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David J. Vitale
President and
Chief Executive Officer

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August 10, 2001

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Jean A. Webb
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

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OFFICE OF THE SECRETARIAT

Re: Restriction of Dual Trading in Security Futures Products by Floor Brokers -
66 Fed. Reg. 36218 (July 11, 2001)

Dear Ms. Webb:

The Board of Trade of the City of Chicago, Inc. ("CBOT®") appreciates the opportunity to comment on the Commodity Futures Trading Commission's ("Commission") proposal to adopt Regulation 41.27 to implement Section 4j of the Commodity Exchange Act ("Act"), as amended by the Commodity Futures Modernization Act of 2000 ("CFMA"). This proposed regulation would restrict dual trading by floor brokers in security futures products on designated contract markets ("DCMs") and registered derivatives transaction execution facilities ("DTFs"), subject to enumerated exceptions.

The Commission has proposed to define a "customer" as an account owner for which a floor broker executes trades, other than a number of defined types of accounts. The CBOT believes that the accounts identified in proposed Regulation 41.27(a)(4)(i) through (iv) are appropriately excluded from the definition of a customer.

In Regulation 41.27(a)(4)(v), the Commission has also proposed to define an account for another member present on the floor, or an account controlled by such other member, as a non-customer. The Commission has also specifically requested comment regarding whether the accounts of all clearing members and the accounts of members not present on the floor of a DCM or DTF should be considered to be non-customer accounts for purposes of the proposed Regulation.

As suggested by the Commission, individual members and member firms may be in a better position to protect themselves against potential dual trading abuses than other customers. Consequently, it is difficult to justify prohibiting a floor broker from trading for his own account and the account of such individuals and firms during the same trading session. However, the CBOT does not believe the Commission should enumerate any of these accounts as non-customer accounts under Regulation 41.27(a)(4). Rather, the CBOT urges the Commission to permit transactions for clearing members other than the floor broker's own clearing member, and members of a DCM or DTF, whether or not

present on the floor, as a specific permitted exception to the dual trading prohibition. In fact, in current Regulation 155.5(c)(4), which lists the permitted exceptions to the applicability of a dual trading prohibition, there is an exception for member customers not present on the floor.

It is clearly the Commission's intent to permit brokers to trade for their own accounts while allowing them to trade for the accounts of other members present on the floor during the same trading session. However, by defining the latter as non-customers, the Commission has proposed to prohibit brokers from trading for these individuals and other customers during the same trading session. Therefore, only a broker who trades for himself or for the house account of his clearing member would be permitted to take an order from another member on the floor. This type of broker may be unwilling or unable to take such an order, and the member present on the floor who would like to place an order may not be able to do so.

Similarly, if the Commission were to define clearing members and members not present on the floor as non-customers, the only brokers who could execute orders for such members would be brokers who only executed such orders and traded for themselves or their own clearing firms. These are not the types of brokers to whom other clearing firms or members would be likely to want to direct their orders. The solution to this dilemma is to permit an exception to the dual trading prohibition for the accounts of clearing firms other than the broker's clearing firm and the accounts of individual members, whether or not present on the floor.

The Commission's proposed definition of dual trading only prohibits such activity when the customer order is executed through open outcry, whether the non-customer trade is executed by open outcry or through an electronic trading system. The dual trading ban would not apply when the non-customer trade is executed through open outcry and the customer order is executed electronically or where both trades are executed electronically. The CBOT agrees with the Commission's position that a dual trading prohibition is not applicable in the latter instances, because there is no "floor broker." However, the CBOT also believes that a dual trading prohibition should only be applicable when both the customer order and the non-customer trade are executed through open outcry.

Section 4j(b) of the Act, as amended, defines "dual trading" as "the execution of customer orders by a floor broker during the same trading session in which the floor broker executes any trade in the same contract . . ." for his own account or other specified types of accounts. Therefore, the statutory dual trading definition refers both to a "floor broker" who "executes" customer orders, and to a "floor broker" who "executes" personal trades. As the Commission has acknowledged, when an order is entered electronically, the broker is not able to control at what price and against whom the order is executed. He can only control when the order is entered into the system. The order is "executed" through the electronic matching of bids and offers pursuant to a predetermined algorithm. Therefore, it is not very likely that a broker would attempt to

engage in dual trading abuses if either order is executed electronically and the other through open outcry, because the broker would be unable to control all of the variables of the electronic execution. It should also be noted that the surveillance necessary to detect and deter possible trading abuses is easily facilitated by the fact that an electronic system records the time of entry.

The language of the statute does not require a dual trading prohibition where either of the trades involved is executed by an electronic trading system. The Commission's own reasons for excluding from the dual trading definition certain situations where one or both trades are executed electronically, apply equally where the personal trade is executed electronically and the customer order is executed through open outcry. Therefore, any dual trading prohibition should not be applicable where either or both trades are executed by an electronic trading system.

The proposed dual trading definition refers to a floor broker executing "directly or indirectly" a transaction for a non-customer account. In its Federal Register release, the Commission has noted that the word "indirectly" is meant to refer to a situation where a floor broker would initiate and pass an order to another broker for execution. Current Regulation 155.5, which the Commission has appropriately proposed to delete, does not use the "directly or indirectly" language. Instead, it refers to a floor broker who "executes directly or initiates and passes to another member for execution" Regulation 155.5(a)(4). The CBOT suggests that the Commission explicitly describe what it means by indirect execution in the proposed regulation, rather than only resolving any ambiguity created by the use of the word "indirectly" in a reference in the Federal Register.

The Commission has proposed to permit certain specific exceptions to the dual trading prohibition for transactions involving the correction of errors, spread transactions, customer consent, and market emergencies. In addition, the Commission has proposed to permit exceptions to the dual trading prohibition to address unique or special characteristics of agreements, contracts, or transactions, or of DCMs or DTFs, on a case-by-case basis. The CBOT agrees with the Commission that each of these proposed exceptions is appropriate and is consistent with the statute.

The CBOT encourages the Commission to add a low volume exception to its proposal. The statute grants the Commission the latitude to do so "to ensure fairness and orderly trading" and "to further the public interest consistent with the promotion of market efficiency, innovation, and expansion of investment opportunities." Section 4j(a)(2)(C) of the Act, as amended. The dual trading prohibition contained in Section 11 of the Securities Exchange Act of 1934 ("Exchange Act"), which will apply to national securities exchanges that offer security futures products, states:

If because of the limited volume of transactions effected on an exchange, it is in the opinion of the Commission impracticable and not necessary or appropriate in the public interest or for the protection of investors to apply [the dual trading

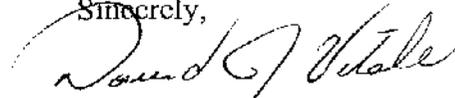
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prohibition], the Commission shall have power, upon application of the exchange and on a showing that the rules of such exchange are otherwise adequate for the protection of investors, to exempt such exchange and its members

Section 11(c) of the Exchange Act. Regulation 155.5(c)(4)(v) contains a low volume exception, and such an exception may assist fledgling security futures products to become established before a dual trading prohibition would become applicable.

The CBOT strongly applauds the Commission's proposal to remove Regulation 155.5 in light of the CFMA's amendment of Section 4j of the Act.

Sincerely,

A handwritten signature in cursive script, appearing to read "David J. Vitale".

David J. Vitale