

CME UPDATE 03-07

July 7, 2003

I. **BOARD APPROVES AMENDMENT TO LIVE CATTLE CONTRACT TO INCORPORATE COUNTRY OF ORIGIN LABELING**

At its Regular Meeting on Wednesday, July 2, 2003, the Board of Directors approved an amendment to the Live Cattle contract to incorporate Country of Origin Labeling (COOL), Public Law 107-171. COOL is part of the 2002 Farm Bill and it will require all meat sold at retail (grocery stores) to carry a label showing the country (or countries) in which the animal was born, raised, and processed. This labeling requirement becomes effective September 30, 2004, and retailers are subject to a \$10,000 fine for each violation. In response to these labeling requirements, retailers are holding their suppliers (meat packers & processors, among others) responsible for meeting these same recordkeeping and documentation requirements, and in turn the packers are holding their suppliers (livestock producers) responsible.

The Live Cattle contract has been amended to incorporate COOL. This change will be effective, pending CFTC approval, with the October 2004 and subsequent contract months. The amendment is as follows with additions underlined:

CHAPTER 101 LIVE CATTLE FUTURES

All rules in this chapter shall be read to include the following:

IF THE SECRETARY OF AGRICULTURE HAS ISSUED REGULATIONS, IN ACCORDANCE WITH 7 USC 1638C, REQUIRING COUNTRY OF ORIGIN LABELING FOR BEEF AND THOSE REGULATIONS ARE, OR ARE SCHEDULED TO BECOME, EFFECTIVE AT ANY TIME DURING THE DELIVERY PERIOD, ALL CATTLE IN THE DELIVERY UNIT MUST BE BORN AND RAISED EXCLUSIVELY IN THE UNITED STATES. THE SELLER MUST TENDER DOCUMENTATION THAT CONFORMS TO INDUSTRY STANDARDS AT THE TIME OF DELIVERY VERIFYING COUNTRY OF ORIGIN INFORMATION REQUIRED BY THE REGULATION.

10100. SCOPE OF CHAPTER

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

Remainder of Chapter unchanged

If you have any questions, please contact Ms. Jennifer Evett, Senior Market Analyst, Commodity Product Development, at (312) 930-4579, or Mr. Paul Peterson, Director, Commodity Product Development, at (312) 930-4587.

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II. BOARD APPROVES AMENDMENTS TO RULE 106.I., RELATED PARTY EMPLOYEE TRANSFERS

At its Regular Meeting on Wednesday, July 2, 2003, the Board of Directors approved amendments to Rule 106.I. – Related Party Employee Transfers.

Previously, CME policy with respect to Rule 106.I. allowed for preferential clearing fees for:

Transactions for the accounts owned by each related party in a chain of related parties, provided that an employee of the related party, that directly or indirectly owns all the related parties in the chain, holds a membership pursuant to Rule 106.I. The initial purchase and any subsequent transfers pursuant to this rule are subject to approval by Exchange staff.

Accordingly, member fees were available to any entity that was 100% owned, either directly or indirectly, by the “holder of the I.” Under the policy, if a chain of related entities wished to secure member fees for the entire chain, the 106.I. membership must be positioned at the top of the chain.

As corporate structures evolve and change, the 106.I. membership occasionally ends up out of position. When this happens, the problem is identified during an audit and the firm is assessed the difference between the member and customer rates for the trades involved. Typically, when an audit uncovers a firm inappropriately charging members rates to an entity outside the umbrella of its existing 106.I. membership, the 106.I. is transferred to the appropriate level in the related party chain or an additional 106.I. membership is purchased.

The Board approved an expansion of the 106.I. policy to allow for trades anywhere in the chain of related parties to receive member rates, independent of the positioning of the 106.I. membership. Interpretations & Special Notices Relating to Chapter 8 in the rulebook is therefore amended to:

CLEARANCE FEE POLICY

- G. Transactions for the accounts owned by each related party in a chain of related parties, provided that an employee of one such related party, which may or may not be a clearing member, holds a membership pursuant to Rule 106.I. and such related party, directly or indirectly, owns either: 1) all of the related parties in the chain, or 2) is itself 100% owned by a single entity that owns, directly or indirectly, 100% of such related party. The initial purchase and any subsequent transfers pursuant to this rule are subject to approval by Exchange staff.

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The text of Rule 106.I. will also be changed as follows with additional language underlined and deletions lined out:

106.I. Related Party Employee Transfers

A "related-party" shall be defined to include a clearing member or a firm that either: 1) owns, directly or indirectly, 100% of a clearing member or 2) that has 100% ownership, direct or indirect, in common with a firm that owns, directly or indirectly, 100% of a clearing member.

A membership and associated Class B Share may be owned by a clearing member or non-member firm under this Rule. The membership may be transferred to an employee of a related party that directly or indirectly owns or is owned by all other related parties within the organization of related parties and be transferred among its employees provided that: (1) the transfer is approved by Exchange staff; (2) the transferee is approved pursuant to the rules of the Exchange; and (3) the transfer is for the legitimate business purposes of the firm. ~~The firm~~ related party shall have the right, at any time, to have the employee disqualified from trading, but must have him disqualified upon termination of his employment with the firm. Notice to have the employee disqualified from trading must be given to the employee's qualifying clearing member. The clearing member or non-member firm shall designate on a form provided by the Exchange a representative who shall be authorized to deal with the Exchange with respect to the membership and associated Class B Share transferred under this Section.

A Rule 106.I. membership may not be transferred pursuant to Rule 106.C., D., F. or G. The membership and associated Class B Share may not be assigned for clearing purposes under Rule 902.

Rule 106.I. non-member firm benefits apply to the proprietary trading activity of any related party within the 100% related party structure. All proprietary positions of the non-member firm and its related parties must be carried by a clearing member(s) in accounts separate from positions of affiliates, subsidiaries, customers and other entities. A current list of all related parties of Rule 106.I. members must be submitted to the Audit Department.

A Rule 106.I. non-member firm may not hold itself out to the public as an Exchange member.

Exchange staff may grant exemptions from the requirements of this Rule.

If you have any questions regarding the Rule 106.I. rule change, please contact Ms. Anne Glass, Director, Audits, at (312) 930-3140, or Ms. Lisa Ezrol, Director, Business Development, at (312) 930-4515.

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III. BOARD APPROVES RULE REGARDING DELIVERY FAIL

At its Regular Meeting on Wednesday, July 2, 2003, the Board of Directors approved a new delivery fail rule. This rule is part of the clearing services provided by CME under the Clearing Services Agreement with the Board of Trade ("CBOT").

CME will provide clearing members with limited replacement risk coverage in the event of a delivery fail with respect to CBOT products. CME's Clearing House will hold performance bond for CBOT products until each delivery is completed which will provide the anticipated delivery replacement costs that CME could potentially incur. Pursuant to the guarantee, CME is responsible for the replacement risk for CBOT deliveries that are not completed as a result of a clearing member's failure to fulfill its delivery obligations. However, CME is not obligated under the rule to: 1) pay any damages greater than the difference between the delivery price when the delivery is actually made and when the delivery is required to be made under the rules, 2) make or accept delivery of the actual commodity, 3) pay damages related to the accuracy of certificates or warehouse receipts, or 4) pay any damages associated with the failure of a bank or any other institution associated with a delivery.

In addition, a non-defaulting clearing member must notify CME within sixty minutes after the time that the delivery obligation was to have been fulfilled or CME incurs no replacement cost expense. Finally, all delivery obligations of a clearing member that are not fulfilled by a clearing member are deemed to be a delivery obligation of such clearing member to CME.

The new rule is set forth below:

771. SETTLEMENTS ON DELIVERY FAILS

In the event a clearing member fails to fulfill its specific delivery obligations regarding a CBOT product pursuant to CBOT rules, the sole obligation of the Exchange is to pay reasonable damages proximately caused by the default, but in no event is the Exchange obligated to either: (1) pay any damages greater than the difference of the delivery price of the specific commodity and the reasonable market price of such commodity at the time delivery is required according to the Rules of the Exchange; or (2) make or accept delivery of the actual commodity; or (3) pay any damages relating to the accuracy, genuineness, completeness, or acceptableness of certificates, instruments, warehouse receipts or other similar documents; or (4) pay any damages relating to the failure or insolvency of banks, depositories, warehouses, or similar organizations or entities that may be involved with a delivery.

Notwithstanding any provision of the rules, the Exchange has no obligation or liability to any clearing member or any other person relating to a failure to fulfill a delivery obligation unless it is notified by the non-defaulting clearing member of such failure as soon as possible, but in no event later than sixty minutes after the time the delivery obligation was to have been fulfilled according to the rules of the CBOT.

All delivery obligations of a clearing member to another clearing member which are not fulfilled by the clearing member shall be deemed an obligation of the defaulted clearing member to the Exchange. These obligations must be fulfilled to the Exchange within sixty minutes of the time the obligations were required to be fulfilled to the non-defaulting clearing member.

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If you have any questions regarding this proposed rule, please contact Mr. Dale Michaels, Director, Clearing House, at (312) 930-3062, or Mr. Stephen Szarmack, Director, Associate General Counsel, at (312) 648-5422.

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IV. REVISED BRITISH POUND FUTURES GLOBEX® NO-BUST RANGE EFFECTIVE TUESDAY, JULY 1, 2003

On Thursday, June 26, 2003, the Board Steering Committee approved a reduction in the no-bust range applied to British Pound futures traded on the GLOBEX® electronic trading platform from the current level of 0.0040 (twenty ticks) to 0.0030 (fifteen ticks). The adjustment was based on customer feedback and volatility analysis. The change was made effective on Tuesday, July 1, 2003.

As currency trading continues to grow on the GLOBEX electronic trading platform, it is increasingly important to strike an appropriate balance between interests that argue for generally wider or narrower no-bust ranges. CME intends to conduct periodic reviews of market conditions – in all Exchange markets - to ascertain that no-bust ranges are appropriately reflective of observed volatility and other relevant factors.

The amendments to the GLOBEX error trade policy are as follows with additions underlined and deletions bracketed and overstruck:

CME GLOBEX ERROR TRADE POLICY

[Rules A to F are unchanged.]

G. Busting Trades After System Freeze

In certain types of GLOBEX system failures, it is possible that the matching engine will freeze with live orders in the queue waiting to be matched. When the system is unfrozen, the pending orders can be matched before the GCC can halt the matching engine. The GCC is authorized to bust trades resulting from matches in these circumstances if, and only if, the price of such trades is outside of the No Bust Range at the time that a confirmation of the trades was sent.

GLOBEX Error Trade Tick Range List

Futures Contract	No Bust Range
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[Eurodollar through Agency Notes entries are unchanged.]

At Currency Futures <u>(except British pound)</u>	20 ticks or less
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British Pound Futures	15 ticks or less
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[S&P 500 and E-mini S&P 500 through remainder of rule are unchanged.]

If you have any questions, please contact Mr. Richard Co, Associate Director, Financial Product Development, at (312) 930-3227, or Mr. Scott Brusso, Director, Foreign Exchange, at (312) 930-3133.