once members are in compliance with the revised rule 1.6 of part 4, they may incorporate into their OTC contracts the same criteria and terms and conditions, where appropriate, as LME registered contracts.

The LME recognises that the issues surrounding year 2000 may mean that members are unable to introduce the necessary changes to their computer systems to meet the requirements of this notice. **The revised rule 1.6 of part 4 of the LME rules will not become effective until 31 March 2000. Members are encouraged to comply with this notice at an earlier date if possible.**

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----*From Executive Director: Regulation and Compliance*

To: ALL MEMBERS

Ref: 99/484 : A472 : R034

Date: 19 October 1999

Subject: **RULES ON HISTORIC/ORIGINAL PRICE CARRIES**

Introduction

Notice 99/260 : A254 dated 22 June 1999 set out proposals for revising notice 97:296 Non Market Price Transactions. The consultation has been completed and 4 written responses were received. Where appropriate substantive issues raised by the consultation have been reflected in the revised rules set out below.

These rules become effective from the date of this notice and replace those contained in notice 97:296 Non Market Price Transactions. It forms part of a series of proposed rule changes necessary to implement the Board's policy on registration of client contracts set out in Market Aberrations: The Way Forward.

A Historic (or Original) Price Carry (HPC) is where an existing, customer's on-exchange position, is date adjusted, to another valid LME date, based upon current market spread rates on the basis of the original contract price of the position. Both the original contract price and the adjusted price should be in the same currency. If the customer requires a currency conversion this should be conducted either before or after the roll in accordance with LME rules

Other transactions that appear not to be at current market price may include "Average Price Trades", "Strips" and OTC contracts brought on exchange at historic prices. Where the price of these transactions can be demonstrated by the member to be a derivation of the current market price(s) at the time of the transaction(s), such transaction(s) will not be



subject to this rule. Such transactions should be dealt with in accordance with the appropriate LME rules contained in notice 99/325:A314: R026.

Prior to transacting HPCs members must:

- 1 Obtain from their customers:
 - a a copy of a resolution passed by the board of directors (or equivalent body) of the customer authorising the use of HPCs; and
 - b either stating that it will review the HPCs undertaken by that customer, or authorising a person such as the chief executive officer or chief financial officer or properly constituted control function, who is (are) held out to be independent of the trading operation who will review that customer's HPCs. Members must be able to demonstrate why they believed that such authorised person was of sufficient standing and authority to act in this role: and
 - c naming such persons in the employ of the customer who are permitted to conduct such transactions;
- 2 Obtain authorisation, by resolution of the member's board (or similar body) that the member may conduct HPCs with each named customer. It should also state that the board will review the HPCs undertaken by that member, or identify a suitable person or persons, such as a chief executive, chief financial officer or a properly constituted control function such as risk management, compliance or finance department, who is (are) not directly involved in trading who will review the HPCs. If the member's authority to conduct HPCs is not provided by their board, an 'appropriate body' will suffice. Members must be able to demonstrate why they consider such a body to be appropriate and that it has sufficient standing and knowledge to evaluate the risks involved in these transactions.
- 3 Issue to any customer with whom they undertake HPCs a risk disclosure statement in respect thereof as detailed in board notice 97:321

After the transaction the member must:

- 4 Send to the person(s) identified in 1(b) above, on a timely basis, fax/telex/electronic confirmations and contract confirmation notes



identifying as HPCs all contracts which are such, on a deal-by-deal basis.

Additional Requirements

- 5 Obtain renewal of the customer authorisations set out in 1(a), (b) and (c) in writing at least every 12 months from that customer's board of directors (or equivalent body).
- 6 Obtain renewal of its authorisations set out in 2 at least every 12 months by the member's board of directors (or appropriate body).
- 7 At all times maintain adequate records and documentation to be able to demonstrate to the Exchange that they are complying with this notice.
- 8 Members are reminded of their obligations under LME rules, the Financial Services Act, FSA's Guidance 'Proper Trades in Relation to On-Exchange Derivatives' and the Money Laundering Regulations.

GUIDANCE

Equivalent Body

In the exceptional circumstances where the corporate structure of a customer may be such as to make it inappropriate for the board of directors to pass the resolutions, a general manager or an executive or management committee who/which is not directly responsible for the relevant trading operation and whom the member reasonably believes to have the necessary authority will satisfy the requirement for an equivalent body to the board of directors. The member will need to be able to demonstrate to the Exchange its reasons for accepting this alternative and what steps it took to determine that the person or committee had such necessary authority.

Independent person

The customer's board resolution should identify an individual/control function who will review its HPCs and is independent of the trading function. Members should conduct and document appropriate due diligence to ensure that this person is independent, such tests include:

- Identifying the individual's role in the organisation



- Considering if the individuals/control function is appropriate to perform the function of independent person as described above.
- Ensuring that the individual/control function is independent of the trading function.

Due diligence should be appropriate to the circumstances and will depend on the organisation being reviewed, the members knowledge of that organisation and the extent and volume of trading being undertaken.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS

Ref: 98/447, A:434

Date: 15 December 1998

Subject: **DISCLOSURE OF INFORMATION ON CONCENTRATION OF WARRANT HOLDINGS**

Introduction

Section 9 of the LME Board's paper "Market Aberrations – The Way Forward", circulated to members under cover of Board notice 98/363, A:351, W:072 of 13 October 1998 announced the Board's intention to publish regular information on an anonymous basis on the holding of large positions of LME warrants.

2 The notice sets out the proposed details of the information and the format in which it is to be published. Concentration of warrant holdings will be published on the LME's website on the internet – www.lme.co.uk - very early in 1999 following this consultation period. The data will also be distributed on the LME's Market Data Services system when it commences operation in the summer of 1999. A further consultation paper on the publication of the concentration of futures position holdings will be published in the first quarter of 1999.

3 Comments on the details of the proposals set out in this notice should be sent to Mrs Joanna Stuart, Head of Market Surveillance, by 26 January 1999.

Identification of Holdings

4 The LME's compliance department receives daily reports of both members' proprietary warrant holdings and the warrant holdings of customer accounts. The identities of those customer accounts are disclosed, on a confidential basis, to the LME compliance department. For the purpose of identifying large warrant holdings, the LME will automatically aggregate a member's holding with those of companies in the same group. Equally, a client's warrant holdings held across more than one member will also be



aggregated automatically. These automatic aggregations will be based on grouping information supplied by member firms.

5 Where the LME compliance department believes that it is appropriate and meaningful, it will also aggregate warrant holdings which are not subject to automatic aggregate described in paragraph 4 above. For example, a member's proprietary holding will be aggregated with those of one or more of its customers if the LME compliance department believes that there is a common purpose in, or a common effect produced by, those holdings. In all such cases, LME compliance will inform the member affected.

Content and Format of the Published Information

6 The information will be published daily, two days after the date on which the published holdings were held. The two day delay is currently required to allow members to report their holdings and the LME to aggregate and check the data. Daily publication will show the build up of large positions.

7 The proposed format of the large warrant holdings information (using a hypothetical example) is set out in the following table:

Large LME Warrant Holdings held on x.x.1999

Warrant holdings/total stocks	Tin	Alloy	Aluminium	Copper	Zinc	Nickel	Lead
30 - <40%	1	2	0	0	0	1	0
40 - <50%	1	0	0	1	0	0	0
50 - <80%	0	0	0	0	0	0	1
80 - <90%	0	0	0	0	1	0	0
90-100%	0	0	1	0	0	0	0
Unreported Warrants(%)	2.43	8.17	5.14	1.18	12.75	25.84	3.48

Footnotes:

- i The figures show LME warrant holdings two business days ago. The positions indicated in this table may no longer be held.
- ii Unreported warrants occur, for example, when warrants are held directly by non-members.
- iii The large positions indicated can be held by individual members, individual clients, linked group companies or can be the combined holding of members and/or clients where the LME compliance department believes there is a common purpose in, or a common effect produced by, those holdings.

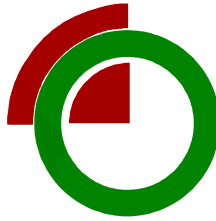


- iv Large warrant holdings will include any qualifying holding held under a financing arrangement.
- v The information contained in this table relates only to LME warrants. It does not include holdings of off-warrant stocks.
- vi This information needs to be interpreted carefully. There should be no automatic presumption that dominant positions will invariably result in a tightness of the market. Equally, because of the possibility of covert collusion between apparently unconnected parties, lack of published dominant positions is not a guarantee that effective large positions do not exist.

8 The LME wishes to stress the importance to members of providing accurate and prompt information not only on their and their clients' warrant holdings but also on their account groupings.

A WHITING

cc: Board of Directors



LONDON METAL EXCHANGE

-----*From Executive Director: Regulation and Compliance*

To: ALL MEMBERS
Ref: 00/383 : A376 : R010
Date: 15 September 2000
Subject: **RULES FOR LME GIVE-UP AGREEMENTS**

The LME board has approved the reissue of its rules on give-ups in order to reflect recent changes in other areas of LME rules. This notice replaces notices 95:365, 96:158, 97:304 and 99/091:A091 which are withdrawn.

For the purposes of this notice “member” means a ring dealing, associate broker clearing or an associate broker member of the LME.

Give-ups

These rules set out the procedures to be used by members who wish to be a party to a give-up trade. The notice also sets out certain of the legal and regulatory responsibilities that such members take on when they transact give-up business.

For the purposes of these rules, a give-up is a new transaction which arises when an executing LME member (‘LME executor’) trades with a third-party entity (‘customer’) who then wants that trade ‘given-up’ to a clearing LME member (‘LME clearer’) for the purposes of open position maintenance and settlement. Give-up trades may only be conducted at certain price references which are indicated later in this document. The give-up trade is the transaction matched in the LME matching system (‘LMEMS’) between the LME executor and the LME clearer in order to allow the movement of the customer trade. Please note that other entities may be party to the agreement but the above is the minimum.



Requirements

Members conducting a give-up trade must comply with the following requirements:

Written agreements

Prior to conducting a give-up trade, members must:

- i have in place a written agreement with the customer, which includes details of the arrangements between the LME clearer and LME executor for dealing with events and consequences of default;
- ii have in place a written agreement with the LME clearer/LME executor confirming the name of the customer (or code see below), the conditions under which give-ups will be accepted and the conditions under which give-ups will be refused;
- iii ensure that the 'effective date' of the agreement (the date on which the give-up agreement is fully completed) is recorded either on the agreement or in the LME members' own records. Members should be able to demonstrate, if required, that a completed give-up agreement was in place prior to trading;
- iv ensure that any material amendments to the terms of completed agreements are countersigned by all the parties to the original give-up agreement, or are set out in a novation letter indicating the changes and the agreements covered. Alternatively, material changes can be dealt with simply by cancelling and re-issuing the agreement. Material changes include a change of name to any of the parties, the addition of an introducing broker (see notice 00/385:A378:R012), or the addition of a new customer;
- v have received confirmation from the LME clearer that it has a written agreement with the customer and that it has carried out all appropriate regulatory and legal procedures;
- vi have received confirmation from the LME executor that it has a written agreement with the customer.



Contents of written agreements

The written agreements referred to above may be in the form of a tripartite give-up agreement. The uniform give-up agreement ('UGA') is recommended for this purpose but is not compulsory. A completed UGA should be sufficient to comply with the requirements of this notice. Please see the attached example. Whichever document is chosen, the give-up agreement must:

- vii contain details of all the parties involved in the transaction. This includes, but is not limited to, the LME executor, the LME clearer, the third-party customer and any agents acting for the customer (commodity trading advisor, introducing broker, futures commission merchant etc);
- viii name either a ring dealing member, an associate broker clearing member or an associate broker member of the LME (ABM) as the LME executor and the LME clearer (subject to ix below);
- ix state the identity of the LME clearing member that will process the give-up transaction in the LMEMS on behalf of the ABM if either the LME executor or the party issuing the LME contract is an ABM;
- x be signed by all parties, including the LME member clearing for the ABM.

Miscellaneous requirements

- i an LME trade may only be transacted under a completed give-up agreement that complies with LME rules;
- ii the customer identity must be the same in the records of both the LME clearer and LME executor;
- iii in order to maintain customer confidentiality, members may use an identity code on give-up agreements. This code must allow the LME clearer, or if appropriate the ABM (if issuing the client contract), to identify a customer which **must be a fully disclosed principal** of the LME clearing member or ABM. However, in certain circumstances, a general code may be used for a group of customers but, again, the customers covered by the code, should be fully disclosed principals of the LME clearer or ABM (if issuing the client contract). If further customers are added to the general code the LME clearer or ABM must agree the addition(s) prior to the trade being effected;



- iv in the event that an introducing broker (IB) of the customer or either LME member, is acting under an LME give-up agreement, the IB must disclose a code or customer name to the LME executor that will be recognised by the LME clearer or, if appropriate, the ABM, as identifying a customer who is its fully disclosed principal. Where an IB is advising more than one customer, a general code may be used as long as it complies with iii above;
- v the LME clearer or ABM (if issuing the client contract) is responsible for the proper and timely allocation of trades given-up pursuant to the IB identity code or name.

Members are reminded that the give-up agreement should reflect the actual relationship of the parties to the agreement; ie customers should not be described as traders and vice versa.

Members are reminded that they must at all times be in compliance with LME rules, with the FSA principles, rules and guidance (including the guidance 'Proper Trades in Relation to On-Exchange Derivatives') and with other legal and regulatory obligations.

Recording of trades in the LME Matching and Clearing System ('LMEMS')

Give-up trades must comprise at least two entries to the LMEMS. The exchange contract must first be matched between the LME executor and the LME clearer to signify the 'movement' of the customer trade. The issuance of an LME client contract is then signified by the registration of the appropriate client contract(s) in the LMEMS by the LME clearer. If an ABM issues the client contracts, then they should be registered in the LMEMS by its LME clearing member. The registered client contract(s) should replicate any instructions received from either the customer or the appointed IB in terms of account allocation.

The trade types for the matching/registration of give-up trades within the LMEMS are contained within LME board notice 00/212: A206: R005.

Members must agree a coding to identify the customer, which may be different to any code used on the actual give-up agreement. This code must be input into the public reference field of the LMEMS in order for matching of the trade to take place. Members must be able to demonstrate how the code used in the public reference field relates to a specific give-up agreement if required to do so.

The time of trade to be used is set out in LME board notice 00/211: A205:R004.



Exchange contracts relating to give-up trades should be matched in the LMEMS no later than the original trade date plus two business days (see notice 00/211: A205: R004). Client contracts relating to give-up trades should also be registered within this time period by the LME clearer. In the event that an exchange trade remains unmatched beyond this point, both LME executor and LME clearer must seek authorisation from the LME Compliance Department **before** attempting to match the trade in the LMEMS. Both members must provide reasons why the trade has not matched and may be required to provide supporting documentary evidence. This process should be followed by the LME clearer for the late registration of client contracts. Examples of acceptable reasons for late matching include:

- i System failure resulting in the inability to match or process trades.
- ii Public holidays in different time zones that prevent instructions being transmitted in a timely manner. In this case the LME will determine whether the issue resulting from the holiday was predictable and as such, should have been accounted for when the transaction took place.
- iii Errors on specific trade details that could not be rectified within the time limits due to time zones. Again the particular circumstances will be evaluated.

Other reasons for trades failing to match within the prescribed time periods may be accepted. The LME will judge each case on its merits but it expects all parties to use best endeavours to comply with the timing requirements. **However, members should note that requests to match/register give-up trades outside the prescribed time periods will not be automatically granted. Repeated material failure to adhere to the prescribed periods could result in disciplinary action.**

Pricing of give-up trades

Give-up trades may be transacted at the following price references:

- i the current, prevailing market price;
- ii the average of the current, prevailing market price over a series of forward prompt dates either as a succession of outright trades ('strip') or as a carry trade;
- iii the final price of an average price contract ('APC').

In all the above examples members may, with the agreement of the customer, amalgamate similar trades to obtain the trade weighted average price of all the trades forming the amalgamation. In this event, the LME executor must



retain sufficient documentary evidence to achieve a full and complete audit trail of the trade(s).

In example (iii) above, the executor must be able to demonstrate how the final price was derived if requested to do so by the customer, the LME, or the FSA.

Single give-up agreements

In the exceptional circumstance where members do not envisage a continuing relationship with a customer, the single trade give-up agreement ('STGA') may be utilised. In this instance, 'single' relates to the isolated use of a give-up agreement and not the number of trades transacted thereunder. Any number of trades may be included as part of the STGA as long as all are transacted/priced on the same trade date. In addition to all the requirements of a give-up agreement, the STGA must also provide full details of the trade(s) covered by the agreement. A copy of the STGA must be retained by both the LME executor and LME clearer to demonstrate that they have complied with these rules.

STGAs may be used more than once with a particular customer but if a pattern develops that indicates an ongoing relationship with that customer the LME will expect the members to replace the STGA with an agreement such as a UGA. Members should use their own judgement to determine what constitutes an ongoing relationship. Factors to be taken into account include the frequency of trading and the continuing nature of the relationship.

The LME does not prescribe the form of STGAs but the attached document is an example that would comply with these rules.

Give-up of off-exchange contracts brought on-exchange

The LME rules on the bringing on-exchange of off-exchange positions and subsequent movement of customer positions among members are covered by board notice 99/587.

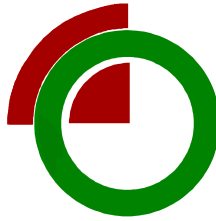
EFFECTIVE DATE

These rules become effective from the date of this notice.

A WHITING

cc: Board directors





LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 00/384 : A377 : R011
Date: 15 September 2000
Subject: **RULES ON EXCHANGE FOR PHYSICALS**

INTRODUCTION

An exchange for physical (EFP) arises when **two** customers offset their futures positions and effect the attendant physical deliveries. The EFP may involve one or two members, on-exchange hedges, or the creation of a new LME contract(s).

The LME has identified two scenarios where members and their customers may effect this type of transaction.

- 1 Where customers swap on-exchange hedges and attendant physical commitments. This is a metal position swap and the relevant LME rules should be followed.
- 2 Where a new LME client contract is created to reflect an underlying swap of customer's physical commitments.

The current rules for EFPs are contained in notice 99/587. OTC future contracts that are converted into LME contracts are not covered by this additional rule; members should refer to notice 99/587.

In all cases involving the swap of customer's physical commitments, the following procedures should be followed.

1 On-Exchange hedge

If the EFP involves on-exchange positions, ie both customers have on-exchange hedges, the EFP will be regarded as a metal position swap and the requirements of notice 00/382:A375:R009 RULES ON THE MOVEMENT OF LME POSITIONS will apply. This transaction may involve one or two members.



2 New hedge

a Single member

If a member wishes to register an EFP which results in the creation of a new LME contract, based on its customer's physical commitments, this contract should be registered at either the prevailing market price, or the price of its customer's physical contract(s). These prices may be adjusted to reflect any premiums or discounts that are part of the EFP or reflect adjustments relating to transaction costs:

Prevailing market price – no adjustments

If the contract does not reflect the adjustments referred to above then it may be registered in the normal manner, subject to the relevant LME rules.

Prevailing market price – with adjustments

If the contract is at prevailing market price but subject to one or more of the adjustments referred to above, the member must submit a fax copy of the agreement, signed by all parties (see appendix 1) to the LME regulation and compliance department setting out details of the transaction and the parties involved before its entry in the LMEMS. This must include the customers' agreement to provide all relevant documentation to support the transaction (if requested by the LME).

The LME regulation and compliance department will contact the member within two hours of the fax being sent by the member to ask for further supporting documentation or approve/reject the registration of the contract.

Physical contract price – with or without adjustments

If the contract is at the physical contract price, then the member must submit a fax copy of the agreement, signed by all parties (see appendix 1) to the LME regulation and compliance department setting out details of the transaction and the parties involved before its entry in the LMEMS. This must include the customers' agreement to provide all relevant documentation to support the transaction (if requested by the LME).

The LME regulation and compliance department will contact the member within two hours of the fax being sent by the member to ask for further supporting documentation or approve/reject the registration of the contract.

General: all pricing mechanisms

There must be **two** customers involved in each transaction, both of which must be commercial users of metal. A commercial user is defined as a company, other than a member, that has a requirement for the use of physical metal and is not a broker of futures and/or options.



The price of the LME contract registered should reflect the commercial reality of the transaction and be capable of such demonstration if requested by the LME, FSA, or other regulatory body. These transactions should be conducted in accordance with the requirements of notice 99/587:A567:R041 RULES ON BRINGING OTC CONTRACTS ON-EXCHANGE AND TAKING ON-EXCHANGE CONTRACTS OFF EXCHANGE. The trade type 'DE' should be used to register the trade. The LME will view EFPs which require the creation of a new contract based on customer' physical commitments as falling within these rules. If the contract(s) is subsequently moved to another member this must be in accordance with the requirements of notice 00/382:A375:R009 RULES ON THE MOVEMENT OF LME POSITIONS.

b Two members

If two members have customers that wish to effect an EFP which results in the creation of a new LME contract(s), based on the customer's physical commitments, they should register/match these contract(s) at either the prevailing market price, or the price of the customer's physical contract(s). These prices may be adjusted to reflect any premiums or discounts that are part of the EFP or reflect adjustments relating to transaction costs:

Prevailing market price – no adjustments

If the contract does not reflect the adjustments referred to above then it may be registered in the normal manner, subject to the relevant LME rules.

Prevailing market price – with adjustments

If the contract is at prevailing market price but subject to one or more of the adjustments referred to above, then both members must submit a fax copy of the agreement, signed by all parties (see appendix 2) to the LME regulation and compliance department setting out details of the transaction and the parties involved before its entry in the LMEMS. This must include the customers' agreement to provide all relevant documentation to support the transaction (if requested by the LME).

The LME regulation and compliance department will contact the members within two hours of the fax being sent by the members to ask for further supporting documentation or approve/reject the registration of the contract.

Physical contract price – with or without adjustments

If the contract is at the physical contract price, then both members must submit a fax copy of the agreement, signed by all parties (see appendix 2) to the LME regulation and compliance department setting out details of the transaction and the parties involved before its entry in the LMEMS. This must include the customers' agreement to provide all relevant documentation to support the transaction (if requested by the LME).



The LME regulation and compliance department will contact the members within two hours of the fax being sent by the members to ask for further supporting documentation or approve/reject the registration of the contract.

General: all pricing mechanisms

There must be two customers involved in each transaction, both of which must be commercial users of metal. A commercial user is defined as a company, other than a member, that has a requirement for the use of physical metal and is not a broker of futures and/or options.

The price of the LME contract registered should reflect the commercial reality of the transaction and be capable of such demonstration if requested by the LME, FSA, or other regulatory body. These transactions should be conducted in accordance with the requirements of notice 99/587:A567:R041 RULES ON BRINGING OTC CONTRACTS ON-EXCHANGE AND TAKING ON-EXCHANGE CONTRACTS OFF EXCHANGE. The LME will view EFPs that require the creation of a new contract based on customer's physical commitment as falling within these rules. The subsequent movement of these positions between members should be in accordance with notice 00/311:A304 RULES ON THE MOVEMENT OF LME POSITIONS.

c Documentation for all transactions

In all cases, EFPs subject to these rules, must be documented on either Appendix 1 or 2. The LME may subsequently ask to review this document and supporting information, which will include that relating to the customer's physical commitments.

The transaction must comply with FSA principles and guidance. It must be for a commercial purpose and not be carried out in order to avoid or evade other LME rules.

EFFECTIVE DATE

These rules become effective from the date of this notice.

A WHITING

cc: Board directors



Appendix 1

EXCHANGE FOR PHYSICAL TRANSACTION

BROKER

[INSERT NAME]

CUSTOMER A

[INSERT NAME]

CUSTOMER B

[INSERT NAME]

TRADE DETAILS

METAL

[If this does not comply with LME specifications, please provide sufficient detail to explain the effect on the price of the transaction]

NUMBER OF LOTS

DELIVERY POINT

[If this does not comply with LME specifications, please provide sufficient detail to explain the effect on the price of the transaction]

PROMPT

PRICE OF EFP PER TONNE

[Please specify if market price or contract price of physical contract]

DISCOUNT OR PREMIUMS IF INCLUDED IN EFP PRICE PER TONNE

[Please provide a full explanation and all details behind the discount or premium included]



BROKER'S STATEMENT

We confirm that [Customers A and B] are direct customers of ours, are believed to be commercial users of the metal concerned and have given us written instructions regarding the above Exchange For Physical transaction. We understand that a full audit trail to the above transaction must be maintained and that the LME may request any supporting documentation for review. We confirm that the EFP relates to an **OTC contract brought on-exchange/physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.

CUSTOMER A's STATEMENT

We confirm that we are a commercial user of the metal concerned and have given written instructions to [Broker A] regarding the above Exchange For Physical transaction. We understand that a full audit trail of the above transaction must be maintained and that the LME may request any supporting documentation for review. This may include any documents relating to my physical commitments that form part of this transaction. We confirm that the EFP relates to an **OTC contract brought on-exchange/physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.

CUSTOMER B's STATEMENT

We confirm that we are a commercial user of the metal concerned and have given written instructions to [Broker B] regarding the above Exchange For Physical transaction. We understand that a full audit trail of the above transaction must be maintained and that the LME may request any supporting documentation for review. This may include any documents relating to my physical commitments that form part of this transaction. We confirm that the EFP relates to an **OTC contract brought on-exchange/an physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.

BROKER
[NAME]

CUSTOMER A
[NAME]

CUSTOMER B
[NAME]

[Signature of authorised
representative]

[Signature of authorised
representative]

[Signature of authorised
representative]



Appendix 2

EXCHANGE FOR PHYSICAL TRANSACTION

BROKER A
[INSERT NAME]

BROKER B
[INSERT NAME]

CUSTOMER A
[INSERT NAME]

CUSTOMER B
[INSERT NAME]

TRADE DETAILS

METAL
[If this does not comply with LME specifications, please provide full details]

NUMBER OF LOTS

DELIVERY POINT
[If this does not comply with LME specifications, please provide full details]

PROMPT

PRICE OF EFP PER TONNE
[Please specify if market price or contract price of physical contract]

DISCOUNT OR PREMIUMS IF INCLUDED IN EFP PRICE PER TONNE

[Please provide a full explanation and all details behind the discount or premium included]



BROKER A's STATEMENT

*We confirm that [Customer A] is a direct customer of ours, is believed to be a commercial user of the metal concerned and has given us written instructions regarding the above Exchange For Physical transaction. We understand that a full audit trail to the above transaction must be maintained and that the LME may request any supporting documentation for review. We confirm that the EFP relates to an **OTC contract brought on-exchange/physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.*

CUSTOMER A's STATEMENT

*We confirm that we are a commercial user of the metal concerned and have given written instructions to [Broker A] regarding the above Exchange For Physical transaction. We understand that a full audit trail of the above transaction must be maintained and that the LME may request any supporting documentation for review. This may include any documents relating to my physical commitments that form part of this transaction. We confirm that the EFP relates to an **OTC contract brought on-exchange/physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.*

*BROKER A
[NAME]*

*CUSTOMER A
[NAME]*

[Signature of authorised representative]

[Signature of authorised representative]



BROKER B's STATEMENT

*We confirm that [Customer B] is a direct customer of ours, is believed to be a commercial user of the metal concerned and has given us written instructions regarding the above Exchange For Physical transaction. We understand that a full audit trail to the above transaction must be maintained and that the LME may request any supporting documentation for review. We confirm that the EFP relates to an **OTC contract brought on-exchange/physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.*

CUSTOMER B's STATEMENT

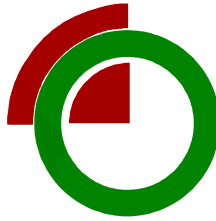
*We confirm that we are a commercial user of the metal concerned and have given written instructions to [Broker B] regarding the above Exchange For Physical transaction. We understand that a full audit trail of the above transaction must be maintained and that the LME may request any supporting documentation for review. This may include any documents relating to my physical commitments that form part of this transaction. We confirm that the EFP relates to an **OTC contract brought on-exchange/an physical contract (delete as appropriate)**. We confirm that we believe that this transaction is in accordance with LME Rules and Regulations or other appropriate legal obligations.*

*BROKER B
[NAME]*

*CUSTOMER B
[NAME]*

[Signature of authorised representative]

[Signature of authorised representative]



LONDON METAL EXCHANGE

-----From Executive Director: Regulation
and Compliance

To: ALL MEMBERS
Ref: 00/385 : A378 : R012
Date: 15 September 2000
Subject: **RULES ON INTRODUCING BROKERS**

The LME board has approved the reissue of its rules on introducing brokers (IBs) in order to reflect recent changes in other areas of LME rules. This notice replaces notice 96:158 which has been withdrawn.

For the purposes of this notice “member” means a ring dealing, associate broker clearing or an associate broker member of the LME. These rules in respect of IBs apply to all existing as well as new customer/IB relationships.

Definition of an IB

An IB is defined, for LME purposes, as:

- i a person who introduces a prospective counterparty to a member (with a view to the counterparty and the member transacting together on a principal to principal basis); or
- ii a person who acts as agent for a counterparty and enters into transactions on behalf of the counterparty with LME members; or
- iii a person who acts as agent for an LME member and enters into transactions on behalf of the member with counterparties.

Whether the IB acts as an agent for counterparty or for a member, the ensuing transaction results in a principal to principal relationship between the counterparty and the member.

When an IB acts as agent for a customer, then the customer is the principal and for disclosure purposes must be named, except in a give-up situation when the customer disclosure requirements for give-ups will apply.

An IB may be an affiliate of a member.

Member's obligations when dealing with IBs

- i When an IB conducts business with a member, that member shall maintain records which will identify the IB and the extent of its activities/authority on behalf of the member or customer. When an IB places an order, seeks an LME quote/price from a member or transacts LME business, it must disclose the identity of its principal (see also rules on give-ups). Members are reminded that they are responsible for ensuring compliance with the LME's trade input rules in respect of LME business transacted with or through IBs and of the strict principal to principal nature of LME contracts.
- ii When a member executes a trade, it is a principal to the identified client. Any subsequent give-up to a clearing member is conducted on a similar basis.
- iii Members are reminded of their obligations for time recording orders, fills etc. and of the requirement to retain records (including evidence of relevant contractual relationships) sufficient to evidence compliance with both the LME's rules (which incorporate the FSA Guidance 'Proper Trades in Relation to On-Exchange Derivatives') the SFA's rules and the money laundering regulations and other legal/regulatory obligations.

In particular, where a person acts or has acted as an IB but in a particular case it (or any of its group undertakings or affiliates) transacts LME metals business as principal with a member, that member shall ensure that there is a demonstrably transparent audit trail in respect of compliance with all relevant regulations. In the event that a member trades in this manner, it should be fully aware of the potential regulatory and commercial risks and take steps to avoid such risks and document these matters.

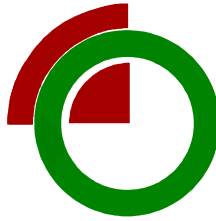
Members are reminded that they are responsible for the actions of each of their IBs when the IB is acting as the member's agent. Members must therefore ensure that IBs acting as their agent do not act in a way that would result in the member breaching the LME rules and regulations.

EFFECTIVE DATE

These rules become effective from the date of this notice.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: RING DEALING MEMBERS AND
ASSOCIATE BROKER CLEARING MEMBERS

Ref: 00/418 : A410

Date: 20 October 2000

Subject: **REGISTRATION OF CLIENT CROSSES**

As you are aware, the LCH and the LME have been working together to modify the London Metal Exchange Matching & Clearing System (LMEMCS) to allow for the processing of a new sub-account for non-segregated client business. These changes are being tested extensively by LCH, LME and those members that participate in the member testing during the period 9 to 20 October 2000.

Pending a successful sign-off at the end of the user acceptance testing phase, the changes to LMEMCS will go live on Monday 30 October 2000. From this date, all non-segregated client crosses must be input using the 'N' sub-account code on the side of the trade (buying or selling) that the client takes. The house side of this trade should be input using the 'H' sub-account code as before. Segregated crosses should be input using 'C' and 'H' sub-account codes as before.

Members should note that the new sub-account will result in a change to notice 00/212: A206: R005 "Rules for the use of trade types for the LME matching and clearing system". With the implementation of the new sub-account, the LME will be able to identify the direction of client crosses in members' house accounts (H and N accounts). Therefore section 13 correction trades will be amended to require the correction of the direction of a cross ie a buy changed to sell or vice versa. This type of correction should be conducted using the 'CR/CT' mechanism (both 'normal' and proxy crosses). Movements from segregated client account to non-segregated client accounts should be registered using the 'SA' trade type. Movements from segregated to non-segregated account using proxy crosses should continue to use the 'PS/PN' trade types.



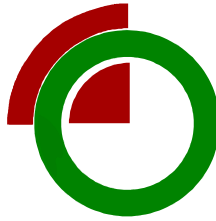
It should be noted that the changes have been limited to the LME matching system only; no changes have been made to the LME clearing system. For clarification, position maintenance, option declaration, deliveries, settlements and initial and variation margin will be maintained as either house (H) or segregated client (C) account level, as at present.

As a result of this implementation a new report has been created, 'End of Day Matched Trades (Non-Seg)', which details all matched trades designated to the non-segregated account.

If members have any queries on the implementation of the non-segregated account, they should direct them to Duncan Stewart (telephone: 0207 264 5693, e-mail: duncan.stewart@lme.co.uk). Queries on the use of trade types should be directed to Julie Russell (telephone: 0207 264 5699, e-mail: julie.russell@lme.co.uk).

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 01/122 : A122
Date: 23 March 2001
Subject: **CONCENTRATION OF WARRANT HOLDINGS**

Introduction

Market Aberrations: The Way Forward was published by the Exchange in October 1998. Section 13 of the document dealt with the Exchange's policy regarding dominant positions. In particular, paragraph 13.24 set out specific Exchange guidance covering lending obligations applying to dominant position holders. The lending obligations result once a person's aggregated warrant holdings, cash today and cash positions exceed certain proportions of total LME stocks. The guidance is aimed at preventing abuse of dominant positions, not at preventing dominant positions themselves.

2 Section 9 of the Market Aberrations document considered the publishing of information on concentration of large positions and warrant holdings. It also discussed the reasons why either positions or warrant holdings across brokers and/or clients might need to be aggregated.

3 In particular, paragraphs 9.5 and 9.6 dealt with types of connected holdings where the LME would aggregate positions. Such connected holdings could include warrant-financing arrangements. Paragraph 9.5 observed that warrant-financing can encompass a wide variety of both arrangements and objectives: under some financing arrangements, the relevant warrants are available to be lent by the party holding the warrants, but under other arrangements, the warrants in practice are not readily available to the market.

4 The LME has recently become aware that new forms of warrant-financing type arrangements have been developed which have the effect of restricting the availability of the relevant warrants to the market.



These arrangements create a connection between the warrants being held by one person under the warrant-financing type arrangement and other warrant holdings of the other party to the warrant-financing type arrangement.

5 This notice deals with the treatment of connected warrant holdings, particularly in relation to financing arrangements, and how these affect the lending obligations of dominant position holders under the market aberrations guidance. It gives additional detail on how the LME will determine whether warrant holdings are connected and hence the basis on which the LME will aggregate holdings both for the publication of large positions and for the lending obligations guidance.

6 The LME's purpose in aggregating connected warrant holdings is to reflect the effect on the market that these holdings may have. It is not, in any way, to discourage commercial arrangements for the financing of warrants.

Effective Control

7 The main principle which will guide the LME in determining whether warrant holdings are connected, is which party effectively controls the availability of those warrants to the market. If effective control of the warrants is with a party other than the party holding the warrants, the LME will aggregate those warrants with all other holdings of the party in control of the warrants in questions.

8 There are a number of ways in which a person can achieve effective control of warrants held by another. The LME's concern is not so much with the mechanism but with the result. The relevant characteristics are:

- a the holder of warrants has an obligation such that he will retain the warrants while the obligation is outstanding;
- b the person to whom the holder of the warrants owes the obligation is aware that the warrants are being held against the obligation; and
- c the person to whom the obligation is owed has effective control over whether those warrants can become available to the market.

9 One mechanism which would have this result is where a person sells warrants to another while at the same time buying from him an



American-style call option over warrants for the same metal, at the same location and of the same brand. The surrounding circumstances of such an arrangement can confirm that both parties expect that exercising the option will result in the same warrants being returned to the person exercising it. While the option is in force, the buyer of it has effective control of the warrants held by the seller of the option and those warrants are not freely available to the market.

10 Another mechanism which would have the same result is where the buyer of an American-style call option knows that the seller of the option is holding warrants against the option and will continue to do so during the exercise period of the option. Again, the surrounding circumstances of such an arrangement can confirm that both parties expect the warrants, or that number of warrants, to remain unavailable to the market during the exercise period of the option. Where the circumstances demonstrate that that is the understanding of the parties to the arrangement, the LME will, in the absence of special circumstances, aggregate the affected warrant holding with the other holdings of the buyer of the option. These particular mechanisms may not be the only ones that have the effect of giving control of warrants to persons other than the holder. The LME will continue to monitor its markets carefully and to aggregate warrant holdings for reporting purposes and the market aberrations guidance where appropriate.

11 Where the LME believes that a person's degree of control is sufficient to require the controlled warrants to be aggregated with any other warrants held by or to his order, the LME will notify that person. This is in line with the LME's policy to inform the member of all non-automatic aggregations (see Notice 99/075 : A075). The result of such notification will be that the total number of warrants will be counted towards that person's warrant holdings, cash today and cash positions, for the purposes of the lending guidance set out in paragraph 13.24 of the Market Aberrations document.

Warrant Reporting

12 LME Notice 99/520 : A505 : R40, issued on 11 November 1999, deals with large position reporting of warrants. The purpose of that notice was to ensure that reporting of warrant holdings was accurate and in particular that reporting avoided double counting of warrants; in particular that the warrants held under financing deals were not reported twice. This notice does not alter the provisions of Notice 99/520. Members holding warrants held under a financing arrangement should continue to report those warrants. In addition, however, warrants which are held against an obligation having the characteristics set out in

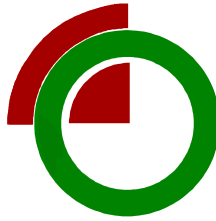


paragraph 8 above, should be separately identified as such, together with the identity of the party to whom the obligation is owed. This will prevent the lending obligations being incorrectly placed on the holder of the warrants and allow the LME to aggregate holdings properly.

13 The LME also requires members to inform the LME compliance department of arrangements to which they are parties where either they or their counterparties/customers do not hold but have effective control over warrants. Such notification should be at the start of such an arrangement and should indicate for how long the arrangement is expected to last. The member should also notify the LME when the arrangement ends. Members with effective control over warrants should not report such warrants in their daily warrant position reports. Daily reporting continues to fall to the member holding the warrants. This notice clarifies the obligation of members to disclose connected holdings, which was set out in paragraph 9.6 of the Market Aberrations document.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS

Ref: 01/232 : A232 : R07

Date: 21 May 2001

Subject: **RULES ON THE MOVEMENT OF LME POSITIONS**

1 INTRODUCTION

- 1.1 Following the end of the recent consultation, the LME board has approved the reissue of its rules on the movement of LME positions. The rules have been revised in order to reflect the results of the consultation.
- 1.2 The new rules include the ability to effect certain customer transactions via the clearing switch mechanism. In addition, the rules relating to bringing OTC contracts on-exchange and taking LME Contracts off exchange have been incorporated into this notice and adjusted to provide the ability to bring contract on-exchange via one member and take them off exchange via another.
- 1.3 This notice replaces notices 00/382: A375: R009 and 99/587: A567: R041 which are withdrawn
- 1.4 For the purposes of this notice "member" means a ring dealing, associate broker clearing or an associate broker member.

2 TRANSFERS

- 2.1 A transfer takes place when a customer with **an existing LME position** wishes to move that from one member ("the first member") to another member. Before a customer can transfer his position, he must have one or more LME registered client contracts which have been recorded as such both in the LME



matching system and in the first member's trading and financial records. In addition, the relevant LME registered client contracts must have been entered into the LME matching system no later than the business day before the transfer takes place. Positions maintained in segregated accounts must be moved into the member's house account before transfer.

2.2 The member receiving the position must keep the contract on-exchange until at least the business day following receipt of the transfer. A client cross should not be registered unless the contract is for a segregated customer of the receiving member. If the purpose of the transfer is to offset a customer's OTC exposure then the procedure detailed in 4 below should be followed.

2.3 The transfer can be made either at:

- a the prevailing market price at the time all parties agree to the transfer; or
- b the actual original contract price of the individual trades making up the position being transferred for each prompt date; or
- c an amalgamation of similar positions to obtain the position weighted average price (based upon the original contract price) of all the positions forming the amalgamation.

Transfers cannot be undertaken using any other pricing basis

2.4 Disclosure of the customer name, or a code, which has been agreed by both the members as representing that customer name, must be made in the public trade reference field in the LME matching system.

2.5 Transfers should be matched in accordance with notice 00/212: A206: R005 and the time of transfer should be in accordance with notice 01/034: A034: R003. The transfer must comply with FSA guidance on 'Proper Trades in Relation to On-Exchange Derivatives' and must not be carried out in order to avoid or evade other LME rules including the give-up rules.

3 CLEARING SWITCHES



- 3.1 A clearing switch takes place when:
- a a customer has existing LME positions with two or more members;
 - b those positions are for cash or cash today (TOM) prompt; and
 - c the customer wishes to reduce/consolidate his warrant delivery obligations or to trade out of the net prompt position more efficiently.
- 3.2 Before a clearing switch can take place, the client must have one or more LME registered client contracts which have been recorded as such both in the LME matching system and in the member's trading and financial records. The relevant LME registered client contracts must have been entered into the LME matching system no later than the business day before the clearing switch takes place.
- 3.3 The only exception to the above will be when a customer, for legitimate commercial reasons, requires to trade on the cash or cash today date, at the official settlement or current market price for the relevant prompt date in order to regularise its deliver commitments. These trades may be included as part of a clearing switch. They should be registered in the LMEMS by the member effecting them, in the normal manner. Members, should retain sufficient records to demonstrate that the trade took place prior to effecting the clearing switch.
- 3.4 A clearing switch:
- a cannot be entered into the LME matching system more than two business days before the relevant prompt date, subject to the LME matching system cash today rules;
 - b must be priced at the official settlement price for the relevant prompt dates; and
 - c must be recorded for the account of the same customer in the books and financial records of the members involved.



3.5 The member must have suitable procedures in place to verify that it can allow or accept the clearing switch. The clearing switch should be matched in accordance with notice 00/212: A206: R005 and the time of transaction entered into the matching system should be in accordance with notice 01/034: A034: R003.

3.6 The clearing switch must comply with FSA guidance on 'Proper Trades in Relation to On-Exchange Derivatives' and must not be carried out in order to avoid or evade other LME rules including the give-up rules.

4 THE MOVEMENT OF AN OFF EXCHANGE POSITION HELD AT ONE MEMBER TO OFFSET AN ON-EXCHANGE POSITION HELD AT ANOTHER MEMBER OR THE MOVEMENT OF AN ON-EXCHANGE POSITION TO OFFSET AN OFF EXCHANGE POSITION

4.1 The LME allows members to bring contracts on exchange at prices away from current market prices in certain circumstances. These transactions fall into a number of categories.

4.2 For the avoidance of doubt the following rules do not apply to average contracts such as strips or APCs derived from market prices, even if the market price was not known at the original date of the transaction. Such contracts should be registered when an appropriate prompt is available or the price for the averaging period is known. They should be matched/registered in accordance with notice 00/212: A206: R005.

MOVEMENT OF POSITIONS ON/OFF EXCHANGE WITHIN THE PREVAILING THREE-MONTH PROMPT STRUCTURE

FUTURES

4.3 In certain circumstances customers may wish to effect a transaction that will result in the closing of an OTC contract and the opening of an LME contract for the same commitment. The LME is concerned that some of these transactions have the potential to cause market disruption and therefore the following rules will apply.



Off exchange contracts offsetting on-exchange commitments

4.4 **Customers** may have on-exchange and off exchange commitments, at different members, that they may wish to offset or off exchange position which they wish to bring on-exchange. Therefore, the following will apply:

- a The member bringing the customer's OTC position on-exchange will register this trade using the 'DE' trade type. This contract may be at original (OTC) contract price, current market price or the official settlement price for the relevant prompt date. Members may average or amalgamate such prices as long as they maintain sufficient audit trail to demonstrate how the average/amalgamation was calculated and which price basis was used. Members may not average/amalgamate different price bases.
- b The position will then be 'switched', **at the price and for the same number of lots as the 'DE' cross**, to the receiving member using the trade type 'OS'. The 'DE' cross and the 'OS' switch should be for the same trade date.

4.5 These procedures may only be adopted in the following circumstances:

- c The customer has an on-exchange commitment with one member that already exists within the three month prompt structure i.e. both sides cannot bring contracts on-exchange within the three month prompt structure.
- d The circumstances surrounding the contract being brought on-exchange were such as to justify use of the procedure i.e. the economic effect on the market should be neutral or immaterial. In addition, when bringing transactions on-exchange, members should have regard to their duty not to create disorderly markets.
- e The member bringing the customer's OTC commitment on-exchange has hedged **its or its affiliates** exposure on-exchange.
- f The position being switched is for the **same customer** at both members.



- g For each contract brought on-exchange the member should be able to provide full details of the relevant OTC commitments, including if appropriate its affiliates commitments. They will need to be able to demonstrate that the price used for the LME Client Contract was a market price at the time the OTC contract was created. The LME Client Contract must be for the same commitment and customer as the OTC contract.

Off exchange contracts offsetting off exchange contracts at different members

4.6 Certain **Customers** may have off-exchange commitments that they may wish to offset using the mechanism of the LME. Therefore, the following will apply:

- h The member bringing the customer's OTC position on-exchange will register this trade using the 'DE' trade type. This contract may be at original (OTC) contract price, current market price or the official settlement price for the relevant prompt date. Members may average or amalgamate such prices as long as they maintain sufficient audit trail to demonstrate how the average/amalgamation was calculated. Members may not average/amalgamate different price bases.
- i The position will then be 'switched', **at the price and for the same number of lots as the 'DE' cross**, to the receiving member using the trade type 'OS'. The 'DE' cross and the 'OS' switch should be for the same trade date.
- j The member receiving the position should then take it off exchange using the trade type 'DQ'. The 'DQ' cross should be **for the same price, number of lots and trade date as the 'OS' switch**.

4.7 These procedures may only be adopted in the following circumstances:

- k The customer holds its OTC positions with LME members or their affiliates.



- l The circumstances surrounding the contract being brought on-exchange were such as to justify use of the procedure i.e. the economic effect on the market should be neutral or immaterial. In addition, when bringing transactions on-exchange, members should have regard to their duty not to create disorderly markets.
 - m Both members have hedged **their or their affiliates** exposure on-exchange.
 - n For each contract brought on-exchange the member should be able to provide full details of the relevant OTC commitments, including if appropriate its affiliates commitments. They will need to be able to demonstrate that the price used for the LME Client Contract was a market price at the time the OTC contract was created. The LME Client Contract must be for the same commitment and customer as the OTC contract.
- 4.8 The position being switched is for the **same customer** at both members.
- 4.9 The LME will review these transactions periodically. Members should be able to produce a full audit trail capable of demonstrating compliance with the above procedures.

Positions taken off-exchange

- 4.10 If a customer wishes to move its on-exchange position to a different member (within the prevailing three-month prompt structure) and then take it off exchange the following procedure will apply.
- a The position should be 'switched' to the receiving member using the trade type 'OS'.
 - b The position may be moved at current market price, Official settlement price for the relevant prompt date, original contract price or an average or amalgamation. **The member taking the position off exchange should ensure that the correct trade type is used.**



- c The member taking the position off exchange will register this trade using the 'DQ' trade type that should replicate the transaction switched. The 'DQ' cross and the 'OS' switch should be for the same trade date.

4.11 These procedures may only be adopted in the following circumstances:

- d The customer has an on-exchange commitment with one member that already exists within the three-month prompt structure.
- e The member taking the customer's position off exchange has hedged **its or its affiliates** exposure on-exchange.
- f The position being switched is for the same customer at both members.
- g The circumstances were such as to justify use of the procedure i.e. the economic effect on the market should be neutral or immaterial. In addition, when taking transactions off exchange, members should have regard to their duty not to create disorderly markets.

4.12 The LME will review these transactions periodically. Members should be able to produce a full audit trail capable of demonstrating compliance with the above.

MOVEMENT OF POSITIONS ON/OFF EXCHANGE OUTSIDE THE PREVAILING THREE-MONTH PROMPT STRUCTURE

4.13 If members wish to bring an OTC contract on-exchange outside the prevailing three-month prompt structure, for each contract the member will need to be able to demonstrate, that the price used for the LME contract was a market price at the time the OTC contract was created. The LME Client Contract must be for the same commitment and customer as the OTC contract.

4.14 These contracts should be registered with the trade type 'DE'. They may be moved to other members by 'switching' as described above. If a transaction is switched outside the three-month prompt structure, it is not necessary to demonstrate that the member bringing the contract on-exchange has hedged its or its affiliates commitment on-exchange.



- 4.15 If a member wishes to take a contract off exchange outside the prevailing three-month prompt structure then this should be effected using the 'DQ' trade type.

OTC CONTRACTS BROUGHT ON EXCHANGE AND RETAINED

- 4.16 Members bringing a customer's OTC contract on-exchange that is retained within their own books should register the contract using the 'DE' trade type. If the position is within the prevailing three-month prompt structure then the procedures set out above in paragraphs 4.4-4.5 should be followed. If the position is outside the prevailing three-month prompt structure then the procedures set out above in paragraphs 4.13-4.14 should be followed.
- 4.17 A Member wishing to take a customer's on-exchange contract off exchange within their own books should register a cross using the 'DQ'. If the position is within the prevailing three-month prompt structure then the procedures set out above in paragraphs 4.10-4.11 should be followed. If the position is outside the prevailing three-month prompt structure then the procedures set out above in paragraphs 4.13-4.15 should be followed.

OPTIONS

Exercise of OTC options into LME futures

- 4.18 In certain circumstances the exercise of an OTC option may be for an LME Client Contract. This is a new LME contract and will require registration. If the exercise of the option follows that of LME traded options i.e. it results in a future for prompt date third Wednesday of the relevant month, with its trade date being the declaration date of that month, the cross should be registered with the trade type 'DE' in the normal manner.
- 4.19 If the resultant future is of a different structure i.e. not resulting in a future for prompt date third Wednesday of the relevant month, with its trade date being the declaration date of that month, the future should be registered with the trade type 'DO'. All trades registered in this manner will be reviewed by the LME. Members should notify the LME of these transactions by either noting 'OTCOPT' in their private reference field or by fax to the LME.



4.20 Members should be able to produce a full audit trail capable of demonstrating compliance with the above procedures and that the circumstances were such as to justify use of the procedure; i.e. the economic effect on the market should be neutral or immaterial. In addition, when bringing transactions on-exchange, members should have regard to their duty not to create disorderly markets.

4.21 In each of these circumstances the member will need to be able to demonstrate that the premium was a market premium at the time the OTC option was created. The resultant LME futures, in both cases, can be switched using the rules above. For each contract brought on-exchange the member should be able to provide full details of the relevant OTC commitments, including if appropriate its affiliates commitments.

Exercise of OTC options into on exchange options

4.22 The exercise of some customers' OTC options may result in the creation of an LME option. The LME option will need to be registered in accordance with LME rules using the trade type 'DE'.

4.23 In each of these circumstances the member will need to be able to demonstrate that the LME option reflects the contractual commitment of the OTC option. For each contract brought on-exchange the member should be able to provide full details of the relevant OTC commitments, including if appropriate its affiliates commitments

EXCHANGE CONTRACTS

4.24 Exchange contracts brought on-exchange must be matched using the trade type 'EE' as detailed in notice 00/212: A206: R005. The use of the 'EE' trade type within the three-month prompt structure is restricted to the circumstances set out in this notice.

RELATIONSHIP WITH PART 1 MEMBERSHIP, ENFORCEMENT AND DISCIPLINE PARAGRAPH 9.1.3 AND PART 3 TRADING REGULATIONS PARAGRAPH 15.1 OF THE LME RULEBOOK



4.25 Paragraph 9.1.3, Part 1 Membership, Enforcement and Discipline of the LME rulebook, authorises the Executive Director: Regulation and Compliance to request information from members in circumstances where, in his opinion, an undesirable situation or improper trading practice has or may occur. In these circumstances, members will be expected to disclose the full details of all OTC relationships with customers that fall within the terms of the enquiry. Paragraph 15.1 Trading Regulations, enables the Special Committee of the LME, if they suspect ‘...the existence or to anticipate the development or likely development of a corner or undesirable situation or undesirable or improper trading practice which in their opinion has affected or is likely to affect the market.’ to take such steps, as in their absolute discretion they deem necessary to contain or rectify the situation. This could include restricting members’ ability to bring OTC contracts on-exchange.

5 METAL POSITION SWAPS

5.1 The term metal position swap describes the practice whereby commercial trade users of physical metal use the LME matching system to swap/exchange a commitment to deliver physical metal between them. The swap is facilitated by two members each of whom has one of the commercial trade users as a customer or by a single member who has both commercial trade users as customers.

Two member metal position swaps

5.2 Before a client can ‘swap’ his position, he must have one or more LME registered client contracts which have been recorded as such both in the LME matching system and in the first member’s trading and financial records. In addition, the relevant LME registered client contracts must have been entered into the LME matching system no later than the business day before the swap takes place.

5.3 Each member must have at least one of these genuine commercial trade users involved in the transaction as an existing customer. A commercial trade user is a company, other than a member (except for an associate trade clearing member), that has a requirement for the use of physical metal and is not a broker of futures and/or options.



- 5.4 The transaction must be properly documented and members should maintain an audit trail sufficient to explain the transaction. In particular, members must retain evidence of their customer's request to move the position. Members may use the form issued by the Exchange (see attached pro forma). Members who are conducting a series of inter linked transactions, such as a 'strip' may record such transactions on a single document.
- 5.5 The metal position swap can only be made at current market price, the actual contract price or an aggregation of these prices for the position(s) being moved for each prompt date.
- 5.6 Metal position swaps should be matched in accordance with notice 00/212: A206: R005 and the time of the transaction should be recorded in accordance with notice 00/211: A204: R004.
- 5.7 A situation is possible where the swap arrangement is between a customer of a member who is a commercial trade user of a metal, and an Associate Trade Clearing member who is also a commercial trade user of the same metal. In such a case the swap arrangement will be subject to the same rules as above except that:
- a the associate trade clearing member will not itself have a customer; and
 - b the customer of the other member must be part of the same group as the associate trade clearing member.
- 5.8 The transaction must comply with FSA guidance on 'Proper Trades in Relation to On-Exchange Derivatives', must not be carried out in order to avoid or evade other LME rules, including the give-up rules, and must be for a commercial purpose.

Single member metal position swaps

- 5.9 If the metal position swap involves a single member it involves the novation of an LME position from one commercial trade user to another. The following procedures should apply:
- a Before a client can 'swap' his position, he must have one or more LME registered client contracts which have been recorded as such both in the LME matching system and in the member's trading and financial records. In addition, the



relevant LME registered client contracts must have been entered into the LME matching system no later than the business day before the novation takes place.

- b This position should be novated from one commercial user to the other. Client crosses should not be registered in the LMEMS to reflect this novation unless it results in the movement of positions between non-segregated and segregated accounts. Any price adjustment should be recorded in the LMEMS using the CR/CT mechanism as prescribed by notice 00/212: A206: R005.
 - c The member should retain sufficient records to justify the transaction. It is recommended that a modified version of the agreement used for two member metal position swaps be used.
- 5.10 The member must have both of these genuine commercial trade users involved in the transaction as existing customers. A commercial trade user is a company, other than a member, that has a requirement for the use of physical metal and is not a broker of futures and/or options.
- 5.11 If a member subsequently wishes to move the position to another member they should follow the appropriate LME rules. This type of transaction should not be moved using the trade type 'MS' which relates solely to two-member metal position swap.
- 5.12 Associate trade clearing members may not conduct single member metal position swaps.
- 5.13 The transaction must comply with FSA guidance on 'Proper Trades in Relation to On-Exchange Derivatives', must not be carried out in order to avoid or evade other LME rules, including the give-up rules, and must be for a commercial purpose.

6 EFFECTIVE DATE

- 6.1 The above rules will take effect from the date of this notice.



A WHITING

cc: Board directors



METAL POSITION SWAP TRANSACTION

BROKER A

[INSERT NAME]

CUSTOMER A

[INSERT NAME]

REFERENCE

[BROKER A]

BROKER B

[INSERT NAME]

CUSTOMER B

[INSERT NAME]

REFERENCE

[BROKER B]

TRADE DETAILS

METAL

LOTS

PROMPT

PRICE PER TONNE

STATEMENT

I confirm that [Customer A] is a direct customer of ours, is a commercial user of the metal concerned and has given us written instructions regarding the above metal position swap transaction. I confirm that we have no reason to doubt that the transaction above is not in breach of LME Rules and Regulations or other appropriate legal obligations.

BROKER A

[Name]

[Signature of authorised
representative]

CUSTOMER A

[Name]

[Signature of authorised
representative]

STATEMENT

I confirm that [Customer B] is a direct customer of ours, is a commercial trade user of the metal concerned and has given us written instructions regarding the above metal position swap transaction. I confirm that we have no reason to doubt that the transaction above is not in breach of LME Rules and Regulations or other appropriate legal obligations.

BROKER B

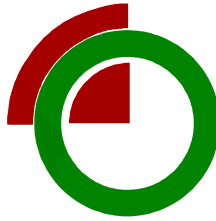
[Name]

[Signature of authorised
representative]

CUSTOMER B

[Name]

[Signature of authorised
representative]



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS

Ref: 01/305 : A305 : R10

Date: 27 July 2001

Subject: **DEFINITION OF END OF BUSINESS DAY FOR OPTION DECLARATION**

INTRODUCTION

1 The introduction of LME Select and the extension of the LME matching system (LMEMS) has necessitated a reassessment of the rules relating to the declaration of traded options and TAPOs because potentially trades could be rejected by the LMEMS.

Current rules

2 The current rules for traded options and TAPOs state that they may be traded '...until the close of business on the Last Trading Day for such Metal Options [or Traded Average Price Options].' This means that they may be traded until the close of matching at 20:00 on the first Tuesday of each month.

3 The LMEMS will calculate closing prices at 18:30. This means that it will not be able to accept new option strikes until the following day; ie it needs to run overnight processing to accept these strikes.

Issues arising from the introduction of LME Select

4 In LME Select the 8 strikes above and below the 'at the money' strike (4 for TAPOs and LMEX) will be automatically available for trading. Therefore, it is possible that a new strike may trade on Select on the last business day before declaration but after the price file has run at 18:30. This means that the trade will be rejected by the LMEMS. Although in normal circumstance the trade could be input on the



following morning this is not the case on the declaration day as the trade needs to be part of the member's open position on the previous evening in order for it to be part of that month's declaration.

RULE

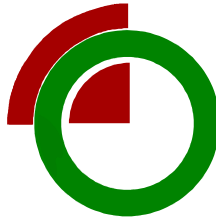
5 In order to address this issue and give certainty to the market, trading in options on the last business day before declaration will be restricted to 07:30-18:00 on LME Select and up to 18:00 in the telephone market. Option trades in the telephone market must be matched by 18:15. Option trades for LME Select will be matched automatically. Trading in options for other months may continue as normal.

EFFECTIVE DATE

6 This notice follows consultation and the incorporation of received comments. The above rule will take effect from the introduction of LME Select on 10 September 2001. The first day to be affected by the Rule will therefore be Tuesday, 2 October 2001.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 01/402 : A402 : R011
Date: 24 October 2001
Subject: **RULES FOR THE USE OF TRADE TYPES FOR THE LME
MATCHING AND CLEARING SYSTEM**

Introduction

This notice contains the trade types to be used for entering trades into the LME matching and clearing system. It has been updated to reflect the introduction of LME Select, to cross reference as appropriate to the current LME rules and to bring all the rules on trade type indicators into one notice. Attention is drawn to the corrections of trades on LME Select. LME Select trades are automatically matched in the LMEMS by the system, so in most circumstances corrections should not be necessary. Therefore, corrections to LME Select trades may only be made with the prior permission of the LME compliance department. As the small number of changes have already been subject to consultation, principally during the introduction of LME Select, there will not be a further consultation period. This notice replaces notice 00/212 : A206 : R005.

This document provides a comprehensive guide to the matching system for compliance officers and members' matching desks. The attached appendices provide short guides for daily use by matching clerks highlighting the trade types that reflect 'normal' business.

A WHITING

cc: Board directors

Rules on the use of Trade Type Indicators

C O N T E N T S

Section A: Introduction

Section B: Trade Type Indicators

- 1 Normal Trades**
- 2 Averages/aggregations**
- 3 Give-up Trades**
- 3.1 'Late' Give-up Trades**
- 4 Average price Contracts**
- 5 Historic/Original price carry Trades ('HPC')**
- 6 Over the Counter ('OTC') Transactions**
- 7 Declaration of options**
- 8 Transfers**
- 9 Clearing Switches**
- 10 OTC Switches**
- 11 Metal Position swaps**
- 12 Currency Conversion**
- 13 Correction Trades**
- 14 Movement of Segregated Client Trades**
- 15 LME Select**
- 16 Others**
- 17 Proxy Trades**

Section C: APPENDICES

- 1 Summary of Normal Trade Types**
- 2 Summary of Proxy Trade Types**
- 3 Summary of Normal Trade Types (LMEX Contract)**
- 4 Summary of Proxy Trade Types (LMEX Contract)**

SECTION A: INTRODUCTION

There are two types of LME Contract:

- 1 An Exchange Contract which is a Contract between two clearing members. An Exchange Contract must be matched; and
- 2 A Client Contract, which is a contract between an LME clearing member and any person other than another clearing member or a contract between an associate broker member and another person. A Client Contract must be registered.

The LME Matching System (LMEMS) is used to match/register these trades. It requires clearing members to use a two-letter trade type to indicate the nature of the transaction entered into the system. Non-clearing members are required to use the services of a clearing member to enter their trades in the LMEMS.

LME Select is the LME's automatic trading system. It allows category 1 and 2 members to trade all LME Exchange Contracts on an inter-member basis. These trades are then matched automatically in the LMEMS. Any client transactions that are priced basis trades conducted on LME Select should be registered in accordance with the appropriate section of this notice.

This guidance sets out the trade type indicators to be used when entering trades into the LMEMS and the circumstances in which they should be used.

All trade types are identified by

Rules relating to all trades

The following rules apply to trades input into the LMEMS. **N.B.** The automatic matching of trades by LME Select ensures that they comply with the appropriate rules set out below:

- The date and time of execution must be recorded and entered in the LMEMS for all trades (Regulation 3.13.1 (g) of part 3 of the LME's rules and regulations). Notice 01/034 : A034 : R003 matching periods for and trade times of trades entered into the LME matching and clearing system.
- All Exchange Contracts must be matched within the prescribed time bands (board notice 01/034 : A034 : R003).
- Client Contracts must be registered within the prescribed time bands (board notice 01/034 : A034 : R003).
- Client Contracts must be registered for all customers, whether they are segregated or non-segregated (Regulation 2.2 of part 3 of the LME's rules and regulations).

- ➔ All trades must be input into the LMEMS using a mandatory two-letter coding (see below).

INTRODUCTION (continued)

- ➔ To demonstrate the principal-to-principal nature of an LME Contract, all Exchange Contracts must be matched into the member's house account at the LCH.
- ➔ Members shall observe high standards of integrity and fair dealing and observe high standards of market conduct as reflected in the FSA Principles and Guidance as published from time to time (Regulation 9.6 (a) of part 2 of the LME's rules and regulations).

There are 16 transaction categories. Within these categories are 37 trade types, comprising 23 Exchange Contract trades, 14 Client Contract trades and two trade types for the correction of either an Exchange or a Client Contract. These trade types apply to futures, carries, options and TAPOs. Not all of the trade types will apply to the LMEX Contract. The appropriate sections of this notice highlight where this is the case.

Carry trades, whether for Exchange or Client Contracts, must be input into the LMEMS using the appropriate carry trade input screen

In addition to the categories mentioned above, there is a separate category for the registration of client trades involving a category 4 member (associate broker member – 'ABM'). These are called proxy trades. Within this category are 15 types of Client Contract trades. For Exchange Contract trades involving an ABM, the trade types to be used are the same as detailed in sections 1-15. The clearing member of the ABM **must** input a three-letter identity code for the ABM in the public reference field of the Exchange trade. If the trade type requires a client identity code in the public reference field then the ABM identity requirement is waived. These trade types are described in sections 3, 8, 9, 10, 11 and 17 of this guidance.

Appendices 1 and 2 provide summaries of the normal and proxy trade types respectively. Appendix 3 is a summary of the normal trade types that may be used to process LMEX trades in the LMEMS. Appendix 4 is a summary of the proxy trade types that may be used to process LMEX trades in the LMEMS.

SECTION B: TRADE TYPE INDICATORS

1 Normal Trades

These are trades (except LME Select trades) executed during the business day at the current market price at the time of execution and are eligible to be matched/registered in the LMEMS.

- The **Exchange Contract** must be matched using **DD**
- The **Client Contract** must be registered using **DC**

Category 3 members cannot execute LME Client Contracts.

2 Averages/Aggregations

These are defined as:

- 1 Trades (except LME Select trades) executed at one average price over a number of different prompt dates, either as a series of outright trades ('strip') or as a carry trade.
- 2 Trades (except LME Select trades) executed at different prices, for the same prompt date on the same business date, which are then 'netted' together to form one entry at one 'aggregate' price to the LMEMS.

In both cases, a full audit trail must be kept to demonstrate the derivation of the final price.

- The **Exchange Contract** must be matched using **AD**
- The **Client Contract** must be registered using **DA**

Category 3 members cannot execute LME Client Contracts.

Trade types AD and DA are not available for LME X Contracts.

3 Give-up Trades

The LME give-up rules are contained in notice 00/383: A376: R010. A give-up is a new trade executed by one member (the executor), to be “given up” to another member (the clearer) for a common customer. Give-up trades cannot be executed on LME Select.

The following matters apply to all give-ups:

- 1 The trade date entered must be the date of execution.
- 2 The public reference field is a **mandatory matching** field and a matching reference code must be agreed between the executor and the clearer to identify the customer. This does not have to be the code specified on the give-up agreement.
- 3 A written give-up agreement must be in place **before** the trade is executed.

The **Exchange Contract** must be matched using the following trade types as appropriate:

- Contracts at market price:
GD by the **executor**- **UD** by the **clearer**
- Contracts at the aggregate price of all the trades to be given-up or the give-up of an average trade (see section 2 - averages/aggregations):
GA by the **executor**- **UA** by the **clearer**
- The final priced trade resulting from an average price contract between the client and the executing member (see section 4 – average price contracts):
GV by the **executor**- **UV** by the **clearer**

3 Give-up Trades (continued)

In all the above cases, the **Client Contract** (registered by the clearer) must be registered using:

- **DG**

If the customer requests that a trade be allocated across a number of accounts held at the clearing member, “DG” crosses must be registered to reflect the correct allocation of the trades i.e. if a customer wishes to receive a LME Client Contract a cross must be registered for that customer reflecting details of such a contract.

An appropriate Client Contract must be registered by the clearer even if the Contract is then taken off Exchange

Category 3 members cannot conduct give-ups.

Trade types GA, UA, GV and UV are not available for LMEX Contracts.

3.1 ‘Late’ Give-up Trades

Give-up trades should be agreed and processed according to the timing periods detailed in LME board notice 01/034 : A034 : R003. Where members may need to process a give-up trade on trade day plus two (see notice 01/034 : A034 : R003) the following trade types should be used.

- The **Exchange Contract** must be matched using:
GL by the **executor** - **UL** by the **clearer**
- The **Client Contract** (registered by the clearer) must be registered using **DL**

For all entries relating to ‘late’ give-up trades, members must use the original trade date of trade, as supplied by the executor.

Where members need to process give-up trades on trade date plus three or thereafter they must contact the LME before attempting to match the trade (see notice 01/034 : A034 : R003).

Members must maintain a full audit trail and be able to explain why the trade(s) were not processed in the prescribed time frame if required to do so.

Trade types GL, UL and DL are not available for LMEX Contracts.

4 Average Price Contracts ('APC')

An APC is a trade where the final contract price is unknown at the outset but is agreed on the basis of a series of future **LME price references**, usually to include a premium or a discount. APCs are not available on LME Select. Members may utilise the LMEMS to process trades relating to an APC:

- 1 When the quotation period of the APC is completed and the resultant final price trade is eligible for entry into the LMEMS;
- 2 To register the fixed price leg of a fixed/floating APC on its original business day, if the intention **from the outset** is to register the floating leg on-Exchange at the end of the quotation period;
- 3 When the fixed price leg of a fixed/floating APC is registered/matched concurrently with the final priced floating leg;
- 4 To process the administrative rollover of futures trades relating to an APC.

The above list is not exhaustive and members should, where possible, match/register all contracts relating directly to an APC if the intention is to issue an LME Client Contract/LME Exchange Contract. LME trades transacted as hedges against an APC should not be processed using the APC trade types.

In all circumstances members must maintain a full audit trail to demonstrate how the final price was derived and how any trades processed using the following trade types relate to an APC.

- The **Exchange Contract** must be matched using **AV**
- The **Client Contract** should be registered using **DV**

4 Average Price Contracts (continued)

The give-up of an APC is limited to the Contract representing the fully priced floating leg of the Client Contract only. The give-up trade types are detailed in section 3. If the APC terms include a fixed price leg, this can be moved to another member in the following circumstances:

- 1 Via the give-up mechanism (section 3) if moved on the trade date when the 'fixed' leg is executed;
- 2 Via the transfer mechanism (section 8) if the executor of the APC registered the fixed leg as a Client Contract in the LMEMS;
- 3 Via the OTC switch mechanism (section 10) if the 'fixed' leg has not been registered as an LME Client Contract by the executor of the APC.

Category 3 members cannot execute LME Client Contracts.

Trade types AV and DV are not available for LMEX Contracts.

5 Historic/Original Price Carry Trades ('HPC')

These are transactions where an **existing on-Exchange client position** is rolled/carried forward to an **LME valid prompt date** on the basis of the original contract price of the position within the same member.

The LME has set out its requirements for the documentation of these transactions in LME board notice 99/484:A472:RO34.

- The **Client Contracts** must be registered using **DH**

An HPC must comprise at least two entries to the LMEMS with the maturing volume fully allocated over the forward prompt date(s). Trades that are processed without a 'nearby' leg (in cases where the prompt date/currency restrictions within the LMEMS are activated) or without a 'forward' leg (in circumstances where the forward date is an invalid LME prompt date) do not comply with the HPC rules. These cannot be registered as LME Contracts.

HPC trades must, in all circumstances, be registered as carry trades.

A code identifying the customer must be input in the private reference field. Members unable to comply with this requirement must make **prior** alternative arrangements with the LME compliance department.

Category 3 members cannot execute LME Client Contracts.

The trade type DH is not available for LMEX Contracts.

6 Over The Counter ('OTC') Transactions

These trade types should be used when an off-Exchange trade is converted to an LME Contract or an LME Client Contract is taken off-Exchange.

The following points apply to both **Exchange and Client Contracts**:

- 1 The trade date is the day the transaction is brought on Exchange.
- 2 The trade date is the day the transaction is taken off-Exchange (applicable to Client Contracts only).
- 3 A code identifying the customer must be input in the public reference field. Members unable to comply with this requirement must make **prior** alternative arrangements with the LME compliance department.
- 4 Proper documentation must be kept relating to the existing contractual commitment (either OTC or LME). This must show the original details of the trade including the date and time of the original trade.
- 5 Members are reminded that OTC contracts brought on-Exchange must not have a material economic effect on the market (LME board notice 01/232 : A232 : R07). Similarly, members have a duty not to create disorderly markets (Part 2 paragraph 9.7 LME rulebook).
- 6 The rules for taking contracts moving contracts on/off exchange should not be used to circumvent other LME rules.

There are two circumstances:

- 1 An OTC Contract is brought on Exchange.
 - The **Exchange contract** must be matched using **EE**
 - The **Client Contract** must be registered using **DE**
- 2 The Contract is taken off-Exchange.
 - The **Client Contract** must be registered using **DQ**

Exchange Contracts cannot be taken off-Exchange.

6 Over The Counter (OTC) Transactions (continued)

The LME's requirements for these trades are set out in board notice 01/232 : A232 : R07. Members must be able to demonstrate that the price used is based upon previous contractual commitments, unless the price used is the prevailing market price. A full audit trail must be maintained for these transactions.

The subsequent movement between members of an OTC position brought on-Exchange or the movement between members, prior to a client position being taken off exchange, is covered in section 10.

Examples of specific usage

- 1 *A metal trade becomes eligible for registration/matching within the LMEMS due to the Contract prompt date now coinciding with a valid LME prompt date.*

Members should use either **EE** (Exchange Contract) or **DE** (Client Contract) to process the trade in the LMEMS.

- 2 *A metal Contract priced in a non-LME accepted currency is converted to an accepted LME currency via an FX conversion.*

In this instance the newly converted trade may be brought on-Exchange using **EE** (Exchange Contract) or **DE** (Client Contract) subject to compliance with LME board notice 01/232 : A232 : R07.

- 3 *An existing LME Client Contract is converted to a non-accepted LME currency prior to the prompt date.*

Here, the Client Contract may be taken off-Exchange using **DQ** subject to compliance with LME board notice 01/232 : A232 : R07. This cannot apply to previously matched LME Exchange Contracts.

- 4 *A metal trade with an invalid LME prompt date is amended (off-Exchange) to a valid LME prompt date.*

Again, the trade may be brought on-Exchange using **EE** (Exchange Contract) or **DE** (Client Contract) subject to compliance with LME board notice 01/232 : A232 : R07.

6 Over The Counter (OTC) Transactions (continued)

- 5 *The declaration of an OTC option results in either an LME futures Contract, or an LME Traded Option Contract, or an LME TAPO Contract.*

In all cases, the resultant LME trade may be processed using **EE** (Exchange Contract) or **DE** (Client Contract). The resultant LME futures Contract must have a prompt date of the third Wednesday in this circumstance (subject to compliance with LME board notice 01/232 : A232 : R07). For OTC options declaring into an LME futures Contract with a different LME prompt date, please refer to section 16.

The above examples have been included for guidance purposes only. They are not intended to cover all the specific scenarios under which this mechanism could be used.

Category 3 members may not conduct LME client business.

Trade types DE, EE and DQ are not available for LMEX Contracts.

7 Declaration of Options

This is the registration/matching of a futures position resulting from the declaration of an **LME Traded Option** or **LME TAPO** in the following circumstances:

- 1 Registration of a futures Contract for a **non-segregated client** resulting from the declaration of an LME client option.
- 2 Late declaration of an Exchange option (after 11:15 on the first Wednesday), with the consent of the counterparty member, the LCH and the LME compliance department.
- 3 Late declaration of a client option (after 11:15 on the first Wednesday), with the consent of the LCH and the LME compliance department.

In all three circumstances described above:

- The **Exchange Contract** must be matched using **ZD**
- The **Client Contract** must be registered using **DZ**

The trade date is the date of the declaration. Sufficient documentation must be kept, which at a minimum must show details of the option including the date and time when the original option was written.

The declaration of an **LME TAPO** for a **non-segregated client** must result in the registration of **two** client crosses in the LMEMS (regulation 10.1 of part 5B of the LME rules and regulations):

- A **DZ** using the original strike price of the TAPO and
- A **DZ** using the settlement price for the TAPO

Again, the trade date to use for these entries, is the date of the TAPO declaration. Sufficient documentation must be retained, which at a minimum must show details of the TAPO including the date and time when the original TAPO was written.

The declaration of an OTC option which results in an LME Traded option, an LME TAPO, or an LME futures trade is covered in section 6, OTC.

Category 3 members may not conduct LME client business.

Trade types ZD and DZ are not available for LME Contracts. This is due to the cash cleared nature of the index Contract.

8 Transfers

A transfer is a transaction in which an **existing LME** registered position is transferred from one member to another for a common customer (LME board notice 01/232 : A232 : R07).

A common customer code must be noted in the public reference field. This is a **mandatory matching** field.

Members must follow the procedures set out below when effecting transfers:

- The member moving the position, the transferor, **must** use the trade type **TT**
- The member receiving the position, the transferee, **must** use the trade type **FF**

In both circumstances, the trade types are mandatory matching codes.

In all cases, the trade date to use is the date the transfer is agreed by all parties.

A **Client Contract need not be registered**, as the transfer must refer to an existing registered position. For specific instructions regarding segregated clients, please refer to section 14 – Movement of Segregated Client Trades.

In all cases, a full audit trail must be maintained.

Category 3 members cannot conduct transfers.

Trade types TT and FF are not available for LMEX Contracts.

9 Clearing Switches

A clearing switch is a transaction in which an existing registered customer position is “switched” between members, for the purpose of reducing or consolidating the customer’s delivery exposure for the cash today (‘tom’) or cash prompt date (LME board notice 01/232 : A232 : R07). **This process can only apply to on-Exchange registered positions.** The transaction must be for a common customer of both members.

The public reference field is a **mandatory matching** field and a code must be agreed by **both** members for **each** customer.

Trades must be matched using the settlement price for the relevant prompt date.

- The transaction must be matched using the mandatory matching code **CS**

A **Client Contract need not be registered**, as the clearing switch refers to an existing client position(s). For specific instructions regarding segregated clients, please refer to section 14 – Movement of Segregated Client Trades.

A full audit trail must be maintained.

Category 3 members cannot conduct clearing switches.

The trade type CS is not available for LMEX Contracts.

10 OTC Switches

In the specific circumstance where a client wishes to offset an on-Exchange position at one LME member with an OTC position at another LME member the following procedure applies:

- 1 An OTC position is brought on-Exchange:
 - member holding the client's OTC position brings it on-Exchange using the trade type **DE**
 - The position is then 'switched' between members using the trade type **OS**

When a client wishes to offset an OTC position at one LME member with an on-Exchange position at another LME member, the following procedure applies;

- 2 An on-Exchange position is taken off-Exchange:
 - The LME position is 'switched' between members using the trade type **OS**
 - The member with the OTC commitment then takes the LME switch off-Exchange using trade type **DQ**

Finally a client may wish to offset on OTC position at one member with an OTC position at another. In these circumstances.

3. OTC movement:
 - A member holding a client's OTC position brings it on-Exchange using the trade type **DE**
 - The position is then 'switched' between members using the trade type **OS**
 - The receiving member with a OTC commitment then takes the LME switch off-Exchange using trade type **DQ**

In all cases, it is the responsibility of the member with the client's OTC commitment to inform the counterparty member that this mechanism should be used. Full details of the criteria required to transact this type of switch are contained within LME board notice 01/232 : A232 : R07.

The public reference field is a **mandatory matching** field for the **OS** trade type and a matching reference code must be agreed between the two members involved in the switch to identify the customer.

Category 3 members may not conduct OTC switch trades.

Trade types OS, DE and DQ are not available for LME Contracts.

11 Metal Position Swaps

A metal position swap is a transaction where **commercial trade users** of physical metal, use the LME matching system to swap/exchange a commitment to deliver physical material between themselves. The swap is carried out via the services of two members, each of whom has one of the **commercial trade users** as a customer. Full rules are provided in LME board notice 01/232 : A232 : R07 .

- The transaction must be matched using the mandatory matching code **MS**

The following applies:

- 1 Both members record the metal swap on the metal swap agreement form which must provide details of the transaction before entering it into the matching system. This form must be signed by all parties.
- 2 Members are required to maintain a complete audit trail of these transactions, including the metal swap agreement. This may be subject to review by the LME compliance department at a later date.

The trade date is the date the metal position swap is agreed by all parties.

The public reference field is **mandatory** and members must input a code that identifies the clients involved.

A **Client Contract need not be registered**, as the metal position swap refers to an existing client position(s). For specific instructions regarding segregated clients, please refer to section 14 – Movement of Segregated Client Trades.

Category 3 members can conduct metal position swaps subject to the specific limitations detailed in LME board notice 01/232 : A232 : R07.

The trade type MS is not available for LMEX Contracts.

12 Currency Conversion

A currency conversion is a transaction in which an existing LME client position is converted from one **LME accepted currency** to another **LME accepted currency**. This can only apply to **Client Contracts**.

- The transactions must be registered using **CX**

Members must adopt the following procedure:

- 1 Input the reverse of the original trade using **CX**.
- 2 Input the newly converted trade using **CX**.

The trade date is the date when the Contract is converted.

Sufficient documentation must be kept to explain the transaction. This must include the original details of the trade including the date and time of the transaction and the details of the FX rate used for conversion.

The CX mechanism should always comprise at least two entries to the LMEMS. In the event that the prompt date/currency processing restrictions within the LMEMS apply, members may not register **either** leg of the transaction. Members should maintain sufficient records to demonstrate why the CX entries could not be registered in the LMEMS.

The only trade details that should be altered for a currency conversion trade are the currency and the price. If the client requires other fields amended at the same time as the conversion, then the **correction** mechanism **must** be used (see section 13 – Corrections). If the conversion would result in a change to the prompt date of the original Client Contract, due, for example, to a banking holiday in one of the currencies, then again the **correction** mechanism should be used.

12 Currency Conversion (continued)

If the conversion is caused by an error at the member firm whereby the correct currency was not applied on the original trade date, then the **correction** mechanism may be used to effect the amendment to the original trade details. The selection of the conversion or the correction mechanism is dependent on the trade date of the FX conversion trade i.e.:

- 1 FX conversion transacted after the trade date of the metal trade – **CURRENCY CONVERSION.**

- 2 FX conversion transacted on the same trade date as the metal trade but not applied to the client cross in the LMEMS – **CORRECTION MECHANISM.**

- 3 FX conversion requested by client at the time of execution, but member did not transact appropriate FX trade on trade date – **EITHER MECHANISM MAY BE USED AS DEEMED APPROPRIATE BY MEMBER.** Members must, in this circumstance, maintain sufficient documentation to justify the method chosen, if required to do so by the LME compliance department.

CX cannot apply to non-LME currencies. In instances where a metal contract is priced in a non-LME accepted currency and subsequently converted into an LME accepted currency, or vice versa, please see section 6, OTC.

Category 3 members may not conduct LME client business.

The trade type CX is not available for the LMEX Contract.

13 **Correction Trades**

This process **must** be used for the correction/amendment of a registered client cross or a matched Exchange contract. It applies to **all** trade types. **Only** the following fields can be corrected:

- price
- metal
- prompt
- volume
- currency (if the CX mechanism does not apply)
- direction of LCH sub-account
- Contract type

Trades, which have been matched/registered with any other incorrect details, should not be amended in the LMEMS. This includes amendments specific to members internal trade records such as commission, client identification, direction of a non-segregated client trade etc. Errors within the trade type, trade date/time fields may **not** be amended either. In the event that such errors are detected, members should maintain appropriate internal records to explain any action taken.

Moving or amending a customer's position from non-segregated to segregated (or vice versa) is covered in section 14 'Movement of Segregated Client Trades'. Changes to the direction of a previously registered segregated Client Contract **must** use the correction mechanism.

The correction mechanism may only be used on LMEX Contracts on the same trade date as the original (incorrect) trade. Post-trade date corrections are NOT PERMITTED.

LME Select trades are automatically matched in the LMEMS by the system, so, in most circumstances, corrections should not be necessary. Therefore, corrections to LME Select trades may only be made with the prior permission of the LME Compliance department. Such requests should be made by email to membersurveillance@lme.co.uk. These requests should provide sufficient information to enable the LME to understand why it is necessary to correct the trade.

Members are required to maintain a complete audit trail of **ALL** corrections.

13 Correction Trades (continued)

- Members **must** use the trade types **CR/CT** and follow the procedure set out below when correcting a registered or a matched Contract:
 - 1 Input the reverse of the initial incorrect trade with its original trade date and time of trade using **CR**.
 - 2 Input the corrected trade, with the original trade date and time of trade using **CT**.
 - 3 If a trade has been registered twice or registered when it should not have been, input the reverse of the initial entry of the trade with its original trade date and time of trade using **CR**. No CT is required.

Trades should be amended as soon as practicable after the error is detected.

If the error is detected on the day of trade, the same procedure as detailed above should be used. However, where a member's system allows the retrieval of trade details before LCH registration CR/CT will not be required. **CR/CT should only be used for trades that have already been 'fired' to the LCH.**

Usage in specific circumstances

- 1 *A correction is required on a Client Contract that was registered using a prompt date that is now past-prompt.*

In this circumstance, the matching system will not accept the registration of the 'CR' trade to reverse the original incorrect trade.

Members may process the corrected version of the trade using **CT** as a single entry but only if the following criteria are met;

the amendment is to the **Prompt Date** field **only**;

the trade is for a non-segregated client account.

13 Correction Trades (continued)

- 2 *A correction is required on a Client Contract but the prompt date/currency restrictions within the LMEMS will not allow the cancellation of the original trade (i.e. the 'CR' entry cannot be processed).*

This is another version of the circumstance described in 1 previously and as such members should comply with the procedure given above.

- 3 *A correction is required to amend the volume of a matched Exchange Contract or a registered Client Contract.*

The entire original incorrect trade must be cancelled using 'CR'; the correct version must then be entered using 'CT'. A 'partial' cancellation using 'CR' for the excess volume is not allowed. Similarly, the 'extra' volume may not be entered using a single entry 'CT'.

Members should note that the first two examples above are now the only circumstances under which the trade type 'CT' may be used as a stand-alone entry within the LMEMS. Members may be required to demonstrate the correct usage of this particular mechanism by providing all appropriate trading records.

CORRECTION TRADES SHOULD NOT BE USED AS A MEANS TO CIRCUMVENT OTHER MATCHING RULES.

14 Movement of Segregated Client Trades

Exchange Contracts may only be booked into or out of a member's house account at the LCH. Any movement into or out of a member's segregated client account at the LCH must be reflected by the registration of a client cross involving the segregated account in the LMEMS. This is normally achieved by the registration of a client cross between the member's house (H) and segregated (C) accounts.

For transfer, clearing switch and the receipt of off-Exchange switch trades, there is normally no requirement for either member involved to register a client cross. However, if the position is held or will be received into a member's segregated client account, a cross must be registered to signify the movement of the position between the house and segregated account prior to remitting, or subsequent to receiving, a segregated position from/to another member.

- The client cross should be registered using **SA**

The trade details should replicate those of the underlying Exchange trade.

This trade type should also be used to correct or change a client position from a segregated account to a non-segregated account or vice versa. For amendments to the **direction** of a previously registered client cross for a segregated account, please refer to section 13 – Correction trades.

Category 3 members may not conduct LME client business.

15. LME Select

LME Select is the LME's automatic trading system. It allows category 1 and 2 members to trade all LME Exchange Contracts on an inter-member basis. These trades are then matched automatically in the LMEMS. Any client transactions that are priced basis trades conducted on LME Select should be registered in accordance with the appropriate section of this notice . LME Select uses two trade types:

- Trades arising from LME Select's order book will be matched automatically with the trade type BB
- Trades arising from the use of the Specific Quote Request functionality in LME Select will be automatically matched with the trade type AB

The LME allows members to correct errors arising from the execution and matching of LME Contracts. Such errors should normally not arise in LME Select and so corrections will only be permitted under the process outlined in Section 13 of this notice.

16 Others

The following trade types should only be used in exceptional circumstances, i.e. when none of the previous trade types can be applied:

- The **Exchange Contract** must be matched using **OD**
- The **Client Contract** must be registered using **DO**

Members must maintain a sufficient audit trail in order to explain why trades were processed using the above indicators.

Special Case

This applies to OTC options declaring into an LME futures Contract. If the prompt date of the resultant LME future is not a third Wednesday then the futures Contract(s) must be processed in the LMEMS using:

- **OD** for an Exchange Contract
- **DO** for a Client Contract

Members should notify the LME of these transactions by either noting 'OTCOPT' in the private or public reference (as appropriate) field or by fax to the LME. Board notice 01/232 : A232 : R07 gives full details of this procedure.

Category 3 members cannot execute LME Client Contracts.

Trade types OD and DO are not available for LMEX Contracts.

17 Proxy Trades

ABMs do not have access to the matching system; they use the services of a clearing member to register their trades. The requirement for LME members to record all LME Contracts in the matching system is set out in part 3 Trading Regulations of the LME rulebook. The recording of trades for an ABM will for the most part result in three principal Contracts being entered into the LMEMS:

- 1 An Exchange Contract between two clearing members: the initial recognition that metal has been sold/bought.
- 2 An administrative cross by the ABM clearer: reflecting the resale/repurchase of the metal to the ABM by its clearer.
- 3 A further client cross by the ABM clearer: reflecting the further resale/repurchase to the ABM client.

The **Exchange Contract** has been addressed in the preceding sections. The clearing member is reminded that it **must** enter an appropriate three- letter mnemonic to identify the ABM in the public reference field for the Exchange Contract. For give-up, transfer, clearing switch, metal position swap and OTC switch Contracts, a code identifying the client must be used instead of the ABM mnemonic (see sections 3, 8, 9,10 and 11 for full details).

The subsequent LME Client Contracts must be registered in the LMEMS by the designated LME clearing member of the ABM. The trade type indicator should reflect the nature of the trade transacted using one of the following trade types:

- **PC** for normal, market price trades – section 1
- **PA** for average/aggregate trades - section 2
- **PG** for give-up trades where the ABM issues the LME Client Contract(s) – section 3
- **PL** for 'late' give-up trades where the ABM issues the LME Client Contract(s) – section 3.1
- **PV** for an APC trade - section 4
- **PH** for historic/original price carry trades - section 5
- **PE** for an OTC contract brought on-Exchange – section 6
- **PQ** for a LME client position taken off-Exchange – section 6
- **PZ** for the declaration of options - section 7

- **PX** for a currency conversion - section 12
- **PO** for exceptional circumstance usage – section 16

Corrections to any of the above should be made using the correction mechanism as detailed in section 13 above.

The administrative crosses should be registered using the following trade type indicators:

- **PS** for the administration of the **segregated** client account of an ABM
- **PN** for the administration of the **non-segregated** client account of an ABM

ABMs should ensure that clear instructions are passed to other members by their customers and their designated clearer. The ABM must supply sufficient instructions to its clearer to enable the clearer to match trades efficiently and process client trades correctly. The ABM must also keep adequate records that maintain a full audit trail of all trades.

The designated LME clearing member of the ABM must keep adequate records to distinguish between the trading of the ABM and its own.

Category 3 members may not act as the designated clearer for an ABM.

Trade types PA, PL, PV, PH, PE, PQ, PZ, PX and PO are not available for LMEX Contracts.

Examples of Specific Usage

The following sections provide a brief outline of the entries required to process specific trades in the LMEMS for an ABM and/or a client of an ABM. For definitions of the specific trade types, please refer to sections 1-15 above.

16.1 Normal Trades

ABM has traded for its own account with another LME clearing member:

- A **DD** Exchange Contract must be matched between the ABM clearer and the ABM counterparty
- A **PC** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM has traded for its own account directly with its designated clearer:

- A **PC** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM has traded for a non-segregated client:

- A **PN** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PC** cross reflecting the further resale/repurchase to the ABM client

ABM has traded for a segregated client:

- A **PS** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PC** cross reflecting the further resale/repurchase to the ABM client

16.2 Averages/Aggregations

ABM has traded for its own account with another LME clearing member:

- An **AD** Exchange Contract must be matched between the ABM clearer and the ABM counterparty
- A **PA** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM has traded for its own account directly with its clearer:

- A **PA** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM has traded for a non-segregated client:

- A **PN** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PA** cross reflecting the further resale/repurchase to the ABM client

ABM has traded for a segregated client:

- A **PS** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PA** cross reflecting the further resale/repurchase to the ABM client

16.3 Give-up Trades

ABM assumes the role of LME executor – ABM client is non-segregated:

- A **PN** administrative cross to 'move' the executed trade to the ABM clearer
- The ABM clearer should then match the Exchange Contract using **GD, GA or GV** as appropriate

16.3 Give-up Trades (continued)

ABM assumes the role of LME executor – ABM client is segregated:

- A **PS** administrative cross to 'move' the executed trade to the ABM clearer (this should, however, be written in the 'house' account of the ABM clearer)
- The ABM clearer should then match the Exchange Contract using **GD, GA or GV** as appropriate

ABM assumes the role of LME clearer – ABM client is non-segregated:

- ABM clearer matches the Exchange Contract using **UD, UA or UV** as appropriate
- A **PN** administrative cross to reflect the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PG** cross to reflect the further resale/repurchase to the ABM client

ABM assumes the role of LME clearer – ABM client is segregated:

- ABM clearer matches the Exchange Contract using **UD, UA or UV** as appropriate
- A **PS** administrative cross to reflect the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PG** cross to reflect the further resale/repurchase to the ABM client (this should be registered in the segregated account of the ABM clearer)

For 'late' give-up trades the appropriate mechanism as detailed above is followed using:

- **GL** for the Exchange Contract when ABM assumes the role of LME executor
- **UL** for the Exchange Contract when ABM assumes the role of LME clearer
- **PL** for the necessary client crosses when ABM assumes the role of LME clearer

16.4 Average Price Contracts ('APC')

ABM has traded for its own account with another LME clearing member:

- A **DV** Exchange Contract must be matched between the ABM clearer and the ABM counterparty
- A **PV** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM has traded for a non-segregated client:

- A **PN** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PV** cross reflecting the further resale/repurchase to the ABM client

ABM has traded for a segregated client:

- A **PS** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PV** cross reflecting the further resale/repurchase to the ABM client

16.5 Historic/Original Price Carry Trades ('HPC')

May only be transacted for clients of the ABM

ABM has traded for a non-segregated client:

- Sufficient **PN** administrative crosses to reflect all the 'legs' of the HPC. This represents the resale/repurchase of the metal to the ABM by the ABM clearer
- Sufficient **PH** crosses to reflect all the 'legs' of the HPC. This reflects the resale/repurchase of the metal to the ABM client

16.5 Historic/Original Price Carry Trades (continued)

ABM has traded for a segregated client:

- Sufficient **PS** administrative crosses to reflect all the 'legs' of the HPC. This represents the resale/repurchase of the metal to the ABM by the ABM clearer
- Sufficient **PH** crosses to reflect all the 'legs' of the HPC. This reflects the resale/repurchase of the metal to the ABM client

16.6 Over the Counter ('OTC') Transactions

ABM wishes to bring an OTC on-Exchange for a trade executed with another LME clearing member:

- An **EE** Exchange Contract must be matched between the ABM clearer and the ABM counterparty
- A **PE** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM has an OTC with its designated clearer that both parties wish to bring on-Exchange:

- A **PE** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer

ABM wishes to bring an OTC on-Exchange for a non-segregated client account:

- A **PN** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PE** cross reflecting the further resale/repurchase of the metal to the ABM client

ABM wishes to bring an OTC on-Exchange for a segregated client account:

- A **PS** cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PE** cross reflecting the further resale/repurchase of the metal to the ABM client

16.6 Over the Counter ('OTC') Transactions (continued)

ABM wishes to take an existing Client Contract off-Exchange for a non-segregated client:

- A **PN** cross, reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PQ** cross to signify the taking off-Exchange of the previously registered LME Client Contract on behalf of the ABM

ABM wishes to take an existing Client Contract off-Exchange for a segregated client:

- A **PS** cross, reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PQ** cross to signify the taking off-Exchange of the previously registered LME Client Contract on behalf of the ABM

16.7 Declaration of Options

ABM declares an LME Traded option for its own account:

- A **PZ** cross representing the repurchase/resale of the futures Contract between the ABM clearer and the ABM

ABM declares an LME Traded option for a non-segregated client:

- A **PN** administrative cross, representing the repurchase/resale of the futures Contract between the ABM clearer and the ABM
- A **PZ** cross reflecting the further resale/repurchase of the futures Contract to the ABM client

16.7 Declaration of Options (continued)

ABM declares an LME Traded option for a segregated client:

- A **PS** administrative cross in the 'house' account representing the repurchase/resale of the futures Contract between the ABM clearer and the ABM

As the LCH will have automatically declared the net option position within the segregated account, the above represents the resale/repurchase of the futures Contract between the ABM clearer and the ABM.

ABM declares an LME TAPO for a non-segregated client:

- **One PN** administrative cross using the strike price of the TAPO
- **One PZ** cross using the strike price of the TAPO
- **One PN** administrative cross using the settlement price of the TAPO
- **One PZ** cross using the settlement price of the TAPO

ABM declares an LME TAPO for a segregated client:

- **One PS** administrative cross using the strike price of the TAPO
- **One PS** administrative cross using the settlement price of the TAPO

As the LCH will have automatically declared the net TAPO position within the segregated account, the above represents the resale/repurchase of the futures contracts between the ABM clearer and the ABM.

16.8 Transfers

For transfer trades, there is normally no requirement for either member involved to register a client cross. However, when an ABM is involved in this type of transaction, a cross or crosses must be registered to signify the movement of the position between the ABM and its designated clearer, prior to remitting, or subsequent to receiving, a client position to/from another member.

16.8 Transfers (continued)

In the following examples, the ABM client has requested an existing LME client position be transferred at original contract price to another LME clearing member.

*The ABM client is a **non-segregated** account:*

- A **PN** administrative cross to reflect the 'receipt' of the ABM client position by the ABM clearer, prior to transfer
- The ABM clearer then matches the Exchange transfer trade using **TT**

*The ABM client is a **segregated** account:*

- A **PS** administrative cross between the house and segregated accounts to reflect the movement of the client position into the ABM house account prior to transfer
- A second **PS** cross in the house account to reflect the 'receipt' of the ABM client position by the ABM clearer prior to transfer
- The ABM clearer then matches the Exchange transfer trade using **TT**

16.9 Clearing Switches

For clearing switches, there is normally no requirement for either member involved to register a client cross. However, when an ABM is involved in this type of transaction, a cross or crosses must be registered to signify the movement of the position between the ABM and its designated clearer, prior to remitting, or subsequent to receiving, a client position to/from another member.

In the following examples, the ABM client has requested an existing LME Client position for the cash prompt is cleared with another LME clearing member.

16.9 Clearing Switches (continued)

*The ABM client is a **non-segregated** account:*

- A **PN** administrative cross in the house account to reflect the 'receipt' of the ABM client position by the ABM clearer prior to clearing
- The ABM clearer then matches the Exchange clearing switch trade using **CS**

*The ABM client is a **segregated** account:*

- A **PS** administrative cross between the house and segregated accounts to reflect the movement of the client position into the ABM house account prior to transfer
- A second **PS** cross in the house account to reflect the 'receipt' of the ABM client position by the ABM clearer prior to clearing the trade
- The ABM clearer then matches the Exchange clearing switch trade using **CS**

16.10 OTC Switches

ABM has an OTC position for a non-segregated client that the client wishes to move to another LME clearing member to offset an on-Exchange LME position:

- A **PE** cross to bring the OTC on-Exchange
- A **PN** administrative cross, to move the position from the ABM to the ABM clearer
- The ABM clearer then 'switches' this position to the other LME clearing member using **OS**

16.10 OTC Switches (continued)

ABM has an OTC position for a segregated client that the client wishes to move to another LME clearing member to offset an on-Exchange LME position:

- A **PE** cross to bring the OTC on-Exchange
- A **PS** administrative cross, to move the position from the ABM to the ABM clearer
- The ABM clearer then 'switches' this position to the other LME clearing member using **OS**

ABM receives a request from a non-segregated client to offset the clients existing LME Client Contract via the receipt of an OTC position held by the client with another LME clearing member:

- The ABM clearer 'receives' the OTC position from the other LME clearing member using **OS**
- A **PN** administrative cross reflecting the resale/repurchase of the metal to the ABM by its clearer

ABM receives a request from a segregated client to offset the clients existing LME Client Contract via the receipt of an OTC position held by the client with another LME clearing member:

- The ABM clearer 'receives' the OTC position from the other LME clearing member using **OS**
- A **PS** administrative cross reflecting the resale/repurchase of the metal to the ABM by its clearer

ABM receives a request from a non-segregated client to accept an existing LME Client Contract held with another LME clearing member to offset an OTC exposure held with the ABM:

- The ABM clearer 'receives' the OTC position from the other LME clearing member using **OS**
- A **PN** administrative cross to represent the resale/repurchase of the metal to the ABM by its clearer
- A **PQ** cross to signify the position being taken off-Exchange on behalf of the ABM

16.10 OTC Switches (continued)

ABM receives a request from a segregated client to accept an existing LME Client Contract held with another LME clearing member to offset an OTC exposure held with the ABM:

- The ABM clearer 'receives' the OTC position from the other LME clearing member using **OS**
- A **PS** administrative cross to represent the resale/repurchase of the metal to the ABM by its clearer
- A **PQ** cross to signify the position being taken off-Exchange on behalf of the ABM

16.11 Metal Position Swaps

ABM receives a request to transact a metal position swap for a non-segregated client:

- A **PN** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- The ABM clearer should then match the Exchange Contract using **MS**

ABM receives a request to transact a metal position swap for a segregated client:

- A **PS** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- The ABM clearer should then match the Exchange Contract using **MS**

16.12 Currency Conversions

The same procedure as outlined in section 12 should be followed but the following trade type indicator should be used:

- **PX**

16.13 Correction Trade

The same procedure as outlined in section 13 should be followed.

16.14 Others

ABM has matched an Exchange Contract for its own account with another LME clearing member using trade type 'OD':

- A **PO** cross must be registered to reflect the resale/repurchase of the metal to the ABM by its clearer

ABM and its designated clearer have transacted a trade and need to use the 'exceptional use' trade type. The trade is for the ABMs own account:

- A **PO** cross must be registered to reflect the resale/repurchase of the metal to the ABM by its clearer

ABM needs to register a Client Contract for a non-segregated client using the trade type 'PO':

- A **PN** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PO** cross reflecting the further resale/repurchase to the ABM client

ABM needs to register a Client Contract for a segregated client using the trade type 'PO':

- A **PS** administrative cross reflecting the resale/repurchase of the metal to the ABM by the ABM clearer
- A **PO** cross reflecting the further resale/repurchase to the ABM client

SECTION 3

SHORT GUIDE TO PROXY TRADE TYPES

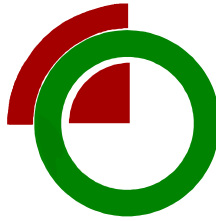
APPENDIX 2

Note	Trade Type	Description of EXCHANGE Contract	Maximum time limit	Note	Trade Type	Description of CLIENT Contract	Maximum Time limit
1	DD	Current, market price trade, eligible for matching	Trade date + 1	1 & 17.1	PC	Current, market price trade, eligible for registration	Trade date + 1
2	AD	Average or amalgamated trade	Trade date + 1	2 & 17.2	PA	Average or amalgamated trade	Trade date + 1
3 & 1	GD	Executing a Give-up trade at current, market price	Trade date & trade date + 1				
3 & 1	UD	Clearing a Give-up trade at current, market price	Trade date & trade date + 1	3 & 17.3	PG	Client cross registered by clearing member to give-up	Trade date & trade date + 1
3 & 2	GA	Executing a Give-up of an average or of an amalgamated trade(s)	Trade date & trade date + 1				
3 & 2	UA	Clearing a Give-up of an average or of an amalgamated trade(s)	Trade date & trade date + 1	3 & 17.3	PG	Client cross registered by clearing member to give-up	Trade date & trade date + 1
3 & 4	GV	Executing a Give-up of a fully-priced floating leg of an average price contract	Trade date & trade date + 1				
3 & 4	UV	Clearing a Give-up of a fully-priced floating leg of an average price contract	Trade date & trade date + 1	3 & 17.3	PG	Client cross registered by clearing member to give-up	Trade date & trade date + 1
3.1	GL	Executing a 'late' give-up trade	Trade date + 2				
3.1	UL	Clearing a 'late' give-up trade	Trade date + 2	3.1 & 17.3	PL	Client cross registered by clearing member of a 'late' give up	Trade date + 2
4	AV	Trade relating to average price contact	Trade date + 1	4 & 17.4	PV	Trade relating to average price contact	Trade date + 1
				5 & 17.5	PH	Historic/Original price carry	Trade date + 1
6	EE	OTC trade being brought on to the LME	Agreed date + 1	6 & 17.6, 10 & 17.10	PE	OTC client trade being brought on to the LME	Agreed date + 1
				6 & 17.6, 10 & 17.10	PQ	Registered LME Client Contract taken off exchange	Agreed date + 1
7	ZD	LME futures trade resulting from the declaration of either an LME traded option or an LME TAPO. PRIOR LME/LCH permission required for LATE declaration.	Declaration date + 1	7 & 17.7	PZ	LME futures trade resulting from LME traded option declaration or LME TAPO. PRIOR LME/LCH permission required for LATE declaration.	Declaration date + 1
8	TT	Transfer of client position. Entered by transferor.	Agreed date + 1	12 & 17.12	PX	FX conversion of previously registered LME client trade in to a different LME accepted currency	NONE
8	FF	Transfer of client position. Entered by transferee.	Agreed date + 1	17	PS	Administration of the segregated client account	NONE
9	CS	Clearing Switch	Agreed date + 1	17	PN	Administration of the non-segregated client account	NONE
10	OS	'Switching' of OTC position for LME position or vice versa	Agreed date + 1				
11	MS	Metal position swap	Agreed date + 1				
13	CR	Reversal OR deletion of a previously matched trade	NONE	13 & 17.13	CR	Reversal OR deletion of a previously registered Client Contract	NONE
13	CT	Corrected version of reversal (CR) trade	NONE	13 & 17.13	CT	Corrected version of reversal (CR) trade	NONE
16	OD	Exceptional circumstance usage	NONE	15 & 17.15	PO	Exceptional circumstance usage	NONE

NOTES

All Exchange trade type indicators are mandatory 2-character matching fields

Time limits for both Exchange and Client Contracts refer to the MAXIMUM permitted. Please refer to board notice [] for the time band limits.



LONDON METAL EXCHANGE

-----**From Executive Director: Regulation
and Compliance**

To: ALL MEMBERS, WAREHOUSE COMPANIES AND
LONDON AGENTS

Ref: 01/492 : A492 : W83

Date: 17 December 2001

Subject: **LME COMPLAINTS ARRANGEMENTS**

Under the Financial Services and Markets Act 2000 (FSMA), which came into force on 1 December 2001, all Recognised Investment Exchanges (RIEs) and Recognised Clearing Houses (RCHs) are required to appoint an independent Complaints Commissioner to oversee their complaints procedures.

2 The LME Board has approved the appointment of Dr Oonagh A McDonald CBE as the LME's Complaints Commissioner with effect from 1 December 2001 for a three year period.

3 Attached to this notice is the LME's new complaints procedure, which incorporates the role and powers of the LME's Complaints Commissioner as laid down in the FSMA. In every other respect, the LME's complaints procedure remains unchanged from that issued on 27 October 1997 (Notice 97:356 W-076/97).

4 The LME will continue to investigate, in the first instance, all complaints about the LME. Prior to the FSMA, if the complainant was dissatisfied with the conduct or outcome of the complaint handling, the complainant could refer the complaint to the Financial Services Authority. Under the new procedures, claimants who are dissatisfied with the handling of their complaint by the LME for complaints arising in connection with the performance of, or failure to perform, any of its regulatory functions, will be able to refer the complaint to the LME's independent Complaints Commissioner.

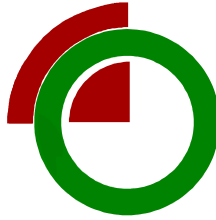


5 I remain the LME's complaints officer.

6 This notice replaces 97:356 W-076/97, which can now be discarded.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

COMPLAINTS PROCEDURE OF THE LONDON METAL EXCHANGE

Complaints

The London Metal Exchange Limited (“LME”) investigates complaints made against the LME, its personnel, its members or its listed warehouses which may involve breaches of statutory duty, the LME rules or the proper operation of the market in relation to:-

- (a) the functions of the Exchange;
- (b) business transacted on the Exchange;
- (c) transactions cleared through the LME matching system;
- (d) LME contracts;
- (e) the conduct of LME members in carrying out LME business;
- (f) the conduct of warehouses listed by LME in carrying out warehousing business in relation to metal on LME warrant, metal taken off LME warrant or metal due to be put on LME warrant;
- (g) the suitability of a brand for listing by the LME; or
- (h) LME warrants and the warranting of metal.

Registering a Complaint

2 The complaint must be made in writing. In the event that it is made by a company, it should be signed by a director or equivalent officer.

3 It should include sufficient information to allow the LME to properly identify the trade(s) or activity complained of, and establish the basis for any alleged loss by the complainant. If insufficient information is provided, the LME may request further information. Where a complaint is made against more than one participant (for example, complaints against two members, or the LME and a member) separate complaints should be made against each



participant, although reference may be made to background material provided with the other complaint.

4 Any information with the complaint or obtained from the complainant in the course of a subsequent investigation may be disclosed to third parties such as other regulatory authorities as the LME considers appropriate but subject to its normal rules and procedures.

5 The complaint must be sent to:-

The Complaints Officer
The London Metal Exchange Limited
56 Leadenhall Street
London EC3A 2DX

Marked “Complaint”

6 There is no filing fee.

7 The complaint will be investigated by the LME Compliance Department who may act in conjunction with the LME Warehousing Department and others as appropriate. The investigation may involve other staff at the LME or outside professional assistance as appropriate.

8 The inquiry will be conducted independently of any LME personnel who may be involved in the subject of the complaint.

9 The LME will aim to complete its investigation within 3 months, or within such further period as the scope of the complaint would reasonably demand.

10 The LME will, insofar as it is consistent with its duties in operating the Exchange and its duties of confidentiality to members or warehouses listed by the LME, advise the complainant and any other relevant parties of the outcome of the investigation, and in particular whether it considers that there are good grounds for complaint against LME, its personnel, its members or warehouses listed by it, in relation to the business of the LME. The LME will also advise the complainant of recommended action arising from the investigation of the complaint.

11 As a result of the LME Compliance Department’s investigation, disciplinary proceedings may be instituted.

12 For complaints arising in connection with the performance of, or failure to perform, any of its regulatory functions, if the complainant is dissatisfied with the investigation of the complaint or with the reported outcome of the



investigation, he may request that the complaint is referred to the LME's independent Complaints Commissioner.

13 The LME's independent Complaints Commissioner has the following powers:-

- (a) to call on all appropriate documentation from all involved parties to form a view on the complaint;
- (b) to permit and/or request the complainant and the LME to provide written submissions in relation to any specific matters that arise;
- (c) to make further requests of all relevant parties and/or take whatever action is considered appropriate which might assist in considering the complaint;
- (d) to conduct the consideration of the issues as is seen fit;
- (e) to report on the result of his investigation to the LME and the complainant;
- (f) to make a recommendation, if appropriate, that the Exchange makes a compensatory payment to the complainant and/or remedies the matter complained of;
- (g) to be able to publish his report (or any part of it) if he considers that it (or any part) ought to be brought to the attention of the public;
- (h) to require the LME to inform the Complaints Commissioner and the complainant of the steps which it proposes to take in response to his report; and
- (i) to require the LME to publish the whole or a specified part of its response to the Complaints Commissioner.

1 December 2001



LONDON METAL EXCHANGE

-----From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 02/150 : A150 : R015
Date: 15 April 2002
Subject: **MATCHING PERIODS FOR AND TRADE TIMES OF TRADES
ENTERED INTO THE LME MATCHING AND CLEARING SYSTEM**

Introduction

The attached notice contains the times that should be used to enter trades into the LME matching and clearing system (matching system). This notice replaces notice 01/034: A034: R003.

Significant changes

The notice reflects changes in the LMEMS to allow the input of the time codes for the extended kerb and to remove some ambiguity from the previous notice.

Effective date

The attached rules will take effect from the 22 April 2002.

A WHITING

cc: Board directors

TIME BANDS FOR INPUT OF METAL AND LME TRADES TO THE LME MATCHING AND CLEARING SYSTEM

The following should be noted:

- All times entered into the LME matching and clearing system (matching system or LMEMS) should be UK time.
- Any trades executed in other time zones should be converted into UK time and equivalent date before entry into the matching system.
- Execution times should be recorded on source documentation.

TIME BANDS FOR METAL TRADES

1 Ring and kerb trades and trades basis ring and kerb prices

- a. Trades between category 1 members conducted **in the rings and kerbs** at current market or average prices must be input and matched within 30 minutes of the end of the relevant ring or kerb. The time of trade entered into the matching system will be denoted by the relevant time code representing the execution time:

- R1: ring 1
- R2: ring 2
- R3: ring 3
- R4: ring 4
- K1: kerb 1
- K2: kerb 2
- K3: kerb 3
- K4: kerb 4
- K5: kerb 5
- K6: kerb 6
- K7: kerb 7
- K8: kerb 8
- K9: kerb 9
- K10: kerb 10

If a trade is conducted on exchange premises between category 1 members or between a category 1 member and another member or customer, **but not in the relevant ring or kerb** then, if it is not a basis trade (see b. below), it should be regarded as a 'timed trade' and dealt with in accordance with section 2 below and the R&K time codes not used. The use of the R & K time codes is restricted to the following trade types, DD, AD, CR and CT. The kerb times are set out in appendix 1.

b. If a category 1 member obtains a price basis a ring or kerb for a category 2, 3 or 4 member or its customer then the time codes, representing the execution time, to be used by both members and the category 1 members' client cross are:

- C1: ring 1
- C2: ring 2
- C3: ring 3
- C4: ring 4
- D1: kerb 1
- D2: kerb 2
- D3: kerb 3
- D4: kerb 4
- D5: kerb 5
- D6: kerb 6
- D7: kerb 7
- D8: kerb 8
- D9: kerb 9
- D10: kerb 10

Trades (other than client crosses) using the C&D time codes should be matched as timed trades in the appropriate time band (see 2 below). If a trade is conducted on exchange premises between a category 1 member and another member or customer, **but not basis the relevant ring or kerb** then it should be regarded as a 'timed trade' and dealt with as set out in section 2 below and the C&D time codes not used. The use of the C & D time codes is restricted to the following trade types, DD, DC, AD, DA, CR and CT. The kerb times are set out in appendix 1.

Category 2, 3 or 4 members trading with customers or with members other than category 1 members, should record the trade in the matching system using the time of execution not the time codes listed above.

2 Timed trades

Timed trades are:

- Exchange Contracts executed by category 1 members **outside of the appropriate ring or kerb sessions** at current market or average prices (for give-ups see 5 below).
- **All** Exchange Contracts executed by category 2 & 3 members, other than those executed with category 1 members basis the appropriate ring or kerb sessions (see 1 above) at current market or average prices (for give-ups see 5 below).

The execution time of all timed trades should be entered into the matching system.

Time of trade	Latest time for matching
19:30:01 – 24:00 (prior business day)	10:00
00:00:01 – 07:30	10:00
07:30:01 – 10:30	11:30
10:30:01 – 11:40	12:30
11:40:01 – 13:30	14:00
13:30:01 – 15:10	16:00
15:10:01 – 17:00	18:00
17:00:01 – 18:00	19:00
18:00:01 – 19:30	20:00

3 Cash today (TOM) trades

Cash today trades are those arising:

- In relation to Exchange Contracts entered into in the period between 19:30:01 hours on one business day and 12:30 hours on the next business day for prompt date the first settlement business day after the latter business day:
- In relation to contracts other than Exchange Contracts entered into in the period between 19:30:01 hours on one business day and 12:20 hours on the next business day for prompt date the first settlement business day after the latter business day.

All cash today trades must be matched/registered by 13:30. The time of execution for these trades should follow the styles outlined in 1&2 above for Exchange Contracts and 4 below for Client Contracts.

4 Client Contracts (client crosses)

A Client Contract is a contract between a clearing member and any other person other than another clearing member or a contract between a member who is not a clearing member and any other person. All Client Contracts should be registered in the matching system. Those executed between 00:00:01 and 19:30 must be registered by 20:00 on that day. A Client Contract (this includes contracts executed for customers of category 4 members) executed by a category 1 member basis a ring or kerb price should be registered using the C&D time codes as described in 1 above.

Client Contracts executed between 19:30:01 and 24:00 must be registered by 10:00 on the next available business day.

Time bands for Client Contracts

Time of trade	Latest time for registration
00:00:01 – 19:30 day 1	20:00 day 1
19:30:01 – 24:00 day 1	10:00 day 2 i.e. next available business day

5 Give-ups

A give-up transaction is one where a customer executes a trade with one member and then requests that it is given-up for clearing to another member. These transactions should be conducted in accordance with notice 00/383: A376: R010 and 01/402: A402: R011. The time of trade that the executor enters into the LMEMS will be the actual trade execution time. The clearer should match the trade using the same trade date as that alleged by the executor. The time of trade of the clearer will be the time the trade is entered into the LMEMS. The clearer should keep an adequate audit trail to demonstrate the timely processing of its customers instructions. The same trade date should also be used for the client cross. The public reference field is a matching field for give-ups to ensure that they are for common customers. The only exception to this process is for late give-ups i.e. those matched on trade date plus three (see below) where the clearing broker should match the trade date supplied by the executor.

All give-ups must be input and matched by 20:00 on trade day plus two. The relevant Client Contract should be registered in accordance with 4 above.

The matching system will reject attempts to match a give-up trade, using the normal trade types after 20:00 on trade day plus one. If members have and document valid reasons, they can match give-ups, up to close of business on trade day plus two, using the appropriate trade type described in notice 01/402: A402: R011 and detailed below. If the members have not been able to match the trade by 20:00 on trade day plus two **both members** should submit faxes to the LME regulation and compliance department, for the attention of member surveillance (020-7264-5513) or email (membersurveillance@lme.co.uk) setting out the details of the transaction and the reason why the trade has not matched, providing supporting evidence as appropriate. The LME will then determine if it will allow the trade to be entered into the LMEMS. **Members must not match the trade without prior authorisation.**

Time bands for give-up trades

Time of trade	Latest time for matching/registration
00:00:01 - 19:30 trade day	20:00 trade day plus 2
19:30:01 - 24:00 trade day	20:00 trade day plus 2

Matching/registering give-up trades

Match period/day	Trade types to be used
07:30:01-20:00 trade date	GD/UD GA/UA GV/UV Cross DG/PG/PS/PN
07:30:01-20:00 trade date+1	GD/UD GA/UA GV/UV Cross DG/PG/PS/PN
07:30:01-20:00 trade date+2	GL/UL Cross GL/PL/PS/PN
trade date+3 and thereafter	Contact LME

6 OTC contracts brought on-exchange

OTC contracts should be brought on-exchange in accordance with notice 01/232: A232: R07 and notice 01/402: A402: R011. The Exchange contract and the cross representing the new Client Contract must be registered on the day the contract is brought on-exchange. The trade date and time will be the date that the contract is brought on-exchange. Where appropriate, members should have a sufficient audit trail to demonstrate the timely processing of their customer's instructions.

7 Transfers, clearing switches and metal position swaps

Transfers are the movement of a customer position from one member to another. A clearing switch is the movement of a customer position between members at the relevant official settlement price. A metal position swap is the transfer of positions between members for different customers, both of which are physical users of metal and have offsetting physical trades. These transactions should be effected in accordance with notice 01/232: A232: R07 and 01/402: A402: R011.

These transactions should be input and matched within 30 minutes of agreement by all parties. The public reference field is a mandatory matching field for transfers and clearing switches to ensure that they are for common customers. The time entered into the matching system should be recorded on supporting documentation and should demonstrate timely processing of the customers' instructions.

8 Currency conversions

A currency conversion is the conversion of a contract from one LME approved currency to another. Members should follow the procedures set out in notice 01/402: A402: R011.

Currency conversions must be entered into the matching system on a timely basis. A currency conversion cannot be used to circumvent other rules: thus conversions into Japanese Yen cannot be conducted for 'cash today' (TOM) trades. The time of trade should be the time the conversion is carried out. Members should be able to demonstrate that they carried out the customers' instructions on a timely basis.

9 Corrections

Corrections should be made to LME contracts in accordance with notice 01/402: A402: R011.

Corrections should be entered into the matching system on a timely basis. The date and time of trade should be that of the original transaction being corrected.

10 Declaration of LME client options

Futures positions are automatically generated upon the declaration of an Exchange option in accordance with the LME rules. Options for non-segregated customers need to be declared by members and the resulting future registered in the matching system using the trade type DZ in accordance with notice 01/402: A402: R011.

Please note that options traded on the business day before their last declaration day **must** be matched/registered in LMEMS by 17:00 on that business day.

The Client Contracts should be registered on a timely basis in accordance with 4 above. The trade date should be the relevant option declaration date; the time of trade should demonstrate timely processing.

11 Proxy trades

Proxy trades are those trades matched/registered by clearing members on behalf of an associate broker non-clearing member.

Proxy trades should follow the conventions of non-proxy trades and follow the procedures set out in notice 01/402:A402: R011.

TIME BANDS FOR LMEX

12 Kerb trades and trades basis kerb prices

- a. LMEX trades between category 1 members in kerbs must be input and matched within 30 minutes of the end of the relevant kerb. The time of trade entered into the matching system will be denoted by the relevant time code representing the execution time:

- K1: kerb 1
- K2: kerb 2
- K3: kerb 3
- K4: kerb 4
- K5: kerb 5
- K6: kerb 6
- K7: kerb 7
- K8: kerb 8
- K9: kerb 9
- K10: kerb 10

If a trade is conducted on exchange premises between category 1 members or between a category 1 member and another member or customer, **but not in the relevant kerb** then if it is not a basis trade (see b. below), it should be regarded as a 'timed trade' and dealt with as set out in section 13 below and the K time code not used. The use of the K time codes is restricted to the following trade types, DD, CR and CT. The kerb times are set out in appendix 1.

- b. If a category 1 member obtains a LMEX price basis a kerb for a category 2, 3 or 4 member or its own customer then the time codes, representing the execution time, to be used for both members and the client cross are:

- D1: kerb 1
- D2: kerb 2
- D3: kerb 3
- D4: kerb 4
- D5: kerb 5
- D6: kerb 6
- D7: kerb 7
- D8: kerb 8
- D9: kerb 9
- D10: kerb 10

Trades using the D time codes should be matched as timed trades in the appropriate time band (see 13 below). If a trade is conducted on exchange

premises between a category 1 member and another member or customer, **but not basis the relevant kerb** then it should be regarded as a 'timed trade' and dealt with as set out in section 13 below and the D time codes not used. Trades using the D time codes should be matched as timed trades in the appropriate time band (see 13 below). The use of the D time codes is restricted to the following trade types DC, CR and CT. The kerb times are set out in appendix 1.

13 Timed trades

Timed trades are Exchange Contracts as defined in 2 above. The execution time of all timed trades should be entered into the matching system.

Time of trade	Latest time for matching
19:30:01-24:00(prior business day)	10:00
00:00:01 – 07:30	10:00
07:30:01 – 10:30	11:30
10:30:01 – 11:40	12:30
11:40:01 – 13:30	14:00
13:30:01 – 15:10	16:00
15:10:01 – 17:00	18:00
17:00:01 – 18:00	19:00
18:00:01 – 19:30	20:00

14 Client Contracts (client crosses)

A Client Contract is defined in 4 above. All Client Contracts should be registered in the matching system. Those executed between 07:30:01 and 19:30 must be registered by 20:00 on that day. A Client Contract (this includes contracts executed for category 4 members) executed by a category 1 member basis a ring or kerb price should be registered using the C&D time codes as described in 1 above. Client Contracts executed between 19:30:01 and 07:30 (next day) must be registered by 10:00 on the next available business day.

Time bands for Client Contracts

Time of trade	Latest time for registration
19:30:01-24:00(prior business day)	10:00
00:00:01 – 07:30	10:00
07:30:01 – 10:30	11:30
10:30:01 – 11:40	12:30
11:40:01 – 13:30	14:00
13:30:01 – 15:10	16:00
15:10:01 – 17:00	18:00
17:00:01 – 18:00	19:00
18:00:01 – 19:30	20:00

15 Give-ups

A give-up transaction is defined in 5 above. These transactions should be conducted in accordance with notice 01/402: A402: R011 and 00/383: A376: R010. The public reference field is a matching field for give-ups to ensure that they are for common customers.

Give-ups transacted between 07:30:01 and 19:30 must be input and matched by 20:00 on that day. Give-ups transacted between 19:30:01 and 07:30 must be matched by 10:00 on the next available business day (trade day plus 1). The relevant Client Contract should be registered in a similar manner.

Attempts to match a give-up trade after 20:00 trade day or 10:00 on trade day plus one (as appropriate) will be considered a breach of LME rules

The executing member should enter the time of execution of the give-up as the time of trade. The clearer should match the trade using the same trade date as that alleged by the executor. The time of trade of the clearer will be the time entered into the LMEMS. The clearer should keep an adequate audit trail to demonstrate the timely processing of its customers instructions. The trade date and time of trade should also be used for the client cross.

The time bands for give-ups are:

Time of trade	Latest time for matching
19:30:01-24:00(prior business day)	10:00
00:00:01 – 07:30	10:00
07:30:01 – 10:30	11:30
10:30:01 – 11:40	12:30
11:40:01 – 13:30	14:00
13:30:01 – 15:10	16:00
15:10:01 – 17:00	18:00
17:00:01 – 18:00	19:00
18:00:01 – 19:30	20:00

16 Second Wednesday (expiry day)

On the second Wednesday of each month (expiry day), LME futures contracts for that date can only be traded up to 17:00, these trades must be matched/registered by 18:00. **Thereafter, it will be a serious breach of LME rules to match, make any alterations or corrections to that LME contract. Please note that on LME only intra-day corrections will be allowed. These time bands relate to both Exchange and Client Contracts.**

Time of trade	Latest time for registration
17:00:01-24:00(prior business day)	10:00
00:00:01 – 08:00	10:00
08:00:01 – 10:30	11:30
10:30:01 – 11:40	12:30
11:40:01 – 13:30	14:00
13:30:01 – 15:10	16:00
15:10:01 – 17:00	18:00

For LME option contracts, the last trading day is the prompt date for that index option i.e. second Wednesday of each month. Please note that this is different to LME base metal options where the last trading day is the business day preceding the last declaration day. On the prompt date, the LME option for that date can only be traded up to 16.35. **These trades must be matched/registered by 18.00. Thereafter, it will be a serious breach of LME rules to match, make any alterations or corrections to that LME option. Please note that on LME only intra-day corrections will be allowed. These time bands relate to both Exchange and Client Contracts.**

Time of trade	Latest time for registration
17:00:01-24:00(prior business day)	10:00
00:00:01 – 08:00	10:00
08:00:01 – 10:30	11:30
10:30:01 – 11:40	12:30
11:40:01 – 13:30	14:00
13:30:01 – 15:10	16:00
15:10:01 – 16:35	18:00

17 Extensions to the matching system

Any requests for extensions of the matching system beyond the 13:30 close for 'cash today' transactions should be submitted to the LME regulation and compliance department by 13:15.

The matching system closes at 20:00. The LME regulation and compliance department will not authorise extensions to the matching system after this time.

MARGIN

The LMEMS is open from 07:30 until 20:00. However, members are reminded that the LCH cannot request additional margin after 18:30. Members should note that the trade suspension function in LME matching will continue to operate in the normal way up to the close of trade input i.e. 20:00. Members are reminded it is their responsibility to ensure that they have sufficient surplus cover with the LCH prior to the matching/registration of trades that may be suspended. If sufficient cover is not available the trades will not be matched/registered and members will be required to re-submit the trade on the next business day.

TIMELY BASIS

The LME requires that members process their customers' instructions on a timely basis. The LME would look to members to explain why instructions had not been acted upon if the delay between receipt and action exceeded a reasonable period. What determines a reasonable period depends on the specific customers' instructions. The LME would consider each circumstance and whether the members' actions were appropriate i.e. did the member's action result in a failure to meet a specific deadline such as that for processing cash today. In summary, when interpreting what constitutes a timely basis, the LME would look at the customer's instructions and the appropriateness of the member's response to that instruction.

APPENDIX 1**SCHEDULE OF KERB TRADE TIMES**

Kerbs	Trades with RDM's	Trades with Non-RDM's
13:15-13:30	K 1	D 1
13:31-13:45	K 2	D 2
13:46-14:00	K 3	D 3
14:01-14:15	K 4	D 4
14:16-14:30	K 5	D 5
14:31-14:45	K6	D6
14:46-15:00	K7	D7
15:01-15:10	K8	D8
16:35:16:45	K9	D9
16:46-17:00	K 10	D10



LONDON METAL EXCHANGE

CLIENT TRADING ON THE LONDON METAL EXCHANGE

GUIDANCE

9 JULY 2003

Introduction

1. This guidance is directed at LME broker members and their staff. It deals with client trades and how those client trades interact with related exchange trades.

Definitions

2. For the purposes of this guidance, the following terms have the following meanings:-

- (a) **Broker:** means a category 1, 2 or 4 member of the LME;
- (b) **Client Contract:** means an LME contract between a Broker and a client¹;
- (c) **Exchange Contract:** means an LME contract between two Brokers²;

Background

3. A dispute between Brandeis (Brokers) Limited and Mr Herbert Black³ has received a certain amount of publicity. On 20 December 2001, the SFA⁴ issued board notice 609, following the settlement of disciplinary proceedings against Brandeis in connection with its dealings with Mr Black in the LME's copper market during 1996 and 1997. That board notice summarised the

¹ This definition is a simplification of the definition in the LME rules and regulations. Contracts between category 4 members and category 1 or 2 members are Client Contracts not Exchange Contracts. Category 4 brokers are not members of the London Clearing House, which therefore does not clear their LME contracts.

² This definition is a simplification of the definition in the LME rules and regulations. In respect of category 4 members, see footnote 1 above. Contracts between associate trade clearing members (category 3) and category 1 or 2 members are Exchange Contracts not Client Contracts. Category 3 members are members of the London Clearing House, which clears their LME contracts.

³ The dispute involved Mr Black and two companies controlled by him; for the purposes of this guidance, references to Mr Black include these two companies.

⁴ The Securities and Futures Authority whose functions have been taken over by the Financial Services Authority since December 2001.

business relationship between Brandeis and Mr Black and the duties owed by Brandeis.

4. Brandeis and Mr Black were also engaged in an arbitration under the LME arbitration regulations⁵ as a result of these dealings in the LME's copper market. This arbitration became public when Brandeis appealed against two awards made by the arbitrators. That appeal was heard in the High Court before Mr Justice Toulson, who issued his judgment on 25 May 2001⁶. In this judgment Mr Justice Toulson quoted from the arbitration awards and analysed the business relationship between Brandeis and Mr Black and the duties owed by Brandeis. Extracts from this judgment are set out in Appendix B to this guidance.

5. The SFA issued guidance on the customer relationship and other conduct of business requirements for firms engaged in metals business (SFA board notice 578) on 16 March 2001. The LME has issued guidance on the structure of, and order execution on, the LME. This was reissued on 12 October 2001 as LME notice 01/385.

6. The SFA board notices and the judgment of Mr Justice Toulson in the arbitration appeal cover a range of issues⁷. This guidance concentrates on:-

- (a) the nature of an LME contract;
- (b) the types of transaction between a Broker and a client;
- (c) client expectations;
- (d) dual capacity;
- (e) competing orders; and
- (f) potential abuse of the Broker/client relationship.

LME contracts

7. The LME definition of "Contract", the Trading Regulations and the Contract Regulations⁸ provide that an LME contract must have the following characteristics:

- (a) it must be a contract between only two parties;
- (b) at least one of those parties must be a Broker⁹;

⁵ Part 8 of the LME rules and regulations.

⁶ Lloyd's Law Reports Part 7 [2001] Vol 2, pages 359 to 372.

⁷ A full list of these documents is set out in Appendix A to this guidance.

⁸ Part 1 (definitions), regulation 2.1 of part 3 (trading regulations), & regulation 2.1 of part 4 (contract regulations) of the LME rules and regulations.

⁹ See paragraph 2 and foot notes 1 & 2 above.

- (c) each party must be acting as a principal; and
- (d) in the case of a metal futures contract, the obligations to take and to deliver metal must remain open until the prompt date¹⁰.

8. An LME metal futures contract is a promise by one party to deliver metal on the prompt date and a promise by the other party to pay for that metal on the prompt date. An LME metal options contract is a promise by one party to enter into an LME metal futures contract and a promise by the other party to pay the premium for being able to choose whether or not to enter into that metal futures contract¹¹. For each type of contract there can only be two persons who make each of these promises.

9. Each person making one of the two promises must be acting for himself and not as agent for another person. This is what is meant by an LME contract being a principal-to-principal contract. This applies both to Exchange Contracts and Client Contracts. Other markets permit the parties to their contracts to act as agents for third parties, which is why they are called agency markets.

10. However, the principal-to-principal nature of an LME contract does not prevent either of the parties using an intermediary to agree the terms of that contract. For example, in a Client Contract the Broker may use an intermediary to communicate with his client. Similarly, a client may use an intermediary to communicate with his Broker. In both cases the Broker and the client will be the parties to the LME contract and will be fully responsible for the promises that they have agreed to make through their intermediaries¹² although there may be additional responsibilities owed by or to the intermediaries.

11. The Trading Regulations and the Contract Regulations set out a number of terms that apply to LME contracts, which cannot be changed. For example, the requirements for settlement and delivery, resolving disputes and default. These compulsory terms are among the benefits of trading on an exchange: standardised contracts. In addition to this, the general law of contract has a number of requirements that must be in place before a valid contract can exist. One of these is certainty.

12. At the time that a contract is made, the parties must be certain about the essential terms. The price is one of these essential terms. However, certainty about the price does not just mean the cash figure; it also includes certainty about how the price will be calculated. For example, a trade where

¹⁰ The LME term for the delivery date.

¹¹ LME metal options contracts are not options on the relevant metal but are options on a futures contract for that metal. The prompt date for that futures contract is agreed when the option is written. The option may be exercised at any time up to expiry but the resulting futures contract will always be for the agreed prompt date.

¹² Depending on the extent of the intermediaries' authority, they may be the agents of the Broker or the client. The significance is that an agent may bring about an LME contract between his principal and someone else but the agent cannot be a party to that contract.

the price will be equal to or based on a subsequent official LME price has sufficient certainty. How the price will be calculated is certain. The price becomes known once the LME publishes the relevant official price. The time that this contract is made is when the parties agree the terms, not when the price subsequently becomes known.

Types of transaction

13. Brokers are often referred to as 'market makers'. In other markets this term has a very precise meaning. It usually means that the 'market maker' is obliged to quote firm two-way prices to the market. The LME rules and regulations do not oblige Brokers to quote firm two-way prices to the market. Brokers are obliged to enter into the LME's market data system indicative bids and offers at which they are prepared to trade with customers of the market. These quotes are not firm quotes¹³. Brokers do not have to quote two-way prices to other Brokers. LME market practice is to call a Broker a 'market maker' if he is prepared (as opposed to obliged) to quote firm bid and offer prices to his clients.

14. There are two basic ways in which Client Contracts arise. The first is the result of the client asking the Broker for a price and then choosing to trade on the basis of that price. The client may get price quotes from a number of Brokers before deciding to trade. It is usual for a client to ask a Broker for his bid and offer price before the client indicates whether he is a buyer or seller. The second basic way in which a Client Contract arises is the result of the client placing an order with the Broker to deal in the market.

15. The LME guidance on the structure of and order execution on the LME¹⁴ identifies a number of order styles common on the LME. These all relate to clients' orders to Brokers to deal in the market. In other words, not the first way of executing a Client Contract but the second way. The overriding requirement in executing an order is that the Broker should be clear about what the client has asked him to do and the client should be clear about what the Broker has undertaken to do.

16. The Broker and client should be clear about how the order will be executed. It could involve the Broker trading metal in the market before trading that volume of metal back-to-back with the client. This would result in the Broker having an Exchange Contract for the same number of lots as the back-to-back Client Contract. This is not always the case. Sometimes an order may require the Broker to execute the Client Contract based on a market price without necessarily having to trade that, or any, amount of metal in the market. For example, an order based on the official prices published by

¹³ Regulation 4 of part 3 (trading regulations) of the LME rules and regulations sets out Brokers' obligations to input indicative current bid and offer prices and, in relation to Carries, price spreads, for all types of Contract into the LME's electronic price-reporting service. LME notice 99/324, dated 22 July 1999 sets out the LME board's policy on price dissemination and the terms and conditions that apply to Brokers who input prices into the LME's electronic price-reporting service.

¹⁴ LME notice 01/385, dated 12 October 2001.

the LME at the end of the second ring. In executing this kind of order the Broker may have made clear to his client that he may aggregate client orders and may or may not trade any or all of that volume in the ring.

17. In his Brandeis judgment, Mr Justice Toulson quoted the arbitrators' descriptions of the two types of LME transaction. These quotes are repeated in Mr Justice Toulson's judgment set out in extract number 1 in Appendix B. The trading which was the subject of the arbitration was almost exclusively of the second type, execution of orders in the market. Mr Justice Toulson's comments, therefore, referred to that type of transaction and not to the first type, direct sales or purchases. Similarly, SFA board notice 578¹⁵ identified the second type of transaction as being an "order" for the purposes of the SFA conduct of business rules.

Client expectations

18. A client's expectations of how a Broker will execute his order will depend on the understanding between the client and the Broker. This understanding can arise in a number of different ways. A Broker's standard terms and conditions of business will set out the basis on which he is prepared to deal with clients. When executing any particular order the standard terms and conditions will apply unless he and the Client agree to vary them. Traditionally, the law has recognised that established customs of a market can apply to transactions in that market. However, these days it would be safer for a Broker to set out in his terms and conditions any customs that he wishes to rely on.

19. The LME rules and regulations and the FSA's rules¹⁶ also govern the understanding between a client and his Broker when entering into an LME contract. As discussed above in paragraph 11, certain contractual terms that are set out in the LME Trading Regulations and Contract Regulations apply to LME contracts and cannot be changed.

20. The guidance in SFA board notice 578 drew attention to the fact that a number of SFA's conduct of business rules applied where a Broker had received a client's order. The ones highlighted in the guidance were 5-36 (dealing ahead of publications), 5-37 (customer order priority), 5-38 (timely execution), 5-39 (best execution), 5-40 (timely allocation), 5-41 (aggregating orders) and 5-42 (fair allocation)¹⁷.

21. The guidance went on to draw attention to the SFA definition of 'order', which is repeated here for convenience:

¹⁵ SFA board notice 578, dated 16 March 2001: guidance on the customer relationship and other conduct of business requirements for firms engaged in metals business.

¹⁶ The FSA's rules came into force in December 2001. Prior to that date, the SFA's rules governed the relationship between a Broker and his client.

¹⁷ The application of some of these rules depends on the status of the client and the contractual terms agreed between the Broker and the client. For example certain clients may chose to opt out of best execution.

“order”, in relation to an order from a customer, means -

- (a) an order to a *firm* from the *customer* to effect a transaction as *agent*;
- (b) any other order to a firm from the *customer* to effect a transaction in circumstances giving rise to similar duties as those arising on an order to effect a transaction as *agent*; or
- (c) a decision by a *firm* in the exercise of discretion for the *customer*;

22. The point that the guidance was trying to highlight was that, although the first part of the definition refers to effecting a transaction as agent, the second part of the definition covers effecting a transaction where the firm is not an agent. The definition recognises that there is a difference between effecting an order as agent and effecting an order when the Broker is not an agent. Otherwise the definition would not have identified the two circumstances separately. This is not always appreciated.

23. Nothing in the SFA guidance was incompatible with LME market practice. When a Broker accepts an order to deal in the market (as opposed to a direct sale or purchase) he will owe duties that are similar to those of a broker in an agency market. For example, an order to deal at ‘best’¹⁸, means that the Broker has undertaken to use his best endeavours to execute the client’s order. For a large order, this may involve the Broker deciding how best to work the volume of metal required. In those circumstances the client is relying on the Broker to act in the client’s best interests, which is a duty similar to the duty an agent would have when carrying out the instructions of his principal.

24. The Brandeis case dealt with the particular relationship between Brandeis and Mr Black. Mr Justice Toulson illustrated the nature of this relationship by quoting a passage from the arbitration award which repeated a telephone conversation between Mr Black and a Brandeis employee. This is set out as extract number 2 in Appendix B.

25. Mr Justice Toulson also commented on the nature of the duties owed by Brandeis to Mr Black. He recognised that Brandeis was not Mr Black’s agent but he accepted that Brandeis owed Mr Black fiduciary duties. It had been put to the judge by counsel for Brandeis that a better description of the duty that Brandeis owed was that it “*should act fairly towards the client and itself in any conflict of interest between them*”. His assessment of that submission was that:

If “fairness” is taken to include that the broker should not take advantage of an order from the client to make an undisclosed profit for

¹⁸ See page 6 of the LME guidance on the structure of and order execution on the LME; notice 01/385, dated 12 October 2001.

itself, there is no conflict between such a term and the form of fiduciary obligation to which I have referred.

This quote is taken from a larger quote set out as extract number 3 in Appendix B.

26. When a Broker accepts an order from a client, he is being asked to act for the benefit of that client. The duty that the Broker owes, whether described as “agency-type duty”, “fiduciary duty” or “duty of fairness”, is to act in the best interests of his client and not to make an undisclosed or secret profit.

Dual capacity

27. Dual capacity in the metal markets arises where a Broker both trades for his own account and accepts orders from clients. Nothing in the Brandeis judgment or the FSA rules prevent dual capacity. Own-account trading has two aspects. First, the Broker may enter into Client Contracts as the result of quoting prices to clients, who then choose whether or not to trade¹⁹. Secondly, the Broker may retain those positions on his books or offset all or part of them by trading with other Brokers or clients. It is in the nature of futures contracts that time is a factor in any offsetting trades. After entering into a Client Contract, the Broker has until the prompt date to decide whether or not to offset the trade in whole or in part. In buying and selling metal over time, the trades that can be said to offset each other may change over that period. When a Broker accepts an order to trade in the market he agrees to take certain actions on behalf of his client. Where he also trades in the market for his own account, he needs to consider whether any conflict may arise between the interests of that client and his own interests and, if so, how to manage that conflict.

28. Conflicting interests arise frequently and need to be managed. The tools for managing conflicts of interest include: avoiding particular situations that give rise to a conflict; creating Chinese walls between different business areas; and disclosure. Where a Broker discloses to a client that there is potential for a conflict of interest, he also needs to disclose how he proposes to manage that conflict.

29. In his judgment in the Brandeis case, Mr Justice Toulson identified that the law regarded it as wrong for Brandeis, when accepting orders from Mr Black to trade in the market, to place its interests above that of Mr Black or to make a profit from its fiduciary position without Mr Black’s “*informed consent*”.²⁰ For example, in the cases of mis-pricing of Mr Black’s orders, it was accepted that Brandeis could make a profit from the trades but only that profit that it had disclosed to, and agreed with, Mr Black. Brandeis had disclosed to Mr Black that Brandeis would profit from his orders by charging an agreed commission; Brandeis had not disclosed to Mr Black that it would

¹⁹ See paragraph 14 above.

²⁰ See the last paragraph of extract number 3 in Appendix B.

also apply a mark-up or mark-down to the price at which Brandeis traded in the market. This undisclosed mark-up or mark-down was a secret profit.

30. Similarly, it would be wrong for a Broker to trade for his own account without disclosing that fact to clients from whom he accepted orders to deal in the market. In making the disclosure, the Broker should also make clear how the Broker proposes to manage any conflict between own-account trading and executing client orders. The FSA rules on customer priority and timely execution deal with some of these issues²¹.

31. Where a customer's order is likely in the Broker's opinion to move the market, two different kinds of issue arise. The first is the general law issue of disclosure and the second is possible market abuse. In his judgment, Mr Justice Toulson discussed the first of these. He identified the situation where Brandeis, after it had received a large order from Mr Black that was likely to move the market, dealt for its own account before executing Mr Black's order. He said that:-

*... for Brandeis to deal ... for its own book ...[in these circumstances]... involved a misuse of confidential information and ... involved or was likely to involve making an undisclosed profit for itself by taking advantage of the state of the market prior to completion of the execution of [Mr Black's] order. Moreover, I cannot see that such conduct was made permissible by anything in the terms of the parties' contracts. In particular, I consider that the "conflicts of interest" paragraph in Brandeis's terms of business letter would need to be a good deal more specific if it was intended to authorise such conduct.*²²

32. Mr Justice Toulson was only dealing with Brandeis's behaviour in the context of its dispute with Mr Black. The judge was not commenting on whether, in taking advantage of its knowledge of Mr Black's order, Brandeis was committing market abuse under the Financial Services and Markets Act 2000. The FSA's code of market conduct²³ gives guidance on what behaviour based on misuse of information constitutes market abuse.

33. Mr Justice Toulson also said that the same issues arose where a Broker accepts orders to deal in the market and has discretionary clients. The quote in paragraph 31 above is set out in full in extract number 4 in Appendix B. The full quote applies the principle of not dealing ahead of executing an order equally to a Broker's dealing for his own-account and his dealing for discretionary clients. Dealing for non-discretionary clients ahead of an order is dealt with in the next section, competing orders.

Competing orders

²¹ COB 7 in the FSA handbook sets out the FSA's dealing rules.

²² See full quote in first paragraph of extract number 4 in Appendix B.

²³ The FSA's code of market conduct is made under section 119 of the Financial Services and Markets Act which requires the FSA to produce a code giving guidance on what does and does not amount to market abuse under the Act.

34. Competing orders do not arise because of dual capacity but are a natural consequence of a Broker accepting orders from more than one client. It follows that the Broker needs to manage the competing interests of those clients. The FSA's rules on customer priority, timely execution, aggregation and allocation govern how a Broker should deal with client orders²⁴.

35. The general principle is that a Broker should manage client orders fairly. The size of orders has an influence both on what may be possible or fair in the circumstances. For example, aggregating orders may give a number of clients access to a better price than would have been available in the market for each of their orders separately. A large order may need to be worked over time because of thin liquidity in the market.

36. There are circumstances where rules can come into conflict. For example, the requirement to deal with client orders in due turn and the requirement not to disclose confidential client information. This could arise where a Broker receives a small order, that was capable of immediate execution, after receiving a large order that needed to be worked. Mr Justice Toulson considered this particular type of competing order:-

*I do have serious doubts whether the same position [giving priority to a client order over own-account or discretionary dealing] would necessarily apply if after receipt of a large order from a client which was likely to take some time to execute, the broker received an order from another client capable of immediate execution. An unexplained refusal by the broker to accept the order for immediate execution might immediately signal that something major was afoot.*²⁵

37. The judge added that he could “see room for nice arguments about what might constitute dealing “fairly and in due turn” within the meaning of SFA Rule 5.37, depending on the facts of the case”. Unfortunately, the judge did not have to give definite answers to these questions. The case before him involved the conflict between the interests of Mr Black and the interests of Brandeis and its discretionary clients; it did not involve competing client orders. However, the judge appears to have suggested that there are circumstances where a Broker might need to execute a small client order out of turn in order to avoid disclosing that the Broker was in the process of working a large client order. The judge also appears to have suggested that dealing with competing client orders, fairly and in due turn, might in certain circumstances require the exercise of judgement.

Abuse

38. The Brandeis case, as reported, concentrated on whether or not Brandeis abused its position as Mr Black's Broker. Mr Justice Toulson's judgment analyses how Brandeis dealt with Mr Black's orders. It discusses whether any abuses took place and then discusses how those abuses could

²⁴ COB rules 7.4, 7.6 & 7.7 in the FSA handbook.

²⁵ Second paragraph of extract number 4 in Appendix B

best be described. The SFA board notice 609²⁶ sets out the misconduct giving rise to disciplinary proceedings against Brandeis and the outcome of those proceedings.

39. The descriptions in both make clear that abuse or misconduct took place. Whether there is full agreement on which abuses or misconduct should be described as “mis-allocation”, “mis-pricing”, “front-running” or “misuse of confidential information” is not important; the actions of Brandeis in the circumstances were clearly wrong²⁷. See extracts number 5, 6 & 7 in Appendix B.

40. One analysis might be that once Brandeis had received a large order from Mr Black it was in possession of confidential information that should only be used for the benefit of Mr Black. As a consequence:-

- (a) other client orders that Brandeis had *already* received from clients ought to have continued to be executed;
- (b) trading decisions that Brandeis had *already* taken for its own account or for discretionary customers should have continued to be effected;
- (c) subsequent client orders should have been dealt with fairly and in due turn²⁸ unless a delay in their execution would have disclosed Mr Black’s intentions; and
- (d) no subsequent decisions should have been made to trade for Brandeis’s own or discretionary customers’ accounts.

41. The point at subparagraph 40(b) above needs some explanation. Decisions that were made before, and without the knowledge of, Mr Black’s large order could still have been effected after Mr Black had given his large order. However, unless Brandeis had been able to demonstrate that the decisions were made before the order was received, the subsequent trading for Brandeis’s own or discretionary customers’ accounts would have had all the appearances of subsequent decisions.

Conclusion

42. Neither the findings of the Brandeis judgment nor the SFA’s conclusions set out in board notice 609 undermine the structure of the LME’s markets. They both support the view that there were correct ways for Brandeis to have established and managed its relationship with Mr Black, which it clearly failed to do. Mr Justice Toulson upheld the findings of the arbitration tribunal. That tribunal was made up of experienced arbitrators who

²⁶ SFA board notice 609, dated 20 December 2001.

²⁷ A similar predicament is said to arise with the elephant: it is an animal that is difficult to define but easy to recognise.

²⁸ Fairly and in due turn includes not just order priority but also timely execution and fair allocation.

understood the LME's markets and had no difficulty in recognising that Brandeis clearly abused its position as Mr Black's Broker.

43. The SFA disciplinary proceedings, set out in board notice 609, identified the same clear instances of abuse. It also identified the issue of mismanagement within Brandeis. In respect of the conflicts of interest arising out of dual capacity and competing client orders, the SFA notice points out that Brandeis:-

- *provided no specific training or guidance on the management of such conflicts of interest, particularly in relation to the dual capacity nature of the market;*
- *implemented no specific procedures to manage such conflicts of interest;*
- *undertook no compliance monitoring to ascertain the manner in which conflicts of interest were being managed.²⁹*

²⁹ Quoted from page 3 of SFA board notice 609

APPENDIX A

LIST OF DOCUMENTS

- (a) SFA board notice 578 dated 16 March 2001: SFA guidance on the customer relationship and other conduct of business requirements for firms engaged in metals business;
- (b) High Court judgment on the Brandeis arbitration, dated 25 May 2001, Lloyd's Law Reports Part 7 [2001] Vol 2, pages 359 to 372;
- (c) LME guidance on the structure of and order execution on the LME reissued on 12 October 2001 as LME notice 01/385; and
- (d) SFA board notice 609 dated 20 December 2001: SFA disciplinary action against Brandeis.

APPENDIX B

**EXTRACTS FROM THE JUDGMENT OF MR JUSTICE TOULSON
DATED 25 MAY 2001
IN THE MATTER OF
BRANDEIS (BROKERS) LIMITED
-V-
HERBERT BLACK AND OTHERS**

The following extracts come from the judgment of Mr Justice Toulson. The case in front of him was an application by Brandeis to challenge two arbitration awards issued on 1 December 1999 and 26 January 2000. In giving his judgment Mr Justice Toulson also quoted from the arbitration awards. In these extracts “[Mr Black]” is used to include Mr Black and the two companies controlled by him.

1 TYPE OF TRANSACTION

Mr Justice Toulson’s quote from a section in the first arbitration award headed “*Types of LME transaction.*”

“The two main types of transaction between a client and a broker are the following:-

“(a) Direct purchase or sales

“The client can deal with the broker directly by buying or selling LME metal from or to the broker. In such a case, the client will usually ask the broker to quote a price. If the broker is not told whether the client is buying or selling this would be a two-way price – one price for a purchase, and another price for a sale. The client and the broker can negotiate and then, if they agree, price and other terms, the transaction is concluded, subject to commission.

“(b) Dealings on the market

“The client can give an order to the broker to buy or sell on the market, that is to say on one of the trading rings of the LME or on the kerb or possibly at other times such as the pre-market (i.e. before the morning rings). The client, in authorising the broker to buy or sell on the market, may give a price limit or some other instructions, e.g. that the dealing must take place during a particular ring or, so far as possible, at the price ruling at the close of a ring. In any event, the effect of the order is that the broker is entrusted with the transaction to be carried out on behalf of the client. When concluded, the transaction would form a contract of purchase or sales. This transaction will be a principal to principal deal although the original order places the broker in a position

similar to that of an agent. The broker will earn a commission on the transaction.

“The transactions in dispute, with which we are concerned in the present case [the arbitration], come almost exclusively into the second category. Mr Black was asking Brandeis to deal for him on the market, subject to commission.

“In the second category of dealings, Brandeis will be carrying out Mr Black’s instructions so far as possible and, having concluded a transaction on the market, will pass on this transaction to Mr Black.

“Thus, if Brandeis had bought copper for Black on the LME at a price of, say, \$2630 per ton, that is the price at which Brandeis will sell the material to Black subject to the addition of the broker’s agreed commission.”

2 UNDERSTANDING BETWEEN THE PARTIES

Mr Justice Toulson’s quote from the arbitration award dealing with the relationship between the parties:

“The [arbitration] tribunal is satisfied that the broker owes fiduciary duties particularly when executing a client’s orders on the market ... The client is trusting and relying on the broker to act for him, as Mr Black specifically pointed out to Mr Penfold [a Brandeis employee] in the course of his telephone conversation at 11.56 a.m. on 17 May 1996 when giving his major selling order for execution in the ring:

H Black: Yeh, OK, um obviously I’m trusting you out there.

S Penfold: O yeh, yeh, please.

H Black: Completely

S Penfold: Yes.

and later:

H Black: And ... Um ah ... Please I’m trusting you.

S Penfold: Yeh, sure I know.

H Black: You know you got my ...

S Penfold: Yeh

H Black: You got my heart in your hands.”

3 FIDUCIARY DUTIES

Mr Justice Toulson said that:

“I accept that Brandeis was not an agent for an undisclosed principal in the sense of creating a contractual relationship between [Mr Black] and the other party involved in the back-to-back purchase or sale. But in all other respects the substance of the relationship between Brandeis and [Mr Black] was much more closely akin to that of agency than that of buyer and seller at arms’ length. Agency is by its nature a form of fiduciary relationship; otherwise an agent would be free to make a profit from his position behind the principal’s back. Therefore, looking at the substance of the matter, I conclude that the arbitrators were right to regard the relationship between the party in respect of the transaction with which the arbitrators were concerned as a fiduciary relationship.”

“[Brandeis] submitted that adequate protection would be given to the client against abuse of the broker’s position by the implication of a contractual term that the broker should act fairly towards the client and itself in any conflict of interest between them. If “fairness” is taken to include that the broker should not take advantage of an order from the client to make an undisclosed profit for itself, there is no conflict between such a term and the form of fiduciary obligation to which I have referred. If, on the other hand, the “fairness” test is intended to give a discretion to the broker to make such a profit, in circumstances where in his honest opinion he considers it fair to do so, then it seems to me to be a rather nebulous test and unsatisfactory as a form of protection for [the] client.”

“... I repeat my comments in relation to the “fairness” test put forward by [Brandeis]. The law regards it as unfair and wrong for a fiduciary to place his interest above that of the client ... or to make a profit from his position, without the latter’s informed consent.”

4 COMPETING ORDERS

Mr Justice Toulson discussed the situation where a broker has orders from more than one client:

“So far as counsel were aware, the only instances of Brandeis dealing for other clients before completing orders received from Mr Black related to discretionary accounts operated by Brandeis. For Brandeis to deal in the manner described either for its own book or for a discretionary account involved in my view a misuse of its fiduciary position, both because it involved a misuse of confidential information and because, in the case of dealing for its own book, it also involved or was likely to involve making an undisclosed profit for itself by taking advantage of the state of the market prior to completion of the execution of the client’s order. Moreover, I cannot see that such

conduct was made permissible by anything in the terms of the parties' contracts. In particular, I consider that the "conflicts of interest" paragraph in Brandeis's terms of business letter would need to be a good deal more specific if it was intended to authorise such conduct.

"I do have serious doubts whether the same position would necessarily apply if after receipt of a large order from a client which was likely to take some time to execute, the broker received an order from another client capable of immediate execution. An unexplained refusal by the broker to accept the order for immediate execution might immediately signal that something major was afoot. Moreover, I can see room for nice arguments about what might constitute dealing "fairly and in due turn" within the meaning of SFA Rule 5.37, depending on the particular facts of the case. However, such questions do not presently arise."

5 MIS-PRICING

Mr Justice Toulson quoted the arbitrators definition of mis-pricing as occurring:

"When a broker executing an order in the market on behalf of a client does not give the correct execution to the client, that is to say, as explained in paragraph 5 above, the broker has executed a transaction at one price but, leaving aside commission, has given a different price."

Mr Justice Toulson went on to comment that Brandeis:

"... submitted that the arbitrators were wrong to include allegations of mis-allocation of transactions under the umbrella of mis-pricing and that they fell into this error through a wrong concept of the scope of Brandeis's duties. The arbitrators found that on a number of occasions, after Mr Black had given Brandeis instructions to buy (or sell) a significant number of lots, Brandeis made purchases (or sales) for its own account or a discretionary client account, before completing Mr Black's instructions, at prices more favourable than subsequent purchases (or sales) allocated to [Mr Black]. The arbitrators treated this as a form of mis-pricing on the basis that the earlier purchases (or sales) ought to have been allocated to [Mr Black]."

6 FRONT-RUNNING

Mr Justice Toulson quoted the arbitrators definition of front-running as follows:

"Front-running occurs where, after a broker has taken an order from a client, the broker goes into the market on its own account (or for the benefit of a discretionary or closely associated client) and carries out a transaction for itself or such other client ahead of the client who has given the order. The broker does this because it believes that the

client's order will move the market. The broker wants to deal ahead of the client so as to benefit from the market movement or confer a benefit on others or to avoid a loss on its existing position as a result of the market movement. The client may well suffer loss or damage because the broker's transaction and others which may be triggered by it could move the market against the client."

Mr Justice Toulson commented on this definition by saying that:

"There was obviously a close similarity between this behaviour and the mis-allocation of transactions classified by the arbitrators as a form of mis-pricing. The distinguishing factor according to the arbitrators' approach was whether the execution of the transaction, at the time in which it was carried out, was within Brandeis's authority on behalf of [Mr Black]. So, for example, if Mr Black gave an immediate order to Brandeis to buy X lots either in the pre-market or on the exchange, and Brandeis thereafter made a purchase which it allocated to its own book before completing Mr Black's instruction, the arbitrators treated it as an instance of mis-pricing. If Mr Black gave an instruction to buy X lots during the morning rings, and Brandeis thereafter brought lots for its own book in the pre-market, the arbitrators classified it as front-running."

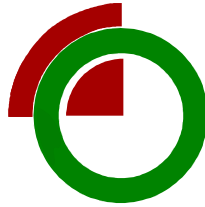
7 MISUSE OF CONFIDENTIAL INFORMATION

Mr Justice Toulson quoted the arbitrators definition of misuse of confidential information as occurring in the following circumstances:

"A broker discloses to outside parties, or uses for its own purposes, confidential information in its possession about a client's positions, transactions or intended transactions. Such information would include information about the client's present own future positions and financial position. Information would not come within this definition if it is in the public domain or merely consists of general gossip or speculation."

Mr Justice Toulson commented that:

"Front-running would be a particular form of misuse of confidential information."



LONDON METAL EXCHANGE

From Executive Director: Regulation and Compliance

To: ALL MEMBERS
Ref: 03/304 : A303
Date: 7 October 2003
Subject: **OMNIBUS ACCOUNTS AND LME CLIENT CONTRACTS**

Members are reminded that an LME client contract is a bilateral contract between an LME category 1, 2 or 4 member ("broker member") and a client. Each LME client contract is separate and creates an obligation whereby the broker member and the client undertake between them that one will buy and the other will sell metal for delivery on the relevant prompt date. The broker member or the client may use an intermediary to bring about the LME client contract but that intermediary cannot have any rights under the LME client contract.

A broker member may, for internal purposes, choose to group together a number of clients who use the same intermediary. However, if those clients are to receive LME client contracts, the broker member must recognise that each client is the broker's counterparty for each LME client contract.

The Exchange recognises that a broker member may deal with an intermediary where either (a) the intermediary's clients are undisclosed, or (b) the intermediary's clients are disclosed but the broker only recognises the intermediary as its client. In those circumstances the broker member must take reasonable steps to ensure that the intermediary makes clear to any of its underlying customers that they cannot be counterparties to LME client contracts. The broker member should ensure that all client and give up agreements clearly reflect this.

A WHITING

cc: Board directors

To: RING DEALING MEMBERS
ASSOCIATE BROKER CLEARING MEMBERS

Ref: 04/087 : A087 : R001

Date: 16 March 2004

Subject: **OBLIGATION TO INPUT PRICES INTO THE LME MARKET
DATA SYSTEM**

Ring dealing and associate broker clearing members are reminded that regulation 4 of part 3 (trading regulations) of the LME rules and regulations creates an obligation on those members notified by the Exchange to input prices into the Exchange's price-reporting service.

2 The Exchange's price-reporting service is an essential part of how the Exchange satisfies its transparency obligations under the Financial Services and Markets Act's recognition requirements for recognised investment exchanges.

3 Regulation 4 and the LME board's policy on price quotations (last published in notice 99/324 dated 22 July 1999) specify that the prices contributed to the Exchange's price-reporting service must indicate the current price at which the contributing member is prepared to trade with users of the market. It follows that when a member inputs into a trading system a bid or offer that is away from the price that it has input into the Exchange's price-reporting service, it should update its contribution to the Exchange's price-reporting service. There is no need to do so for bids or offers input into LME Select as those are automatically reported by the Exchange's price-reporting service.

A WHITING

cc: Board directors



LONDON METAL EXCHANGE

----- Executive Director: Regulation and Compliance

To: ALL MEMBERS, WAREHOUSE COMPANIES AND LONDON AGENTS

Ref: 04/258 : A257

Date: 2 August 2004

Subject: LME COMPLAINTS OFFICER

I have replaced Mr Alan Whiting as the LME's complaints officer.

The LME's complaints procedures remain unchanged and are set out in LME notice 01/492 : A492 : W83 dated 17 December 2001.

Diarmuid O'Hegarty

cc: Board directors

-----*From Executive Director: Regulation and Compliance*

To: ALL MEMBERS

Ref: 05/002 : A002

Date: 5 January 2005

Subject: **MATCHING OF TRADES FOR NON LME BUSINESS DAYS**

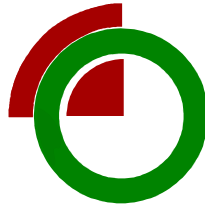
It has come to our attention that some members are registering LME Contracts with trade dates that are non LME business days.

Members are reminded that a 'Business Day' is defined in the LME Rule Book as "any day except Saturday, Sunday or any public or bank holiday in England..."

Accordingly, an LME contract (Exchange or Client) cannot be written for a trade date when the London Metal Exchange is closed. Trades executed on non LME business days are considered as OTC contracts, but can be brought on Exchange by subsequent registration in accordance with Board Notice 01/232:A232:R07, Rules On The Movement of LME Positions, and 01/402:A402:R011 Rules on Trade Type Indicators.

DIARMUID O'HEGARTY

cc: Board directors



LONDON METAL EXCHANGE

-----*From Joanna Stuart: Head of Market Surveillance*

To: Category 1, 2 & 3 Members
Date: 30 August 2005
Ref: 05/258 : A252 : R014
Subject: **NEW RULES ON MATCHING DEADLINES**

Summary

1 This notice confirms the proposed changes to the matching times for LME member-to-member telephone DD trades. The new matching times set out in the attached schedule will take effect on 3 October 2005.

Background

2 Notice 05/127 : A125 : R007 dated 29 April 2005 put forward proposals and a time table for changes to tighten the matching deadlines for LME member-to-member telephone DD trades. The notice also discussed a number of other issues related to matching times. Eight category 1 Ring Dealing Members and eight category 2 ABCMs responded to the notice. The main themes of their responses are summarised below.

3 All members who responded were generally in support of the matching deadlines being tightened. One member suggested that telephone DD trades should have one hour to match. Another member suggested one-hour deadlines for all trades. Two members did not agree that a deadline of 30 minutes should apply to Basis trades. The remaining members who responded supported the proposed deadlines of 30 minutes. In view of the responses, the changes will become effective on 3 October 2005 as proposed.

4 One member who supported the tighter deadlines suggested that, for Basis trades, category 2 members should be able to enter actual times to match with category 1 members' time codes thus making the time of trade a non-matching field. The LME has not adopted this suggestion. The use of matching time codes by both category 1 and 2 members for Basis trades is important in establishing a reliable audit trail for all trades executed on the basis of ring or kerb prices.

5 Nine out of 16 members who responded expressed concerns over the administration of automatic fines and any naming and shaming exercises. The concerns were that technical IT problems and busy market conditions could adversely affect input performance and that the LME should be fair and take

mitigating circumstances into account. The LME recognises that these are legitimate concerns and will adopt a pragmatic approach in dealing with those members who have persistent and continuous poor trade input performance. LME Compliance staff will deal with each of these members on a case by case basis for the first six months in an attempt to explore how the process could be improved. A regime of automatic sanctions will not be implemented until six months after the new deadlines have been implemented when a further review of the trade input performance will be undertaken to assess what sanctions would provide an appropriate deterrent. We hope that this will allow members sufficient time to identify issues and problems and to make the necessary improvements and changes to systems and processes.

6 Two category 2 ABCMs were concerned that they would be fined because of poor performance caused by Basis trades executed by Ring Dealing Members who failed to report their fills promptly to the category 2 members. During the monitoring period before the introduction of automatic sanctions, LME Compliance will assess the effect of late confirmations of Basis trades on the matching performance of category 2 members. One category 1 Ring Dealing Member suggested that the counterparty that inputs first should not be fined even though the entry was incorrect and had to be amended after the deadline had expired. The LME believes that prompt input should not be at the expense of accurate inputs. Each member should take responsibility for its own timely and accurate trade inputs. The LME and members have devoted a great deal of effort to creating a monitoring regime which will recognise when a member has made an accurate input within the deadline even if the trade fails to match within the deadline.

7 The LME have also committed to deliver to members a file of all their trade inputs so that members can identify for themselves how accurate and timely their own inputting had been for the month. LME will also consider providing members with a monthly benchmarked performance chart in an effort to encourage members to improve on their performance.

8 Ring Dealing Members' comments on whether they believe that electronic hand-held devices would improve efficiency on the floor were mixed. The same applied to introducing intervals between kerb trading sessions to enable floor clerks to check trades and reconcile positions. In view of a lack of consensus, no changes are proposed in this area at present. All Ring Dealing Members agreed that the deadline for matching K9 trades should be the same as K10 which is 17:30. This change will be take effect on 3 October 2005.



Joanna Stuart
Head of Market Surveillance

cc: Board directors

MATCHING TIMES FOR MEMBER TO MEMBER DD TRADES

			Basis Trades
Ring 1		R1 Matching Deadline	C1 Matching Deadline
11:45-11:50	Aluminium Alloy/NASAAC	12:20	12:20
11:50-11:55	Tin	12:25	12:25
11:55-12:00	Primary Aluminium	12:30	12:30
12:00-12:05	Copper	12:35	12:35
12:05-12:10	Lead	12:40	12:40
12:10-12:15	Zinc	12:45	12:45
12:15-12:20	Nickel	12:50	12:50
12:20-12:25	Plastic	12:55	12:55
12:25-12:30	Interval		

			Basis Trades
Ring 2		R2 Matching Deadline	C2 Matching Deadline
12:30-12:35	Copper	13:05	13:05
12:35-12:40	Aluminium Alloy/NASAAC	13:10	13:10
12:40-12:45	Tin	13:15	13:15
12:45-12:50	Lead	13:20	13:20
12:50-12:55	Zinc	13:25	13:25
12:55-13:00	Primary Aluminium	13:30	13:30
13:00-13:05	Nickel	13:35	13:35
13:05-13:15	Interval		

				Basis Trades
Kerbs (1-8)		Kerb Matching Deadline	Trades With Non-RDMs	Deadline for D
13:15-13:30	K1	14:00	D1	14:00
13:31-13:45	K2	14:15	D2	14:15
13:46-14:00	K3	14:30	D3	14:30
14:01-14:15	K4	14:45	D4	14:45
14:16-14:30	K5	15:00	D5	15:00
14:31-14:45	K6	15:15	D6	15:15
14:46-15:00	K7	15:30	D7	15:30
15:01-15:10	K8	15:40	D8	15:40

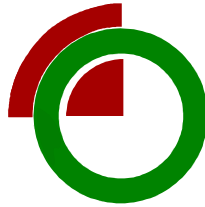
			Basis Trades
Ring 3		R3 Matching Deadline	C3 Matching Deadline
15:10-15:15	Aluminium Alloy/NASAAC	15:45	15:45
15:15-15:20	Interval		
15:20-15:25	Lead	15:55	15:55
15:25-15:30	Zinc	16:00	16:00
15:30-15:35	Copper Grade A	16:05	16:05
15:35-15:40	Primary Aluminium	16:10	16:10
15:40-15:45	Tin	16:15	16:15
15:45-15:50	Nickel	16:20	16:20
15:50-15:55	Interval		

			Basis Trades
Ring 4		R4 Matching Deadline	C4 Matching Deadline
15:55-16:00	Interval (Plastic)	16:30	16:30
16:00-16:05	Lead	16:35	16:35
16:05-16:10	Zinc	16:40	16:40
16:10-16:15	Copper	16:45	16:45
16:15-16:20	Primary Aluminium	16:50	16:50
16:20-16:25	Tin	16:55	16:55
16:25-16:30	Nickel	17:00	17:00
16:30-16:35	Aluminium Alloy/NASAAC	17:05	17:05

				Basis Trades
Kerbs (9 & 10)		Kerb Matching Deadline	Trades with Non-RDMs	Deadline for D
16:35-16:45	K9	17:30	D9	17:30
16:46-17:00	K10	17:30	D10	17:30

TIMED TELEPHONE DD TRADES

Time of Trade	Matching Deadline
19:30:01-24:00 (prior business day)	08:30
00:00:01-08:00	08:30
08:00:01-19:30	30 mins after time of trade



LONDON METAL EXCHANGE

-----*From Executive Director: Regulation and Compliance*

To: ALL MEMBERS
Ref: 05/377 : A370 : R016
Date: 15 December 2005
Subject: **LENDING GUIDANCE FOR LME METALS**

Summary

1 Market Aberrations: The Way Forward was published by the Exchange in October 1998 as an attachment to LME notice 98/363 : A351 : W072. Paragraph 13.24 of the Market Aberrations document sets out the Lending Guidance that applies to the holders of dominant long positions in the LME metal markets.

2 At its meeting on the 15 December 2005 the board of the LME decided to formalise with immediate effect the rules and procedures relating to the operation of the Lending Guidance.

3 Schedule 1 to this notice sets out clarification and explanation of a number of practical aspects of the Lending Guidance.

4 Schedule 2 sets out new rules that explicitly require members to comply with the Lending Guidance and deal with any actual or likely failure by a non-member to abide by the Lending Guidance.

Background

5 The market aberrations document dealt with a number of issues relating to the LME metal markets and their regulation. The document was the result of a consultation process that started in October 1997 and included the Solutions to Market Aberrations consultation document (attached to LME notice 98/007 : A007 : W011) published in March 1998. The full Market Aberrations document is available on the LME website www.lme.com in a printable format.

6 The Solutions to Market Aberrations consultation document proposed a number of mechanisms for dealing with dominant positions in the LME metal



markets. The Lending Guidance was formulated by the Board as the solution that best fitted the structure of the LME metal markets.

7 Prior to the introduction of the Lending Guidance, the Exchange's response to the effect of dominant positions in the metal markets was to introduce backwardation limits. However, there were two aspects of this use of backwardation limits that were heavily criticised. First, the backwardation limits were not specific to dominant position holders and obliged all long position holders to lend their positions for a day at no more than a premium set by the Exchange. Secondly, the need to announce the imposition of the backwardation limits with immediate effect, gave the markets no notice and made the application of backwardation limits unpredictable.

8 The Lending Guidance addresses both of these concerns. It creates an obligation on the holder or holders of a dominant position to lend at the required levels but creates no obligation on the holder of a long position that is not dominant. The market aberrations document provides that a dominant position can be created by two or more parties acting together. The circumstances in which the Lending Guidance takes effect are known in advance which introduces an element of predictability in the event that there is a dominant position in any of the metal markets.

9 It has been argued before the LME Special Committee that the Lending Guidance is in itself the cause of market distortion where warranted stocks are low. In the Committee's view, if there is such distortion, it is minimal and is more than offset by the maintenance of orderly trading for the nearest prompt dates.

10 Compliance with the Lending Guidance is an accepted market practice under the FSA's Code of Market Conduct and under the Market Abuse Directive.

Clarification and Explanation

11 The terms of the Lending Guidance are clear in their intent and in the behaviour expected of a dominant position holder. However, the Board recognises that trading on the LME metal markets requires a certain level of expertise and that it would be useful for participants in the market if the Exchange set out clarification and explanation of a number of practical aspects of the Lending Guidance. These are set out in Schedule 1. A draft of Schedule 1 was circulated to category 1, 2 and 4 members for comment. The final text of Schedule 1 has benefited from the comments that were made.

New Rules

12 The Lending Guidance sets out the behaviour required of holders of dominant long positions in the LME metal markets. The Lending Guidance is designed to deal with the effect of dominant positions in the nearby prompt



dates so as to maintain order in those metal markets. Deliberate failure to comply with the Lending Guidance would expose a dominant position holder to a charge that it was attempting to create disorder in the market or was attempting to manipulate the market. The new rules set out in Schedule 2 are being introduced by the Board in order to reinforce the importance of the Lending Guidance in maintaining order in the LME metal markets. The new rules are without prejudice to the Special Committee's powers to act under Regulation 15 of the Trading Regulations.

Diarmuid O'Hegarty

cc: Board directors
Special Committee



Schedule 1

LENDING GUIDANCE

CLARIFICATION AND EXPLANATION

15 DECEMBER 2005

LENDING GUIDANCE

1 Paragraph 13.24 of Market Aberrations: The Way Forward (published by the Exchange in October 1998) sets out the terms of the Lending Guidance as follows:-

- [a] If at any time a member or client holds 50% or more of the warrants and/or cash today/cash positions in relation to stocks, he should be prepared to lend, if asked, at no more than a premium of $\frac{1}{2}\%$ of the cash price for a day. After five successive days, he should be prepared to lend, if asked, at no more than a premium of $\frac{1}{4}\%$ of the cash price for a day.
- [b] If at any time a member or client holds 80% or more of the warrants and/or cash today/cash positions in relation to stocks, he should be prepared to lend, if asked, at no more than a premium of $\frac{1}{4}\%$ of the cash price for a day. After five successive days, the maximum premium would fall to 0.15%.
- [c] If at any time a member or client holds 90% or more of the warrants and/or cash today/cash positions in relation to stocks, he should be prepared to lend, if asked, at no more than the cash price.
- [d] As with the publication of large position information, in determining the application of the guidelines, it would be appropriate for the LME to aggregate the positions of a client across all brokers in reaching its estimate of dominant positions. Likewise it would be appropriate to aggregate the positions of a member, its related group companies and its clients unless the firm could demonstrate that the positions were independent.

HOW TO CALCULATE A DOMINANT POSITION

2 The basis of a relevant position in any metal for the purposes of the Lending Guidance is the total of a person's warrant holding ("W"), net Tom trading positions ("T") and net cash trading positions ("C"). This is referred to as the net WTC position and is expressed in lots. That net WTC position is divided by the number of live LME warrants for that metal. The result of (W +



$T + C) \div (\text{live warrants})$ is expressed as a percentage to two decimal places. For example, a warrant position of 123 warrants, a net Tom position of 456 lots and a net cash position of 789 lots will equal 1,368 lots. If the total number of live LME warrants were 1,500, the WTC position would be 91.20%.

$$\frac{(123 + 456 + 789)}{1,500} = 91.20\%$$

3 The denominator used is live warrants rather than total stock. Total LME stock in each metal is the sum of live warrants and cancelled stock. This means that if a dominant position holder reduces his warrant holding by cancelling warrants, he will also be reducing the denominator used to calculate the size of his dominant position.

4 The resulting percentage forms the basis for calculating the number of lots that a dominant position holder must be prepared to lend. The Lending Guidance treats a WTC position of 50% and above as dominant. This means that a position holder is subject to the Lending Guidance until his WTC position is reduced to 49.99%. For practical reasons, these percentages need to be expressed in lots as whole numbers. In the above example, 50% of 1500 lots equals 750 lots. Therefore, 749 lots equals less than 50%. The dominant WTC position $(123 + 456 + 789)$ equals 1,368 lots. The holder would have to be prepared to lend 619 lots to reduce his WTC position down to 749 lots. Expressed as percentages, this means that the dominant position holder must be prepared to lend 41.21%, rounded up to the nearest lot.

5 The figures used in calculating a WTC position are those reported by members to the Exchange by 8.30am each business day. The figures relate to the WTC positions as at the close of business on the previous business day. Each member's reports separately identify the W, T and C positions held on behalf of the member and the W, T and C positions held by each of its clients, including any of the member's affiliate companies. The Exchange is able to aggregate the WTC positions held by a single client or group of connected clients across a number of members. LME notice 01/122, dated 23 March 2001, sets out the Exchange's approach for attributing and aggregating warrant holdings for the purposes of the Lending Guidance.

6 The net WTC positions are divided by the number of live warrants as at the same point in time, the close of business the previous day. The live warrant figures used are the same as those included in the stock figures published by the Exchange at 9.00am each business day.

7 As WTC positions are calculated each morning on the basis of figures as at the close of business on the previous day, the reported T trading position will have become a delivery obligation for that day and the reported C position will have become a Tom position for that day. In order to reduce that reported WTC position in line with the Lending Guidance, the dominant position holder should be prepared "to lend" Tom/next (or one of the Tom date carries).



HOW A DOMINANT POSITION TRIGGERS THE LENDING GUIDANCE

8 The Lending Guidance operates in three effective bands. The first is where a WTC position is 50% or more but less than 80% of live warrants. The second band is where a WTC position is 80% or more but less than 90% of live warrants. The third band is where a WTC position is 90% or more of live warrants.

9 The effect of this banding is that where a person's WTC position is above 90% of live warrants he should be prepared to lend for a day:

- (a) at no premium (i.e. "level") a sufficient number of lots to reduce his position below 90%;
- (b) at a premium of no more than ¼% of the cash price a sufficient number of lots to reduce his position below 80%; and
- (c) at a premium of no more than ½% of the cash price a sufficient number of lots to reduce his position below 50%.

10 The cash price used to calculate the premium each business day is the LME official cash settlement price published the previous business day. The maximum premium percentage is expressed as a US dollar amount rounded down to the nearest cent.

11 In the following example the notional WTC figures are the same as those used in paragraphs 2 and 4 above, i.e. the dominant position of 91.20% requires the holder to be prepared to lend 619 lots to reduce his position below 50%. The notional cash price being used is \$2,000.

Lending Guidance Percentage Bands	Position Holder's Dominance in lots	Maximum Premium
90% and above	19	level
80% to 89.99%	150	\$5.00
50% to 79.99%	<u>450</u>	\$10.00
	total 619	

12 The Lending Guidance states that a dominant position holder "should be prepared to lend, if asked". This expression means that the dominant position holder should respond to demand in the market for borrowing at the premium set by the Lending Guidance. The dominant position holder is not obliged to lend if the market demand for Tom/next borrowing is at a backwardation premium below that specified by the lending guidance. In the example at paragraph 11 above, the dominant position holder should be prepared:-

- (a) to lend at least 19 lots at level if the Tom/next backwardation premium bid in the market reaches level. If the backwardation premium bid in



the market stays below \$5.00 he is not obliged to lend more than those 19 lots;

- (b) to lend an additional 150 lots at a premium of no more than \$5.00 if the backwardation premium bid in the market reaches \$5.00. If the backwardation premium bid in the market stays below \$10.00 he will not be obliged to lend more than 169 lots (i.e. 150 lots at no more than \$5.00 and 19 lots at no more than level);
- (c) to lend an additional 450 lots at a premium of no more than \$10.00 if the backwardation premium bid in the market reaches \$10.00. Once he has reduced his position below 50% he is no longer obliged to lend and those who wish to borrow will have to bid out the price until someone is prepared to lend.

13 If the dominant position holder chooses to continue lending, the maximum backwardation premium does not apply to any additional lending done after he has reduced his position below 50%.

14 Lending Tom/next involves selling for the Tom Prompt Date and buying for the cash Prompt Date. Where a dominant position holder reduces his WTC position on one day by lending Tom/next, he will be adding to his C position for the purposes of calculating his WTC position the next morning. This explains how a person may abide by the Lending Guidance but maintain a dominant position on successive days.

15 Dominant positions are also subject to reduced maximum premiums after the dominant position has been held for more than five successive business days. On the sixth and subsequent successive business days a WTC position of 50% or more but less than 80% of live warrants is subject to a maximum premium of $\frac{1}{4}\%$ of the cash price. On the sixth and subsequent successive days a WTC position of 80% or more but less than 90% of live warrants is subject to a maximum premium of 0.15% of the cash price. The purpose of this reduction in the maximum premium is to take account of the effect of a dominant position over time.

16 If, for example, a dominant position has fluctuated between 60% and 85% for five successive days, the reduced maximum premium of $\frac{1}{4}\%$ will apply to the WTC position of 50% or more but less than 80%; no reduction will apply to the position of 80% or more until that has been maintained for five successive days. The calculation of successive business days recommences following any day on which the Tom/next market in the relevant metal did not trade at a backwardation but only traded at level or at a contango.

HOW TO COMPLY WITH THE LENDING GUIDANCE

17 The Lending Guidance is an obligation placed on those who hold a dominant long position in any of the LME metal markets. The holder of the dominant position is ultimately responsible for his own compliance with the Lending Guidance. This is the case both for members and non-members. In



the case of a non-member, compliance with the Lending Guidance requires the non-member to give appropriate instructions to one or more of his brokers.

18 The LME Compliance Department calculates dominant positions on the basis of position reports submitted electronically by members. Members must notify the Exchange of the identity of all position holders and of any connections between two or more position holders. Details of new account holders must be notified to the Exchange before that new account starts trading. Where the LME Compliance Department identifies a dominant position, the holder of that position will be contacted both to confirm the figures used to calculate the dominant position and to discuss any steps to be taken. These steps could include adjustments to a WTC position to account for OTC business being brought on Exchange that day. Many non-members prefer to have these discussions direct with the LME Compliance Department rather than go through one or more of their brokers. Although, both members and non-members may discuss their WTC positions with the LME Compliance Department, the holder of a dominant position is best placed to know the size of his own WTC positions. Once the LME stock figures are published at 9.00am, a position holder is able to calculate whether or not his net WTC position triggers the Lending Guidance.

19 Increases or decreases in the LME warrant figures from the previous day's figures may affect whether a WTC position is dominant or whether the dominance exceeds the 80% or 90% thresholds and by how many lots. For this reason a dominant position holder is entitled to wait until the LME stock figures are published before complying with the Lending Guidance. However, if a dominant position holder chooses to lend before 9.00am, that lending must be in compliance with the Lending Guidance. If there has been a material change in the live warrant figures, the dominant position holder may have to adjust some of the trades he did before the LME stock figures were published in order to ensure that his lending has complied with the Lending Guidance.

20 Lending in compliance with the Lending Guidance must be done in the correct order. If a dominant WTC position is above 90%, the position holder must lend at level a sufficient number of lots to bring his position below 90% before he may lend at a premium of $\frac{1}{4}\%$ of the cash price. Similarly, he must lend at a premium of no more than $\frac{1}{4}\%$ of the cash price a sufficient number of lots to bring his position below 80% before he may lend at a premium of $\frac{1}{2}\%$ of the cash price. He must have reduced his position below 50% before he may lend at a premium greater than those specified by the Lending Guidance.

21 The LME provides three forums for trading: in the ring, on LME Select and on the telephone. A dominant position holder should be prepared to respond to requests for borrowing in all three forums. A dominant position holder is not obliged to verify if the person borrowing from him is doing so to cover a short. However, the purpose of the Lending Guidance is to address the effect of his dominant position on those who are short. It would be an abuse of the Lending Guidance for a dominant position holder to contrive to



lend to another person at the specified premium with the intention that that other person could lend in the market at a higher premium.

Lending on LME Select

22 A bid on LME Select is a request to the market. A dominant position holder must respond to bids on LME Select where those bids reach the premium at which the dominant position holder must be prepared to lend. The mechanisms for ensuring orderly trading on LME Select mean that a lower offer entered into the system will trade with an existing higher bid. If there is a bid in LME Select that is at a higher premium than that prescribed by the Lending Guidance, a dominant position holder must trade with that bid to identify the borrower and subsequently adjust the price back to the correct premium. This adjustment cannot be done on LME Select but requires a reversal trade and a new trade at the correct premium to be negotiated on the telephone. If the circumstances suggest that bids for Tom/next borrowing on LME Select will be higher than the backwardation premiums at which the dominant position holder will be obliged to lend, the dominant position holder should behave prudently and consider placing offers on LME Select to anticipate bidding. This will avoid the need for adjustment trades.

23 If the dominant position holder is not a clearing member, he must make arrangements with his broker to take the necessary steps to respond to bids on LME Select and to make adjustments where necessary.

Lending in the Ring

24 A bid in the ring is also a request to the market. The first ring session for each metal is the last opportunity to lend or borrow Tom/next by open outcry. A dominant position holder who has not reduced his WTC position below 50% by the start of the first ring must respond to bids in the ring where those bids reach the premium at which the dominant position holder must be prepared to lend.

25 The mechanisms for ensuring orderly trading in the ring mean that once a bid to borrow has been made a lender must either accept that bid or make a higher offer. It is a breach of the ring trading regulations to make an offer that is lower than a prevailing bid. If a dominant position holder's WTC position remains at 50% or above by the start of the first ring, he must ensure that he responds to bids and that any lending he does is at premiums no higher than the premium prescribed by the Lending Guidance. In order to ensure this and to abide by the ring trading regulations, it may be necessary for the dominant position holder to offer to lend. If the circumstances suggest that Tom/next trading in the ring is likely to start at higher premiums, the dominant position holder should be prepared to open the ring with an offer before any bid is made.

26 If the dominant position holder in these circumstances is not a ring dealing member, he must make arrangements in good time for a ring dealing member to effect the necessary lending on his behalf.



BROKERS INSTRUCTED BY DOMINANT CLIENTS

27 There are a number of considerations that a member must take into account when acting for a client who is dominant. In particular, the member must ensure that his actions comply with the FSA Code of Market Conduct and the FSA Conduct of Business Rules.

28 If a member is instructed by a client to lend a number of lots at a particular backwardation premium, that instruction is an order for the purposes of FSA rules. In executing that order, the member must manage any conflicts of interest, must not misuse customer information or breach the FSA Code of Market Conduct. For example, it is clearly wrong for a member who is acting for a dominant position holder to borrow from that dominant position holder, or to collude with someone else to borrow from that dominant position holder, at the premium prescribed by the Lending Guidance with a view to lending in the market at a higher premium. Nothing that the member does should frustrate the dominant client's willingness or ability to lend to bidders in the market.

29 A member who receives an order from a client to lend in accordance with the Lending Guidance may already have orders from other clients to borrow. In situations like that, the member must be careful to comply with the FSA's rules on order priority and fair allocation. In those circumstances the member must also keep in mind the responsibility on a dominant position holder to respond to bids on LME Select or in the ring. If he receives an order from a client to lend in accordance with the Lending Guidance and already has a bid on LME Select that represents a client wishing to borrow he should cancel that bid on Select before crossing the borrowing client's order with the dominant client's lending order.

30 When a member receives instructions from a client to lend in accordance with the Lending Guidance, that member will be in possession of privileged customer information. The member must be careful not to take advantage of that information and should give priority to his own clients who are short and to bids on LME Select or in the ring over his house shorts.

CONCLUSION

31 Those who would like any further clarification or explanation of the Lending Guidance should contact the Market Surveillance department at the Exchange.



Schedule 2

Amendments to part 1, Definitions, and part 3 Trading Regulations of the LME rules and regulations

Part 1, Definitions

“Lending Guidance” paragraph 13.24 of Market Aberrations: The Way Forward, published by the Exchange in October 1998, setting out the behaviour required of the holders of dominant long positions in the Exchange’s metal markets, including any clarification or explanation of that behaviour issued by the Exchange from time to time;

Part 3, Trading Regulations

16. **POSITION LIMITS FOR PLASTICS CONTRACTS AND LENDING GUIDANCE FOR METALS**

16.1 [no change]

16.2 [no change]

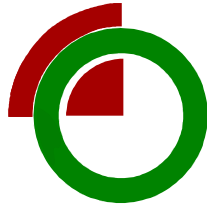
16.3 Members shall comply with the Lending Guidance and shall co-operate with the Exchange to ensure that each of their Clients shall comply with the Lending Guidance.

16.4 Where the Exchange has reasonable cause to suspect that a Client has failed or is likely to fail to comply with the Lending Guidance, the Exchange may give directions to one or more Members with whom that Client has Client Contracts to take action designed to make the same number of lots available for borrowing in the market as would have been the case if the Client were prepared to abide by the Lending Guidance. Such directions to a Member may include but are not limited to:-

- (a) lending or offering to lend, at no more than a level premium, the number of Exchange Contract positions equal to or less than the Client’s long position holding of 90% or more as calculated by the Exchange in accordance with the Lending Guidance; and/or



- (b) lending or offering to lend, at no more than a premium of 0.50% of the previous day's Cash price, the number of Exchange Contract positions equal to or less than the Client's long position holding of 80% or more but less than 90% as calculated by the Exchange in accordance with the Lending Guidance; and/or
 - (c) lending or offering to lend, at no more than a premium of 0.25% of the previous day's Cash price, the number of Exchange Contract positions equal to or less than the Client's long position holding of 50% or more but less than 80% as calculated by the Exchange in accordance with the Lending Guidance; and/or
 - (b) trading out of sufficient Client Contract positions with that Client to reduce that Member's (or, if two or more Members are directed, those Members') net exposure to that Client in line with the action taken in compliance with the directions under (a) to (c) above.
- 16.5 Compliance with the Lending Guidance is subject to the power of the Special Committee to take steps or give directions under Regulations 15.1 to 15.3 above. Without prejudice to the generality of Regulations 15.1 to 15.3 above, such steps or directions may include suspending, amending or supplementing the Lending Guidance for such period or in respect of such metals as the Special Committee in its absolute discretion deems necessary.



LONDON METAL EXCHANGE

-----*From Executive Director: Regulation and Compliance*

To: All Members
Ref: 06/067 : A067
Date: 22 February 2006
Subject: **REVISED GUIDANCE ON THE STRUCTURE OF AND ORDER EXECUTION ON THE LONDON METAL EXCHANGE**

Following the introduction of the plastics contracts, Polypropylene, (PP), and Linear Low Density Polyethylene, (LL), the LME has updated Board Notice 01/385 A385 for distribution to all new customers as part of the members' account opening procedures. This document will also be available on the LME website.

Diarmuid O'Hegarty

cc: Board directors



A GUIDE TO THE STRUCTURE AND MARKET TERMINOLOGY OF THE LONDON METAL EXCHANGE

[Revised 21.2.2006]

INTRODUCTION AND PURPOSE

This document is designed to provide customers of the London Metal Exchange (LME) with an overview of the structure of the LME, market terminology, and order execution. It is not a comprehensive trading guide, nor a complete guide to market terminology. Customers should always ensure that their requirements are explained in detail to the member responsible for order execution.

THE LME

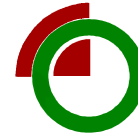
Principal Nature

There are two types of contracts traded on the LME - Exchange Contracts and Client Contracts. Exchange Contracts are contracts between clearing members of the LME. Client Contracts are contracts between customers and ring dealing members (RDMs), or associate broker clearing members (ABCMs), or associate broker members (ABMs)¹. Only RDMs, ABCMs and ABMs may issue Client Contracts. Open Position Statements issued to clients must state clearly '**THIS IS AN LME REGISTERED CLIENT CONTRACT**'. Contract criteria relating to LME contracts, including metal/plastic specifications, acceptable currencies, prompt dates, option strike prices for metals etc. are detailed in the LME rulebook and appropriate notices.

Exchange Contracts are traded between members, **matched** in the LME matching and clearing system (LMEMS) and margined by LCH.Clearnet (LCH). Client Contracts are **registered** at the LCH but margining arrangements are left to members to agree with their customers (subject to LME rules).

All LME contracts are between parties acting as principals. This prevents any party entering into an LME Contract as agent for someone else but does not prevent an agent effecting a contract between two parties if the resulting LME contract is between disclosed parties, each acting as a principal. It is an essential requirement of an LME Client Contract that one party must be an RDM, ABCM or ABM. A list of members is available from the LME, and on the LME website: www.lme.com. A principal relationship does not mean that members do not take on quasi-fiduciary responsibilities when they effect trades for customers. In particular, if a member undertakes to deliver a particular service, for example deal a specific number of lots 'in the Ring' (see

¹ For the purposes of this document these categories of members will be referred to as LME members, members or by the appropriate abbreviation.



below), then it should take care to ensure that it complies with all the terms of such a transaction.

In respect of Exchange Contracts, an LME broker buying metal or plastic under an Exchange Contract from another LME broker cannot do so as agent for his customer. Where an LME broker buys metal or plastic under an Exchange Contract with a view to selling that metal or plastic to his customer, this is achieved by entering into a back-to-back Client Contract with the customer. Brokers and customers can agree the conditions that apply to their Client Contracts. For example, a customer may make it a condition of his Client Contract that the broker must enter into a back-to-back Exchange Contract for the metal or plastic being bought or sold. This does not make the customer a party to the Exchange Contract but does create additional duties and obligations owed by the broker under the Client Contract.

Customers should be clear about conditions that apply to their Client Contracts and about the obligations and duties that the broker owes as a result of those conditions.

Brokers should be clear about the duties and obligations they owe as a result of conditions attaching to their Client Contracts. They should also be clear about the duties they owe to their customers under the FSA's Conduct of Business Rules (COB).

Dual Capacity

LME members may act both in the capacity of market maker and broker. They may act in a particular manner depending on a number of circumstances, including the size of the order, the liquidity of the market at the time the order was placed, and, not least, the customer's instructions. Customer orders may be filled directly from a member's 'book' or following the purchase/sale of metal or plastic in the LME market. Furthermore, customer orders may be offset, amalgamated, broken-up or netted for execution. These methodologies apply equally to orders whether any resulting Exchange Contract is effected in the ring, in the inter-office market, or on LME Select.

Customers with specific order requirements must make these known to the member at the time the order is placed. Customers wishing to know how their order was executed should request such information from the member.

Trading on the LME

Trading takes place on the LME by open outcry in the rings and kerbs, between members in the inter-office, and over the Exchange's electronic trading system LME Select.

Open Outcry



Historically, during ring and kerb sessions, the majority of customer business reflects prices traded in the open outcry sessions. Customers can follow the market activity by monitoring quoted and traded prices disseminated via the LME market data system (MDS), or by listening to the simultaneous floor commentary provided by member(s). The MDS publishes prices traded during ring and kerb times on price vendor information services such as Reuters.

Members can continue to 'make a market' when requested by a customer during the ring and kerb sessions, although this is entirely at the member's discretion. Alternatively, the customer can decide whether to place an order using the 'order styles' mentioned below.

Inter-office

Inter-office trading is conducted between members by telephone or by electronic means. On contacting an LME member for a quote, customers will usually be provided with the member's current bid and offer. The customer may trade on this quote, call another member in an attempt to improve the quote, leave a resting order with a member, or wait and monitor prices on the LME market data system. If an order cannot be filled from the member's book, it may be executed via a back-to-back Exchange Contract agreed via a telephone deal with another member or executed via an electronic trading system.

LME Select

LME Select allows members to trade LME futures contracts in metals and plastics, traded options and TAPOs², and an Index future and option. Some brokers offer their customers an order-routing facility via an API³ where they can view Select prices, execute trades, and place resting orders. All trading on LME Select is in US dollars.

LME Select replaces neither inter-office trading nor trading in the ring. Depending on the time of day, it is possible for members to deal by telephone or electronically in the inter-office, by LME Select, or in the rings. Customers should specify which mechanism their broker should use to effect an order, where they have a preference.

Firm prices of the best bid and offer available on LME Select, the total volumes available at these prices, and the price and volume of each trade transacted are distributed to and displayed in real time by information vendors. Only LME Select prices are displayed, not those of other third party electronic trading systems providing LME prices. Only RDMs and ABCMs are eligible to become LME Select Participants and to have direct access to the system. Customers may effect back-to-back Client Contracts with RDMs and

² TAPO traded average price option

³ API Application Protocol Interface



ABCMs based upon prices available on LME Select, whether on the telephone or via electronic order-routing systems.

ORDER STYLES

Ring

Customer orders are not traded in the rings or kerbs, so an order using the term 'in/on/during the ring/kerb' will be executed on the basis of the prices traded/quoted during the particular session. If a customer requires their order to be 'shown' or traded across the ring/kerb then they should make this requirement known to their executor, who may or may not accept this as a term of the order. The equivalent Exchange Contract for a customer order may not replicate its terms. As the customer is **not** a party to any Exchange Contracts i.e. those traded in open outcry between members in the ring/kerb sessions, in specifying ring/kerb, the customer is merely identifying a pricing mechanism. A member which undertakes to match a price traded in the ring/kerb is not necessarily undertaking that it will trade during that ring/kerb, only that it may do so. However, a customer may place an order with the specific request that the member trades an Exchange Contract replicating its order in the ring. In such circumstance the RDM can only trade this order by open outcry in the ring.

If a customer trades at the prevailing market quote proffered in the ring/kerb, their executor is not necessarily obliged to effect an Exchange Contract at the same price. This can lead to situations where the customer has traded at the prevailing market quote, without that same price trading in open outcry across the floor of the Exchange. However, if the instructions from the customer are to achieve a specific price i.e. close of ring 2, then this is the price that should be given, if that specific order is accepted.

Market

In normal circumstances a market order is one executed on a timely basis at the prevailing market price. As mentioned above, at certain times of the business day, trading is taking place simultaneously in the ring or kerb, on LME Select, and in the inter-office market. Traditionally, when open outcry trading is in session, the market is defined by activity within the ring/kerb. At other times, the market is split between inter-office trading and trading on LME Select. During inter-office sessions, indicative quotes are available on the MDS; firm prices are available on LME Select and the LME Select page on information vendors' systems. The indicative prices might not be available to all parties.

Best

Order styles on the LME using the word 'best' confer some discretion upon the members when executing the order, requiring them to use their 'best endeavours' on the customer's behalf. The extent of the discretion is fixed by



the terms of the order. This type of order is distinct from 'best execution' as defined by the FSA.

Best orders may be executed both in rings/kerbs, inter-office and on LME Select. Inter-office trades rely upon the members' skill in determining the level of the market at any particular time. Best orders received during ring/kerb times may not result in the customer receiving the 'best' price achieved during the session if the price improves after the member has booked the metal or plastic intended to fill the order. At any given time, the best price on LME Select will be displayed on the system and by the information vendors. Customers should be aware that depending on market conditions, the best price may move during the period from when the order was placed and when it was executed.

Close

Most orders placed 'on the close' are for either the close of the second ring (official LME prices) or the final kerb (closing prices). Both these prices are demonstrable because of the publication of official and closing prices. Closing prices for other sessions are harder to determine, although the LME does publish unofficial prices which are established at the close of the fourth ring. In all circumstances, customers and members need to agree the style of execution i.e. bid/offer, mean or traded price. Members may not always be able to guarantee execution (price or volume) due to prevailing market conditions. A closing price on LME Select is the last price traded before the system closes.

Open

Customers placing orders to trade on the opening of a market session must provide clear instructions to the LME member which indicate how this order should be activated i.e. basis the opening bid/offer or basis the first trade in the session. Customers will also need to inform their executor of their requirements if the executor is unable to fill the order basis the 'opening' price in its entirety, due to market constraints such as insufficient liquidity. Customers may place orders with members for LME Select that can be placed into the system for activation when the market opens.

Resting Orders

When placing resting orders such as 'good 'til cancelled' ('GTC', or any derivations thereof) or stop loss orders, customers should ensure that they are in agreement with their executor's definition of the 'trigger' point of the order. Usually, this is interpreted as being the point when the order price is seen to be trading in the market, but it is possible to request the order be activated when the order level is either bid or offered as appropriate, via the prevailing market quote. Stop loss orders become market orders when a trade, or a bid or an offer triggers the stop, with members then executing the order at the current market price.



It is possible for a customer not to receive a 'fill' on a resting order despite the 'trigger' point being 'touched'. This could be due to a number of circumstances such as order priority, illiquidity, prevailing market conditions etc. Whatever the reason, the executor should be able to provide the customer with a full explanation of why it was unable to fill the order.

Customers should be aware that resting orders might be activated during periods of illiquidity in the market. As previously mentioned, this could result in the trade not being filled, or for 'stop' orders, a worse fill than anticipated ('slippage'). Customers should ensure the executor is fully aware of their requirements regarding the execution of an order, and adheres to any limitations, especially if the customer is not in contact with the market/member when the trigger point is reached.

It is possible for customers to ask members to place resting orders in LME Select. Where the broker has an order routing system into Select, customers will be able to place orders more directly. The system accepts GTC and Good for Day (DAY) orders. DAY orders are automatically deleted from the system at close of trading.

Conclusion

The above order styles do not represent all possible methods of order execution on the LME. Members and customers should ensure that orders are communicated in meaningful terms that deliver the required execution in accordance with LME rules.



LONDON METAL EXCHANGE

To: Category One and Category Two Member Firms

Ref: 06/324 : A320

Date: 21 November 2006

Subject: **INTRODUCTION OF AN ORDER TO TRADE RATIO CHARGING POLICY ON LME SELECT**

Following approval from Excom, the following procedures come into effect from **Monday 4 December 2006**.

Members who exceed an average ratio of twelve order actions per trade, during one business day, will incur a charge of £1,000 per day. Each order entry, modify, inactivate, reactivate and cancel constitutes one order action. The policy is in force during the whole of LME Select opening hours of 1am to 7pm London time and includes all metal, plastic and LMEmini contracts. The policy includes all order actions from GUI and FIX API logins from a member. Excom will review the policy on a regular basis.

Members would be notified the following day if they exceed the ratio and invoiced on a monthly basis for only the days the ratio has been exceeded. December 2006 invoices will be sent in January 2007.

In addition to the charge above, the exchange retains the right to restrict or suspend access should the Exchange determine that message usage by any Member becomes capable of impairing the orderly conduct of trading on LME Select.

It is the responsibility for members who currently offer the facility for clients to order route to LME Select to ensure they are fully aware of these procedures.

If you have any questions on this matter, please contact the LMEhelpdesk on 0207 488 2500 or by email at lmehelpdesk@lme.com.

Glen Chalkley
Head of LME Select

cc. Board directors
Trading committee
LMEmini advisory group

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LONDON METAL EXCHANGE

-----From Joanna Stuart: Head of Market Surveillance

To: CATEGORY 1, 2 AND 3 MEMBERS
Ref: 07/068 : A066
Date: 15 March 2007
Subject: **MATCHING PERFORMANCE**

Introduction

LME Notice 06/294:A290 issued on 2 November 2006 set out a plan to improve the matching performance of members by monitoring the timeliness of members' trade inputs each month. This plan was to identify those members that had more than 30% of their trade inputs late in February 2007.

After consultation with members, various issues have been identified some of which will require changes to the LME matching system in order to produce fair and accurate measurement of each member's performances. The LME have therefore decided to postpone the exercise to identify those firms that have more than 30% of their trade inputs late for six months until September 2007. This delay is to allow members sufficient time to co-ordinate and implement their own back office system changes consistent with those that will be made in the LME matching system.

Impact of the revised afternoon kerb session times

The LME has reviewed the impact of the time change of Kerb sessions K7, K8 and K9. These kerbs are now continuous and last longer. As a consequence an extra 15 minutes will be added to the matching deadline for these kerbs; the new matching deadline will be 17.45 instead of 17.30.

Lateness caused by trades based on the evening closing prices

The LME matching system currently cannot accept abbreviated codes for closing prices although abbreviated codes (S, S+/-) are used for settlement prices. As more business is now transacted during the day based on closing prices, this means that trades cannot be matched until the closing prices are known at the end of day and input as absolute numbers into the matching system. It is proposed that an abbreviated code will be available in future for closing prices in the matching system.

Lateness caused by trades based on Settlement prices

It is disappointing that there are still firms that are unable to process "S" abbreviated codes for the Settlement prices in the matching system. The LME identified this problem with the "S" price in a member survey conducted in January 2005 and subsequently published a notice 05/127:A125:R007 on the new rules on matching deadlines stating that members would be given sufficient time (in this case 5 months) to make the necessary system changes for them to comply with the new deadlines effective in October 2005. Those members who have not yet made the necessary changes should do so by September 2007.

Unmatched trades at close of business

Unmatched trades are cleared down automatically at the end of day in the matching system. Trade halves have to be re-input the next morning using the previous trade date and time. It would be unfair to penalise those firms who invest in resources to enter their trade half correctly on time. It is therefore proposed that all unmatched trade inputs will remain in the matching system for one day. After trade day + 1, any unmatched trade halves will be automatically cleared down. Members should ensure that their own back office interface will be able to handle this change. Unmatched trades left in the system from the previous day that use abbreviated codes such as "S" will use Settlement prices from the previous day. Likewise, abbreviated codes for Prompt dates such as "C" for Cash and "3" for 3 Month will be based on the previous day's Cash date and yesterday's 3 Month Prompt date.

Adjusted Trades

Due to the complex date structure of our contracts of which a large proportion are calendar spreads, it is more practical to do these type of trades on the telephone as the majority of LME spread trades are referenced against the Three-Month Prompt price and are subsequently date and/or price adjusted. The process involves both sides committing to a Three-Month trade which is then date/price adjusted. Members have raised concerns that "Adjusted trades" are inevitably late as the price and date elements are not usually confirmed within 30 minutes after the commitment to trade with the counterparty has been made. The LME firmly believe that if a trade does not have its key attributes confirmed, in this case we are referring to its Price or its Prompt date, it cannot be classified as an executed trade. The recorded time of an executed trade must be the time when these details are finally confirmed. We believe that this is consistent with our rules and FSA requirements. We believe that 30 minutes to match the trade details from the time when all the details have been confirmed is achievable and reasonable.

Process of confirming the performance benchmarks

In order to guard against material errors in trade input performance records, the LME proposes that members are given three weeks from the time they