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January 4, 2010

Gary Gensler,
Chairman,
Commodity Futures Trading Commission,
Three Lafayette Center,
1155 21st, N.W.,
Washington, D.C. 20581.

Re: ELX Futures, L.P./Exchange of Futures for Futures Rule

Dear Chairman Gensler:

On behalf of ELX Futures, L.P. (“ELX”), I am writing to follow up on our recent meeting with you and members of the staff of the Commission regarding ELX Rule IV-15 (the “EFF Rule”), which authorizes the execution of Exchanges of Futures for Futures (“EFFs”) on ELX. The EFF Rule was approved by the Commission on October 14, 2009. We very much appreciated the time that you and the staff devoted to meeting with us and considering this issue. The meeting was very helpful and productive and we valued the opportunity to share our views and to gain a better understanding of your thinking on the issue. The purpose of this letter is respectfully to request that the Commission take appropriate action to effectuate the Commission’s approval of the EFF Rule and to permit ELX to implement the Rule in accordance with that approval.

As you know, the EFF Rule authorizes participants on ELX to liquidate positions in futures on the same underlying commodity traded on another exchange and to re-establish those positions on ELX. Conversely, two participants may, under the EFF Rule, liquidate an ELX position and re-establish a position on another exchange. The EFF mechanism, which has been widely used by other exchanges, including exchange subsidiaries of the CME Group, Inc. (“CME Group”), is an important tool by which market participants are able to manage their positions and margin funds in an efficient and cost-effective manner. In this regard, while we believe that market participants will find the EFF vehicle useful, we do not believe that it will become the dominant form of execution on ELX, and that belief has been supported by our discussions with market participants. At the same time, however, those discussions have underscored the importance and utility of the EFF structure.

The EFF Rule was submitted to the Commission for approval and was, as noted, affirmatively approved by the Commission. The Commission is required under the Commodity Exchange Act (the “CEA”) to approve a rule submitted for approval by a designated contract market (“DCM”) “unless the Commission finds that the new contract or instrument, new rule, or rule amendment would violate” the CEA. The Commission, therefore, in order to approve the EFF Rule, had to have determined that the Rule, and transactions executed pursuant to the Rule, would not be in violation of the CEA.

Notwithstanding the Commission’s action, on October 19, 2009, five days following the Commission’s approval, the Chicago Board of Trade (“CBOT”), a subsidiary of CME Group, which also owns the Chicago Mercantile Exchange (“CME”) and the New York Mercantile Exchange (“NYMEX”), issued an Advisory Notice (the “Advisory”) entitled “Prohibition of Exchange of Futures for Futures (EFF) Transactions.” In the Advisory, the CBOT stated that “CBOT rules do not permit the execution of Exchange of Futures for Futures (EFF) transactions. The CBOT, as a designated contract market, establishes its rules in accordance with the Commodity Exchange Act and CFTC regulations” (emphasis in original). The Advisory went on to state that, because a futures contract is not an over-the-counter swap or other over-the-counter instrument, it does not qualify as one of the many types of “exchange for risk” transactions permitted under CBOT rules. In other words, the Advisory asserted that EFFs are prohibited because they are not currently provided for under CBOT rules and that, at least by implication, that EFFs could not be permitted under such rules because they are not “in accordance with the Commodity Exchange Act and CFTC rules.” This contention was subsequently made more explicitly by representatives of CME Group in public statements. For example, Rick Redding, head of products and services for CME Group, was quoted in a media report as saying that “trades designed to move Treasury futures positions out of CME’s clearinghouse and into a competitor’s would violate the Commodity Exchange Act.” “CME Says Moving Futures Trades Prohibited by Law,” Dow Jones Market Talk, November 5, 2009. Mr. Redding was further quoted in that article as saying “Essentially, it becomes a wash trade by definition of the CEA, so we couldn’t accept it.”

The Advisory and other statements by the CME Group were intended to, and did, have a significant chilling effect that has prevented market participants from executing a single EFF into or out of ELX since the approval of the EFF Rule. Indeed, no rational market participant would execute an EFF involving ELX when it has been advised that it may face enforcement action from CME Group, the dominant exchange in the marketplace. As a result, CME Group has thus far been able to use its overwhelming market power to deny a small, newly organized competitor – and market participants –

the use of an effective and desirable tool to manage positions and margin in an efficient manner.

Moreover, as set forth below, the statements in the Advisory are false and misleading, and contrary to the Commission's action in approving the EFF Rule as well as the history of EFFs being permitted and aggressively marketed by the CBOT's affiliate, NYMEX. The Commission cannot and should not countenance this challenge to its authority and the language and purposes of the CEA. We respectfully request that the Commission act promptly to effectuate its approval of the EFF Rule by requiring the CBOT to permit the execution of EFFs between ELX and CBOT and prohibiting the CBOT or CME Group from threatening or bringing enforcement action in connection with the execution of EFFs.

1. The EFF Rule Does Not Violate the CEA.

The Commission, not another designated contract market subject to the Commission's jurisdiction, is responsible for determining whether the EFF Rule violates the CEA. By approving the EFF Rule, the Commission has clearly concluded that the Rule, and the transactions that are permitted under the Rule, do not violate the CEA and the CME Group cannot usurp the Commission's statutory role by making and acting upon a contrary interpretation. Moreover, the CME Group's conclusion – that EFFs violate the CEA because they “essentially” constitute “wash trades” is simply incorrect as a matter of law and must be rejected. Wash trading has historically been prohibited under the CEA because it “is the archetypical form of fictitious trading,” which “gives the appearance of being a purchase and sale” that is competitively executed in the market when in fact it is designed to mislead the market by making a fictitious trade appear to be bona fide. Pouncy, The Scierter Requirement and Wash Trading in Commodity Futures: The Knowledge Lost in Knowing, 16 Cardozo Law Rev. 1625 (1995): “Wash trading is inimical to the pricing and risk shifting functions of the futures markets because it can result in the reporting of prices for commodity futures contracts that are not true and bona fide prices, and it can result in the promulgation of inaccurate information concerning the futures contracts being traded.” *Id.* For this reason, the Commission has stated that “the common denominator of the specific abuses prohibited in Section 4c(a) – wash sales, cross trades, and accommodation trades – and the central characteristic of the general category of fictitious sales, is the use of trading techniques that give the appearance of submitting trades to the open market while negating the risk or price competition incident to such a market.” In re Collins, CFTC Docket No. 77-15, April 4, 1986.

EFFs, unlike wash trades executed on a single exchange, involve actual changes in position – the liquidation of a position on one exchange and the establishment

of a position on another. Because a futures position on a second exchange is a fundamentally different instrument, involving the credit of a different clearing house and rules and operations of a separate exchange, it cannot be equated to a wash trade executed on the same exchange, involving a simultaneous purchase and sale at or about the same price. EFFs, therefore, cannot be characterized as wash trades. Moreover, in contrast to wash trades, EFFs will not necessarily be executed with the legs of the trade priced the same.

In any event, none of the various types of non-competitive trades that are permitted under the CEA or that have been approved by the Commission – including exchanges of futures for physicals, exchange of futures for swaps, and EFFs -- are considered wash trades because they do not falsely create the appearance of bona fide competitive trading in the market that distorts the pricing mechanism. To the contrary, permissible non-competitive trades, including EFFs, are subject to procedures designed to ensure that the transactions do not have a distortive effect and are executed and reported in a manner that cannot possibly mislead the market. Accordingly, CME Group's contention is completely without merit and, as noted below, is contrary to the longstanding practices of its own exchange subsidiaries. The argument is therefore disingenuous at best and reflects a transparent attempt to suppress competition in the markets that CME Group dominates.

For the same reasons, EFFs cannot be considered “transitory” or “contingent” trades. Transitory or contingent trades are exchanges of futures for physicals (“EFPs”) involving offsetting cash market transactions that result in no change in ownership of the physical commodity. See, Execution of Transactions: Regulation 1.38 and Guidance on Core Principle 9, 73 Fed. Reg. 54,097 (Sept. 18, 2008). Specifically, because a bona fide EFP, by its terms, requires that there be a legitimate cash market transaction that is linked to the futures transaction, a transitory transfer of ownership of the physical commodity, contingent on a transfer back to the original owner, could, depending on the circumstances, convert a permissible EFP into an illegal off-exchange futures transaction. An EFF involves an actual liquidation on one exchange and an actual establishment of a position on the second exchange. There is no transitory feature to the transaction at all. Indeed, under an EFF, there is no cash market transaction, or any offsetting leg of the transaction that could even allegedly be part of a transitory trade and, for this reason, neither the Commission nor any of the CME Group exchanges has previously applied the concepts of “transitory” or “contingent” trades to EFFs. CME Group's contention that EFFs constitute transitory or contingent trades is just another baseless attempt to undermine a permissible type of transaction that has been approved by the Commission in connection with ELX and the CME Group exchanges themselves.

The Commission has determined that the EFF Rule and the transactions permitted thereunder do not violate the CEA. Another exchange cannot eviscerate that approval, effectively reversing the Commission's decision, by substituting its own conclusions for those of the Commission.

2. The Advisory is Inconsistent with the Rules and Actions of the CME Group and was Clearly Issued for Anticompetitive Reasons.

As ELX has previously detailed in its prior submissions to the Commission, the CME Group exchanges have long permitted EFFs, as well as related types of permissible non-competitive transactions, to be executed and cleared through their facilities. See, Letter of ELX to David Stawick, Secretary of the Commission, dated November 12, 2009. Indeed, NYMEX, a CME Group subsidiary and an affiliate of the CBOT, developed the first EFF in 2002, and has introduced several variations on its original structure in the years since that time. In addition, NYMEX has a long history of allowing block trades to be used to exchange positions between NYMEX and IntercontinentalExchange, Inc. ("ICE"). See, http://www.nymex.com/notice_to_member.aspx?id=ntm110&archive=2007.¹ These trades have a practical effect that is substantially equivalent to that of EFFs, provided that the small minimum block trade requirement (200 contracts in the case of the NYMEX crude oil contract) is satisfied. CME Group cannot have it both ways – it cannot assert that EFFs and similarly structured transactions are fully permissible and provided for under its Rule 538 when executed on its exchanges while contending that ELX's EFF transaction violates the CEA and Commission regulations when executed through an exchange it considers a competitor.

Moreover, both CBOT and CME, as well as NYMEX, permit various types of "exchange for risk" transactions under rules that are sufficient, in their current form, to accommodate the execution of EFFs, without additional rule changes. In particular, CME Rule 538 broadly covers various types of "exchange for related position"

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In a related context, CME has interpreted its rules to prohibit block trades (aimed at a competitive effort by the LIFFE Exchange) to prevent transferring Eurodollar contracts to another market. On June 24, 2004 CME self-certified Rule 4.32.D Interpretation, Submission No. 04-61, which states: *CME Rule 432.D. prohibits fictitious trades. A prearranged trade wherein the parties agree to a transaction at CME which is reversed, in whole or in part, by another transaction at CME or at another Board of Trade is a fictitious trade prohibited by CME rules. CME facilities that permit prearrangement of trades (Rule 526 – Block Transactions ...) may not be used to facilitate a fictitious trade as defined above.* (Emphasis added).

transactions, or “EFRPs.” In an FAQ on Rule 538, issued with an Advisory dated October 2, 2009, the CME answered the question “What are EFRP transactions” as follows:

EFRP is an acronym for Exchange for Related Positions. Exchange for Physical (“EFP”), Exchange for Risk (“EFR”) and Exchange of Options for Options (“EOO”) transactions are collectively known as EFRP transactions. . . .

An EFR transaction is a privately negotiated and simultaneous exchange of a futures position for a corresponding OTC swap or other OTC derivative in the same or a related instrument (emphasis added).

An exchange of an OTC futures trade (which is OTC, from the perspective of the CME, because it is not executed on the CME) for an on-exchange futures position, pursuant to ELX’s EFF Rule, is the “simultaneous exchange of a futures position for a corresponding OTC swap or other OTC derivative” within the meaning of Rule 538. This conclusion is underscored by the fact that the CME has in effect two rules of its NYMEX affiliate expressly covering EFFs and has recently “harmonized” its rules across its exchange affiliates.²

Moreover, all of the types of EFRPs permitted under Rule 538 involve non-competitive executions of futures transactions in a manner that is substantially the same as the execution of EFFs, except that they take place within one exchange rather than between exchanges. We recognize, of course, that there are differences between these types of transactions and EFFs. However, all of these categories, including EFFs, involve non-competitive executions of trades that, but for their permissibility under the CEA and Commission regulations and orders, might otherwise violate the CEA prohibition on non-competitive trades. Here as well, if the conduct related to the execution of these transactions is permissible when applied within an exchange, it cannot become illegal when utilized in transactions effected between exchanges. Indeed, as noted, the Commission has found that such transactions are permissible under the CEA.

The Advisory disingenuously notes that CBOT rules do not permit EFFs. That statement, while technically accurate, is seriously misleading, and intentionally so.

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Prior to the Issuance of CME Advisory Notice RA0910-5, which sought the “harmonization of EFRP Rules across markets, and was made effective October 5, 2009, the NYMEX rulebook contained EFF Rules for natural gas and crude markets: Rule 6.21B Exchange of NYMEX Futures, Section B. Exchange of NYMEX Cash Settled “Penultimate Big” Futures for, or in Connection with, NYMEX “Physical” Futures Transactions

While nothing in CBOT rules expressly sanctions EFFs, the rules also do not prohibit such transactions. Moreover, and more importantly, CME Group has been in the process of harmonizing the rules of its various exchanges, and particularly the rules governing permissible non-competitive transactions. See, CME Group Advisory RA0910-5 (October 2, 2009). That harmonization process left untouched, and therefore retained, two of the NYMEX rules permitting EFFs, specifically those related to the “e-mini” contracts in natural gas and crude oil. If the CME Group believes that EFFs violate the CEA and Commission regulations, why does it continue to permit them in certain of its markets? The answer, of course, is obvious – it believes such transactions to be permitted but only asserts their alleged illegality in connection with the rules of another exchange which it views as a competitor. It is therefore apparent that the Advisory was issued solely for the purpose of undermining a nascent competitor seeking to challenge the overwhelming dominance of the CBOT, and CME Group generally, in the market.

Finally, we note that CME Group has taken a similar position with respect to block trades, which makes it difficult or impossible for market participants to utilize the block trade mechanism as a means of liquidating a position on one exchange and reestablishing it on another. Specifically, in interpretations issued in 2004 and 2008, CME Group stated that using a block trade for this purpose would constitute a “fictitious trade,” in violation of CME Rule 432.D. Rule 432.D Interpretation dated July 9, 2004 and Special Executive Report S-4735, dated July 21, 2008. As a result, CME Group has foreclosed the use of this trading approach – which is perfectly permissible and has been approved by CME Group and the Commission in other contexts – for purposes that it believes pose a competitive threat to its market dominance. We note that the use of block trades is not an effective alternative to EFFs in any event, because the substantial minimum size requirements imposed on block trades by CME Group operate as a deterrent on its use for this purpose. However, the actions of CME Group in connection with the use of block trades further underscores the anticompetitive nature of its conduct.

3. The Commission is Authorized and Required to Take Action
Against CME Group's Anti-Competitive Conduct.

One of the fundamental purposes of the CEA and the regulatory scheme administered by the Commission is “to promote responsible innovation and fair competition among boards of trade, other markets and market participants.” CEA, §3(b). For this reason, “in requiring or approving any bylaw, rule, or regulation of a contract market,” the Commission is required to “take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the objectives” of the rule or other action. CEA, §15(b). The purpose of the EFF Rule is to facilitate competition in the market for Treasury futures contracts and other products that now or in the future may be listed by ELX and the CME Group exchanges. In particular, the ELX Rule will provide market participants with the ability to execute transactions on the exchange of their choice with the knowledge that they will be able to liquidate the resulting positions and re-establish them on another exchange. This in turn will allow for more efficient management of positions, margin requirements, hedging needs and recordkeeping. Moreover, the ability to liquidate and re-establish positions via an EFF will benefit both exchanges involved, by increasing liquidity on, and generating fees for, each of them. While not commenting on at what level such fees can of themselves be anti-competitive, we note that the CME has in the past imposed surcharges on similar types of transactions (it currently places a surcharge of \$0.75/side in addition to regular transaction fees on Treasury futures transactions). The EFF Rule, therefore, is clearly pro-competitive and should be given full effect.

By blocking implementation of the EFF Rule through the Advisory, the CBOT and the CME Group have used their market dominance for anti-competitive purposes to deny market participants the advantages of this important tool, in violation of the CEA. Indeed, beyond the provisions cited above, the CEA expressly requires contract markets to “endeavor to avoid (A) adopting any rules or taking any actions that result in any unreasonable restraints of trade; or (B) imposing any material anticompetitive burden on trading on the contract market.” CEA, §5(d)(18). The Advisory is unquestionably an action that results in an unreasonable restraint of trade, by prohibiting market participants from engaging in transactions that the Commission has concluded are permissible under the CEA, that the CME Group itself permits in other contexts and that would promote competition in a market overwhelmingly dominated by a single player. The Commission is therefore compelled to use its authority “to promote responsible innovation and fair competition among boards of trade” by requiring CME Group to permit EFFs between ELX and the CBOT.

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Accordingly, we respectfully request that the Commission take appropriate action to require the CBOT to refrain from threatening or initiating enforcement action in connection with EFFs between the CBOT and ELX and to permit such EFFs to be executed. In this regard, the Commission clearly has the authority under the CEA to require a DCM to take action, or to refrain from taking action, as may be necessary in order to ensure its compliance with the Core Principles. Specifically, the CEA expressly provides that the Commission is authorized “to alter or supplement the rules of a registered entity insofar as necessary or appropriate by rule or regulation or by order, if after making the appropriate request in writing to a registered entity that such registered entity effect on its own behalf specified changes in its rules and practices, and after appropriate notice and opportunity for hearing, the Commission determines that such registered entity has not made the changes so required, and that such changes are necessary or appropriate for the protection of . . . traders or to insure fair dealing in commodities traded for future delivery on such registered entity. Such rules, regulations, or orders may specify changes with respect to such matters as— . . . the form or manner of execution of purchases and sales for future delivery . . .” CEA, §8a(7). The Commission is also authorized, under Section 6b of the CEA, to order any registered entity to cease and desist from violations of the CEA or Commission regulations or orders. The statute therefore provides the Commission with ample authority, and in fact requires that the Commission take action, to effectuate the implementation of the EFF Rule it has approved.

In our meeting with you and members of your staff, the staff raised an issue regarding the effect of the antitrust laws, and particularly the U.S. Supreme Court’s decision in the Trinko case, Verizon Communications, Inc. v. Trinko, 540 U.S. 406 (2004), on this analysis and on the Commission’s authority to take action in this instance. While the conduct of the CBOT and CME Group described above, in addition to violating the CEA and the Commission’s regulations, could also constitute a violation of the antitrust laws, that question is not properly directed to the Commission. However, the status of their conduct under the antitrust laws has no bearing on the CEA analysis, and the Commission remains obligated to take action if it concludes, as we believe it must, that the conduct violated the CEA and Commission regulations. Accordingly, regardless of whether the antitrust laws provide further support for the action we are requesting here, they cannot in any event preclude such action.

For these reasons, we do not believe that the Trinko case has any applicability to the circumstances presented here. Nevertheless, in response to the questions raised by the staff, we have analyzed the Trinko case in this context and have concluded that, to the extent that it is applicable, it supports, rather than undermines, the illegality of the conduct of the CBOT and CME Group under the antitrust laws. In

Trinko, the Supreme Court held that a telecommunications carrier that was a monopolist in the relevant market did not violate the antitrust laws by refusing to provide competitors with access to its operation support system. In reaching this conclusion, the Court distinguished the facts in Trinko from those presented in Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985). In Aspen, a monopolist unilaterally terminated a voluntary agreement with a competitor to bundle lift tickets and thereafter refused to sell such tickets to its competitor even at the retail price. The Court held in that case that the monopolist's conduct in Aspen "suggested a willingness to forsake short-term profits to achieve an anticompetitive end. . . . [T]he defendant's unwillingness to renew the ticket *even if compensated at retail price* revealed a distinctly anticompetitive intent" (emphasis in original). In contrast, the Court in Trinko found that the defendant did not engage in behavior that could be explained only or primarily by reference to an anticompetitive motive. Here, the anticompetitive intent of the CBOT and CME Group is patently obvious and cannot be denied. CME Group permits EFFs and other forms of non-competitive trading in other markets, the Advisory was issued only days after the Commission's approval of the EFF Rule and, like the defendant in Aspen, CME Group is willing to forsake profits – which it would earn through the fees it could collect on the execution of EFFs -- to achieve an anticompetitive objective. To the extent that Trinko is relevant here at all, therefore, which we believe it is not, it supports our conclusion that CBOT and CME Group have engaged in illegal conduct that must be remedied.

Moreover, we note that the plaintiff in Trinko was seeking to require Verizon to take affirmative steps that would adversely affect Verizon's own customers, by making capacity available to customers of a competitor, thereby reducing the level of service to its own customers. In the case of EFFs, as in Aspen, no affirmative conduct by the CME is required in order to effectuate the purposes and intent of the EFF Rule; CME simply needs to allow its facilities to be used to execute EFFs, to the benefit of its own market participants, and itself (in the form of additional fees). There are no new "facilities" that need to be created, and CME's "customers" will not be adversely affected. To the contrary, they are the intended beneficiaries of the EFF Rule. This factor as well underscores the anti-competitive purpose of the CME Group's actions.

For the foregoing, reasons, we respectfully request that the Commission promptly take appropriate action to require the CBOT to permit EFFs to be executed by market participants between CBOT and ELX, pursuant to the EFF Rule, and to refrain from threatening or initiating enforcement action in connection with the execution of such EFFs. We defer to the Commission's judgment as to the type of action that would be most appropriate in this instance. However, as an initial matter, we respectfully request that the Commission stay the effectiveness of the Advisory and any statements by

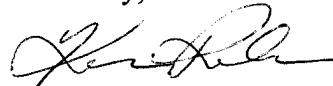
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the CBOT or CME Group that enforcement action will be taken against market participants executing EFFs. In addition, we respectfully request that the Commission direct CBOT and CME Group, by order or otherwise, to permit the execution of EFFs between ELX and CBOT, in accordance with the EFF Rule that the Commission has approved. We would of course be pleased to discuss these issues further with the Commission or its staff and to address the various types of remedial action that are available.

We very much appreciate your consideration of this important matter and look forward to our further discussions of the issue.

Sincerely,



Kenneth M. Raisler

cc: Mr. David Stawick
(Secretary)

Mr. Michael Dunn
(Commissioner)

Mr. Bart Chilton
(Commissioner)

Ms. Jill Sommers
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