



REGULATORY ADVISORY

Division of Market Regulation

TO: All Members and Clearing Member Firms **RA-03-08**
FROM: Market Regulation
DATE: October 8, 2003
SUBJECT: Block Trading Regulatory and Audit Trail Requirements – Reminder

Block trades are subject to the terms and conditions of Chicago Mercantile Exchange Inc. ("CME") Rule 526 ("Block Transactions"). A block trading Questions & Answers document, including a list of eligible products and current minimum block transaction quantities, is attached to this advisory.

Members and clearing members are reminded that only Eligible Contract Participants as defined in Section 1a(12) of the Commodity Exchange Act may participate in block transactions. Such Eligible Contract Participants include Exchange members and member firms, broker/dealers, government entities, pension funds, commodity pools, corporations, investment companies, insurance companies, depository institutions, and high net-worth individuals. Further, Rule 526 provides for the participation of Commodity Trading Advisors (CTAs) and registered investment advisors with net assets under management of at least \$25 million.

Market Regulation reminds members and clearing member firms that they must comply with the following regulatory and audit trail requirements when participating in block transactions:

- Recordkeeping and audit trail requirements associated with a block trade are identical to the requirements associated with any other futures or options transaction. Accordingly, all block trades for the account of a customer or clearing member firm must be reduced to writing on order tickets and include appropriate timestamps, in addition to timing information corresponding to the actual execution time. Block trades made by members must be recorded by the member on a pre-sequenced trading card, or, alternatively, be reduced to writing on an order ticket pursuant to the requirements described immediately above. Clearing firms must ensure that the time of execution is submitted to the Exchange in the time of execution field when the trade is keypunched.
- Block trades must be reported to the Exchange within five (5) minutes of execution, except in the case of blocked Eurodollar futures and options transactions, which must be reported within fifteen (15) minutes of execution. It is generally the responsibility of the seller (i.e., the seller's clearing firm) to provide the block trade report. This report must contain the identification of the selling clearing member's firm number, the buying clearing member's firm number, the contract, contract month(s), transacted price, quantity and time of execution (and for options, whether the block trade is a put or a call, and the strike price).
- Block trades must be transacted at prices that are "fair and reasonable" in light of the size of the order, prices in related cash, futures and options markets and the circumstances of the participants. The trade price must also adhere to the minimum tick and price validation requirements of the market in question.

If you have any questions regarding this matter, please contact Kathleen Zaino, Associate Director, Market Regulation, at (312) 930-2341, Richard Gustafson, Manager, Market Regulation, at (312) 930-8512, or the Market Regulation Hotline at (312) 930-3333.

The following questions and answers (Q&A) explain the execution, reporting, and submission of block trades.

Q1: What is a block transaction?

A1: It is a privately negotiated futures or option transaction executed apart from the public auction market. A block transaction may be executed either on or off the Exchange trading floor. These trades are governed by CME Rule 526, BLOCK TRANSACTIONS. See the Appendix to this document for the current language of Rule 526.

Q2: How does a block transaction differ from an All-Or-None (AON) transaction - or from an Exchange-for-Physical (EFP) transaction?

A2: An AON transaction is executed by open outcry in a designated area on the trading floor. A block transaction may be executed privately on or off the trading floor provided that all other requirements of Rule 526, BLOCK TRANSACTIONS, are fulfilled. An EFP entails the simultaneous exchange of a futures position for a corresponding cash position (*i.e.*, a basis trade) while a block transaction involves only futures, or options on futures.

Q3: What products currently are eligible for block transactions?

A3: For a detailed enumeration of markets where block trading is permitted, please refer to the table "Minimum Block Transaction Quantities" below. The Exchange introduced block trading in the futures markets denoted below on November 29, 2000; block trading in standard option markets commenced on January 16, 2001; and block trading in flex options commenced on April 30, 2001. Block trading of flex options is restricted to the extent that the futures contract must be listed and the flex option strike price must be at a valid underlying futures price.

Q4: What are the minimum transaction quantities?

A4: The minimum quantities for block transactions are determined by the Board of Directors and are subject to CFTC review. The minimum quantities for block trades in various markets are indicated in the table below.

These minimum order size requirements refer to the order size for individual instruments, spreads or combinations. *I.e.*, a unified strategy controlled by a single entity and executed for a single account or group of eligible accounts. For example, a two legged vertical spread in Eurodollar options may be block traded given a minimum order size of 2,000 contracts in each leg of the spread – or 4,000 contracts to comprise the spread. Or, one may block trade a 25-lot spread between nearby and deferred Russell 2000[®] futures – for a total of 50 contracts on the ticket.

Minimum Block Transaction Quantities

	Futures	Options	Flex Options
Eurodollars executed between the hours of 6:00 am-4:00 pm Monday–Friday on Regular Business Days	4,000 contracts – or 1,000 contracts provided that a minimum of 1,000 contracts are transacted in yrs 6-10	4,000 contracts	Na
Eurodollars executed during all hours outside of 6:00 am - 4:00 pm Monday–Friday on Regular Business Days	500 contracts	500 contracts	Na
T-Bills	100 contracts	100 contracts	Na
Euroyen	200 contracts	200 contracts	Na
One-Month Libor	400 contracts	400 contracts	Na
2-, 5- and 10-Year Swap Rates executed between the hours of 6:00 am-4:00 pm Monday–Friday on Regular Business Days	500 contracts	Na	Na
2-, 5- and 10-Year Swap Rates executed during all hours outside of 6:00 am-4:00 pm Monday–Friday on Regular Business Days	100 contracts	Na	Na
28-Day Mexican TIE	2,400 contracts	Na	Na
S&P 500[®] *	na	250 contracts	250 contracts
NASDAQ-100[®] *	200 contracts – outrights only	100 contracts	100 contracts
FORTUNE e-50	50 contracts	Na	Na
S&P MidCap 400[™], Russell 2000, Russell 1000[®], S&P/BARRA Growth[™], S&P/BARRA Value[™], Nikkei[®] 225	50 contracts	250 contracts	250 contracts
S&P 500 Technology SPCTR[™], S&P 500 Financial SPCTR	200 contracts	-	-
Long-Term Technology TRAKRSSM Index	100,000 contracts	Na	Na
Goldman Sachs Commodity Index[®] (GSCI[®])	50 contracts outright – 300 contracts for each leg of a spread transaction	Na	Na
Foreign exchange, including Euro FX, Japanese Yen, Swiss Franc, British Pound, Canadian Dollar, Mexican Peso, Australian Dollar, Brazilian Real, New Zealand Dollar, Russian Ruble, South African Rand, Euro FX/British Pound, Euro FX/Japanese Yen, Euro FX/Swiss Franc, CME\$INDEX*	Na	250 contracts	Na
Weather Contracts (Heating and Cooling Degree Days)	20 contracts	20 contracts	Na
Benzene, Mixed Xylenes	10 contracts	Na	Na

* NOT applicable to E-mini[™] stock indexes or E-mini currencies.

Q5: Who may participate in block transactions?

A5: Eligible participants in block transactions are delineated in Rule 526.B. of the CME Rulebook. Such eligible participants include Exchange members and member firms, broker/dealers, government entities, pension funds, commodity pools, corporations, investment companies, insurance companies, depository institutions, and high-net worth individuals. Further, Rule 526 provides for the participation of Commodity Trading Advisors (CTAs) and registered investment advisors - with net assets under management of at least \$25 million – in block transactions. See the Appendix to this document for the language of Rule 526.

Q6: Can any order of the requisite size be executed as a block transaction?

A6: No, the order must specifically be designated as block transaction-eligible by the customer.

Q7: What are the hours for block trading?

A7: Block transactions in futures and standard options may be executed at any time. Due to technical reporting limitations, block trades in flex options will be limited to Regular Trading Hours (RTH) of stock index products from 8:30 a.m. to 3:15 p.m. weekdays.

Q8: Are there any restrictions upon the transaction price of a block trade?

A8: Block trades must be transacted at prices that are “fair and reasonable” in light of the size of the order, prices in related cash, futures and option markets and the circumstances of the participants. Further, the trade price must adhere to the minimum tick and price validation requirements of the market in question.

Q9: What recordkeeping and audit trail requirements are attendant to a block trade?

A9: The recordkeeping and audit trail requirements associated with a block trade are identical to the requirements associated with any other futures or option transaction. In addition to the normal recordkeeping and audit trail requirements, however, there is the additional proviso that a Block Trade Report shall be provided to the Exchange within five (5) minutes of execution – except in the case of blocked Eurodollar futures and option transactions which must be reported within fifteen (15) minutes of execution.

Q10: What information must be included in the Block Trade Report - and to whom must the said information be reported?

A10: The Block Trade Report shall include: identification of the selling clearing member's firm number, the buying clearing member's firm number, the contract, contract month, transacted price, quantity and time of execution. In the case of an option transaction, the Report must further include identification of whether the option is a put or call, and the strike price. In the case of flex options, the Report must further identify the expiration date and the underlying futures contract.

If the trade is to be given-up, the Report shall further include identification of the firm numbers of the executing clearing member and the buying and selling clearing members as well as quantities given-up to each clearing firm.

If the block trade is executed off the trading floor or during hours outside of Regular Trading Hours, it may be reported to the GLOBEX® Control Center ("GCC") by calling 312-456-2391. If the block trade is executed on the trading floor during Regular Trading Hours, it may be reported to Exchange price reporting staff in the Interest Rate quadrant on the upper trading floor (x2494); or, to Exchange price reporting staff in the Equity quadrant on the lower trading floor (x3935). Note that all block trades executed outside of Regular Trading Hours *must* be reported to the GCC. When the GCC is closed and it is impossible to report a block trade during the requisite 5 or 15 minute reporting period – for example during weekends - the Block Trade Report must be made within 5 or 15 minutes, as applicable, from the scheduled recommencement of Electronic Trading Hours (ETH) – typically 5:30 p.m. on Sundays.

Flex options are further restricted to Regular Trading Hours of stock index products between 8:30 a.m. and 3:15 p.m. weekdays. Blocked flex option transactions must be reported to Exchange price reporting staff at the equity pulpit on the lower trading floor and not to the GCC. These restrictions are technical in nature.

Q11: Block trades must be reported to the Exchange within 5 minutes of execution — or 15 minutes in the case of blocked Eurodollar futures and option transactions — for the purposes of price dissemination. Who is responsible for this Block Trade Report?

A11: It is generally the responsibility of the seller (*i.e.*, the seller's clearing firm – not the buyer's clearing firm) to provide the Block Trade Report – which shall be used for the purposes of price dissemination – in an effort to prevent duplicate reporting of the same transaction. Both the seller's and buyer's clearing firm must also report the trade for the purposes of clearing as described in Question 16. There is a limited exception to this policy in the case of blocked transactions which are given-up for clearing – such that the executing broker is responsible for the Block Trade Report – as described in Question 17.

In the event that the seller is an individual member (*e.g.*, on the trading floor), it is the individual member's responsibility to provide the Block Trade Report. In the case of recognized spreads or combinations executed as a block transaction, the seller of the spread or combination is likewise responsible for reporting the transaction. In the case of options, the net seller of premium is considered the seller of the spread or combination and is responsible for the provision of the Block Trade Report.

Block Trade Reports shall be made to the Exchange by Authorized Block Trade Reporters who are so designated by clearing members to the GCC in advance. The clearing firm shall be responsible for block transactions reported to the Exchange by such designates.

Q12: Must block trades be "brokered" by an Exchange member or clearing member?

A12: No - presuming that the clearing member(s) has so authorized, block transactions may be negotiated directly between non-member "eligible participants" (customers). In the event, however, that customers directly negotiate block trades, the affected clearing members are responsible for the timely capture and reporting of all required information including the time of execution. Clearing Members are urged to convey a clear understanding to their customers of their reporting responsibilities in this regard.

Q13: Who is responsible for recording the execution time?

A13: Ultimately, the clearing member is responsible for providing accurate execution times to the Exchange.

Q14: Can spreads or combination trades be executed as block trades?

A14: Yes. Unless otherwise specified – see table entitled “Minimum Block Threshold Quantities” above - spreads or combinations may be block traded provided the trade represents a unified strategy controlled by a single entity and executed for a single account or group of eligible accounts. Further, the trade must conform to the minimum order quantity requirements. For purposes of compliance with the minimum order quantity requirements, one may generally aggregate all legs of the spread or combination.

For example, one may transact 2,000 Eurodollar calendar spreads (between the hours of 6:00 am to 4:00 pm Mondays–Fridays on Regular Business Days) - totaling 4,000 contracts - to meet the minimum 4,000 contract block requirement. Or, one may transact 25 Russell 2000 calendar spreads – totaling 50 contracts – to meet the minimum 50 contract block requirement.

An exception is found in the context of GSCI futures where the block minimum is 300 spreads or combinations. *I.e.*, in order to be blocked, a GSCI spread or combination must include 300 contracts per leg. Thus, one can block 300 GSCI calendar spreads for a total of 600 contracts; or, 300 GSCI butterflies for a total of 1,200 contracts. Note, however, that the minimum for outright GSCI block trades is 50 contracts.

Inter-market spreads and combinations may also be eligible to be block traded provided that all legs of the trade are within contracts for which block trading is permitted. For purposes of complying with the minimum order quantity requirement, one may aggregate all legs of an inter-market spread or combination. The applicable minimum quantity shall be the amount associated with the block eligible contract that has the greatest minimum quantity requirement. For example, if one were to block a combination of Russell 2000 futures and options on Russell 2000 futures, the applicable minimum requirement shall be the 250 contract minimum associated with Russell 2000 options – not the 50 contract minimum associated with Russell 2000 futures.

Q15: May eligible account managers use the post execution allocation procedure for block trades – as specified in Rule 536.E.?

A15: Yes – for details, please refer to Rule 536., RECORDS FOR ORDERS AND PERSONAL TRANSACTIONS DURING REGULAR TRADING HOURS, Part E., Customer's Orders.

Q16: What are the trade entry procedures for submitting block trades to the clearing system?

A16: There are major differences in the trade entry requirements for blocked futures, blocked standard option and blocked flex option transactions as summarized below.

BLOCKED FUTURES trades must be submitted through the CLEARING 21[®] online EFP system and distinguished from EFPs by entering an order type “B” in the order type field on the entry screen. Consistent with the “seller” reporting procedure described in Question 11, the seller is responsible for inputting the trade and allocating it to the buyer. The buyer will then claim its side of the trade on the system’s claim screen. Upon a successful claim, confirmation records will be routed back to firms for bookkeeping purposes. Note that, when reporting spread transactions, each leg must be entered individually. (Blocked options *cannot* be entered via the online EFP system like blocked futures trades.)

BLOCKED STANDARD OPTION trades – must be entered via the Trade Entry System (TES) or submitted as TREX messages from a firm’s back-office trade entry terminal. Like block futures trades, however, the trade type must be reported as a type “9” and the order type must be reported as a type “B.” Block option trades are subject to exchange trade matching. Block options can only match with other block options (order type “B”).

BLOCKED FLEX OPTION trades must be entered by trading floor staff using the same entry terminals currently used for (non-blocked) flex options and designated as order type “B.” Block trades on flex options are restricted to Regular Trading Hours of stock index futures, *i.e.*, 8:30 a.m. to 3:15 p.m. weekdays. Note that block flex option trades must be reported to trading floor staff – not to the GCC – within the normal 5 minute window or 15 minute window in the case of Eurodollar futures and options.

For firms that receive outbound TREX confirmation records, block futures, standard option and flex option trades will be identified as Trade Type “1” instead of “9” so that the block is not reported in bookkeeping and customer statements as an EFP. Firms that do not accept TREX confirmation records must ensure that block trades are not reported to customers as EFP trades.

Q17: May block trades be given-up?

A17: Yes – but with the following distinction between futures, standard options and flex options.

Blocked futures and standard option transactions may be given-up through the Clearing Member Transfer Agreement (“CMTA”) system, where the executing broker delivers the order tickets to representatives of the customer’s clearing firm(s) after execution for reporting and clearing purposes.

Note that, similar to other give-up transactions, the executing broker is responsible for the transaction until such time that buying and selling clearing members accept such transactions for the purposes of clearing. Accordingly, it is the responsibility of the executing broker – and not the responsibility of the respective clearing members who ultimately clear the transaction - to provide the Exchange with the Block Trade Report described above in a timely fashion.

Note that block trades can not be given-up through the Give-Up System (“GUS”) at the present time insofar as GUS does not currently accept trades designated as type “9.” As such, the Exchange will not provide billing services per the GAINS system. The Exchange suggests that clearing members provide for such billing per Give-Up Agreements they may maintain with other firms.

Finally, note that block flex option trades are not eligible to be given-up. These restrictions are technical in nature.

Q18: Can orders be bunched to constitute one side of a block transaction?

A18: Yes, provided that the order is entered by a single controlling entity. For example, a CTA eligible to transact blocks may bunch orders entered on behalf of multiple accounts over which the CTA exercises power of attorney, provided that the aggregate order meets the minimum quantity requirements. Two or more traders who generally act independently with respect to accounts with different beneficial ownership may not bunch their orders for purposes of meeting the block trade minimum order quantity requirements. .

Q19: What fees are associated with block transactions?

A19: Block transactions shall be assessed a fee as determined by the Board of Directors. The Board has approved a \$1.75/side surcharge per contract – except in blocked Eurodollar futures and option transactions where a \$1.00/side surcharge per contract is applied and in blocked TIE futures transactions where a \$0.25/side surcharge per contract is applied - in addition to other fees normally applicable to the trading of CME futures and options. Block transaction surcharges may be waived in select futures and options at certain times by the Board of Directors.

Q20: How can one learn about the details of executed block transactions?

A20: The particulars of block transactions are reported on the MerQuote system upon receipt of the Block Trade Report. The MerQuote system carries information including the contract in which the transaction occurred and the executed price. However, clearing firms participating in a block transaction will not be identified on the MerQuote system consistent with block trading practices elsewhere. These reports may be accessed by entering the code “BLK” into the MerQuote system.

Rule 526, Block Transactions

526. Block Transactions: Notwithstanding Rule 520. – TRADING CONFINED TO EXCHANGE FACILITIES –, the Board or a Committee appointed by the Board shall, from time to time, determine the minimum thresholds for and the commodities in which Block Transactions (privately negotiated transactions) shall be permitted. The following shall govern Block Transactions:

- A. A member may execute a Block Transaction for a specified quantity at or in excess of the applicable minimum threshold designated by the Board.
- B. Each party to a Block Transaction must be an Eligible Contract Participant as that term is defined in Section 1a(12) of the Act.
- C. A member shall not execute any order by means of a Block Transaction unless that order meets the applicable minimum threshold and includes specific instructions to execute a Block Transaction.
- D. The price at which a Block Transaction is executed must be “fair and reasonable” in light of (i) the size of such Block Transaction, (ii) the prices and sizes of other transactions in the same contract at the relevant time, (iii) and the prices and sizes of transactions in other relevant markets, including without limitation the underlying cash and futures markets, at the relevant time, and (iv) the circumstances of the parties to such Block Transaction.
- E. Block Transactions shall not set off conditional orders (e.g., Stop Orders, MIT Orders, etc.) or otherwise affect orders in the regular market.
- F. Block Transactions must be reported to a designated Exchange official within five minutes of the time of execution; except that Block transactions in Eurodollar futures and options must be reported within fifteen minutes of the time of execution. The report must include the contract, contract month, price, and quantity of the transaction. The Exchange shall immediately publish such information separately from the reports of transactions in the regular market.
- G. Clearing firms must report Block Transactions to the Exchange Clearing House, including the time of execution, in accordance with the Clearing House Manual of Operations.
- H. Brokers executing Block Transactions must maintain a record of said transaction, in accordance with Rule 536. – RECORDS FOR ORDERS AND PERSONAL TRANSACTIONS DURING REGULAR TRADING HOURS.
- I. In the application of paragraphs A., B., and C. of this Rule to a commodity trading advisor (“CTA”) registered under the Act, including without limitation any investment advisor registered as such with the Securities and Exchange Commission that is exempt from regulation under the Act or Commission Regulations thereunder, with total assets under management exceeding \$25 million, the CTA, and not the CTA’s customers, shall be the applicable entity for purposes of said paragraphs A., B., and C.
- J. In the application of paragraphs A., B., and C. of this Rule to a foreign Person performing a similar role or function to a CTA or investment advisor as described in paragraph I, and subject as such to foreign regulation, with total assets under management exceeding \$50 million, the CTA, and not the CTA’s customers, shall be the applicable entity for purposes of said paragraphs A., B., and C.