

## Memorandum

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### FEE POLICY BULLETIN

TO: Chief Financial Officers #08-02  
Chief Compliance Officers  
Corporate Members  
New Firm Approval Contacts  
Firm EFS Contacts

FROM: Audit Department, Clearing House Division

DATE: December 9, 2008

SUBJECT: Clearing and Globex® Fees for Member Firm Accounts

CME Group Inc. ("CME Group") sets the fee policies for its four subsidiary exchanges - Chicago Mercantile Exchange Inc. ("CME"), Chicago Board of Trade, Inc. ("CBOT"), New York Mercantile Exchange, Inc. ("NYMEX") and Commodity Exchange, Inc. ("COMEX"). In response to market participant feedback, CME Group is enhancing and clarifying documentation of, and where possible harmonizing, its fee policies for CME, CBOT, NYMEX and COMEX.

In February 2007, CME issued Fee Policy Bulletin ("FPB") #07-01 concerning Clearing and Globex Fees. CME Group is issuing this FPB to enunciate CME, CBOT, NYMEX, and COMEX member fee eligibility policies and to update and clarify them as needed. This FPB supersedes all previous bulletins discussing fee policy issues for member firm accounts.

CME Group has met with several CME, CBOT, NYMEX, and COMEX trading firms to better understand their operations and the impact of our fee policies. From these meetings, the overwhelming consensus was the desire for clear, defined, and harmonized fee policies between the four exchanges. This FPB seeks to achieve these goals.

The trading activity of member firms must adhere to our policies in order to be granted member fees – equity member or preferential fees as applicable. CME Group has established member firm trading policies to ensure that the trading activity conducted for the member firm account is for the sole benefit of the member firm itself and not the trading activity of individual customers/traders conducted in the name of the firm; i.e. to prevent arcade type trading under the guise of member firm trading and the "selling" of member firm rates. To that end, the financial benefit and risk of the trading activity must be solely of the member firm. Further the member firm may only profit/benefit from the member firm trading activity through the performance of the trade and not from any other source such as a commission or charge for trade execution.

The trading environment and the customer base has evolved and expanded over the years. We have seen a tremendous growth in both clearing and corporate membership for trading groups. These trading groups have their own unique capitalization, ownership structures, trader compensation and trading styles.

This FPB presents both Requirements (Absolutes) and Best Practices for defining when member firm trading activity will be granted member fees. In recognition of the varying trading operations, Best Practices were established to allow member firms to utilize certain business practices (most not allowed in the past) which are generally prohibited. In order to do so, the member firm must clearly demonstrate to CME Group their application of these non-compliant practices is not inconsistent with CME Group's goal of providing member fees for trading activity for the account and sole benefit of the member firm.

## 1. **REQUIREMENTS**

### 1.1 **Member Firm Trading Account**

In order to obtain member clearing fees, CME Group rules require that the member firm trading account of CME, CBOT, NYMEX and COMEX clearing members<sup>1</sup>, NYMEX and COMEX non-clearing members, CME and CBOT Rule 106.H. trading members, CBOT Rule 106.J. equity members, CME and CBOT Rule 106.I. affiliated members, CME and CBOT Rule 106.R. electronic corporate members and CME and CBOT Rule 106.S. family of funds members must be 100% owned by the firm.<sup>2</sup>

- For CME clearing members the CME trading activity conducted for the account of 100% owned subsidiaries is entitled to equity member clearing fees.
- For CBOT clearing members the CBOT trading activity of 100% owned subsidiaries is not entitled to member clearing fees unless the subsidiary itself qualifies as an Affiliate Member Firm/Affiliate Umbrella Member Firm under CBOT Rule 106.I. That is, CBOT clearing membership fee benefits do not flow down to 100% owned subsidiaries.
- For NYMEX and COMEX clearing members and non-clearing members the NYMEX and COMEX trading activity of 100% owned subsidiaries is not entitled to member clearing fees. That is, NYMEX and COMEX clearing and non-clearing membership fee benefits do not flow down to 100% owned subsidiaries. Furthermore, affiliates and subsidiaries of NYMEX and COMEX clearing and non-clearing members must become member firms themselves in order to receive membership benefits. Note: A COMEX Option Only non-clearing member is only entitled to member clearing fees on COMEX option contracts.
- For CME and CBOT Rule 106.H./I./S. and CBOT Rule 106.J./R. corporate members to receive member fees, all member firm trading must be conducted within the division of membership held. Member firm trading activity of such corporate members outside the division of membership held will receive non-member customer fees.

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<sup>1</sup> For clarity, clearing member includes CME corporate equity member (formerly known as inactive clearing member).

<sup>2</sup> For purposes of this FPB, clearing members referenced without a preceding CME, CBOT, NYMEX or COMEX designation, include CME, CBOT, NYMEX and COMEX clearing members.

- For CME Rule 106.R. corporate members to receive member fees, all member firm trading must be conducted in accordance with the Questions & Answers Guide for Electronic Corporate Members under CME Rule 106.R. which may be found on CME's Web site at <http://www.cmegroup.com/company/membership/files/ECMQA.pdf>.
- Affiliates and subsidiaries of CME and CBOT Rule 106.H./J./R. corporate members are not entitled to the membership benefits of the corporate member.

A member firm trading account is evidenced through:

- The financial benefit and risk shall be solely of the member firm – only firm capital is at risk of loss.
- No non-owner traders may make any contributions, loans (including subordinated loans) or payments to the member firm or member firm trading account nor have any capital at risk in connection with their trading of the member firm account.
- All contributions by owners of the member firm are subject to risk of loss from any and all trading and business activities of the firm.
- All profits and losses of the member firm account are written off to the income of the member firm and are taxed to the member firm in accordance with IRS regulations.

These accounts must be registered in CME's Exchange Fee System ("EFS"), CBOT's Exchange Fee System ("CFS") and/or NYMEX's Billing System ("NBS")<sup>3,4</sup> as member firm accounts of the clearing, NYMEX and COMEX non-clearing, CME and CBOT Rule 106.H./I./R./S. or CBOT Rule 106.J. member as appropriate.

#### 1.1.1 Joint Accounts with Individual Equity/Lessee<sup>5</sup> Members

A clearing, NYMEX and COMEX non-clearing, CME and CBOT Rule 106.H./I./R./S. or CBOT Rule 106.J. member may have a joint account with an equity or lessee member and receive preferential fees on contracts under the lowest division of membership held. These accounts must be registered in the Fee System under the joint account owner with the lowest division of membership held. Further the account title field in the Fee System must identify all owners of the joint account.

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<sup>3</sup> For purposes of this FPB, the term "Fee System" will include CME's fee system referred to as EFS, CBOT's fee system referred to as CFS and NYMEX's fee system referred to as NBS.

<sup>4</sup> Effective with the consolidation of NBS into EFS, expected to occur April 1, 2009, all NYMEX and COMEX fees will be processed through EFS. At that time, all NYMEX and COMEX clearing and non-clearing member firm accounts and traders must be registered in EFS in order to receive equity member fees.

<sup>5</sup> For clarity, lessee includes delegate; CBOT previously defined individuals leasing a membership (lessees) as delegates.

## 1.2 Member Firm Traders<sup>6</sup> for Globex Activity

The member firm trading activity must be conducted by traders including operators/administrators of Automated Trading Systems (“ATS”) that are:

- Bona-fide IRS Form W-2 (“W-2”) employees (or equivalent W-2 of a foreign jurisdiction) of the member firm; or
- Independent contractors and other self-employed individuals of the member firm whose total compensation (that is, all compensation) is reported on an IRS Form 1099-MISC (“1099-MISC”) (or equivalent document of a foreign jurisdiction); or
- Owners who maintain at least \$500,000 in bona-fide capital for CME, CBOT, NYMEX, and COMEX clearing, NYMEX and COMEX non-clearing, CME and CBOT Rule 106.I., and CBOT Rule 106.J. members<sup>7</sup>; or
- Bona-fide owners of the firm for CME and CBOT Rule 106.H./R. members; or
- Individual equity members<sup>8</sup> of CME, CBOT, NYMEX and COMEX trading within their respective exchange and division of membership except for CME Rule 106.R. members. Traders of CME Rule 106.R. members may not own, hold, or have owned or held a membership in any of CME’s divisions within the past two years; or
- CME and CBOT Rule 106.F. Clearing Member Transfer and CME and CBOT Rule 106.I. Related Party Transfer members; or
- Registered Commodity Trading Advisors (“CTAs”), exempt CTAs under CFTC Regulations 4.14(a)(4), 4.14(a)(5), 4.14(a)(8)(i)(D) or 4.14(a)(10), and Investment Managers authorized by the Financial Services Authority (“FSA”).

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<sup>6</sup> For CBOT clearing members and CBOT Rule 106.H./I./J. members, the memberships status of the individual entering the trade will impact the level of member fee charged. Please refer to the current CBOT Clearing Fee Schedule at <http://www.cmegroup.com/company/clearing-fees/index.html>.

<sup>7</sup> The acceptable bona-fide capital level for owners of CBOT clearing members and CBOT Rule 106.I./J. members is increasing from \$200,000 to \$500,000 effective January 1, 2009. All owners of such CBOT member firms with a bona-fide interest of at least \$200,000 as of December 31, 2008 will be grandfathered in at the \$200,000 level. Note that the grandfathering will be specific to the individual owners and the particular CBOT member firm and cannot be transferred.

<sup>8</sup> For clarity, individual members participating in the Clerk for Member Program may not utilize their clerks to enter orders for member firm trading. That is, the Clerk for Member Program does not apply to member firm trading; it is only applicable to the trading of individual members. Such clerks themselves must be qualified traders for member firm trading.

All member firm traders must be assigned unique trader IDs, those IDs and the associated member firm trader must be appropriately registered in the Fee System, and all Globex trades (orders) must be identified with the registered ID of the trader executing the trade.<sup>9</sup>

- Clearing, NYMEX and COMEX non-clearing, CME and CBOT Rule 106.I./S., and CBOT Rule 106.H./J./R. member firm traders must be further defined as “W-2 Employee”, “Commodity Trading Advisor”, “Independent Contractor 1099-MISC”, “Rule 106.F. Trader”, “Owner w/ Acceptable Interest”, or for CBOT clearing and CBOT Rule 106.H./I./J. as “Member” as applicable.
- Clearing, NYMEX and COMEX non-clearing, CME and CBOT Rule 106.I./S., and CBOT Rule 106.H./J./R. member firm traders which are compensated through a W-2 or 1099-MISC for their trading profitability must be registered in EFS as “W-2 Employee” or “Independent Contractor 1099-MISC”, as appropriate, even if they are an owner of the firm with less than an acceptable interest in bona-fide capital.
- For operators/administrators of an ATS and for the ID under which an ATS submits orders, the “ATS” box on the Fee System registration screen must be checked.

### 1.2.1 Bona-fide Employees

Bona-fide employees of the member firm are evidenced through:

- Issuance of an W-2, or foreign equivalent, for all compensation (i.e. salary and bonus) to the trader by the member firm;
- Inclusion in the firm’s payroll tax records; and
- The trader has no income until the firm pays the trader.

### 1.2.2 Independent Contractors

1099-MISC independent contractors/self-employed individuals of a member firm may receive member fees when trading a member firm’s account.

The member firm trading activity of independent contractors and other self-employed individuals whose compensation is reported on an IRS Form 1099 which is not a 1099-MISC (e.g. an IRS Form 1099-B (“1099-B”)) or equivalent document of a foreign jurisdiction will be assessed fees based on the lowest division of membership held by both the firm and the independent contractor/self-employed individual.<sup>10</sup>

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<sup>9</sup> Effective with the consolidation of NBS into EFS, expected to occur April 1, 2009, all NYMEX and COMEX fees will be processed through EFS. At that time, all NYMEX and COMEX clearing and non-clearing member firm accounts and traders must be registered in EFS in order to receive equity member fees.

<sup>10</sup> Traders receiving compensation reported on a 1099-B are regarded as “holders” of the positions and, as such, the account would not qualify as a member firm account.

If the 1099-B independent contractor/self-employed individual is not an equity, lessee or Rule 106.F. member and is trading a member firm account, non-member customer fees will apply on trades executed by the individual. These accounts should not be registered in the Fee System as member firm accounts and are not eligible for firm-based incentives or discounts.

### 1.2.3 Bona-fide Owners

Individual owners are considered to have an acceptable proprietary interest in the member firm as follows:

- CME, CBOT, NYMEX and COMEX clearing, NYMEX and COMEX non-clearing, CME and CBOT Rule 106.I. and CBOT Rule 106.J. members - \$500,000 in bona-fide capital.
- CME and CBOT Rule 106.H./R. members – no specific dollar level; only bona-fide capital interest.

For individual owners, the bona-fide capital interest must be in the form of an equity investment; it cannot take the form of a loan including a subordinated loan.

Individual owners of member firms who maintain an acceptable proprietary interest of bona-fide capital in the firm may receive member fees on their trading activity of the member firm's account. Further, individual owners with acceptable proprietary interests who share in the profit split of a team of traders must share in the profits/losses of the overall firm (e.g. customer business and other proprietary trading activities) in order to be considered a bona-fide owner. If such individual owners do not share in the overall firm profits/losses, their share of the profit split from the team of traders must be reported on a W-2 or 1099 MISC in order to receive member fees on the trading activity of the trader team.

Individual owners of member firms who do not maintain an acceptable proprietary interest of bona-fide capital in the firm are not entitled to receive member fees on their trading activity of the member firm's account unless their trading profitability is reported to them on a W-2 or 1099-MISC or they are on one of the clearing member firm's Rule 106.F. memberships.

Individual owners of member firms with less than an acceptable proprietary interest of bona-fide capital who trade the member firm account and whose trading profitability is reported on a form other than a W-2 or 1099 MISC (e.g. an IRS Form K-1) are assessed fees based on the lowest division of membership held by the owner and the firm. If such owners are not equity, lessee or Rule 106.F members themselves, non-member customer fees will apply and these accounts should not be registered in the Fee System and are not eligible for firm-based incentives or discounts.

An investing LLC is prohibited from trading and/or having a specific interest in a member firm account eligible for equity member rates unless (1) the investing LLC maintains an investment of an acceptable proprietary interest of bona-fide capital in the member firm for each owner (that is owner, member and/or equity participation member) of the investing LLC and (2) the trading is conducted by and only by individual owners of the investing LLC.<sup>11</sup>

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<sup>11</sup> There are no restrictions on passive investing LLCs of members firms. Passive investing LLCs do not trade or have a specific interest in a trading account(s) and their return is based on the overall firm's profitability.

#### 1.2.4 Individual Equity/Lessee Members

A member firm account traded by an equity/lessee member who is not a W-2 employee, 1099-MISC independent contractor/self-employed individual or Rule 106.F. member is assessed fees based on the lowest membership status of the firm and the equity/lessee member. These accounts must be registered in the Fee System under the party with the lowest division of membership held. Further the account title field in the Fee System must identify the member firm as the account owner.

#### 1.2.5 Rule 106.F. Clearing Member Transfers

Traders on a clearing member's Rule 106.F. membership may receive their compensation in any manner including a W-2, 1099-MISC, 1099-B, or K-1 for their (not of a team/division) trading activity of the clearing member firm account. All other requirements for member firm trading must be met.

### **1.3 Member Firm Traders for Open Outcry Activity**

#### 1.3.1. CME Open Outcry

The member firm trading of a CME clearing member or CME Rule 106.H./I./S. member is entitled to member clearing fees when an individual owning and holding a membership or the firm's CME Rule 106.F. or CME Rule 106.H./I./S. member executes it on the floor of the exchange in open outcry.

The member firm trading of a CME clearing member or CME Rule 106.H./I./S. member conducted with discretion by a CME Rule 106.D. lessee member on the floor of the Exchange in open outcry will be charged fees based on the lowest membership status of the firm and the CME Rule 106.D. lessee member regardless if the lessee member is a firm W-2 employee or 1099-MISC independent contractor/self-employed individual. The CME Rule 106.D. lessee member must be registered as an account controller for the clearing or CME Rule 106.I./S. member firm account in the Fee System.

#### 1.3.2. CBOT Open Outcry

The member firm trading of a CBOT clearing member or CBOT Rule 106.H./I./J./S. member is entitled to member clearing fees when an equity member or lessee or the firm's CBOT Rule 106.F. or CBOT Rule 106.H./I./J./S. member executes it on the floor of the exchange in open outcry.

#### 1.3.3. NYMEX and COMEX Open Outcry

The member firm trading of a NYMEX and COMEX clearing member or non-clearing member is entitled to member clearing fees when an equity member or lessee executes it on the floor of the exchange in open outcry.

#### **1.4 Member Firm Trader Compensation and Profit Splits**

Member firm trading and trader compensation must meet the following requirements:

- Traders cannot be responsible for losses beyond their share of profits earned and maintained in the account which have not yet been distributed to the trader.
- The firm must be allocated both a portion of the profits and losses of the member firm account.
- The profit split on agreements with any trader, including owners acting as traders, may not exceed 80/20 (i.e. 80% to the trader/20% to the firm).
  - For member firm trading conducted by a team of traders, the profit split to the team in total may not exceed 80/20 (i.e. 80% to the trader team/20% to the firm).
  - Further the 80% limit on profit splits to a trader or team of traders includes any individual who has a specific interest in its profitability including those involved in the supervision/training of the account(s) and/or trader(s).
- Non-owner traders cannot leave their share of profits in the firm for greater than one year without becoming an equity owner.
  - Non-owner trader's share of capital in an account may not exceed the trader's share of net profit/loss in the previous 12 month period.
  - If a trader leaves their share of any profits in the account for greater than one year, they must become an equity owner.
- The firm is prohibited from:
  - Setting minimum account balances for its traders.
  - Charging margin on positions to traders.
  - Charging fees on draws taken by traders.
  - Requiring or accepting security deposits from its traders.

## **2. BEST PRACTICES**

### **2.1 Description of Best Practices**

CME Group recognizes that certain business practices may be utilized when conducting customer business as well as member firm trading activities. The Best Practices were established to allow member firms to utilize certain business practices (most not allowed in the past) which are generally prohibited. In order to do so, the member firm must clearly demonstrate to CME Group their application of these non-compliant practices is not inconsistent with CME Group's goal of providing member fees only for member firm trading activity. Such practices will be reviewed individually and in the aggregate in relation to the firm's entire trading activities and operation.



Review of such non-compliant practices will reflect the following key principles of CME Group's member firm trading policies. First and foremost, the trading activity eligible for member fees must be conducted for the account and sole benefit of the member firm itself. The trading activity of individual customers/traders conducted in the name of the firm is not eligible for discounted member firm fees in order to prevent arcade type trading under the guise of member firm trading and to prevent the "selling" of member firm rates. Further, a member firm may only profit/benefit from the member firm trading activity through the performance of the trade and not from any other source such as a commission or charge for trade execution.

Non-compliance with the Best Practices below is generally prohibited as it is indicative of arcade type trading, the selling of rates, and/or profiting from sources other than the performance of the member firm trade. **As such, while the Best Practices are not absolutes as the Requirements are, any non-compliance of the Best Practices will be carefully reviewed with the burden of responsibility on the member firm to clearly support and demonstrate to CME Group's satisfaction that the trading is of the member firm itself. Under limited circumstances in reviewing the totality of the member firm's trading operations and the violative practice(s), CME Group may deem the member firm's trading activities in accordance with our policies for member firm trading activity that is eligible for member firm fees.**

#### 2.1.1 Interest

The firm may not charge interest on debit balances to traders nor may it pay interest on credit balances to traders except where an options trading strategy is utilized in which interest on the premium is a key component of the overall profitability of the strategy.

The firm may not pay interest on holdbacks where holdbacks are permitted.

The firm may not pay interest on capital contributions.

#### 2.1.2 Allocated Expenses

A firm may not allocate expenses to trades or traders in excess of actual direct and indirect expenses of the individual member firm trades or traders. Only actual expenses incurred may be allocated – a mark up on expenses is not permitted. Further, opportunity costs may not be allocated.

Expense allocations may be made on a per trade/contract basis and/or monthly, quarterly, yearly, or other time period basis.

Direct expenses may include items such as clearing and Globex fees, brokerage commissions (those charged by member firm's clearing firm), software, connection/line charges, licensing fees, and market subscriptions. Indirect expenses may include items such as rent, utilities, membership/share costs, and firm costs for accounting, legal, back-office, compliance, strategy development, programming, and human resource services.

For all expenses allocated the firm must maintain records of actual costs incurred. All rebates of expenses incurred must also be reflected in the allocated costs. Further total costs incurred may not be allocated only to traders but must be allocated to all areas of the member firm's

operations which benefit; for example rent should be allocated across all areas of the firm utilizing office space. If an expense is otherwise allocated directly to a trader (for example a line charge) such expense may not be included in the allocated costs.

The total amount of expenses allocated must be reasonable to the actual costs incurred. Allocated expenses must be reviewed, and if necessary adjusted, routinely to ensure they continue to be reasonable in relation to actual expenses. Member firms must maintain and provide adequate supporting calculations and documentation of such allocated expenses and their reasonableness.

### 2.1.3 Capital Usage Fee

A firm may not charge a fee for capital usage to individual traders of the member firm's accounts.

### 2.1.4 Cost of Capital Fee

A firm may not charge a fee for the cost of capitalizing the firm (and thus the member firm's trading accounts) to individual traders.

### 2.1.5 Owners Interest in Member Firm Accounts

Individual owners and investing LLCs (as permitted) of a member firm may not have a specific interest in the profitability of a member firm account or group of accounts other than a member firm account that the individual owners or owners of the investing LLC trade or provide direct supervision/training to. Thus, an individual owner/investing LLC may not be entitled to a direct percentage of the profits of a member firm account traded by a specific "independent" employee(s) or contractor(s) of the member firm.

## **2.2 Application of Best Practices**

As previously stated non-compliance with the Best Practices is indicative of profiting from sources other than the performance of the member firm trade and is generally indicative of a customer relationship versus a member firm trader relationship. Non-compliance with the above practices will be carefully reviewed with the burden of responsibility on the member firm to clearly support and demonstrate the trading as of the member firm itself. Upon review of the practice, CME Group will in its sole judgment determine whether the member firm's practices are consistent with CME Group's policies for member firm trading activity that is eligible for member firm fees.

If a member firm has any questions concerning the acceptability of its current or potential business practices that may appear inconsistent with the Best Practices, please contact the Audit Department at (312) 930-3230 for forwarding to the Fee Policy Team for discussion and review.

**3. PENALTIES**

**The policies set forth herein will be strictly enforced by the Exchange. A member, clearing member, or corporate member found to have engaged in fraudulent or dishonest conduct or to have acted in bad faith will be subject to a charge of a major rule violation. Major rule violations are punishable by a fine up to \$1,000,000 plus the monetary value of any benefit received as a result of the violative activity.**

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