

## Memorandum

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### FEE POLICY BULLETIN

TO: Individual Members 07-03  
Chief Compliance Officers  
New Firm Approval Contacts  
Firm EFS Contacts

FROM: Audit Department, Clearing House Division

DATE: August 16, 2007

SUBJECT: CME - Individual Member Trading on Globex

CME Group Inc. ("CME Group") sets the fee policies for its two subsidiary exchanges - Chicago Mercantile Exchange Inc. ("CME") and Chicago Board of Trade Inc. ("CBOT"). In response to market participant feedback, CME Group is enhancing and clarifying documentation of its fee policies. This Fee Policy Bulletin ("FPB") updates and clarifies CME individual member fee policies. The FPB only applies to products listed on CME.

CME has membership categories for individuals (equity member and lessee) and corporate entities (corporate, electronic corporate, and clearing member<sup>1</sup>) each with their own unique requirements and benefits. CME spends considerable time with market participants to understand their evolving trading operations to continually refine and clarify member fee policies to be consistent with market trends. For instance, the challenges of electronic trading is creating a growing desire by individual members to utilize employees, third parties and Automated Trading Systems ("ATs") for execution of trades held in individual member accounts. These trends require clarification of CME fee policies for individual members particularly with respect to:

- Account ownership; and
- Trade execution/order submission including those resulting from the collective activities of a group/team of individuals and the utilization of ATs.

This FPB clarifies CME's fee policies with respect to these issues as well as consolidates all individual member fee policies for electronic trades.

CME distinguishes individual member trading from member firm and non-member trading based upon the presumption that the individual member is:

- Actively identifying potential trades and making trading decisions;
- Executing those trades himself or through another member in his personal account; and
- Personally realizing his trading profits and losses.<sup>2</sup>

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<sup>1</sup> For clarity, clearing member includes inactive clearing member.

<sup>2</sup> CME has also allowed other individual members to have discretion over the trading of an individual member(s) account.

CME grants individual member fee privileges to electronic trades executed in this spirit. This FPB presents several examples where ownership and trade execution are consistent with this spirit and eligible for individual member fees.

Electronic trades executed inconsistently with this spirit are ineligible for individual member fees. For instance, trades executed as a result of the collective activities of a group/team of individuals, either directly or through an ATS, are inconsistent with this spirit and are more consistent with trading by member firms, Commodity Trading Advisors (“CTAs”), or money management groups.

Therefore, to treat corporate members and individual members equitably and consistently, CME cannot automatically consider trades for an individual member account executed by a team or an ATS as individual member trades for fee purposes. If, however, the team supported trading and/or use of an ATS is conducted in the spirit of individual member trading, CME, in its sole discretion, will approve eligibility of these electronic trades for reduced individual member fees.

This FPB clarifies and consolidates CME Group policies for applying reduced fees on trades of CME products for individual member accounts. The fee policies detailed in this FPB do not apply to the trading of CBOT products.

## **1. Individual CME Member**

Any adult of good moral character, reputation and business integrity, with adequate financial resources to assume the responsibilities and privileges of membership, is eligible for individual membership of CME.

Individual members of CME may either purchase a membership (equity member) or lease a membership (lessee member) in the division in which they wish to receive equity member/lessee member fees<sup>3</sup>, as applicable.

In general, a benefit of individual membership is the application of member fees, within the division of membership held, to the trading:

- Conducted for the member’s account and benefit,
- Entered by the member, another member or a clearing firm, and
- At the discretion and direction of an individual member.

Detailed below are the requirements for individual member trading to be eligible for member fees including guidelines and specific instances for member fee eligibility.

## **2. Individual CME Member Obtaining Membership**

An individual CME member must own or lease a membership themselves; held in their own name.

- The financing to purchase a membership must be of the individual’s own funds or through a bona-fide loan. An individual who finances directly or indirectly their membership purchase from a CME member or individual/entity affiliated with a CME member may only be eligible

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<sup>3</sup> For clarity, individual CME members refers to both equity members and lessee members and member fees refers to both equity member and lessee fees.

for lessee rates in the division of membership held when trading an account in which the CME member/lender has an interest.<sup>4, 5</sup>

- An individual leasing a membership may receive financing for the lease from any third party including a CME member. The individual lessee may be eligible for lessee rates on their trades conducted in the division of membership held.

### **3. Individual CME Member Trading Account Ownership**

CME recognizes two types of account ownership as individual member accounts eligible to receive member fees due to the individual membership status of its owners:

#### **3.1 Single Individual Member Account Ownership**

- The account is 100% owned by one individual member of CME or by a corporate entity which is owned 100% by one individual member of CME.
- All funding of and contributions to the account must be 100% made by the individual member of CME.
- All profits and losses of the account must be 100% allocated to and taxed to the individual member of CME.
- Only the individual CME member owning the account may benefit in, share in any profitability, or earn any return based on the account's performance.

#### **3.2 Joint Individual CME Member Account Ownership**

- The account is 100% jointly owned by more than one individual all of whom must be members of CME, or solely owned by a corporate entity which is jointly owned 100% by more than one individual all of whom must be members of CME.
  - Owners must be individual members.
  - A member firm cannot be an owner of a joint individual member account.<sup>6</sup>
- All funding of and contributions to the account must be 100% made by the joint account owners or joint owners of the corporate entity.

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<sup>4</sup> In such case, the CME member or individual/entity affiliated with the CME member who financed or who otherwise assisted financially in the membership's purchase in order for the individual to trade an account in which the CME member/lender has an interest, will be considered, in essence, leasing the membership to the individual.

<sup>5</sup> CME members may guarantee a bona-fide loan from a financial institution for an individual purchasing a membership without impacting the fees for which the individual is eligible.

<sup>6</sup> If a member firm owns an account jointly with an individual member, the account will be considered a joint individual member/member firm account subject to the most restrictive fee policies of either individual membership or firm membership regarding ownership, eligible traders, trader compensation, and trade execution/order submission including the utilization of ATSS. In such case, discounted fees will be based on the lowest category and division of membership held by the parties.

- All joint account owners must contribute capital in the form of cash and/or other tangible assets to the joint account or corporate entity jointly owned.
  - The capital contribution must be of an amount sufficient so as to be considered by a reasonable person that one is a bona-fide owner of the firm. In determining if a capital contribution is satisfactory to consider one a bona-fide owner for fee purposes, CME will factor in the amount of the contribution and its relationship to the capital of the entire joint account or corporate entity jointly owned.
    - Individual members who contribute \$100,000 or more of their own funds will be considered without question to have met the capital contribution requirement for joint individual member account ownership.
    - While contributions of services and/or “sweat equity” are valuable, they will not be considered a bona-fide contribution to establish ownership for fee purposes of a joint individual member account.
- All profits and losses of the account must be 100% allocated to and taxed to the joint account owners.
- All joint owners must share directly in the profitability of the account and are directly responsible for losses of the account.
  - Each joint account owner must share directly in the profits and losses in portion to their capital contribution, services, responsibilities, and trading activities.
    - A joint account owner directly sharing in at least 20% of the profits and losses will be considered without question sharing directly in the profitability of the account.
- Only the owners of the joint account or of the corporate entity owning the joint account may benefit in, share in any profitability, or earn any return based on the account’s performance.

The joint owners must demonstrate to CME’s satisfaction the above requirements for a joint account are met for trades in that account to be eligible for member fees based on individual CME membership.

#### **4. Individual CME Member Trade Execution/Order Submission**

Eligibility for reduced fees for trades made for an individual member account is based on how the decision to trade is made and who enters the orders.

##### **4.1 Non-Automated Trading System Orders**

###### **4.1.1 Discretionary Trading by a Trader/Operator through a Non-ATS**

To be eligible for member fees, the individual member account may only be traded by:

- **An individual member or members of CME.** The individual member must be the sole decision-maker in the submission of each order and must physically enter each order.

Orders that result from the collective activity and decision making of a group/team of individuals (not all of whom are individual members) will not be considered traded by an individual member eligible for member fees. CME has sole discretion to determine the universe of individuals who are part of the group/team involved in trading.

Keep in mind, an individual who finances directly or indirectly their membership purchase from a CME member or individual/entity affiliated with a CME member may only be eligible for lessee rates in the division of membership held when trading an account in which the CME member/lender has an interest.

Discretionary trading of an individual member account by a non-member such as a non-member individual, non-member employee of a CME member firm or CTA is not eligible for member fees.

#### 4.1.2 Non-Discretionary Order Entry through a Non-ATS

To be eligible for member fees, orders must be at the direction of a member and may only be entered for the individual member account by:

- **An individual member or members of CME.** Such individual member(s) who are non-owners of the individual member account may not share in the profitability of the account either directly or indirectly.
- **Bona-fide W-2 employees and 1099-MISC independent contractors of a CME clearing member firm.** Such employees/independent contractors may only enter orders at the direction of the individual CME member(s) and may not share in the profitability of the account either directly or indirectly. Individuals may not become W-2 employees/1099-MISC independent contractors of a clearing member firm simply to accommodate the trading of an individual member(s). Furthermore, W-2 employees/1099-MISC independent contractors primarily working for an individual member "on behalf" of a clearing member will be closely scrutinized with the burden of proof on the clearing member to demonstrate to CME's satisfaction a bona-fide employment or contractor relationship.
- **Individuals as permitted and registered in special programs implemented by CME.** Such individuals must comply with all the rules and requirements governing the program.
  - As of the date of this FPB, registered clerks of an individual member or members of CME owning the account who are properly registered in and in full-compliance with the Clerk for Member Program may enter orders. Such clerks may only enter orders at the direction of the CME member and may not share in the profitability of the account either directly or indirectly. Refer to the Clerk for Member Program for details and requirements.

Orders entered by an individual sharing in the profitability of the account either directly or indirectly will be considered discretionary trades for fee purposes.

Orders that result from the collective activity and decision making of a group/team of individuals (not all of whom are individual members) will not be considered traded by an individual member eligible for member fees. CME has sole discretion to determine the universe of individuals who are part of the group/team involved in trading.

Individuals not identified above, such as non-members, CTAs, money managers or employees of non-CME clearing member firms, are not eligible to trade or enter orders for the accounts of individual members eligible for member fees.

## 4.2 Automated Trading System Orders

### 4.2.1 The ATS Policy

ATSs often function for periods of time independently or with minimal oversight from a single trader/operator and, in fact, can operate like multiple traders. Additionally, ATSs, despite their occasional independence, often require substantial collective oversight of a team of individuals who influence the orders submitted by the ATS.<sup>7</sup>

As a result, CME cannot presume without validation for fee purposes that orders submitted by an ATS for an individual member account are the direct trading of an individual member and ensure consistency with the spirit of CME's fee policy that excludes the collective activities of a group/team of individuals from qualifying for individual membership rates unless all individuals of the group/team are individual members.

**Therefore, with respect to the trades of an ATS for an individual member account, the following policies will apply:**

- **ATS trades will not be automatically considered individual trades.**
  - Generally, trades from an ATS require a "corporate entity" membership status in order to be eligible for reduced rates.
  - In the case of a corporate entity owned by an individual member(s), the entity itself must maintain membership privileges versus the individual owner(s) of the entity for ATS trades to be eligible for reduced fees.
- **Under very limited circumstances wherein the specific usage of an ATS is consistent with the spirit of individual member trading, CME will grant individual member fees for trades by an ATS for an individual member account.**

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<sup>7</sup> CME has sole discretion to determine the universe of individuals who are part of the group/team involved in trading.

Generally, the utilization of an ATS suggests that there is a group/team of individuals who are (1) Developing software, strategies, and risk overlay programs; (2) Initiating and disabling particular algorithms and strategies; (3) Directing and controlling trading decisions; (4) Establishing and adjusting trading parameters, inputs, and alerts; (5) Monitoring trading performance, system performance, (e.g. network connections and latencies) and trading alerts; and/or (6) Controlling and/or monitoring trading and/or position risk.

Collectively such responsibilities are referred to as administrating, operating, controlling and monitoring the ATS; for ease, operating and supporting the ATS. The monitoring, operating, and/or supporting of an ATS is considered discretionary trading for fee purposes. Because these activities have a direct effect on the orders submitted by the ATS, orders submitted by the ATS reflect group/team trading, rather than the trading of one individual. Therefore, for fee purposes, CME presumes that ATS trading is not the trading of an individual member.

#### 4.2.2. Member Developed/Operated ATS

Individual members may develop their own ATS hardware and software. Wherein CME determines in its sole discretion that the ATS is solely developed by individual members and is solely operated and supported by individual members, the trading activity executed through the ATS for an individual member account may be eligible for member fees.

The burden of proof will be on the individual member utilizing an ATS to provide clear evidence to CME's satisfaction that the third party ATS is solely operated and supported by the individual member in order to receive member rates based on individual membership status. As such, the individual member must:

- Make all trading decisions and be solely responsible for determining all trading strategies, parameters, inputs, and alerts; and
- Be solely responsible for operating and administrating the system and for monitoring trading performance, system performance and alerts.

#### 4.2.3 Third Party ATS

Individual members may wish to utilize third party developed ATS hardware and software in their trading activities. In limited circumstances wherein such third party ATS is solely operated and supported by the individual member once acquired<sup>8</sup>, such trading activity may be eligible for member fees.

For an ATS to be considered a "third party ATS":

- The individual member can not have any affiliation including ownership interest with the third party provider; and
- The third party developer may not receive any compensation (including any set percentage or discretionary bonus) based on the performance of the ATS.<sup>9</sup>

The burden of proof will be on the individual member utilizing an ATS to provide clear evidence to CME's satisfaction that the third party ATS is solely operated and supported by the individual member in order to receive member rates based on individual membership status. As such, the individual member must:

- Make all trading decisions and be solely responsible for determining all trading strategies, parameters, inputs, and alerts; and
- Be solely responsible for operating and administrating the system and for monitoring trading performance, system performance and alerts.

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<sup>8</sup> For clarity, third party developers may provide data center administration, hardware, and software updates.

<sup>9</sup> To clarify, third party developers may be compensated per a set amount on a monthly, quarterly, yearly or other time period basis and/or on a set amount per trade.

## **5. Individual Member Trading - Application of Fees**

An account owned and traded by members will receive member fees based on the lowest common denominator of membership held by the account owner(s) and trader/operator.

- For non-discretionary orders entered by bona-fide W-2 employees/1099-MISC independent contractors of a CME clearing member firm, only the membership status of the account owner(s) will impact the fees assessed.
  - To reiterate, the monitoring, operating, and/or supporting of an ATS is considered discretionary trading, not order entry, for fee purposes.
- For non-discretionary orders entered by individuals in approved special programs of CME, the individual's impact to the fees charged will be governed by the program.
  - For registered clerks of the individual member or members owning the account in the Clerk for Member Program, only the membership status of the account owner(s) will determine the fees assessed on non-discretionary orders.
- Keep in mind, an individual who finances directly or indirectly their membership purchase from a CME member or individual/entity affiliated with a CME member may only be eligible for lessee rates in the division of membership held when trading an account in which the CME member/lender has an interest.

For individual member fee incentive eligibility such as Globex fee capping, tier pricing, and market maker programs, refer to the requirements as outlined in the Clearing Fee Schedule and Individual Programs.

## **6. Member Firm Trading**

Firms/entities may become corporate members, electronic corporate members, and clearing members under CME rules. For complete requirements regarding Clearing and Globex Fees for Member Firm Accounts including the requirements for Member Firm Trading Accounts, Member Firm Traders and Member Firm Trader Compensation and Profit Splits, refer to Fee Policy Bulletin #07-01 dated February 1, 2007.

If you have any questions, please call the Audit Department at (312) 930-3230.