

## MARKET REGULATION ADVISORY NOTICE

Exchange	CBOT
Subject	Pre-Execution Communications Prohibited in CBOT Products
Rule References	CBOT Rules 539 & 5B.13
Advisory Date	February 7, 2008
Advisory Number	CBOT RA0802-1

**CBOT Rules 539 (“Prearranged, Pre-Negotiated and Noncompetitive Trades Prohibited”) and 5B.13 (“Trading Against Customer Orders and Crossing Orders”) prohibit pre-execution communications in all CBOT products at all times, except as specifically permitted in connection with EFP, EFR or Block transactions.** While both rules contain the same prohibition on pre-execution communications, CBOT Rule 539 is applicable to CBOT products traded on CME Globex and CBOT Rule 5B.13 is applicable to CBOT Metals contracts which continue to trade on e-cbot.

This Advisory does **not** apply to CME products traded on CME Globex. Please refer to CME Advisory RA0801-2 for information on the rules governing pre-execution communications in CME products executed on CME Globex.

The text of CBOT Rule 539 appears below:

### **CBOT Rule 539**

#### **539.A. General Prohibition**

No person shall prearrange or pre-negotiate any purchase or sale or noncompetitively execute any transaction, except in accordance with Section C. below.

#### **539.B. Pre-Execution Communications Regarding Globex Trades Prohibited**

Pre-execution communications are communications between two market participants for the purpose of discerning interest in the execution of a transaction prior to the entry of an order on the Globex platform. Pre-execution communications and transactions arising from such communications are prohibited in all products during all hours.

#### **539.C. Exceptions**

The foregoing restrictions shall not apply to block trades pursuant to Rule 526 or Exchange of Futures for Related Position transactions pursuant to Rule 538.

Member firms are encouraged to ensure that their traders, account executives, order entry personnel and direct access clients are fully informed regarding CBOT Rules 539 & 5B.13 as violation of the rules may result in disciplinary action by the Exchange.

Please see the Q&A below for answers to frequently asked questions concerning the prohibition on pre-execution communications in CBOT products.

## **CBOT Q&A REGARDING PRE-EXECUTION COMMUNICATIONS**

### **1. What is a pre-execution communication?**

Pre-execution communications are communications between market participants for the purpose of discerning interest in the execution of a transaction prior to the exposure of the order to the market. Pre-execution communications involving CBOT products are prohibited at all times with respect to transactions executed in either the electronic or open outcry venue. This prohibition does not apply to privately negotiated transactions executed outside of the central market (i.e. EFP, EFR and Block trades).

### **2. If a customer has an interest in a particular transaction and requests a market, how can the salesperson obtain a market for the customer?**

In the open outcry venue, a market would be requested from the trading pit. In the electronic venue, the salesperson identifies the bid/offer and depth of market posted on the electronic trading platform. If the posted bid/offer is deemed too wide or insufficiently deep, it is recommended that a Request for Quote ("RFQ") be submitted. This action will typically generate additional interest and, in the case of products supported by a market-maker program, market makers are obliged to respond to a specified percentage of RFQs.

### **3. What if an RFQ is submitted and there is no response or an inadequate response in terms of the tightness or depth of the market?**

In this circumstance, another RFQ should be submitted. With an active RFQ, it is also permissible to contact potential counterparties (i.e. market makers), alert them to the RFQ and ask them to submit a market or to tighten/deepen the existing market. An RFQ is considered active for 60 seconds following submission. To ensure that such communications do not become prohibited pre-execution communications, only the information disclosed via the RFQ may be disclosed in such communications.

### **4. If an order has been submitted on the electronic platform, are there any restrictions on communicating with potential counterparties?**

With a resting order exposed on the electronic platform, it is permissible to contact potential counterparties to solicit interest in trading against the order. In any such communications, no non-public information (i.e. information not represented in the terms of the order exposed to the market) may be disclosed. For example, if the represented offer is for 250 contracts, it would be a violation of the rules to disclose that there are an additional 500 contracts to sell because that information has not been disclosed to the market.

### **5. Is it permissible to contact other market participants to obtain general market color?**

Communications to obtain general market color are permissible provided there is no express or obviously implied arrangement to execute a specified trade and no non-public information is communicated regarding an order.

### **6. How should an order for a spread or combination not supported by the electronic platform be handled?**

The electronic platform supports a wide array of strategies covering most of the spreads and combinations participants commonly trade. There are, however, some types of spreads or combinations that are not supported by the platform. Orders for an unsupported spread or combination must be legged on the electronic platform or entered in the open outcry venue. RFQs can be submitted for the legs of the strategy to ascertain the levels at which the spread could possibly be legged.

**7. Under what circumstances can orders be crossed on the electronic platform?**

In accordance with CBOT Rules 533 (“Simultaneous Buy and Sell Orders for Different Beneficial Owners”) and 5B.13, *independently initiated* orders on opposite sides of the market for different beneficial account owners that are immediately executable against each other may be entered without delay provided that the orders did not involve pre-execution communications and that each of the orders is entered immediately upon receipt.

Opposite orders for different beneficial accounts that are simultaneously placed by a party with discretion over both accounts may be entered provided that one order is exposed on the electronic platform for a minimum of 5 seconds in the case of futures orders and a minimum of 15 seconds in the case of orders involving options.

An order allowing for price and/or time discretion, if not entered immediately upon receipt, may be knowingly entered opposite a second order entered by the same firm only if the second order has been entered immediately upon receipt and has been exposed on the electronic platform for a minimum of 5 seconds for futures orders and a minimum of 15 seconds for orders involving options.

**8. Assuming there have been no pre-execution communications, is it permissible for a firm to knowingly trade for its proprietary account against a customer order entered by the firm?**

Yes, provided that, in accordance with CBOT Rules 531 (“Trading Against Customers’ Orders Prohibited”) and 5B.13, the customer order has been entered immediately upon receipt and has first been exposed on the electronic platform for a minimum of 5 seconds for futures orders and a minimum of 15 seconds for orders involving options.

Questions regarding this advisory may be directed to the following individuals in Market Regulation:

Kathleen Zaino, Associate Director, 312.930.2341

Jennifer Baum, Associate Director, 312.341.3124

Robert Sniegowski, Associate Director, 312.648.5493