

## MARKET REGULATION ADVISORY NOTICE

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Exchange	CME, CBOT, NYMEX & COMEX
Subject	Pre-Execution Communications
Rule References	Rule 539
Advisory Date	December 6, 2011
Advisory Number	CME Group RA1106-5
Effective Date	December 11, 2011 (for trade date December 12, 2011)

This Advisory Notice supersedes CME Group Market Regulation Advisory Notice RA1004-5 issued on April 6, 2010. It is being reissued to reflect upcoming changes to the required waiting period between the entry of a Request for Quote ("RFQ") and the associated Request for Cross ("RFC") order on CME Globex in CME and CBOT interest rate options orders that result from pre-execution communications.

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. Any communication that involves discussion of the size, side of market or price of an order, or a potentially forthcoming order, constitutes a pre-execution communication.

**Effective on Sunday, December 11, for trade date Monday, December 12, 2011**, the waiting period between the entry of the RFQ and the RFC in CME and CBOT interest rate options will be modified to require the RFC to be entered no earlier than **five (5) seconds** and no more than thirty (30) seconds after entry of the RFQ.

Market participants are reminded that until December 11, the RFC order in CME and CBOT interest rate options may be entered no earlier than fifteen (15) seconds and no more than thirty (30) seconds after entry of the RFQ, pursuant to the requirements of CME Group Market Regulation Advisory Notice RA1004-5 from April 6, 2010.

Information on the revised requirements for CME and CBOT interest rate options transactions executed pursuant to pre-execution communications begins on page 2 of this Advisory Notice.

**As a reminder, CME, CBOT, NYMEX and COMEX rules expressly prohibit pre-execution communications in connection with pit transactions executed on the trading floor. Additionally, CBOT rules prohibit pre-execution communications in all CBOT futures contracts and all CBOT agricultural options contracts traded on CME Globex.**

### **General Requirements for Allowable Pre-Execution Communications on CME Globex**

In products where pre-execution communications are allowed, such communications may occur only when the party for whose benefit the trade is being executed has previously consented to such communications.

Additionally, parties who have been involved in a pre-execution communication may not disclose the details of that communication to other parties, nor may a party place any order to take advantage of the information conveyed in such communications except to facilitate the trade in accordance with the rule.

All transactions arising from permitted pre-execution communications must be executed in accordance

with the requirements set forth in Rule 539.C.

### **Pre-Execution Communications in Futures on CME Globex**

Pre-execution communications are permitted in all CME, NYMEX and COMEX futures products traded on CME Globex and are prohibited in all CBOT futures products traded on CME Globex.

For transactions in CME, NYMEX and COMEX futures products which involve pre-execution communications, the order of the party who initiated the pre-execution communication must be the first order entered into CME Globex. At least 5 seconds must elapse after the entry of the first order before the opposing order can be entered. No RFQ is required.

### **Pre-Execution Communications in Options on CME Globex**

Pre-execution communications are permitted in all CME, NYMEX and COMEX options products traded on CME Globex and are permitted in CBOT Interest Rate, Ethanol and Dow options traded on CME Globex. Pre-execution communications are prohibited in all CBOT agricultural options traded on CME Globex.

Opposing buy and sell orders intended for execution pursuant to a pre-execution communication in an eligible options product (including options spreads and combinations and options/futures spreads) require the entry of an RFC order, which is an order that includes both the buy and sell orders arising from the pre-execution communication. Prior to the entry of the RFC, an RFQ must be entered into CME Globex for the relevant option or options strategy. In CME and CBOT equity and interest rate options, the RFC order must be entered no less than 5 seconds and no more than 30 seconds after the entry of the RFQ. In all other eligible options, the RFC order must be entered no less than 15 seconds and no more than 30 seconds after the entry of the RFQ.

Failure to enter the RFC order within the applicable time parameters will require a new RFQ to be entered prior to the entry of the RFC order. In all cases, the entry of the RFC order must comply with the applicable time parameters set forth in Rule 539. These requirements ensure transparency and competitive execution by requiring solicitation of interest from all market participants via an RFQ prior to submission of the RFC order.

Numerous Independent Software Vendors support RFQ and RFC functionality. For market participants using the Exchange-provided CME EOS Trader application, functionality built into the application will prevent the entry of the RFC outside of the prescribed time requirements. For example, in Standard & Poor's 500 Stock Price Index options, the system will preclude the entry of the RFC until at least 5 seconds after the entry of the associated RFQ and will also prevent the entry of the RFC if more than 30 seconds have elapsed following the entry of the RFQ. This functionality was added to facilitate compliance with the relevant entry time requirements.

**Market participants engaging in pre-execution communications involving options must be able to enter the required RFQ and RFC or have another party enter the required RFQ and RFC on their behalf as it is impermissible to enter the two orders via separate entries into CME Globex and remain in compliance with Rule 539.C.**

Further information on the relevant rules and requirements related to pre-execution communications is included on pages 3-6.

The text of revised CME, NYMEX and COMEX Rule 539 appears on page 8 and the text of CBOT Rule 539 appears on page 9 of this Advisory Notice.

1. **Requirements for Pre-Execution Communications in Eligible Option Products**

- a) Pre-execution communications are permitted in all options products except for CBOT agricultural options.
- b) Prior to the entry of orders arising from pre-execution communications, the market participant **must** submit an RFQ.
- c) Subsequent to submitting the RFQ, the orders to be executed pursuant to such communications **must** be initiated by the entry of an RFC order, an order which includes both the buy and sell orders arising from the pre-execution communications.

In CME and CBOT equity options and interest rate options, the RFC order **must** be entered no less than 5 seconds and no more than 30 seconds after issuing the RFQ.

In all other eligible options, the RFC order **must** be entered no less than 15 seconds and no more than 30 seconds after issuing the RFQ.

- d) If an RFC order is not entered within 30 seconds after the RFQ, any subsequent trade to be executed pursuant to pre-execution communications must be preceded by the entry of a new RFQ and, thereafter, the RFC order must be entered in accordance with the time parameters set forth above.

2. **RFC Matching Algorithm**

- a) **The RFC price improves both the best bid and best offer in the order book or there is no bid/offer in the order book.**

If the RFC price improves both the best bid and best offer in the order book or if there is no bid/offer in the order book, 100% of the RFC quantity will match at the RFC price immediately upon submission of the RFC.

- b) **The RFC price matches or is outside the best bid or best offer in the order book.**

If the RFC price matches or is outside the best bid or offer in the market, the applicable side of the RFC order will immediately match against the orders in the book at a price better than or equal to the RFC price.

Immediately thereafter, 100% of the smaller quantity remaining on one side of the RFC will match against the order on the opposite side of the RFC at the RFC price.

Any unmatched balance on one side of the RFC will remain in the order book unless it is cancelled by the user.

3. **Questions and Answers Regarding Pre-Execution Communication Requirements in Eligible Options Executed on CME Globex**

- a) Is a client's consent to pre-execution communications necessary?  
Yes.
- b) May the parties involved in pre-execution communications disclose the details of those communications to other parties?  
No.
- c) If a party has participated in a pre-execution communication where non-public information has been disclosed about an order or a potential order and the party does not agree to take the other side of the trade, may the party subsequently enter an order into the market to take advantage of the non-public information?  
No.
- d) Are there any options listed on CME Globex in which pre-execution communications are not permitted?  
*Yes, pre-execution communications are not permitted in CBOT agricultural options, but are permitted in all other options available for trading on CME Globex.*
- e) Is an RFQ required to be submitted prior to engaging in pre-execution communications?  
No.
- f) After a pre-execution communication has taken place, must an RFQ be submitted prior to entering a Request for Cross ("RFC") in order to proceed with the transaction?  
Yes.
- g) In CME and CBOT equity options and interest rate options, must the RFC be entered no less than 5 seconds and no more than 30 seconds after issuing the RFQ?  
Yes.
- h) In all other eligible options, must the RFC be entered no less than 15 seconds and no more than 30 seconds after issuing the RFQ?  
Yes.
- i) Is the price or quantity of the orders on the RFC displayed to the marketplace prior to the execution of the RFC?  
*No. Market participants will observe an RFQ prior to the submission of the buy and sell orders corresponding to the RFC; however the RFQ will not reflect a price or quantity.*
- j) Is there any information in the RFQ that identifies that a RFC may be forthcoming?  
*No. The RFQ is displayed in the same manner as any other RFQ.*

- k) If the RFC is not entered within the required time parameters after issuing the RFQ, is a new RFQ required to be issued and active for the required time parameter prior to entering the RFC?  
Yes.
- l) May an RFC be entered outside the time parameters set forth in g) and h) above after entry of the required RFQ?  
No.
- m) Are there any alternative methods of complying with Rule 539.C. other than through the entry of an RFQ followed by the entry of an RFC as described above?  
No.

4. **Questions and Answers Regarding Pre-Execution Communication Requirements in Eligible Futures Products Executed on CME Globex**

- a) Is a client's consent to pre-execution communications necessary?  
Yes.
- b) May the parties involved in pre-execution communications disclose the details of those communications to other parties?  
No.
- c) If a party has participated in a pre-execution communication where non-public information has been disclosed about an order or a potential order and the party does not agree to take the other side of the trade, may the party subsequently enter an order into the market to take advantage of the non-public information?  
No.
- d) Are there any futures listed on CME Globex in which pre-execution communications are not permitted?  
*Yes, pre-execution communications are not permitted in CBOT futures products, but are permitted in all other futures available for trading on CME Globex.*
- e) Is an RFQ required to be issued prior to engaging in pre-execution communications involving futures?  
No.
- f) If pre-execution communications have occurred in an eligible futures contract, must the order of the initiator of the pre-execution communication be entered prior to the entry of the opposing order?  
Yes.

- g) Must a minimum of 5 seconds elapse after the entry of the first order before the entry of the second order?  
Yes.
- h) Can an RFC be used to cross futures orders?  
No.

5. **Questions and Answers Regarding Products in Which Pre-Execution Communications on CME Globex are Prohibited**

- a) In which products are pre-execution communications prohibited?  
*Pre-execution communications are prohibited in all CBOT futures products and all CBOT agricultural options products.*
- b) If a customer has an interest in a particular transaction in these products 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 CME Globex. 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.*
- c) 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.*
- d) Is it permissible to contact other market participants to obtain general market color without violating the prohibition on pre-execution communications?  
*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.*
- e) If an order has been submitted on CME Globex, are there any restrictions on communicating with potential counterparties?  
*With a resting order exposed on CME Globex, 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.*

6. **Crossing of Simultaneous Buy and Sell Orders That Do Not Involve Pre-Execution Communications and Trading Against Customer Orders on CME Globex**

- a) What are the requirements for handling simultaneous buy and sell orders for different beneficial owners that did not involve pre-execution communications?  
*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.*

*In accordance with Rule 533 ("Simultaneous Buy and Sell Orders for Different Beneficial Owners"), 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 CME Globex 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 CME Globex for a minimum of 5 seconds for futures orders and a minimum of 15 seconds for orders involving options.*

- b) 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 Rule 531 ("Trading Against Customers' Orders Prohibited") the customer order has been entered immediately upon receipt and has first been exposed on CME Globex 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:

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**CME & NYMEX Rule 539**  
**PREARRANGED, PRE-NEGOTIATED AND NONCOMPETITIVE TRADES PROHIBITED**

**539.A. General Prohibition**

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

**539.B. Exceptions**

The foregoing restriction shall not apply to block trades pursuant to Rule 526 or Exchange for Related Positions transactions pursuant to Rule 538.

**539.C. Pre-Execution Communications Regarding Globex Trades**

Parties may engage in pre-execution communications with regard to transactions executed on the Globex platform where one party (the first party) wishes to be assured that a contra party (the second party) will take the opposite side of the order under the following circumstances:

1. A party may not engage in pre-execution communications with other market participants on behalf of another party unless the party for whose benefit the trade is being made has previously consented to permit such communications.
2. Parties to pre-execution communications shall not (i) disclose to a non-party the details of such communications or (ii) enter an order to take advantage of information conveyed during such communications except in accordance with this rule.
3. In the case of futures orders, the first party's order must be entered into the Globex platform first and the second party's order may not be entered into the Globex platform until a period of 5 seconds has elapsed from the time of entry of the first order.
4. In the case of options orders, subsequent to the pre-execution communication, a Request for Quote ("RFQ") for the particular option or option spread or combination must be entered into Globex. Thereafter, in equity and interest rate options, a Request for Cross ("RFC") order which contains both the buy and the sell orders must be entered into Globex no less than five (5) seconds and no more than thirty (30) seconds after the entry of the RFQ in order to proceed with the trade. In all other options, the RFC order must be entered no less than fifteen (15) seconds and no more than thirty (30) seconds after the entry of the RFQ in order to proceed with the trade. The RFQ and the RFC order must be entered within the same trading session. Failure to enter the RFC order within 30 seconds after the entry of the RFQ will require a new RFQ to be entered prior to the entry of the RFC order, which must be entered in accordance with the time parameters described above in order to proceed with the trade.

**CBOT Rule 539**  
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**539.B. Exceptions**

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**539.C. Pre-Execution Communications Regarding Globex Trades in Interest Rate, Ethanol and Dow Options**

Parties may engage in pre-execution communications with regard to Interest Rate, Ethanol and Dow options transactions executed on the Globex platform where one party wishes to be assured that a contra party will take the opposite side of the order under the following circumstances:

1. A party may not engage in pre-execution communications with other market participants on behalf of another party unless the party for whose benefit the trade is being made has previously consented to permit such communications.
2. Parties to pre-execution communications shall not (i) disclose to a non-party the details of such communications or (ii) enter an order to take advantage of information conveyed during such communications except in accordance with this rule.
3. Reserved.
4. Subsequent to the pre-execution communication, a Request for Quote ("RFQ") for the particular option or option spread or combination must be entered into Globex. Thereafter, in equity and interest rate options, a Request for Cross ("RFC") order which contains both the buy and the sell orders must be entered into Globex no less than five (5) seconds and no more than thirty (30) seconds after the entry of the RFQ in order to proceed with the trade. In Ethanol options, the RFC order must be entered no less than fifteen (15) and no more than thirty (30) seconds after the RFQ in order to proceed with the trade. The RFQ and the RFC order must be entered within the same trading session. Failure to enter the RFC order within 30 seconds after the entry of the RFQ will require a new RFQ to be entered prior to the entry of the RFC order, which must be entered in accordance with the time parameters described above in order to proceed with the trade.