

BOARD APPROVES CONTINUOUS LINKED SETTLEMENT PROCESS FOR CURRENCY DELIVERIES

At its Regular Meeting on Tuesday, June 3, 2003, the Board of Directors approved the Continuous Linked Settlement process ("CLS") as an optional delivery method for currency futures.

CME has analyzed the use of CLS to reduce risk and increase efficiency of its currency delivery process. CLS does not guarantee delivery of a currency, but it is designed to virtually eliminate settlement risk. If a settlement fails due to a default by a FX counterparty, CLS will return paid-in funds of the non-defaulting counterparty thereby eliminating the gross portion of currency settlement risk. CLS will facilitate currency delivery in a much more efficient and cost-effective way than the current delivery mechanism, orders to pay ("OTP").

Currently, the Clearing House's solution to manage settlement risk has been to require the long currency futures holders to either pay the US dollars a day early or get a short term bank letter of credit known as an OTP, which guarantees payment of the dollar obligations on settlement date. Most long currency futures holders have OTP to guarantee their obligations. The OTP is not required from the short currency futures holders (other than Mexican Peso and South African Rand) because they fund their FX payments during the Asian or European time zones. If they fail to fund their FX payment obligations, they will not receive the US dollars.

The OTP has been an effective risk management tool, however it is an expensive process for our firms. CLS Bank International ("CLS Bank") is a specially created institution incorporated in New York with operations centered in London, designed specifically to settle foreign exchange transactions through its CLS service. Currently seven currencies can be settled through their system: the Australian, Canadian, and U.S. Dollars; the euro; the yen the Swiss franc and the pound sterling. Shortly, Singapore dollar, Swedish Krona and Danish and Norwegian krone are expected to become eligible.

CLS's controls and safeguards are designed to greatly reduce settlement risk based on the principal of Payment vs. Payment or PVP. CLS has coordinated with the central banks and relevant payments systems of the seven eligible currencies, a common 5 hour (3 hour window for Asia) common operating window between 7:00 CET and 12:00 CET to facilitate PVP currency settlement. In its simplest form, if two banks want to settle a currency delivery obligation through CLS Bank, they will both submit settlement instructions to CLS Bank. Each bank will pay-in its settlement obligation to CLS Bank's account at the

respective central bank Real-time Gross Settlement payment system. CLS Bank will simultaneously release the funds to the banks once both banks have funded their obligations. If one side defaults on its pay-in obligation, CLS Bank refunds the pay-in amount of the non-defaulting bank so that its principal is not at risk.

Proposed rule amendments to implement the CLS system are set forth below with additions underlined and deletions lined out.

CHAPTER 7

DELIVERY FACILITIES AND PROCEDURES

GENERAL

Additions are underlined and deletions are bracketed and lined out.

Rules 700 through 729 are unchanged.

NON-CLS (LEGACY) CURRENCY DELIVERIES

Rules 730 through 739 are unchanged.

CLS CURRENCY DELIVERIES

(Effective for June 2003 Euro futures deliveries only)

740. DELIVERY THROUGH CLS BANK AND/OR THE CME CLS AGENT BANK

CME currency futures contract customers may elect for physical delivery and delivery position netting through the CLS (Continuous Linked Settlement) Bank and/or the CME CLS Agent Bank. The Board of Directors shall determine the CME CLS Agent Bank for facilitating the delivery of currencies through CLS Bank. CME currency futures contract customers must use an approved CLS agent bank for elected deliveries through CLS Bank, which may be the CME CLS Agent Bank or any other approved CLS agent bank. If practicable and by election of the customer, in those situations where CME currency futures contract customers use the CME CLS Agent Bank for delivery, then physical delivery and delivery position netting may occur within the CME CLS Agent Bank and not be submitted to the CLS Bank.

741. FOREIGN CURRENCY BUYER'S DUTIES FOR CLS DELIVERIES

A clearing member representing a customer that intends to accept delivery of a foreign currency through the CLS System to liquidate a net long position in that foreign currency shall, no later than 11:00 a.m. Chicago time on the last day of trading, present to the Clearing House a Buyer's CLS Delivery Commitment, which identifies the CLS agent bank used by the buyer and the number of contracts and their value for delivery (settlement price times trading unit times number of contracts delivered). The clearing member and the customer's CLS agent bank shall assign a transaction reference number to the delivery transaction represented by the Buyer's CLS Delivery Commitment. By 1:00 p.m. Chicago time on the last day of trading, the clearing member/customer shall enter the required delivery information into the Clearing 21 Currency Delivery System. Also, the clearing member/customer shall then arrange with its CLS agent bank to input the relevant banking instructions into the CLS System no later than 1:00 p.m. Chicago time on the business day preceding the delivery day. The CME Clearing House will arrange with the CME CLS Agent Bank to input the Exchange's relevant contra-side banking instructions into the CLS System. (The CME Clearing House is the seller to every buyer and the buyer to every seller in the currency delivery process through the CME CLS Agent Bank.)

A match of delivery information must occur in order for a delivery transaction to be finalized. In the event that clearing member/customer banking instructions are not entered into the CLS System by 1:00 p.m. Chicago time on the business day preceding the delivery day, then the unmatched transaction may not be completed and paid on the delivery date through the CLS System. In such event, delivery instructions may be resubmitted to the CLS agent bank for delivery on the subsequent business day. Also in such event, the Clearing House may assess fines for the delayed delivery. Further, if the delivery instructions remain unmatched by 1:00 p.m. Chicago time on the business day preceding the delivery day, the Clearing House may require the buyer of the foreign currency to post an Order to Pay to the appropriate Agent Bank by no later than the close of business that day, in addition to complying with other procedures as outlined in the Clearing House Manual.

The clearing member representing a customer accepting delivery shall define the payment method for each individual currency in a delivery at the time of setting up an account with its CLS agent bank. It is the responsibility of the clearing member/customer to make timely payment of currency in the delivery process.

If the Buyer's CLS Delivery Commitment is received later than 11:00 a.m. Chicago time on the last day of trading, but not later than 8:00 a.m. Chicago time on the following day, the buyer's clearing member shall be assessed a fine on a per contract basis, the amount to be determined by the Board. Any papers received subsequent to 8:00 a.m. Chicago time on the day following the last day of trading shall be deemed a default and acted upon in accordance with Rule 747.B. The buyer shall have made all provisions necessary to receive delivery within the country of issuance.

742. FOREIGN CURRENCY SELLER'S DUTIES FOR CLS DELIVERIES

A clearing member representing a customer delivering foreign currency through the CLS System to liquidate a net short position in that foreign currency shall, no later than 11:00 a.m. Chicago time on the last day of trading, present to the Clearing House a Seller's CLS Delivery Commitment, which identifies the CLS agent bank used by the seller and the number of contracts and their value for delivery (trading unit times number of contracts delivered). The clearing member and the customer's CLS agent bank shall assign a transaction reference number to the delivery transaction represented by the Seller's CLS Delivery Commitment. By 1:00 p.m. Chicago time on the last day of trading, the clearing member/customer shall enter the required delivery information into the Clearing 21 Currency Delivery System. Also, the clearing member/customer shall then arrange with its CLS agent bank to input the relevant banking instructions into the CLS System no later than 1:00 p.m. Chicago time on the business day preceding the delivery day. The CME Clearing House will arrange with the CME CLS Agent Bank to input the Exchange's relevant contra-side banking instructions into the CLS System. (The CME Clearing House is the buyer to every seller and the seller to every buyer in the currency delivery process through the CME CLS Agent Bank.)

A match of delivery information must occur in order for a delivery transaction to be finalized. In the event that clearing member/customer banking instructions are not entered into the CLS System by 1:00 p.m. Chicago time on the business day preceding the delivery day, then the unmatched transaction may not be completed and paid on the delivery date through the CLS System. In such event, delivery instructions may be resubmitted to the CLS agent bank for delivery on the subsequent business day. Also, in such event, the Clearing House may assess fines for the delayed delivery. Further, if the delivery instructions remain unmatched by 1:00 p.m. Chicago time on the business day preceding the delivery day, the Clearing House may require the seller of the foreign currency to comply with other procedures as outlined in the Clearing House Manual.

The clearing member representing a customer making delivery shall define the payment method for each individual currency in a delivery at the time of setting up an account with its CLS agent bank. It is the responsibility of the clearing member/customer to make timely payment of currency in the delivery process.

If the Seller's CLS Delivery Commitment is received later than 11:00 a.m. Chicago time on the last day of trading, but not later than 8:00 a.m. Chicago time on the following day, the seller's clearing member shall be assessed a fine on a per contract basis, the amount to be determined by the Board. Any papers received subsequent to 8:00 a.m. Chicago time on the day following the last day of trading shall be deemed a default and acted upon in accordance with Rule 747.B. The seller shall have made all provisions necessary to make delivery within the country of issuance.

743. DELIVERY DATE

Delivery of a foreign currency contract shall be completed in accordance with the specifications of the separate contracts.

744. SETTLEMENT FINALITY OF PAYMENT

Settlement finality of payment results when a transaction is irrevocable. In the CLS System, this occurs from the synchronized exchange of both sides of the foreign exchange settlement instructions with payment versus payment. Under the CLS System operational time frames, payments begin for matched transactions on the delivery day at 12:00 midnight Chicago time (6:00 a.m. Central European Time) and end at 5:00 a.m. Chicago time (11:00 a.m. Central European Time). The CME Clearing House's obligation to the delivery transaction ends when payment is made through the CLS System.

745. CLS OPERATIONAL DEADLINES AND COSTS OF DELIVERY

When buyers and sellers elect to do currency deliveries through the CLS System, they agree to abide by the deadlines and compensation conventions established by their CLS agent bank, the CME CLS Agent Bank and the CLS Bank.

746. EMERGENCIES, ACTS OF GOD, ACTS OF GOVERNMENT

If it is determined by the Board or the Business Conduct Committee that delivery or any precondition or requirement thereof is prevented by an act of government, act of God, or other emergency, it may take such action as it deems necessary and reasonable under the circumstances. Its decision shall be binding upon all parties to the contract. The procedural requirements detailed in Rule 411.B. shall be followed in the implementation of this rule.

747. DELIVERY INFRACTIONS

747.A. Late or Inaccurate Delivery

1. If a clearing member with a Delivery Commitment to pay funds pursuant to Rules 741 or 742 fails to deposit such funds in order to make timely payment on the date required in Rules 741 and 742, the clearing member may be charged the current overdraft rate applicable to the Exchange's foreign currency delivery account with the CME CLS Bank or any other compensation due to the late or inaccurate delivery.

If by 9:30 a.m. Chicago time on the day following the date required in Rules 741 and 742, such deposit is not made, the clearing member shall be deemed in default, and the matter be acted upon pursuant to Section B of this Rule.

Funds deposited pursuant to Rules 741 and 742 earlier than the required date of deposit shall not earn interest for the early time period.

2. If the information contained in either the Buyer's CLS Delivery Commitment or the Seller's CLS Delivery Commitment is inaccurate so that delivery cannot be accomplished in a timely manner, fines or damages may be assessed as in Section B below.

747.B. Default

If a clearing member with a CLS Delivery Commitment fails to perform all acts required by this chapter, or is otherwise deemed in default, it shall be liable to the Clearing House for any loss sustained, which loss shall be computed as follows:

1. The President or his designee shall determine the change, if any, from the final settlement price on the last day of trading to the spot rate on the first day on which the transaction could be consummated on the spot market. The spot market rate for purposes of this computation shall be the means of the spot rates between a group of Chicago, Illinois banks selected for this purpose by the Board at the earliest time it is determined the transaction can be completed in the spot market.

2. The related charges suffered by the Clearing House at any of its designated banks.
3. A sum not to exceed 1% of the U.S. dollar value of the contract. (Such amount shall be set by the President or his designee, acting in his sole discretion, and shall be binding upon both parties to the contract, except no such sum shall be assessed where default is occasioned by the circumstances delineated in Rule 746.)

748. CLEARING MEMBER DUTIES TO CLEARING HOUSE

Upon request, every clearing member with an open long or short position in foreign currency as of the close of business on the Wednesday prior to delivery day shall present to the Clearing House an inventory with such open positions in a form as the Clearing House may prescribe. Upon request thereafter, accurate daily offset memoranda shall be submitted to the Clearing House through and including the final day of trading.

749. DELIVERY NETTING

CME currency futures contracts delivered through the CLS Bank and/or the CME CLS Agent Bank shall be netted at the clearing member/customer's CLS agent bank and not in the CME delivery system.

(Next Rule 750)

If you have any questions, please contact Mr. Morgan Culverhouse,
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