

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-51959; File No. SR-CME-2005-01)

June 30 , 2005

Self-Regulatory Organization; Chicago Mercantile Exchange; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Listing Standards for Security Futures Products

Pursuant to Section 19(b)(7) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-7 thereunder,² notice is hereby given that on May 4, 2005, the Chicago Mercantile Exchange (“CME” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I, II, and III below, which Items have been prepared by CME.

CME has also certified the proposed rule change with the Commodity Futures Trading Commission (“CFTC”) under Section 5c(c) of the Commodity Exchange Act (“CEA”)³ on May 4, 2005. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

CME proposes to amend its Security Futures Product Listing Standards (“Listing Standards”) for purposes of Section 6(h) of the Act.⁴ These amendments are intended to conform CME Listing Standards for physically settled security futures products, including exchange traded funds (“ETFs”), trust issued receipts (“TIRs”), closed-end funds and narrow-based indices (“NRIs”), to current industry practices. The text of the proposed rule change is

¹ 15 U.S.C. 78s(b)(7).

² 17 CFR 240.19b-7.

³ 7 U.S.C. 7a-2(c).

⁴ 15 U.S.C. 78f(h).

below. Proposed new language is italicized; and proposed deletions are in [brackets].

CHAPTER 700: SECURITY FUTURES PRODUCT LISTING STANDARDS

70000. SCOPE OF CHAPTER

No change.

70001. SINGLE SECURITY FUTURES – INITIAL LISTING STANDARDS

For a Security Futures Product, that is physically settled, to be eligible for initial listing, the security underlying the futures contract must meet each of the following requirements:

- 1.-5. No change.
6. In the case of an underlying security other than an ETF Share, TIR or Closed-End Fund Share, it must have had [an average daily trading volume (in all markets in which the underlying security has traded) of at least 109,000 shares or receipts evidencing the underlying security in each of the preceding 12 months.] total trading volume (in all markets in which the underlying security is traded) of at least 2,400,000 shares or receipts evidencing the underlying security in the preceding 12 months.

Interpretation of Requirement 6 as Applied to Restructure Securities

No change.

7. No change.
8. [It must have had a market price per security of at least \$7.50, as measured by the lowest closing price reported in any market in which it has traded, for the majority of business days during the three calendar months preceding the date of selection.] If the underlying security is a “covered security as defined under Section 18(b)(1)(A) of the Securities Act of 1933, the market price per share of the underlying security has been at least \$3.00 for the previous five consecutive business days preceding the date on which the Exchange commences to list and

trade the Security Futures Product on said underlying security. For purposes of this provision, the market price of such underlying security is measured by the closing price reported in the primary market in which the underlying security is traded.

Interpretation of Requirement 8 as Applied to Restructure Securities

Look-Back Test: In determining whether a Restructure Security that is issued or distributed to the shareholders of an Original Equity Security (but not a Restructure Security that is issued pursuant to a public offering or rights distribution) satisfies this requirement, the Exchange may “look back” to the market price history of the Original Equity Security prior to the ex-date of the Restructuring Transaction if the following Look-Back Test is satisfied:

- a. The Restructure Security has an aggregate market value of at least \$500 million;
- b. The aggregate market value of the Restructure Security equals or exceeds the Relevant Percentage (defined below) of the aggregate market value of the Original Equity Security;
- c. The aggregate book value of the assets attributed to the business represented by the Restructure Security equals or exceeds both \$50 million and the Relevant Percentage of the aggregate book value of the assets attributed to the business represented by the Original Equity Security; or
- d. The revenues attributed to the business represented by the Restructure Security equals or exceeds both \$50 million and the Relevant Percentage of the revenues attributed to the business represented by the Original Equity Security.

For purposes of determining whether the Look-Back Test is satisfied, the term “Relevant Percentage” means: (i) 25%, when the applicable measure determined with respect to the Original Equity Security or the business it represents includes the business represented by the Restructure Security; and (ii) 33-1/3%, when the applicable measure determined with respect to the Original Equity Security or the business it represents excludes the business represented by the Restructure Security.

In calculating comparative aggregate market values, the Exchange will use the Restructure Security’s closing price on its primary market on the last business day prior to the Selection Date, or the Restructure Security’s opening price on its primary market on the Selection Date, and will use the corresponding closing or opening price of the related Original Equity Security.

Furthermore, in calculating comparative asset values and revenues, the Exchange will use the issuer’s (i) latest annual financial statements or (ii) most recently available interim financial statements (so long as such interim financial statements cover a period of not less than three months), whichever are more recent. Those financial statements may be audited or unaudited and may be pro forma.

Restructure Securities Issued in Public Offering or Rights Distribution: In

determining whether a Restructure Security that is distributed pursuant to a public offering or a rights distribution satisfies requirement [(viii)] 8, the Exchange may look back to the market price history of the Original Equity Security if: (i) the foregoing Look-Back Test is satisfied; (ii) the Restructure Security trades “regular way” on an exchange or automatic quotation system for at least five trading days immediately preceding the Selection Date; and (iii) at the close of trading on each trading day on

which the Restructure Security trades “regular way” prior to the Selection Date, as well as at the opening of trading on Selection Date, the market price of the Restructure Security was at least [\$7.50] \$3.00.

Limitation on Use of Look-Back Test: Except in the case of a Restructure Security that is distributed pursuant to a public offering or rights distribution, the Exchange will not rely upon the market price history of an Original Equity Security for any trading day unless it also relies upon the trading volume history for that trading day. In addition, once the Exchange commences to rely upon a Restructure Security’s trading volume and market price history for any trading day, the Exchange will not rely upon the trading volume and market price history of the related Original Equity Security for any trading day thereafter.

9. If the underlying security is not a “covered security as defined under Section 18(b)(1)(A) of the Securities Act of 1933, the market price per share of the underlying security has been at least \$7.50 for the previous five consecutive business days preceding the date on which the Exchange commences to list and trade the Security Futures Product on said underlying security. For purposes of this provision, the market price of such underlying security is measured by the closing price reported in the primary market in which the underlying security is traded.

Interpretation of Requirement 9 as Applied to Restructure Securities

Look-Back Test: In determining whether a Restructure Security that is issued or distributed to the shareholders of an Original Equity Security (but not a Restructure Security that is issued pursuant to a public offering or rights distribution) satisfies this requirement, the Exchange may “look back” to the market price history of the Original

Equity Security prior to the ex-date of the Restructuring Transaction if the following Look-Back Test is satisfied:

- a. The Restructure Security has an aggregate market value of at least \$500 million;
- b. The aggregate market value of the Restructure Security equals or exceeds the Relevant Percentage (defined below) of the aggregate market value of the Original Equity Security;
- c. The aggregate book value of the assets attributed to the business represented by the Restructure Security equals or exceeds both \$50 million and the Relevant Percentage of the aggregate book value of the assets attributed to the business represented by the Original Equity Security; or
- d. The revenues attributed to the business represented by the Restructure Security equals or exceeds both \$50 million and the Relevant Percentage of the revenues attributed to the business represented by the Original Equity Security.

For purposes of determining whether the Look-Back Test is satisfied, the term “Relevant Percentage” means: (i) 25%, when the applicable measure determined with respect to the Original Equity Security or the business it represents includes the business represented by the Restructure Security; and (ii) 33-1/3%, when the applicable measure determined with respect to the Original Equity Security or the business it represents excludes the business represented by the Restructure Security.

In calculating comparative aggregate market values, the Exchange will use the Restructure Security’s closing price on its primary market on the last business day prior

to the Selection Date, or the Restructure Security's opening price on its primary market on the Selection Date, and will use the corresponding closing or opening price of the related Original Equity Security.

Furthermore, in calculating comparative asset values and revenues, the Exchange will use the issuer's (i) latest annual financial statements or (ii) most recently available interim financial statements (so long as such interim financial statements cover a period of not less than three months), whichever are more recent. Those financial statements may be audited or unaudited and may be pro forma.

Restructure Securities Issued in Public Offering or Rights Distribution: In

determining whether a Restructure Security that is distributed pursuant to a public offering or a rights distribution satisfies requirement 9, the Exchange may look back to the market price history of the Original Equity Security if: (i) the foregoing Look-Back Test is satisfied; (ii) the Restructure Security trades "regular way" on an exchange or automatic quotation system for at least five trading days immediately preceding the Selection Date; and (iii) at the close of trading on each trading day on which the Restructure Security trades "regular way" prior to the Selection Date, as well as at the opening of trading on Selection Date, the market price of the Restructure Security was at least \$7.50.

Limitation on Use of Look-Back Test: Except in the case of a Restructure Security that

is distributed pursuant to a public offering or rights distribution, the Exchange will not rely upon the market price history of an Original Equity Security for any trading day unless it also relies upon the trading volume history for that trading day. In addition, once the Exchange commences to rely upon a Restructure Security's trading volume and

market price history for any trading day, the Exchange will not rely upon the trading volume and market price history of the related Original Equity Security for any trading day thereafter.

[9.] 10. If the underlying security is an ADR:

- a. The Exchange must have an effective surveillance sharing agreement with the primary exchange in the home country where the stock underlying the ADR is traded;
- b. The combined trading volume of the ADR and other related ADRs and securities in the U.S. ADR market, or in markets with which the Exchange has in place an effective surveillance sharing agreement, represents (on a share equivalent basis) at least 50% of the combined worldwide trading volume in the ADR, the security underlying the ADR, other classes of common stock related to the underlying security, and ADRs overlying such other stock over the three-month period preceding the dates of selection of the ADR for futures trading (“Selection Date”);
- c.
 - (1) The combined trading volume of the ADR and other related ADRs and securities in the U.S. ADR market, and in markets where the Exchange has in place an effective surveillance sharing agreement, represents (on a share equivalent basis) at least 20% of the combined worldwide trading volume in the ADR and in other related ADRs and securities over the three-month period preceding the Selection Date;

- (2) The average daily trading volume for the ADR in the U.S. markets over the three-month period preceding the Selection Date is at least 100,000 receipts; and
- (3) The daily trading volume for the ADR is at least 60,000 receipts in the U.S. markets on a majority of the trading days for the three-month period preceding the Selection Date.

Or

- d. The Securities and Exchange Commission and Commodity Futures Trading Commission have otherwise authorized the listing.

[10.] 11. The Exchange will not list for trading any SFP where the underlying security is a Restructure Security that is not yet issued and outstanding, regardless of whether the Restructure Security is trading on a “when issued” basis or on another basis that is contingent upon the issuance or distribution of securities.

70002. SINGLE SECURITY FUTURES – MAINTENANCE LISTING STANDARDS

1. [Absent exceptional circumstances, the] The Exchange will not open for trading any SFP, that is physically settled, with a new delivery month, and may prohibit any opening purchase transactions in the SFP already trading, to the extent it deems such action necessary or appropriate, unless the underlying security meets each of the following maintenance requirements; provided that, if the underlying security is an ETF Share, TIR or Closed-End Fund Share, the applicable requirements for initial listing of the related SFP (as described in Rule 70001 above) shall apply in lieu of the following maintenance requirements:
 - a. It must be registered under Section 12 of the Exchange Act.

[a.]b. There must be at least 6,300,000 shares or receipts evidencing the underlying security outstanding that are owned by persons other than those who are required to report their security holdings pursuant to Section 16(a) of the Exchange Act.

[b.] c. There must be at least 1,600 securityholders.

[c.] d. It must have had an average daily trading volume (across all markets in which the underlying security is traded) of least 82,000 shares or receipts evidencing the underlying security in each of the preceding 12 months.

Interpretation of Requirement [1.c.] 1.d. as Applied to Restructure Securities

If a Restructure Security is approved for a SFP trading under the initial listing standards in [Section I] Rule 70001, the average daily trading volume history of the Original Equity Security (as defined in [Section I] Rule 70001) prior to the commencement of trading in the Restructure Security (as defined in [Section I] Rule 70001), including “when-issued” trading, may be taken into account in determining whether this requirement is satisfied.

[d.] The security underlying the Security Futures Product must have had a market price of at least \$5.00, as measured by the highest closing price reported in any market in which it has traded, for a majority of business days during the preceding six calendar months; provided, however, that the Exchange may waive this requirement and open for trading a SFP with a new delivery month, if:

- (1) The aggregate market value of the underlying security equals or exceeds \$50 million;
- (2) Customer open interest (reflected on a two-sided basis) equals or exceeds 4,000 contracts for all delivery months;
- (3) Its average daily trading volume (in all markets in which the underlying security

is traded) has been at least 109,000 shares or receipts evidencing the underlying security in each of the preceding 12 months; and

- (4) The market price per share or receipt of the underlying security closed at \$3.00 or above on a majority of the business days during the preceding six calendar months, as measured by the highest closing price for the underlying security reported in any market in which the underlying security traded, and the market price per share or receipt of the underlying security is at least \$3.00 at the time such additional series are authorized for trading. During the next consecutive six calendar month period, to satisfy this paragraph, the market price per share or receipt of the underlying security must be at least \$4.00.]

e. The market price per share or receipt of the underlying security has not closed below \$3.00 on the previous trading day to the Expiration Day of the nearest expiring Contract on the underlying security. The market price per share of the underlying security will be measured by the closing price reported in the primary market in which the underlying security traded.

Interpretation of Requirement [d] 1.e. as Applied to Restructure Securities

If a Restructure Security is approved for SFP trading under the initial listing standards per Rule 70001[.8], the market price history of the Original Equity Security prior to the commencement of trading in the Restructure Security, including “when-issued” trading, may be taken into account in determining whether this requirement is satisfied.

[e.] f. If the underlying security is an ADR and was initially deemed appropriate for SFP trading per Rule 70001.10.b or Rule 70001.10.c.[.8.b. or 70001.8.c.], the Exchange will not open for trading SFPs having additional delivery months on the ADR unless:

- (1) The percentage of worldwide trading volume in the ADR and other related securities that takes place in the U.S. and in markets with which the Exchange has in place effective surveillance sharing agreements for any consecutive three-month period is: (1) at least 30%, without regard to the average daily trading volume in the ADR; or (2) at least 15% when the average U.S. daily trading volume in the ADR for the previous three months is at least 70,000 receipts;
- (2) The Exchange has in place an effective surveillance sharing agreement with the primary exchange in the home country where the security underlying the ADR is traded; or
- (3) The Securities and Exchange Commission and Commodity Futures Trading Commission have otherwise authorized the listing.

2.-4. No change.

70003. SFPs BASED ON INDEX COMPOSED OF TWO OR MORE SECURITIES – INITIAL LISTING STANDARDS

No change.

70004. SFPs BASED ON INDEX COMPOSED OF TWO OR MORE SECURITIES – MAINTENANCE LISTING STANDARDS

The Exchange will not open for trading SFPs, that are physically settled, based on an index composed of two or more securities with a new delivery month unless the underlying index:

1. No change.
2. Meets the following requirements:
 - a.-i. No change.

Interpretation of Requirement 2.i. Regarding Procedures for Rebalancing

[The date of determination for the mandatory annual rebalancing of an approximately equal dollar-weighted index underlying a physically settled security futures product as

described in the first sentence of (i) will initially be the last trading day of the year, except that, if the Exchange has rebalanced such index on an interim basis as described in the second sentence of (i), any following annual rebalancing of such index will occur on the anniversary date of the interim rebalancing. New contracts issued on or after a date on which the corresponding index is rebalanced in accordance with (i) will be based on an index consisting of the original component securities, weighted applying the methodology described under (i) above on the basis of security prices on the rebalancing date. Outstanding contracts will not be affected by any rebalancing.]

In the case of a physically settled SFP based on an approximately equal dollar-weighted index composed of one or more securities, each component security will be weighted equally based on its market price on the Selection Date, subject to rounding up or down the number of shares or receipts evidencing such security to the nearest multiple of 100 shares or receipts.

j.-1. No change.

* * * * *

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects or such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange has Listing Standards applicable to physically settled security futures products (“SFPs”) for NBIs and for single security products, including ETFs, TIRs, and shares of registered closed-end management investment companies (“Closed-End Fund”).⁵ The Exchange proposes to amend its Listing Standards to conform to current industry practices. In particular, the Exchange proposes to amend the current requirement that a security underlying a SFP, other than an ETF, TIR, or Closed-End Fund share, must have had an average daily trading volume of at least 109,000 shares or receipts evidencing the underlying security in each of the preceding 12 months to adopt a requirement, in conformance with current industry practice (and the standards for an ETFs, TIRs, and Closed-End Fund share), that such security must evidence total trading volume of at least 2,400,000 shares or receipts evidencing the underlying security in the preceding 12 months. Finally, the Exchange also proposes to adopt other minor or technical amendments to its Listing Standards to conform with industry practices, such as adjusting the market price per share of a security underlying a SFP to distinguish between a covered security as defined under Section 18(b)(1)(A) of the Securities Act of 1933 and a security that is “not covered.”⁶

⁵ See Securities Exchange Act Release No. 46975 (December 9, 2002), 67 FR 77297 (December 17, 2002) (SR-CME-2002-02).

⁶ The joint order by the CFTC and the Commission modifying the requirement specified in Section 6(h)(3)(D) of the Act and the criterion specified in Section 2(a)(1)(D)(i)(III) of the CEA to permit an ETF share, TIR or Closed-End Fund share to underlie a security future also provides that the market price of the underlying share be \$7.50 for the majority of business days during the three calendar months preceding listing of the SFP and that the issuer of the ETF, TIR, or Closed-End Fund be in compliance with all of the applicable requirements of the Act. See Securities Exchange Act Release No. 46090 (June 19, 2002), 67 FR 42760 (June 25, 2002). CME intends to comply with this joint

Section 6(h)(3) of the Act Requirements

Section 6(h)(3) of the Act⁷ contains listing standards and conditions for trading SFPs. Below is a summary of each such requirement or condition, followed by a brief explanation of how CME would comply with it, whether by particular provisions in CME Listing Standards or otherwise.

Clause (A) of Section 6(h)(3) of the Act⁸ requires that any security underlying a SFP be registered pursuant to Section 12 of the Act.⁹ This requirement is addressed by CME Rules 70001.2, 70003.2.b, 70004.2.a, and proposed CME Rule 70002.1.a.

Clause (B) of Section 6(h)(3) of the Act¹⁰ requires that a market on which a physically settled SFP is traded have arrangements in place with a registered clearing agency for the payment and delivery of the securities underlying the SFP. CME has reached an agreement with a participant of DTC, a registered clearing agency, to facilitate the delivery-versus-payment transactions which result from an agreement to make or take delivery of the underlying security by the market participant.¹¹ This DTC participant would provide CME with a dedicated DTC account. This account would be a sub-account of the participant's main account and would be utilized solely for CME activity with respect to the delivery of, and payment for, securities

order. Telephone conversation between John Labuszewski, Managing Director, CME, and Florence E. Harmon, Senior Special Counsel, Division of Market Regulation ("Division"), Commission, on June 28, 2005.

⁷ 15 U.S.C. 78f(h)(3).

⁸ 15 U.S.C. 78f(h)(3)(A).

⁹ 15 U.S.C. 78l.

¹⁰ 15 U.S.C. 78f(h)(3)(B).

¹¹ The Exchange clarified its arrangement for the payment and delivery of securities underlying the SFPs. Telephone conversation between John Labuszewski, Managing Director, CME, and Florence E. Harmon, Senior Special Counsel, Division, Commission, on June 9, 2005.

delivered against CME SFPs. CME would act as a contra party to each delivery transaction. The CME Clearing House would submit a delivery instruction for each transaction to DTC by electronic interface provided by the DTC participant. Market participants would be required to provide proof to CME outlining their operational and legal ability to make or take delivery of the underlying securities. These agreements and relevant procedures would be fully operational prior to any possible delivery event associated with such SFPs.

Clause (C) of Section 6(h)(3) of the Act¹² provides that listing standards for SFPs must be no less restrictive than comparable listing standards for options traded on a national securities exchange or national securities association registered pursuant to Section 15A(a) of the Act.¹³ For the reasons discussed herein, notwithstanding specified differences between the Sample Listing Standards and CME Listing Standards, CME believes that the latter are no less restrictive than comparable listing standards for exchange-traded options.

Clause (D) of Section 6(h)(3) of the Act¹⁴ requires that each SFP be based on common stock or such other equity securities as the Commission and CFTC jointly determine are appropriate. This requirement is addressed by CME Rules 70001.1, 70002.1., 70003.2., and 70004.2.

Clause (E) of Section 6(h)(3) of the Act¹⁵ requires that each SFP be cleared by a clearing agency that has in place provisions for linked and coordinated clearing with other clearing agencies that clear SFPs, which permits the SFPs to be purchased on one market and offset on another market that trades such product. CME proposes to clear SFPs traded through Exchange

¹² 15 U.S.C. 78f(h)(3)(C).

¹³ 15 U.S.C. 78o-3(a).

¹⁴ 15 U.S.C. 78f(h)(3)(D).

¹⁵ 15 U.S.C. 78f(h)(3)(E).

facilities through CME Clearing House. CME Clearing House would have in place all provisions for linked and coordinated clearing as mandated by law and statute as of the effective date of such laws and statutes.

Clause (F) of Section 6(h)(3) of the Act¹⁶ requires that only a broker or dealer subject to suitability rules comparable to those of a national securities association registered pursuant to Section 15A(a) of the Act¹⁷ effect transactions in a SFP. CME clearing members and their correspondents are bound by the applicable sales practice rules of the National Futures Association (“NFA”), which is a national securities association. As such, the sales practice rules of NFA are, perforce, comparable to those of a national securities association registered pursuant to Section 15A(a) of the Act.¹⁸ Moreover, the application of NFA sales practice rules is extended beyond the CME clearing membership to the extent that NFA By-Law 1101 provides that “[n]o member may carry an account, accept an order or handle a transaction in commodity futures contracts for or on behalf of any non-Member of NFA.”

Clause (G) of Section 6(h)(3) of the Act¹⁹ requires that each SFP be subject to the prohibition against dual trading in Section 4j of CEA²⁰ and the rules and regulations thereunder or the provisions of Section 11(a) of the Act²¹ and the rules and regulations thereunder. CME Rule 123 requires Exchange members to comply with all applicable “provisions of the Commodity Exchange Act and regulations duly issued pursuant thereto by the CFTC.”

¹⁶ 15 U.S.C. 78f(h)(3)(F).

¹⁷ 15 U.S.C. 78o-3(a).

¹⁸ 15 U.S.C. 78o-3(a).

¹⁹ 15 U.S.C. 78f(h)(3)(G).

²⁰ 15 U.S.C. 4j.

²¹ 15 U.S.C. 78k(a).

Further, the prohibition of dual trading in SFPs per Regulation §41.27²² adopted pursuant to Section 4j(a) of CEA²³ applies to a contract market operating an electronic trading system if such market provides participants with a time or place advantage or the ability to override a predetermined matching algorithm. The Exchange intends to offer SFPs on CME exclusively on its CME Globex electronic trading platform. To the extent that the conditions cited above do not exist in the context of the CME Globex system, the CME Rulebook contains no specific rule relating to dual trading in an electronic forum.

Clause (H) of Section 6(h)(3) of the Act²⁴ provides that trading in a SFP must not be readily susceptible to manipulation of the price of such SFP, nor to causing or being used in the manipulation of the price of any underlying security, option on such security, or option on a group or index including such securities. CME believes that CME Listing Standards are designed to ensure that CME SFPs and the underlying securities would not be readily susceptible to price manipulation. Under CME Rule 432, an activity “to manipulate prices or to attempt to manipulate prices” is a “major offense” punishable, per CME Rule 430, by “expulsion, suspension, and/or a fine of not more than \$1,000,000 plus the monetary value of any benefit received as a result of the violative action.”

Clause (I) of Section 6(h)(3) of the Act²⁵ requires that procedures be in place for coordinated surveillance amongst the market on which a SFP is traded, any market on which any security underlying the SFP is traded, and other markets on which any related security is traded to detect manipulation and insider trading. The Exchange has surveillance procedures in place to

²² 17 CFR 41.27.

²³ 7 U.S.C. 6j(a).

²⁴ 15 U.S.C. 78f(h)(3)(H).

²⁵ 15 U.S.C. 78f(h)(3)(I).

detect manipulation on a coordinated basis with other markets. In particular, CME is an affiliate member of the Intermarket Surveillance Group (“ISG”) and is party to an affiliate agreement and an agreement to share market surveillance and regulatory information with the other ISG members. Further, CME is party to a supplemental agreement with the other ISG members to address the concerns expressed by the Commission with respect to affiliate ISG membership.²⁶ Finally, CME Rule 424 permits CME to enter into agreements for the exchange of information and other forms of mutual assistance with domestic or foreign self-regulatory organizations, associations, boards of trade, and their respective regulators.

Clause (J) of Section 6(h)(3) of the Act²⁷ requires that a market on which a SFP is traded have in place audit trails necessary or appropriate to facilitate the coordinated surveillance referred to in the preceding paragraph. The Exchange states that it relies upon its Market Regulation Department and its large, highly trained staff to actively monitor market participants and their trading practices and to enforce compliance with CME rules. CME Market Regulation Department staff is organized into Compliance and Market Surveillance Groups. In performing its functions, CME Market Regulation Department routinely works closely with CME Audit Department, CME Clearing House, CME Legal Department, CME Globex Control Center, and CME Information Technology Department.

CME Compliance is responsible for enforcing the trading practice rules of the Exchange through detection, investigation, and prosecution of those who may attempt to violate those CME Rules. Further, CME Compliance is responsible for handling customer complaints, ensuring the

²⁶ See Securities Exchange Act Release No. 45956 (May 17, 2002), 67 FR 36740 (May 24, 2002) (joint CFTC and Commission rule relating to cash settlement and regulatory halt requirements for SFPs).

²⁷ 15 U.S.C. 78f(h)(3)(J).

integrity of the Exchange's audit trail, and administering an arbitration program for the resolution of disputes. CME Compliance employs investigators, attorneys, trading floor investigators, data analysts, and a computer programming and regulatory systems design staff.

CME believes that CME Market Regulation Department has created some of the most sophisticated tools in the world to assist with the detection of possible rule violations and monitoring of the market. Among the systems it uses are the Regulatory Trade Browser ("RTB"), the Virtual Detection System ("VDS"), the Reportable Position System ("RPS"), and the RegWeb Profile System ("RegWeb"). These systems include information on all CME Globex users, all transactions, large positions, and statistical information on trading entities.

CME Market Surveillance is dedicated to the detection and prevention of market manipulation and other similar forms of market disruption. As part of these responsibilities, CME Market Surveillance enforces the Exchange's position limit rules, administers the hedge approval process, and maintains the Exchange's RPS system.

CME believes that the foundation of the CME Market Surveillance program is the deep knowledge of its staff about the major users, brokers, and clearing firms, along with its relationship with other regulators. Day-to-day monitoring of market positions is handled by a dedicated group of surveillance analysts assigned to specific market(s). Each analyst develops in-depth expertise of the factors that influence the market in question. The Exchange estimates that perhaps 90% of the market users at any single time are known to the Exchange. Daily surveillance staff activities include:

- Monitoring positions for size based on percentage of open interest and historic user participation in each contract.
- Aggregation of positions across clearing members with the use of CME trade

reporting systems to account for all positions held by any single participant. CME believes that this daily review permits the surveillance analyst to promptly identify unusual market activity.

- As a contract approaches maturity, large positions are scrutinized to determine whether such activity is consistent with prior experience, allowing prompt regulatory intervention if necessary.
- Analysts closely monitor market news through on-line and print media.
- Staff conducts on-site visits to large market participants periodically.

CME Market Regulation staff investigates possible misconduct and, when appropriate, initiates disciplinary action. CME Rule 430 empowers the Exchange's disciplinary committees to discipline, limit, suspend, or terminate a member's activities for cause, amongst other sanctions. Further, per CME Rule 123, the Exchange requires its members to be responsible for "the filing of reports, maintenance of books and records, and permitting inspection and visitation" in order to facilitate such investigations by Exchange staff.

CME Rule 536 requires that certain information be recorded with respect to each order, including: time entered, terms of the order, order type, instrument and contract month, price, quantity, account type, account designation, user code, and clearing firm. This information may be recorded manually on timestamped order tickets, electronically in a clearing firms system, or by entering the orders with the required information into CME Globex immediately upon receipt. A complete CME Globex electronic audit trail is archived and maintained by CME for at least a five year period. Clearing firms must also maintain any written or electronic order records for a period of five years.

Clause (K) of Section 6(h)(3) of the Act²⁸ requires that a market on which a SFP is traded have in place procedures to coordinate trading halts between such market and any market on which any security underlying the SFP is traded and other markets on which any related security is traded. The Exchange filed with the Commission CME Rules establishing a generalized framework for the trade of SFPs.²⁹ In particular, proposed CME Rule 71001.F. provides, in accordance with Regulation §41.25(a)(2) of CEA,³⁰ that “[t]rading of Physically Delivered Single Security Futures shall be halted at all times that a regulatory halt, as defined per SEC Rule 6h-1(a)(3) and CFTC Regulation §41.1(l), has been instituted for the underlying security.”

Clause (L) of Section 6(h)(3) of the Act³¹ requires that the margin requirements for a SFP comply with the regulations prescribed pursuant to Section 7(c)(2)(B) of the Act.³² CME has margin rules in place.³³ Thus, CME believes that its customer margin rules are consistent with the requirements of the Act.

For the reasons described above, CME believes that CME Listing Standards submitted herewith satisfy the requirements set forth in Section 6(h)(3) of the Act.³⁴

2. Statutory Basis

The Exchange believes that its proposed rule change is consistent with Section 6(b) of the

²⁸ 15 U.S.C. 78f(h)(3)(K).

²⁹ See SR-CME-2005-03.

³⁰ 17 CFR 41.25(a)(2).

³¹ 15 U.S.C. 78f(h)(3)(L).

³² 15 U.S.C. 78g(c)(2)(B).

³³ See Securities Exchange Act Release No. 46637 (October 10, 2002), 67 FR 64672 (October 21, 2002) (SR-CME-2002-01).

³⁴ 15 U.S.C. 78f(h)(3).

Act,³⁵ in general, and furthers the objectives of Section 6(b)(5) of the Act,³⁶ in particular, in that it is designed to remove impediments to and perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

CME does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from members or other interested parties.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing proposed rule change has become effective pursuant to Section 19(b)(7) of the Act.³⁷ Within 60 days of the date of effectiveness of the proposed rule change, the Commission, after consultation with the CFTC, may summarily abrogate the proposed rule change and require that the proposed rule change be refiled in accordance with the provisions of Section 19(b)(1) of the Act.³⁸

³⁵ 15 U.S.C. 78f(b).

³⁶ 15 U.S.C. 78f(b)(5).

³⁷ 15 U.S.C. 78s(b)(7).

³⁸ 15 U.S.C. 78s(b)(1).

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-CME-2005-01 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-CME-2005-01. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Section. Copies of such filing also will be available for inspection and copying at the principal office of CME. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to

make available publicly. All submissions should refer to File Number SR-CME-2005-01 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.³⁹

Margaret H. McFarland
Deputy Secretary

³⁹ 17 CFR 200.30-3(a)(12).