

November 28, 2005

## **NOTICE**

### **SETTLEMENT PROCEDURES FOR EXPIRING TREASURY FUTURES TO BE BASED EXCLUSIVELY ON e-cbot ACTIVITY**

**(Pilot Program Beginning with December 2005 Expirations)**

The Board of Directors has determined, on a pilot basis, to modify the procedure for determining final settlement prices for expiring U.S. Treasury Bond and Note futures. During this pilot program, the final settlement prices at contract expiration will be based exclusively on e-cbot market activity rather than open auction market activity. The pilot program will apply to the December 2005 and March 2006 expirations, after which the program results will be evaluated.

#### **Expiration Procedures**

The Exchange will determine the final settlement price for expiring Treasury futures according to the procedure detailed below. All references to time of day are Chicago time.

1. The closing range in the expiring contract will be based upon the prices traded on e-cbot from 12:00:00 noon to 12:01:00 p.m., and will include any bid higher than the traded range, or offer lower than the traded range, that is represented at the close of trading.
2. The following calculation, informed by both outright trade in the expiring contract on e-cbot and trade in the companion reduced-tic spread on e-cbot, will be performed to determine the volume-weighted average price of the expiring contract during the period between 12:00:00 noon and 12:01:00 p.m. on the expiring contract's last day of trading:

$$(w_x/w)*p_x + (w_s/w)*p_s \text{ where}$$

$p_x$  = volume-weighted average trade price in the expiring contract

$p_s$  = volume-weighted average price of the expiring contract implied by the trade price of the reduced-tic spread and the trade price of the deferred contract nearest to the time of the trade in the reduced-tic spread (but not later than 12:01).

$w_x$  = cumulative traded volume in the expiring contract

$w_s$  = cumulative traded volume in the reduced-tic spread

$$w = w_x + w_s$$

3. The final settlement price will be the volume-weighted average price as computed in Step 2, rounded to the nearest tradeable tic. In the case that the volume-weighted average price is the midpoint between two tradeable tics, the price will be rounded to the tic closer to the last trade price in the expiring contract.

As such, the final settlement price may penetrate unfilled bids or offers and, under certain circumstances, may settle outside of the closing range for outright trades in the expiring contract, as established in Step 1.

4. In the absence of trade in both the expiring contract and the companion reduced-tic spread during the last minute, the settlement price will be the best bid or best offer in the outright expiring contract at 12:00:50 p.m., whichever is closer to the last trade price. If there is not a bid/offer pair in the expiring contract at that time, the settlement price will be the best bid or best offer implied by the reduced-tic spread bid/offer at 12:00:50 p.m., whichever is closer to the last trade price in the outright expiring contract. For any bid or offer to be considered in this scenario, the bid or offer must remain active through contract expiration at 12:01:00.
5. In the absence of (a) trade during the last minute, (b) a bid/offer pair in the expiring contract at 12:00:50 p.m., and (c) a bid/offer pair in the reduced-tic spread at 12:00:50 p.m., the settlement price will be based on the most recent of (a), (b) or (c) occurring prior to 12:00:50 p.m.
6. Notwithstanding the foregoing, if the aforementioned calculations cannot be made or are otherwise determined, in the Exchange's sole discretion, not to be representative of the fair value of the contract, the Exchange will determine the final settlement price. In such a scenario, the Market Operations staff may consult non-conflicted market participants.

### **Modified Closing Call**

Following the expiration, there will be a Modified Closing Call (MCC), exclusive to the open auction market, that will begin at 12:09 p.m. If extenuating circumstances arise, the Pit Committee may delay the beginning of the MCC until 12 minutes after the completion of the close (12:13 p.m.). Outright trading in the expiring contract may occur during the MCC only within the closing range for the expiring contract, as established in Step 1 above. Spread transactions involving the expiring contract may be executed during the MCC provided that (a) the legs of the spread have previously opened during the trading day or (b) the spread has previously traded during the trading day.

No new customer orders may be entered into the MCC except to cover errors that have occurred as a result of mishandling of orders, or to cover errors in the transmission of orders. Additionally, it is not permissible to modify the order instructions for a customer order after 12:01 p.m., except to reduce the order quantity or to cancel the order.

Individual members trading for their own accounts and member firms trading for their proprietary accounts may initiate trades and enter orders for execution through the conclusion of the MCC.

**Responsibility of Market Participants During the Expiration**

**All market participants are reminded of their responsibility to ensure that their activity during the expiration period is orderly. Additionally, all bids and offers entered on e-cbot must be entered in good faith for the purpose of executing bona fide transactions. Any market participant who engages in disorderly activity, or activity that is intended to disrupt or manipulate the settlement process, will be subject to disciplinary action by the Exchange.**

Questions regarding this notice may be directed to the following individuals in the Office of Investigations and Audits:

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