

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](mailto:rule-comments@sec.gov). Please include File Number SR-CME-2005-02 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-2005-02. 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-2005-02 and should be submitted on or before August 1, 2005.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>38</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-51957; File No. SR-CME-2005-03]

### Self-Regulatory Organization; Chicago Mercantile Exchange; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change and Amendment No. 1 Thereto Relating to Rules Governing Contract Specifications for Physically Delivered Single Security Futures

June 30, 2005.

Pursuant to Section 19(b)(7) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-7 thereunder,<sup>2</sup> 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 the Exchange. On May 31, 2005, CME filed Amendment No. 1 to the proposed rule change.<sup>3</sup> The Commission is publishing this notice, as amended, to solicit comments on the proposed rule change from interested persons.

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")<sup>4</sup> on May 4, 2005.

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

CME proposes to adopt rules governing the trade of physically delivered single security futures products ("SFPs"). Further, the Exchange hereby certifies the listing of futures on Exchange Traded Funds ("ETFs"), specifically, the Nasdaq-100 Tracking Stock<sup>SM</sup> ("QQQ"), Standard & Poor's Depository Receipts<sup>®</sup> ("SPDR"), and IWM.<sup>5</sup> The Exchange

<sup>1</sup> 15 U.S.C. 78s(b)(7).

<sup>2</sup> 17 CFR 240.19b-7.

<sup>3</sup> See letter from John W. Labuszewski, Managing Director, CME, to Florence E. Harmon, Senior Special Counsel, Division of Market Regulation ("Division"), Commission, on May 31, 2005. ("Amendment No. 1"). In Amendment No. 1, the Exchange proposes to amend the size of its iShares Russell 2000 ("IWM") futures contract to 200 instead of 100 shares. The Exchange believes that this implies that the value of the \$0.01 minimum price fluctuation shall be \$2.00 instead of \$1.00. Also, the Exchange proposes to amend the launch date for IWM futures to June 20, 2005 from June 6, 2005.

<sup>4</sup> 7 U.S.C. 7a-2(c).

<sup>5</sup> The Exchange proposes to make the proposed rule change effective on June 6, 2005 when it intends to list for trading futures based on SPDRs and QQQs. The Exchange proposes to list futures based on IWMs on June 20, 2005. See Amendment No. 1, *supra* note 3.

believes that these contract specifications are substantially similar to contract specifications currently in use with respect to physically delivered single security futures traded elsewhere. Proposed new language is *italicized*.

#### CHAPTER 710: PHYSICALLY DELIVERED SINGLE SECURITY FUTURES

##### 71000. SCOPE OF CHAPTER

*This chapter is limited in application to contract specifications applied to security futures contracts that require the physical delivery of a single security (a "Physically Delivered Single Security Futures"). Single securities that are eligible for listing per this Chapter 710 include those that meeting the initial listing standards per Exchange Rule 70001 and the maintenance listing standards per Exchange Rule 70002.*

##### 71001. FUTURES CALL

###### 71001.A. Trading Unit

*Physically Delivered Single Security Futures contracts shall require the delivery of a particular number of shares, as specified per Rule 71004, of common stock; an exchange traded fund ("ETF Share"); a trust issued receipt ("TIR"); a registered closed-end management investment company ("Closed-End Fund Share"); or, American Depository Receipts ("ADR").*

###### 71001.B. Price Increments

*Physically Delivered Single Security Futures contracts shall be traded in U.S. Dollars with a minimum price increment as determined by the Board of Directors as depicted in Rule 71004.*

###### 71001.C. Trading Schedule

*Physically Delivered Single Security Futures contracts may be traded during such hours, for delivery in such months as determined by the Board of Directors.*

###### 71001.D. Termination of Trading

*All trading in a particular Physically Delivered Single Security Futures contract shall terminate at the close of business on the third Friday of the contract month.*

###### 71001.E. Position Limits

*Position limits shall be applied on Physically Delivered Single Security Futures contracts such that, during the last five trading days of an expiring contract month, a person shall not own or control more than a specified number of contracts net long or net short in the expiring contract month, as depicted in Exchange Rule 71004. Position limits for each Physically Delivered Single Security Futures contract shall be*

<sup>38</sup> 17 CFR 200.30-3(a)(12).

determined on a case-by-case basis at levels no greater than those prescribed by CFTC Regulation § 41.25(a)(3).

**71001.F. Price Limits and Trading Halts**

There is no daily price limit for Physically Delivered Single Security Futures contracts. Trading 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.

**71002. SETTLEMENT PRICE**

**71002.A. Daily Settlement Price**

Except for the last day of trading on an expiring contract, daily settlement prices shall be determined per Rule 813.

**71002.B. Final Settlement Price**

On the last day of trading for an expiring contract, the Final Settlement Price is determined in accordance with Rule 71002.A. unless the Final Settlement Price is fixed in accordance with Rule 70120.

**71003. DELIVERY**

Three (3) business days after the last trading day for an expiring contract, the National Securities Clearing Corporation and Depository Trust Corporation will facilitate delivery of, and payment for, the underlying common stock, American Depository Receipts, shares of exchange-traded funds, shares of closed-end

management investment companies, or trust issued receipts whereby: a seller (i.e., the holder of a net short position) delivers the securities underlying the contract to a respective buyer (i.e., the holder of a net long position); and, in exchange, that buyer pays his respective seller the aggregate dollar amount of the Expiration Day Settlement Price multiplied by the quantity of the underlying securities delivered.<sup>6</sup>

**71004. APPROVED SECURITIES**

The following securities have been approved by the Board of Directors as the subject of Physically Delivered Single Security Futures Contracts:

Approved security	Unit of trading	Minimum fluctuation	Position limit in expiring contract in last 5 trading days
Nasdaq-100 Tracking Stock <sup>SM</sup> ("QQQQ") .....	200 shares .....	\$0.01 or \$2.00 per contract .....	11,250
Standard & Poor's Depository Receipts <sup>®</sup> ("SPDR").	100 shares .....	\$0.01 or \$1.00 per contract .....	22,500
iShares Russell 2000 ("IWM") .....	200 shares .....	\$0.01 or \$2.00 per contract .....	<sup>7</sup> 11,250

<sup>7</sup> Trading in physically settled futures on IWMs did not qualify for the 22,500 position limit pursuant to CFTC Regulation § 41.25(a)(3)(i)(A) prior to the 2-for-1 split with an ex-date of June 9, 2005. However, after the split, futures based on IWMs do qualify for a net position limit no greater than 22,500 (100 share contract) pursuant to this CFTC Regulation. To the extent that CME amended the IWM contract size from the originally proposed 100 share contract to 200 share contract as a result of the split, the applicable position limit for futures on IWM contracts pursuant to CFTC Regulation § 41.25 would be 11,250. Telephone conversation between John Labuszewski, Managing Director, CME, and Florence E. Harmon, Senior Special Counsel, Division, Commission, on June 28, 2005.

**71005. EMERGENCIES, ACTS OF GOD, ACTS OF GOVERNMENT**

If delivery or acceptance or any precondition or requirement of either is prevented by a strike, fire, accident, action of government or act of God, the seller or buyer shall immediately notify the Exchange President. If the President determines that emergency action may be necessary, he shall call a special meeting of the Board of Directors and arrange for the presentation of evidence respecting the emergency condition. If the Board determines that an emergency condition exists, it shall take such action as it deems necessary under the circumstances and its decision shall be binding upon all parties to the contract.

**INTERPRETATIONS & SPECIAL NOTICES RELATING TO CHAPTER 710**

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**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, as amended. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared

<sup>6</sup> The Exchange has clarified that Depository Trust Corporation will facilitate delivery of, and payment for, the underlying common stock, American Depository Receipts, shares of exchange-

traded funds, shares of closed-end management investment companies, or trust issued receipts via a participant of DTC with whom CME has a dedicated account. Telephone conversation

between John Labuszewski, Managing Director, CME, and Florence E. Harmon, Senior Special Counsel, Division, Commission, on June 9, 2005.

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 proposes to adopt contract specifications governing physically delivered single security futures. Further, the Exchange proposes to list for trading, per such rules, futures on ETFs, specifically, QQQQ, SPDR, and IWM. The Exchange intends to offer physically delivered single security futures exclusively on CME's GLOBEX® electronic trading platform as opposed to trading on the floor of the Exchange.

*Contract Size*—CME Rule 71001.A., Trading Unit, specifies that "Physically Delivered Single Security Futures contracts shall require the delivery of a particular number of shares, as specified per CME Rule 71004, of common stock; an exchange traded fund ('ETF Share'); a trust issued receipt ('TIR'); a registered closed-end management investment company ('Closed-End Fund Share'); or, American Depository Receipts ('ADR')." CME Rule 71004, Approved Securities, provides that futures based on SPDRs shall be traded in units of 100 shares. SPDRs closed at \$117.96 on March 31, 2005. The Exchange believes that this implies a contract valuation of \$11,796.

However, the Exchange proposes to trade QQQQs and IWMs based upon a 200-share unit. The Nasdaq-100 Tracking Stock closed at \$36.57 on March 31, 2005, which equates to a contract value of \$7,314. IWMs closed at \$124.24 on March 31, 2005 but are scheduled to be split on a 2-for-1 basis on June 9, 2005 which, the Exchange believes, implies a post-split share value of \$62.12 or a contract value of \$12,424 based upon a 200-share contract.

The Exchange believes that these values are generally somewhat smaller than the size of the E-mini S&P 500, E-mini Russell 2000, and E-mini Nasdaq-100. The Exchange further believes that they are generally, with the exception of QQQQs and IWMs, consistent with practices in the context of other SFPs and with ETF-based options traded on stock option exchanges, which are generally based upon a 100-share trading unit.

*Quotation Specification*—CME Rule 71002.B., Price Increments, provides that "Physically Delivered Single Security Futures contracts shall be traded in U.S. Dollars with a minimum price increment as determined by the Board of Directors as depicted in Rule 71004." CME Rule 71004, Approved Securities, provides that ETF futures would be quoted in minimum increments of \$0.01 per share. The Exchange believes that this equates to a \$1.00 tick in the context of SPDRs and

a \$2.00 tick in QQQQs and IWMs. The Exchange further believes that this provision is not inconsistent with provisions associated with other extant SFPs or stock options based on ETFs. Moreover, the Exchange believes that a penny tick matches practices in the underlying ETF markets.

*Position Limits*—CME Rule 71001.E., Position Limits, provides that "[p]osition limits shall be applied on Physically Delivered Single Security Futures contracts such that, during the last five trading days of an expiring contract month, a person shall not own or control more than a specified number of contracts net long or net short in the expiring contract month, as depicted in CME Rule 71004. Position limits for each Physically Delivered Single Security Futures contract shall be determined on a case-by-case basis in accordance with CFTC Regulation § 41.25(a)(3)." CME Rule 71004, Approved Securities, provides that the position limit applied to futures based on QQQQs and IWMs during the last five trading days of an expiring contract month shall be 11,250 contracts and 22,500 contracts for SPDRs. The Exchange represents that these figures were determined by reference to CFTC Regulation § 41.25(a)(3),<sup>8</sup> which prescribes appropriate position limits by reference to the average daily volume (ADV) in the security over the prior six (6) months and the shares outstanding.

	ADV (10/04–3/05)	Shares outstanding (000)
SPDRs .....	51,890,256	425,860 (4/22/05)
IWMs (pre-split) .....	8,022,330	40,950 (4/22/05)
IWMs (post-split) .....	16,044,660	81,900 (4/22/05)
QQQQs .....	98,137,035	520,900 (4/21/05)

The Exchange believes that the 11,250 contract limit adopted in the context of IWMs and QQQQs is in conformance with CFTC Regulation § 41.25(a)(3)(i)(A)<sup>9</sup> which specifies that "where the average daily trading volume in the underlying security exceeds 20 million shares, or exceeds 15 million shares and there are more than 40 million shares of the underlying security outstanding, the designated contract market \* \* \* may adopt a net position limit no greater than 22,500 (100-share)

contracts." However, to the extent that the Exchange proposes to adopt a 200-share contract with respect to IWMs and QQQQs, the 22,500 limit need be halved to 11,250 contracts. Finally, the Exchange believes that SPDRs likewise exceed the parameters specified per CFTC Regulation § 41.25(a)(3)(i)(A).<sup>10</sup> Thus, the Exchange proposes to adopt a 22,500 limit, noting the proposed 100-share contract size.

*Trading Schedule*—The CME Board has determined that trading in futures on the three ETFs mentioned above

shall be conducted from 8:30 a.m. to 3:15 p.m., Mondays through Fridays (Chicago time), when the underlying markets for the ETFs are open.<sup>11</sup> The CME Board has further determined initially to list futures for delivery in the first two quarterly delivery months in the March, June, September, and December cycle plus the first two non-quarterly or "serial" months (January, February, April, May, July, August, October, November) per CME Rule 71001.C., Trading Schedule.

<sup>8</sup> 17 CFR 41.25(a)(3). IWMs qualify for the 22,500 position limit on a post-split basis because the trading volume and shares outstanding doubled due to the 2-for-1 split on June 9, 2005. Because of the split, the average daily trading volume is considered doubled for the most recent six-month period in compliance with CFTC Regulation

§ 41.25. Telephone conversation between John Labuszewski, Managing Director, CME, and Florence E. Harmon, Senior Special Counsel, Division, Commission, on June 28, 2005.

<sup>9</sup> 17 CFR 41.25(a)(3)(i)(A).

<sup>10</sup> 17 CFR 41.25(a)(3)(i)(A).

<sup>11</sup> CME confirmed that futures on the three ETFs would not be traded during holidays and other periods when the underlying markets for the ETFs are not open. Telephone conversation between Richard Co, Director of Financial Research, CME, and Florence E. Harmon, Senior Special Counsel, Division, Commission, on June 24, 2005.

SUMMARY TERMS AND CONDITIONS

Contract Size .....	One-hundred (100) ETF shares of S&P 500 (SPDR); or two-hundred (200) shares of Nasdaq-100 Tracking Stock <sup>SM</sup> (QQQQ) or iShares Russell 2000 (IWM).
Contract Months .....	March Quarterly Cycle plus first two serial months.
Trading Hours .....	Traded on the GLOBEX <sup>®</sup> electronic trading platform from 8:30 am to 3:15 pm Mondays through Fridays (Chicago times).
Minimum Price Fluctuation .....	\$0.01 or \$1.00 per contract in context of SPDRs; \$2.00 per contract in context of QQQQs and IWMs.
Trading Halts .....	Trading halts are coordinated with halts in the underlying ETFs.
Position Limits .....	11,250 contracts for QQQQs and IWMs and 22,500 contracts for SPDRs net long or short during the last five (5) trading days of an expiring contract.
Final Settlement Date .....	Third Friday of the Contract Month.
Last Trading Day .....	Trades until the normal close of trading on the Final Settlement Date.
Final Settlement .....	Final settlement is accomplished through delivery of the requisite number of ETF shares.

*Trading Halts*—CME Rule 71001.F., Price Limits and Trading Halts, provides that there would be no daily price limit for Physically Delivered Single Security Futures contracts. However, trading of Physically Delivered Single Security Futures shall be halted at all times that a regulatory halt, as defined in CFTC Regulation 41.1(1),<sup>12</sup> has been instituted for the underlying security. The Exchange believes that this provision is consistent with the prescriptions of CFTC Regulation § 41.25(a)(2)(i)<sup>13</sup> and Rule 6h-1(a)(3) of the Act.<sup>14</sup>

*Daily Settlement*—Settlement prices on a daily basis shall be established per current Exchange practices as defined in CME Rule 813, Settlement Price.

*Final Settlement*—Final settlement would be accomplished through the delivery of the underlying securities against the expiring contract per the provisions of CME Rule 71003, Delivery. Specifically, CME Rule 71003 provides that “[t]hree (3) business days after the last trading day for an expiring contract, the National Securities Clearing Corporation (“NSCC”) and Depository Trust Corporation (“DTC”) will

facilitate delivery of, and payment for, the underlying \* \* \* [security] \* \* \* whereby: A seller \* \* \* delivers the securities \* \* \* and, in exchange, that buyer pays his respective seller the aggregate dollar amount of the Expiration Day Settlement Price multiplied by the quantity of the underlying securities delivered.”<sup>15</sup> The invoice amount would be established per CME Rule 71002.B., Final Settlement Price, as the closing price of the futures contract established per normal settlement procedures.<sup>16</sup> Deliveries shall be facilitated through the CME Clearing House and its designated facilitating agents.

*Compliance With Listing Standards*—Single securities eligible for listing per these proposed rules would be governed by Chapter 700 of the Exchange’s Rulebook (“Rulebook”), which specifies initial and maintenance listing standards for physically delivered single security futures and for security futures based on an Index of two or more securities.<sup>17</sup> The Exchange believes that Chapter 710 of the Rulebook governing physically delivered single security

futures is based closely upon the specifications under which single security futures are traded elsewhere.

In order to attain initial eligibility for listing, a security must comply with certain requirements with respect to activity and issue size as discussed below. As illustrated in the accompanying table, all three of the subject securities meet the qualifications for initial listing as specified above.

- Per CME Rule 70001.1., “[t]here must be at least seven million shares or receipts evidencing the underlying security outstanding.”
- Per CME Rule 70001.7, “it must have had a total trading volume \* \* \* of at least 2,400,000 shares or receipts evidencing the underlying security in the preceding 12 months.”
- Per CME Rule 70001.8, “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.”<sup>18</sup>

	Shares outstanding (000)	Total volume (4/04–3/05)	Price (3/31/05)
SPDRs .....	425,860 (4/22/05)	11,841,058,200	\$117.96
IWMs .....	40,950 (4/22/05)	1,849,663,900	112.15
QQQQs .....	520,900 (4/21/05)	24,973,601,523	36.57

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

<sup>12</sup> 17 CFR 41.1(1).  
<sup>13</sup> 17 CFR 41.25(a)(2)(i).  
<sup>14</sup> 17 CFR 240.6h-1(a)(3).  
<sup>15</sup> As described below, CME has reached an agreement with a participant of DTC, a registered clearing agency, to facilitate the delivery-versus-payment transactions that result from an agreement to make or take delivery of the ETFs.  
<sup>16</sup> See Amendment No. 1, *supra* note 3.  
<sup>17</sup> Chapter 700 of the CME Rulebook has been developed for purposes of compliance with Section 6(h) of the Act. CME believes that CME Listing Standards are generally identical to the sample listing standards published in the Commission’s,

Division of Market Regulation Staff Legal Bulletin No. 15, as supplemented by the Joint Order of the Commission and CFTC identifying listing standards for shares of ETFs, TIRs, and Closed-End Fund. See Commission, Division: Staff Legal Bulletin No. 15: Listing Standards for Trading Security Futures Products (September 5, 2001). See also Securities Exchange Act Release No. 46090 (June 19, 2002), 67 FR 42760 (June 25, 2002).  
<sup>18</sup> 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 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.

Section 6(h)(3) of the Act<sup>19</sup> 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 Act<sup>20</sup> requires that any security underlying a SFP be registered pursuant to Section 12 of the Act.<sup>21</sup> 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 Act<sup>22</sup> 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.<sup>23</sup> 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 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 Act<sup>24</sup> 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.<sup>25</sup> 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 Act<sup>26</sup> 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 Act<sup>27</sup> 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 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 Act<sup>28</sup> 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 Act<sup>29</sup> 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.<sup>30</sup> 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 Act<sup>31</sup> requires that each SFP be subject to the prohibition against dual trading in Section 4j of CEA<sup>32</sup> and the rules and

regulations thereunder or the provisions of Section 11(a) of the Act<sup>33</sup> 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."

Further, the prohibition of dual trading in SFPs per Regulation § 41.27<sup>34</sup> adopted pursuant to Section 4j(a) of CEA<sup>35</sup> 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 Act<sup>36</sup> 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 Act<sup>37</sup> 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 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

<sup>19</sup> 15 U.S.C. 78f(h)(3).

<sup>20</sup> 15 U.S.C. 78f(h)(3)(A).

<sup>21</sup> 15 U.S.C. 78l.

<sup>22</sup> 15 U.S.C. 78f(h)(3)(B).

<sup>23</sup> 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.

<sup>24</sup> 15 U.S.C. 78f(h)(3)(C).

<sup>25</sup> 15 U.S.C. 78o-3(a).

<sup>26</sup> 15 U.S.C. 78f(h)(3)(D).

<sup>27</sup> 15 U.S.C. 78f(h)(3)(E).

<sup>28</sup> 15 U.S.C. 78f(h)(3)(F).

<sup>29</sup> 15 U.S.C. 78o-3(a).

<sup>30</sup> 15 U.S.C. 78o-3(a).

<sup>31</sup> 15 U.S.C. 78f(h)(3)(G).

<sup>32</sup> 15 U.S.C. 4j.

<sup>33</sup> 15 U.S.C. 78k(a).

<sup>34</sup> 17 CFR 41.27.

<sup>35</sup> 7 U.S.C. 6j(a).

<sup>36</sup> 15 U.S.C. 78f(h)(3)(H).

<sup>37</sup> 15 U.S.C. 78f(h)(3)(I).

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.<sup>38</sup> 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 Act<sup>39</sup> 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 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 Act<sup>40</sup> 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.<sup>41</sup> In particular, proposed CME Rule 71001.F. provides, in accordance with Regulation § 41.25(a)(2) of CEA,<sup>42</sup> 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 Act<sup>43</sup> requires that the margin requirements for a SFP comply with the regulations prescribed pursuant to Section 7(c)(2)(B) of the Act.<sup>44</sup> CME has margin rules in place.<sup>45</sup> 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.<sup>46</sup>

## 2. Statutory Basis

The Exchange believes that its proposed rule change, as amended, is consistent with Section 6(b) of the Act,<sup>47</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>48</sup> 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

<sup>40</sup> U.S.C. 78f(h)(3)(K).

<sup>41</sup> See SR-CME-2005-03.

<sup>42</sup> 17 CFR 41.25(a)(2).

<sup>43</sup> 15 U.S.C. 78f(h)(3)(L).

<sup>44</sup> 15 U.S.C. 78g(c)(2)(B).

<sup>45</sup> See Securities Exchange Act Release No. 46637 (October 10, 2002), 67 FR 64672 (October 21, 2002) (SR-CME-2002-01).

<sup>46</sup> 15 U.S.C. 78f(h)(3).

<sup>47</sup> 15 U.S.C. 78f(b).

<sup>48</sup> 15 U.S.C. 78f(b)(5).

<sup>38</sup> 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).

<sup>39</sup> 15 U.S.C. 78f(h)(3)(J).

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, as amended, 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, as amended, has become effective pursuant to Section 19(b)(7) of the Act.<sup>49</sup> Within 60 days of the date of effectiveness of the proposed rule change, as amended, 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.<sup>50</sup>

### **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](mailto:rule-comments@sec.gov). Please include File Number SR-CME-2005-03 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-2005-03. 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-2005-03 and should be submitted on or before August 1, 2005.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>51</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

[FR Doc. E5-3618 Filed 7-8-05; 8:45 am]

**BILLING CODE 8010-01-P**

## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-51959; File No. SR-CME-2005-01]

### **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**

June 30, 2005.

Pursuant to Section 19(b)(7) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-7 thereunder,<sup>2</sup> 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")<sup>3</sup> 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.<sup>4</sup> 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 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

<sup>51</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(7).

<sup>2</sup> 17 CFR 240.19b-7.

<sup>3</sup> 7 U.S.C. 7a-2(c).

<sup>4</sup> 15 U.S.C. 78f(h).

<sup>49</sup> 15 U.S.C. 78s(b)(7).

<sup>50</sup> 15 U.S.C. 78s(b)(1).