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SPECIAL EXECUTIVE REPORT

S-3996

September 17, 2003

“STOP LOGIC” Rules Effective September 28, 2003

At its regularly scheduled meeting of Wednesday, September 3, 2003, the Board of Directors amended rules governing the execution of stop orders on the GLOBEX® electronic trading platform. These Rules shall become effective on Sunday, September 28, 2003. Specifically, the GLOBEX system is programmed to prevent the continuing execution of orders when it detects certain conditions. Per Rule 580, GLOBEX TRADE ALGORITHMS:

1. The system checks to determine if the execution of a stop order or series of stop orders would result in an executed price that falls outside a threshold bounded by the last traded price (prior to the execution of the first stop) plus/minus X ticks. The number X to be determined by the Exchange from time to time. Initially, X shall be established at the current no-bust range in the particular market.
2. If so, the market enters a “reserved state” for Y seconds, during which time orders may be entered, cancelled or modified but not executed. The time period Y to be determined by the Exchange from time to time. Initially, Y shall be established at five seconds. The system will disseminate an “Indicative Opening Price” (IOP) that represents the price at which the market theoretically will reopen.
3. If, at the conclusion of the initial Y-second reserved period, the opening price would fall within a range bounded by the last traded price plus/minus two times (2x) X, then normal trading resumes. If the opening price would fall outside that range, the reserved state continues for a subsequent Y-second period.
4. The procedure described in number 3 above continues until either: (i) the indicative opening price is within a range bounded by the last traded price plus/minus the number of reserved periods, plus one, times X, (e.g., at the conclusion of a second Y-second reserved period, the relevant range is the last price plus/minus three times (3x) X, at the conclusion of the third reserved period, the relevant range is the last price plus/minus four times (4x) X, etc., etc.) at which point normal trading resumes; or (ii) a total of twelve (12) Y-second reserved periods is concluded, at which point normal trading resumes regardless of the opening price.

STOP LOGIC RULES (S-3996)

September 17, 2003

Page 2 of 3

These procedures shall be applied in the context of stock index futures and currency futures at this time. Note that these measures shall not apply to options to the extent that stop loss orders are not accepted in the context of options traded on GLOBEX. The Exchange shall retain flexibility to alter the relevant range (X) and duration of the reserved time period (Y) from time to time as warranted by market conditions in the specific market. However, X shall initially be established at the no-bust range for each market while the duration of the reserved period shall be five (5) seconds.

The text of the proposed amendments is provided below - additions are underlined and deletions are bracketed and overstruck.

580. GLOBEX TRADE ALGORITHMS

1. Market orders that are entered into the GLOBEX System shall be converted into limit orders at a price at or above (in the case of a buy order) or at or below (in the case of a sell order) the last price shown on the GLOBEX system. Any part of such order that is not filled at the limit price or better shall remain as a resting order at such limit price until filled or cancelled.
2. Stop limit orders are activated and placed into the order book when the order's specified stop price is traded, at which time the order may be executed at the best available price at or between the specified limit price and the specified stop price. Any part of such order that is not filled shall remain as a resting order at such limit price until filled or cancelled.
3. If the execution of a stop order would result in an execution price that is above (below) the last traded price plus (minus) X ticks, the market shall be placed in a "reserved state." During the reserved state, orders may be entered, modified or cancelled but orders may not be executed. The GLOBEX System will disseminate an "Indicative Opening Price" (IOP) during the reserved state representing the price at which the market could trade if the reserved state were to conclude immediately. If, at the conclusion of the initial reserved state period, the IOP is within a range bounded by the last traded price plus or minus two times (2x) X ticks, then normal execution of trades shall resume. If the IOP is outside such range, the market shall remain in a reserved state for a subsequent period. A series of reserved state periods shall ensue until either (i) the IOP is within a range bounded by the last traded price plus (minus) the number of reserved state periods, plus one, times X ticks at the conclusion of such reserved state periods, at which point normal trading shall resume; or (ii) a total of twelve (12) reserved state periods are concluded, after which normal trading shall resume regardless of the opening price.

This process shall be applied to such markets as determined by the Exchange. The value X and the duration of a reserved state period shall be determined by the Exchange.

STOP LOGIC RULES (S-3996)

September 17, 2003

Page 3 of 3

4. Unless otherwise specified by the Exchange, orders entered into the GLOBEX System will be matched in accordance with an algorithm that gives first priority to orders at the best price and that gives priority among orders entered at the same price based on their time of entry into the system, with the first order entered receiving first priority, the second order entered receiving second priority, etc. (First In, First Out or “FIFO” Allocation Algorithm). The Exchange may use a different matching algorithm for particular contracts by giving written notice of such algorithm to members and firms using GLOBEX at least ten days before use of such algorithm is implemented. See Interpretation of Rule 580–GLOBEX TRADE ALGORITHMS at the end of Chapter 5.

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