# SUBMISSION COVER SHEET

**Exchange Identifier Code (optional)** 06-76 **Date** October 17, 2006

| **ORGANIZATION** | Chicago Mercantile Exchange |
|---|---|

**FILING AS A:** ☒ **DCM** ☐ **DCO** ☐ **DTEF**

**TYPE OF FILING**

- **Rule Amendments**

  ☐ Self-Certification Under Reg. 40.6(a)

  ☐ Commission Approval Requested Under Reg. 40.5 or 40.4 (a)

  ☐ Notification of Rule Amendment Under Reg. 40.6(c)

  ☐ Non-Material Agricultural Rule Change Determination Under Reg. 40.4(b)

2. **New Products**

  ☐ Self-Certification Under Reg. 40.2 or 41.23

  ☒ Commission Approval Requested Under Reg. 40.3

**RULE NUMBERS**

New Rule Chapter 455

**DESCRIPTION (Rule Amendments Only)**

CME is introducing CME Credit Event Futures contracts

Chicago Mercantile Exchange

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October 17, 2006

Ms. Eileen Donovan
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre, 1155 21st Street, NW
Washington, DC 20581

RE: Voluntary Submission of CME Credit Event Futures for Commission Review and Approval per Sec. 5c(c)(2) of the CEA and Regulation §40.3 Thereunder.
CME Submission # 06-76

Dear Ms. Donovan:

Chicago Mercantile Exchange ("CME" or "the Exchange") hereby submits CME Credit Event Futures for Commission review and approval in accordance with Section 5c(c)(2) of the Act and Regulation §40.3, thereunder. This initiative was approved by the Exchange's Approving Officers per authority delegated by the Exchange's Board of Directors on September 21, 2006 per CME Rule 230.j.

We have submitted this document electronically to submissions@cftc.gov. Further, we are hand delivering a hard copy of this document hand to the your offices along with a check made out to the Office of the Secretariat, Commodity Futures Trading Commission in the amount of $7,200 (seven-thousand two-hundred dollars) per Regulation §40.3(a)(8) and Appendix B to Part 40 of the Regulations. Note that the Exchange is applying to list three (3) CME Credit Event Futures contracts.

Please do not hesitate to contact Mr. John E. Nyhoff, Director, Research & Product Development at 312-930-2310 or john.nyhoff@cme.com if any questions arise during the processing of this submission. Please reference our CME Submission #06-76 on all future correspondence for this submission.

Sincerely,

John W. Labuszewski, Managing Director
Research & Product Development

Encl.

CC: Mr. Thomas Leahy, CFTC Division of Trading and Markets

Commodity Futures Trading Commission
525 West Monroe Street, Suite 1100
Chicago IL 60661
Attn: Director, Central Region

# Voluntary Submission of CME Credit Event Futures for Commission Review and Approval per Sec. 5c(c)(2) of the CEA and Regulation §40.3 Thereunder

**October 17, 2006**

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## 1. Introduction

Chicago Mercantile Exchange ("CME" or "the Exchange") hereby voluntarily submits CME Credit Event Futures for Commission review and approval in accordance with Section 5c(c)(2) of the Act and Regulation §40.3, thereunder.

Per Commission Regulation §40.3(a)(1), this document is submitted to the Secretary of the Commission via e-mail at submissions@cftc.gov. Further, we are hand delivering a hard copy of this document to the Commission's Washington offices along with a check made out to the Office of the Secretariat, Commodity Futures Trading Commission in the amount of $7,200 (seven-thousand two-hundred dollars) per Regulation §40.3(a)(8) and Appendix B to Part 40 of the Regulations, noting that the Exchange is applying to list three (3) CME Credit Event Futures contracts. Finally, a hard copy has been sent to the Commission's Chicago office at 525 West Monroe Street, Suite 1100, Chicago IL 60661. Per Commission Regulation §40.3(a)(2), we have included a copy of the submission cover sheet in accordance with the instructions in Appendix D to Part 40.

Section 2 of this document includes explanations in narrative form, in accordance with Commission Regulation §40.3(a)(4), to the degree not self-evident from the Rules, as to how the specific terms and conditions satisfy acceptable practices set forth in Guideline No. 1, Appendix A to Part 40 of the Commission's Regulations. Note that the proposed contract provides for a cash settlement. Accordingly, we have included an explanation of the mechanics of this cash settlement, further explaining how said cash settlement will not be subject to manipulation or distortion. Note that this cash settlement does not rely upon a cash price series *per se* given the binary nature of the settlement.

Section 3 of this document provides a brief description of the cash market for credit derivatives per Commission Regulation §40.3(a)(4)(iv). The proposed contract does not rely upon any agreements or contracts with third parties, as discussed in Commission Regulation §40.3(a)(5).

Section 4 of this document includes a copy of the Rules that set forth the contract terms and conditions, in accordance with Commission Regulation §40.3(a)(3).

Certifications per Commission Regulation §40.3(a)(6) are inapplicable insofar as the proposed contract is carefully constructed so that it may not be characterized as a security future or securities futures product per Sections 1a(31) or 1a(32) of the Act. In particular, it is not a contract for future delivery of a single security; or, for delivery of any measure of value based on a single security or an index of securities. The Final Settlement Price is binary in nature and fixed in advance of listing and does not vary in relation to the price of any obligation issued by the reference entity.

Per Commission Regulation §40.3(a)(9), the Exchange stands ready to support this submission for Commission review and approval with additional information as requested by the Commission.

## 2. CME Credit Event Futures Design

CME Credit Event Futures are intended to provide a transparent, liquid and facile means of acquiring protection against the risk of a bankruptcy, default, non-payment, debt restructuring or other credit events. As such, CME intends to extend the benefits of exchange-traded product to the credit derivatives industry which heretofore has only been available on an over-the-counter (OTC) basis.

They are designed to dovetail with current futures accounting practices, *i.e.*, they require an initial performance bond deposit and are subsequently marked-to-market (MTM) on a daily basis. As the expiration date of a CME Credit Event Futures contract draws near, the entire value of the protection will have been paid from long to short through the MTM process. If a Credit Event occurs prior to the expiration date, the Credit Event Futures contract will terminate and the short position is marked-to-market at a fixed amount as defined by the Exchange.

Thus, CME Credit Event Futures merge the benefits of OTC credit default swaps with the benefits of trading futures. Specifically, CME Credit Event Futures are cleared and guaranteed by the CME Clearing House. This may result in capital efficiencies for institutions that may cross-margin CME Credit Event Futures against other CME Credit Event Futures … or against other interest rate futures cleared by CME.

***Binary Event Futures Concept*** – CME Credit Event Futures call for a final cash settlement which is binary in character. In the absence of any credit events associated with the Reference Entity, the Final Settlement Price of the contract will be established at zero ($0) as of the Final Settlement Date. However, if there is a credit event, the Final Settlement Price will be established at some non-zero value.

Should a credit event be declared with respect to the Reference Entity on or before determination of the Final Settlement Price on the Final Settlement Date, then the Final Settlement Price, expressed in basis points is established as equal to the Final Settlement Rate (F), as defined by the Exchange. The monetary value of the Final Settlement Price may be calculated as the Final Settlement Rate (F) applied to the Notional Value (NV) of the contract.

For example, assume that the Final Settlement Rate (F) is established at 45% and the contract is based upon a Notional Value of $100,000. This implies a Final Settlement Price of 0.45 or 4,500 basis points. This equates to a Final Settlement Value of $45,000 (=45% of $100,000). The Exchange may offer several contracts with varying Ntional Values (*e.g.,* $50,000, $100,000, $200,000, etc.) or Final Settlement Rates (*e.g.,* F=40%, 50%, 60%, etc.) based on the same Reference Entity.

Thus, these futures contracts may be characterized as a form of binary event futures. The "event" is a defined Credit Event suffered by the Reference Entity. We have carefully constructed the contract so that it may not be characterized as a security futures contract. In particular, it is not a contract for future delivery of a single security; or, for delivery of any measure of value based on a single security or an index of securities. The Final Settlement Price is binary in nature and fixed in advance of listing and does not vary in relation to the price of any obligation issued by the Reference Entity.

## Summary of CME Credit Event Futures

| | |
|---|---|
| **Final Settlement** | Final Settlement Price set at Final Settlement Rate (F) with Final Settlement Value equal to F applied to Notional Value (NV) of contract, as established by the Exchange, upon occurrence of a "Credit Event" prior to expiration. *E.g.,* Final Settlement Value of a contract with a Final Settlement F=45% and a Notional Value NV=$100,000, is equal to $45,000. Contract expires at $0 if no Credit Event occurs before expiration. |
| **Reference Entities** | Contracts shall be listed based on the following specified Reference Entities (or their successor reference entities) … (1) Cendant Corp.; (2) Jones Apparel Group, Inc.; (3) Tribune Corporation. Additional Reference Entities may be listed at discretion of CME. |
| **Credit Event** | Credit Event deemed to occur in the event of … 1. Bankruptcy, 2. Obligation Acceleration, 3. Obligation Default, 4. Failure to Pay, 5. Repudiation/Moratorium, or 6. Restructuring … per Article IV of 2003 ISDA Credit Derivatives Definitions. |
| **Quotation Convention** | Quoted as total price of credit protection for remainder of term, expressed as fraction of Notional Value in basis points (bps). *E.g.,* a contract valued at 50 bps per annum with ¾ year to expiration may be quoted at 37.5 bps. The "time decay" in total price allows buyer effectively to compensate seller for cost of credit protection over time. |
| **Tick Size** | Generally established at 0.5 Basis Points (bps), *e.g.,* if Notional Value = $100,000 *THEN* 0.5 bps = $5.00 |
| **Contract Months** | Listed five (5) years in advance of Final Settlement Date in June and December. |
| **Last Trading Day** | Trading terminates at 12:00 noon on the Final Settlement Date. |
| **Final Settlement Date** | 2nd Business Day preceding the third Wednesday of contract month. |
| **Trading Hours** | Offered exclusively on CME Globex® electronic trading platform on Sundays thru Thursdays from 5:00 pm-4:00 pm (Chicago time) the following day. Daily shutdown from 4:00 pm-5:00 pm. |

***Credit Event Definitions*** - CME Credit Event Futures are triggered by the same events as standard OTC CDSs using ISDA conventions. Specifically, these contracts rely upon credit event definitions per Article IV of the 2003 ISDA Credit Derivatives Definitions, subject to confirmation from public sources, also per ISDA conventions. As such, the event triggering cash settlement of the contract cannot be subject to manipulation or distortion." Because of the binary nature of this contract, it does not rely upon a cash price series *per se* for purposes of final cash settlement. Therefore the value of the contract on settlement is not subject to manipulation or distortion as prescribed by Guideline No. 1, Appendix A to Part 40 of the Commission's Regulations.

***Cash Flows*** – From a cash flow perspective, CME Credit Event Futures operates akin to other cash settled futures contracts. One may buy or sell a contract, at which point, one is required to post an initial performance bond (or "initial margin"). Subsequently, the price of the contract may fluctuate up or down resulting in variation margin payments on a daily mark-to-market ("MTM") basis. CME will list Credit Event Futures maturing on the 2nd business day preceding the third Wednesday of the contact months of June and December extending out five years into the future. (Note that the most popular OTC credit derivatives typically carry a five-year term.)

Unlike other futures contracts, however, the contract may terminate prior to the regularly scheduled maturity date if a credit event such as a bankruptcy or debt restructuring should occur. At this point, the contract is promptly settled during the next clearing cycle at a value of C% of the notional value. *E.g.,* if the Final Settlement Rate is established at 50% for a contract with a Notional Value of $100,000 then both long and short are marked-to-market at a Final Settlement Price of 5,000 basis points (bps) or a Final Settlement Value of $50,000 (= 50% x $100,000).

It is reasonable to anticipate that the market prices will tend to rise in anticipation of the occurrence of a credit event. *I.e.,* the market should be efficiently priced. As such, the daily mark-to-market process will have the effect of transferring the value of the protection associated with the contract from protection seller to protection buyer. Effectively, shorts will pay longs an amount equal to the Final Settlement Price less the original transaction price through the accumulation of daily MTM pays and collects. Because this process will tend to be gradual in nature, risks to the clearinghouse are mitigated.

Contracts are quoted as the total remaining value of the credit protection in minimum increments of 0.5 basis points. In the case of a contract with a Notional Value established at $100,000, this equates to $5 (= 0.005% x $100,000) or $10 per full basis point. *E.g.,* a 5-year contract quoted as 250 bps implies an annualized quote of ≈ 50 bps. Daily mark-to-market procedures ensure that the value of the protection is transferred from buyer to seller as maturity approaches in the absence of a credit event. Or, that the value of the fixed payout is transferred from seller to buyer as contracts are cash settled early, triggered by a credit event.

***Settlement at Zero*** - Assume it is June 19, 2006 and you purchase one (1) CME Credit Event Futures contract tied to the debt of XYZ Corporation, with a Notional Value established at $100,000, at a price of 200.0 bps maturing June 14, 2010 (4-year term). While the price of 200.0 bps represents $2,000 (= 2.00% x $100,000), the buyer does not actually pay $2,000 in cash but rather secures this transaction with funds sufficient to cover the initial performance bond requirement. Assume that the initial performance bond requirement equals $800. Although our example is constructed from the perspective of the buyer, both buyer and seller must post the initial performance bond and both are marked-to-market as market values fluctuate.

Assume that the Reference Entity is stable throughout the next 4 years until full term. Under these circumstances, one would expect the market price to wind down to zero by the time the contract matures. Upon final settlement at a price of 0.0 bps, the initial performance bond is released back to buyer and seller. If both buyer and seller retain their long and short positions, respectively, and do not offset them during the next 4 years, the contract value winds down to 0.0 bps … perhaps taking a circuitous path but winding down to zero nevertheless. As such, the buyer, through a series of MTM pays and collects, compensates the seller with the original 200.0 bps or $2,000.

| Date | Action | Market Price | Cash Flows |
|---|---|---|---|
| 6/19/06 | Buy 1 XYZ Credit Event Futures | 200.0 bps | Posts $800 initial margin |
| 6/20/06 | | 198.0 bps | MTM pay of $20 |
| 6/21/06 | | 197.0 bps | MTM pay of $10 |
| 6/22/06 | | 200.5 bps | MTM collect of $35 |
| 6/23/06 | | 203.0 bps | MTM collect of $25 |
| … | … | … | … |
| 6/8/10 | | 2.0 bps | Accumulated pays of $1,800 |
| 6/9/10 | | 1.0 bps | MTM pay of $10 |
| 6/10/10 | | 0.5 bps | MTM pay of $5 |
| 6/11/10 | | 0.5 bps | - |
| 6/14/10 | Final Cash Settlement | 0.0 bps | MTM pay of $5 |
| | | | **TOTAL PAYS = $2,000** |

***Occurrence of Credit Event*** – Assume that one buys the same CME Credit Event Futures contract tied to the debt of XYZ Corporation, with a Notional Value established at $100,000, and at a price of 200.0 bps maturing 4 years hence. But this time, credit anxieties begin to mount. The price of the CME Credit Event Futures contract tied to Reference Entity XYZ increases as the market factors in a higher probability for the occurrence of a credit event. Commensurate with increasing volatility, performance bond requirements are increased by CME Clearing House. Assume that performance bond requirements had been raised to $1,200 and are increased to $1,800 on April 16, 2008.

What if a Credit Event should occur? Assume that by September 2008, a Credit Event is imminent and initial performance bonds had been increased previously to $10,000. By the time a Credit Event is declared and final settlement occurs, the protection buyer has effectively received from the protection seller the entire $50,000 (= 50% x $100,000) less the original 200 bps ($2,000) or $48,000 net through the mark-to-market process.

| Date | Action | Market Price | Cash Flows |
|---|---|---|---|
| 6/19/06 | Buy 1 XYZ Credit Event Futures | 200.0 bps | Posts $800 initial margin |
| 6/20/06 | | 198.0 bps | MTM pay of $20 |
| 6/21/06 | | 197.0 bps | MTM pay of $10 |
| 6/22/06 | | 200.5 bps | MTM collect of $35 |
| 6/23/06 | | 203.0 bps | MTM collect of $25 |
| … | … | … | … |
| 4/14/08 | Credit concerns mounting | 321.0 bps | Accumulated collects of $1,210 |
| 4/15/08 | | 325.0 bps | MTM collect of $40 |
| 4/16/08 | CH increases margin requirement to $1,800 from $1,200 | 338.0 bps | MTM collect of $130<br>Post $600 in additional performance bonds |
| 4/17/08 | | 339.0 bps | MTM collect of $10 |
| … | … | … | … |
| 9/5/08 | | 4,050.0 bps | Accumulated collects of $38,500 |
| 9/8/08 | | 4,500.0 bps | MTM collect of $4,500 |
| 9/9/08 | | 4,900.0 bps | MTM collect of $4,000 |
| 9/10/08 | | 5,000.0 bps | MTM collect of $1,000 |
| 9/11/08 | Credit Event Declared | 5,000.0 bps | - |
| 9/12/08 | Final Cash Settlement | 5,000.0 bps | - |
| | | | **TOTAL COLLECTS = $48,000** |

***Position Limits*** – Proposed Rule 45502.D., Position Limits, provides that “[a] A person shall not own or control more than a specified number of contracts net long or short positions in any single contract as determined by the Board of Directors as depicted in Rule 45502.B..” Rule 45502.B. establishes the position limit at 5,000 contracts.

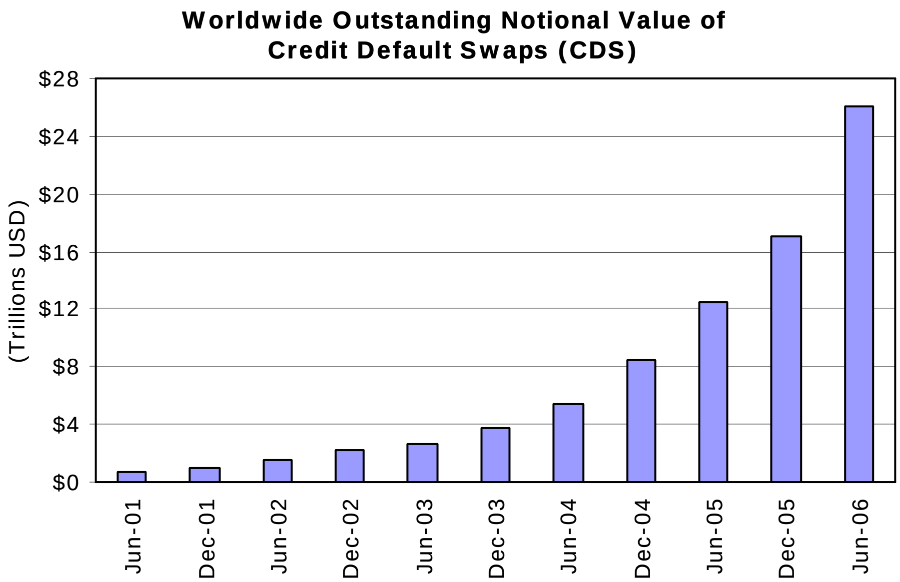
Note that 5,000 contracts is identified as a “standard” limit for “Nonspot individual month or all months combined” per Guideline No. 1, Appendix A to Part 40 of the Commission’s Regulations. Note further that position limits are intended to limit the potential for disruption in the underlying market(s) as a result of excessive positions in the related futures contracts. It is unclear how one might affect the underlying or spot item … credit events … by carrying large positions in CME Credit Event Futures. Proposed Rule 45502.E., Accumulation of Positions, is effectively identical to the language of Commission Regulation §150.5(g) and is identical to previous language put in place by the Exchange with respect to the aggregation of positions.

***Reporting Level*** – The reporting level for CME Credit Event Futures shall be established at a level equal to levels specified in Commission Regulation §15.03.

***Block Trades*** - The Exchange shall permit block trading to be conducted in the context of the CME Credit Event Futures with a twenty (20) contract minimum transacted quantity requirement.

## 3. Description of the Credit Derivatives Market

The credit derivatives industry has experienced remarkable growth over the past decade and now represents the fastest growing segment of the over-the-counter (OTC) derivatives market by far. While credit default swaps (CDSs) are a relatively new form of derivative product, having emerged in the mid- to late 1990s, the outstanding notional value of this marketplace has grown to ≈ \$26 trillion by mid 2006.




A "credit event" includes bankruptcy, obligation acceleration, obligation default, failure to pay, debt repudiation/moratorium, or restructuring. These credit events may reference a corporate obligation such as a corporate bond, bank loan or other evidence of corporate indebtedness; a sovereign debt obligation; asset backed securities including commercial mortgage backed securities; or, possibly other debt instruments. These obligations may be issued by various reference entities including corporations and sovereign entities. These credit events are generally defined by Article IV of the 2003 International Swaps & Derivatives Association's (ISDA) Credit Derivatives Definitions. These definitions and standards are well established and adopted for widespread use in the OTC markets.

***Measuring Credit Risk* -** Rating agencies such as Moody's, S&P and Fitch have provided credit ratings for a considerable period of time. Note that debt rated BBB- or higher is considered investment grade debt. The higher the credit grade listing, the more creditworthy the reference entity is considered to be. Debt rated BB+ or lower is considered to be non-investment grade debt. Non-investment grade bonds are often referred to as high yield bonds. Lower rated high yield bonds are often referred to in the vernacular as junk bonds.

U.S. Treasury securities are generally viewed as the U.S. dollar benchmark for default free or risk-free fixed income securities. U. S. Treasuries securities will always imply an element of market risk associated with interest rate fluctuations but are nonetheless viewed as implying zero credit risk.

## Rating Agency Credit Descriptions

| Moody's | S&P | Fitch | Description |
|---|---|---|---|
| **Investment Grade Debt** | | | |
| Aaa | AAA | AAA | Prime. Maximum Safety |
| Aa1 | AA+ | AA+ | High Grade High Quality |
| Aa2 | AA | AA | |
| Aa3 | AA- | AA- | |
| A1 | A+ | A+ | Upper Medium Grade |
| A2 | A | A | |
| A3 | A- | A- | |
| Baa1 | BBB+ | BBB+ | Lower Medium Grade |
| Baa2 | BBB | BBB | |
| Baa3 | BBB- | BBB- | |
| **Non Investment Grade or "High-Yield" Debt** | | | |
| Ba1 | BB+ | BB+ | |
| Ba2 | BB | BB | Speculative |
| Ba3 | BB- | BB- | |
| B1 | B+ | B+ | Highly Speculative |
| B2 | B | B | |
| B3 | B- | B- | |
| Caa1 | CCC+ | CCC | Substantial Risk |
| Caa2 | CCC | - | In Poor Standing |
| Caa3 | CCC- | - | |
| Ca | - | - | Extremely Speculative |
| C | - | - | May be in Default |
| - | - | DDD | Default |
| - | - | DD | |
| - | D | D | |

Credit ratings cited in the accompanying tables are reference points to establish a credit spread for the relative default or non-payment risk associated with corporate debt instruments. Credit spreads are a function of both credit rating and yield to maturity. A credit spread may be aggregated with the yield on a comparable maturity Treasury security yield to determine the credit-adjusted corporate bond yield. Higher (lower) corporate bond credit ratings imply smaller (larger) credit spreads.

As creditworthiness decreases, credit spreads increase. *E.g.,* the buyer of a 5-year corporate bond might demand a 35.6 basis point credit spread premium from an AAA corporate borrower. Alternatively, the buyer of a 5-year corporate bond would demand a much greater credit spread premium of perhaps 80 basis points from a BBB+ corporate borrower.

## Treasury & Corporate Bond (Industrials) Yields (%)

| | US Treasury | AAA Corporate | AA Corporate | A Corporate | BBB+ Corporate | BBB Corporate | BBB- Corporate |
|---|---|---|---|---|---|---|---|
| 1-year | 4.985 | 5.158 | 5.243 | 5.346 | 5.467 | 5.612 | 5.627 |
| 2-year | 4.920 | 5.221 | 5.263 | 5.368 | 5.525 | 5.693 | 5.725 |
| 3-year | 4.923 | 5.229 | 5.323 | 5.424 | 5.600 | 5.741 | 5.818 |
| 5-year | 4.946 | 5.302 | 5.462 | 5.548 | 5.746 | 5.877 | 6.046 |
| 10-year | 5.100 | 5.741 | 5.762 | 5.878 | 6.100 | 6.277 | 6.442 |
| 30-year | 5.125 | 5.696 | 6.013 | 6.188 | 6.423 | 6.691 | 6.789 |

Source: Bloomberg as of 10 AM on Monday, April 17, 2006

Further, borrowers will typically demand a higher credit spread premium as the term to maturity of a corporate bond increases due to the increased probability of credit default over a longer term time horizon.

## Bond (Industrials) Yield Spread to U.S. Treasuries (Basis Points)

| | US Treasury | AAA Corporate | AA Corporate | A Corporate | BBB+ Corporate | BBB Corporate | BBB- Corporate |
|---|---|---|---|---|---|---|---|
| 1-year | 0 | 17.3 | 25.8 | 36.1 | 48.2 | 62.7 | 64.2 |
| 2-year | 0 | 30.1 | 34.3 | 44.8 | 60.5 | 77.3 | 80.5 |
| 3-year | 0 | 30.6 | 40.0 | 50.1 | 67.7 | 81.8 | 89.5 |
| 5-year | 0 | 35.6 | 51.6 | 60.2 | 80.0 | 93.1 | 110.0 |
| 10-year | 0 | 64.1 | 66.2 | 77.8 | 100.0 | 117.7 | 134.2 |
| 30-year | 0 | 57.1 | 88.8 | 106.3 | 129.8 | 156.6 | 166.4 |

Source: Bloomberg as of 10 AM on Monday, April 17, 2006

***Credit Default Swaps*** **-** The credit default swap (CDS) market may be divided into three sectors: (i) corporate bonds and loans; (ii) bank credits; and (iii) emerging market sovereigns. CDS can reference a single reference obligation or credit (a single bond or single loan) or a basket/portfolio of credits. A CDS index may reference a standard or customized portfolio or basket of reference obligations agreed upon by the buyer and seller. The most frequently traded maturity for a CDS is five years though the range of CDS maturities may extend from one to 10 years. The CDS swap premium or cost of a credit default swap attempts to capture the economic value of the credit risk associated with corporate or sovereign debt.

What constitutes a credit event? Any possible circumstance that may lead to a diminished market value for a reference entity might be viewed as a credit event. Under the current, standard International Swaps & Derivatives Association (ISDA) credit default swap agreement, a default event may be defined as: (i) bankruptcy; (ii) failure to pay; (iii) debt restructuring; (iv) obligation default; (v) obligation acceleration; (vi) debt payment moratorium.

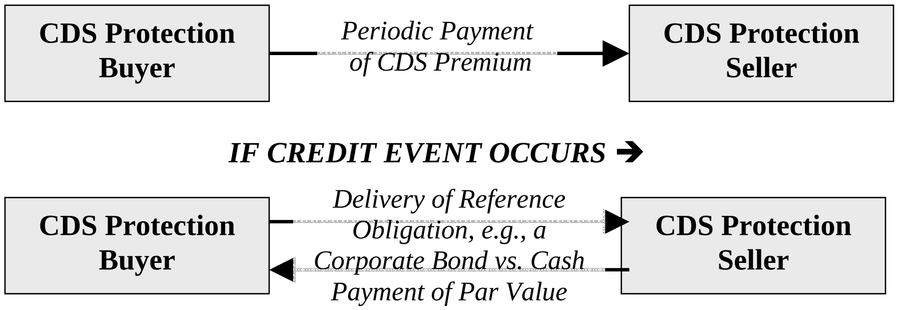
A *"Bankruptcy"* event implies that the reference entity for the CDS has become insolvent or lacks the financial capacity to meet its debt obligations. A *"Failure to Pay"* event implies that the reference entity for the CDS simply fails to make a scheduled interest or principal payment. A *"Debt Restructuring"* event is one where the seniority of a payment due to the holder of the reference obligation has been degraded. An *"Obligation Default or Acceleration"* event represents one where a debt covenant(s) for the reference entity has been violated, thereby making the debt obligation come due prior to the original maturity date. A *"Debt Payment Moratorium"* event arises when the reference entity refuses to make scheduled debt service payments.

When "restructuring" is included as a default event for a CDS, it has the potential to generate controversy. Some bank purchasers of CDS protection have also been purported to have outstanding loans to the reference entity for a CDS. These banks, on the buy side of CDS protection, may be in a position to approve or accept a debt restructuring by that obligor, which would then trigger a payment (to the protection buyer) under a CDS agreement.

There may further be situations where a debt restructuring has not resulted in financial harm to the debt holder. Protection sellers sometimes object to making payment to a protection buyer under this type of circumstance. Thus, there are pros and cons of including restructuring as a default event.

***CDS Structure*** - In a typical single name CDS the "Protection Buyer" agrees to make periodic payments over a designated period of time to the "Protection Seller." In exchange for this "swap" payment, or premium, the Protection Buyer establishes the right to sell a specific reference obligation (*e.g.,* a corporate bond) issued by a reference entity (*e.g.,* a corporation) to the Protection Seller at the par value, if a credit event occurs.

## Plain Vanilla Credit Default Swap (CDS)



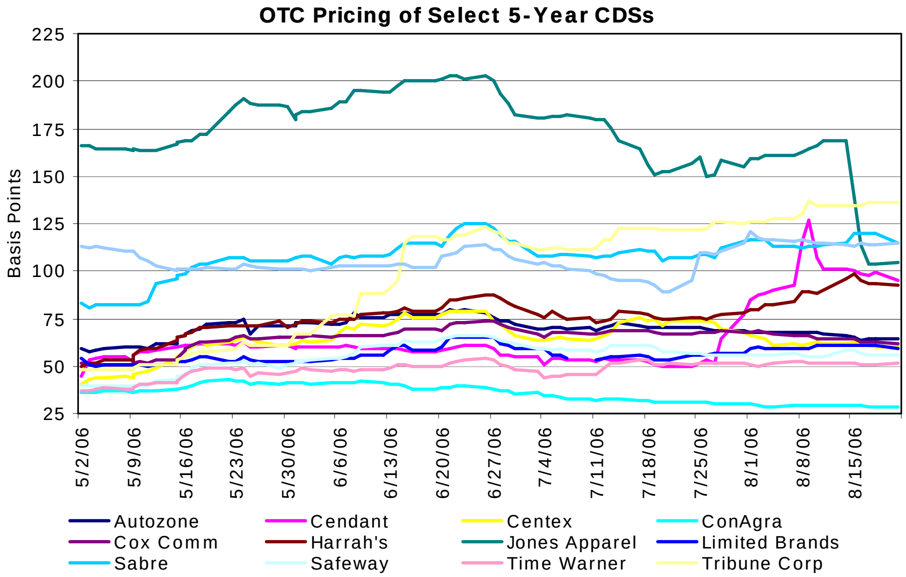

In effect the Protection Buyer is reducing or hedging the credit risk component of the reference bond by transferring the credit risk to the Protection Seller. The Protection Buyer's asset remains subject to non-credit related elements of market risk. At the time a CDS is created, neither the protection buyer nor the protection seller has a comparative advantage. The present value of the payments made by the protection buyer is approximately equal to the expected value of the payment to be received from the protection seller.

***CDS Pricing*** - Two factors are key to pricing of a credit default swap: (i) the *probability* that the reference entity will default; and (ii) the *recovery rate, i.e.,* the amount the protection seller expects to recover in the event a default occurs.

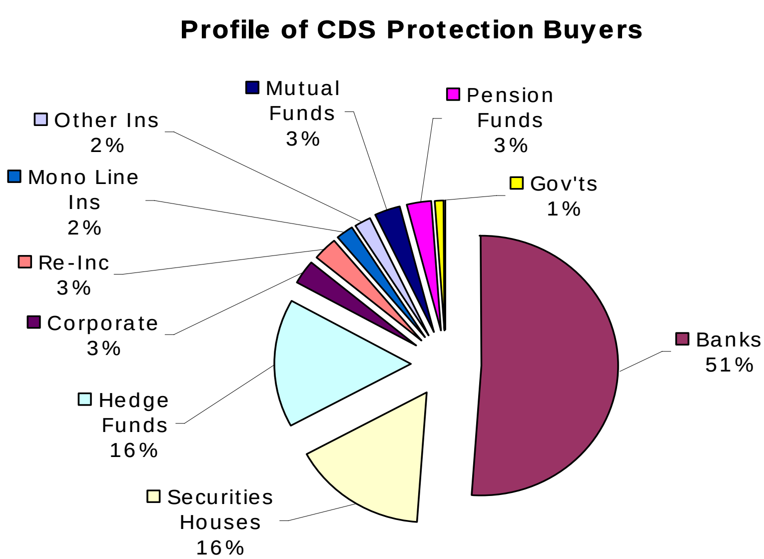
Changes in expected default probability and/or the recovery rate will have an impact on CDS valuation. The larger the anticipated probability of default, the larger the credit default swap premium will be. If the market perceives that a reference entity's financial condition is improving, the CDS swap premium will tighten, *i.e.,* the CDS swap price will cheapen. If the price for CDS protection on a specific name is widening significantly, this is generally an indication that perceived credit quality is rapidly deteriorating.

The CDS market often responds more quickly than the cash market to changes in credit perception. Hence prices in the CDS market may serve as an important leading indicator that credit spreads on a particular bond issue are likely to change.

Taking on the role of a protection seller via a CDS is akin to taking a long position in a corporate bond with the interest rate risk fully hedged. Another way of viewing this risk is that it is equivalent to purchasing a corporate bond with funds obtained by shorting an equivalent duration Treasury note. Any change in the value of this (long corporate/short Treasury) bond position would be attributable to a change in the reference entity's credit spread, *i.e.* attributable to a change in the perceived credit quality of the corporate bond issuer. Buying CDS protection may be viewed as taking a short position on corporate credit, which in the corporate bond cash market is generally not practicable.

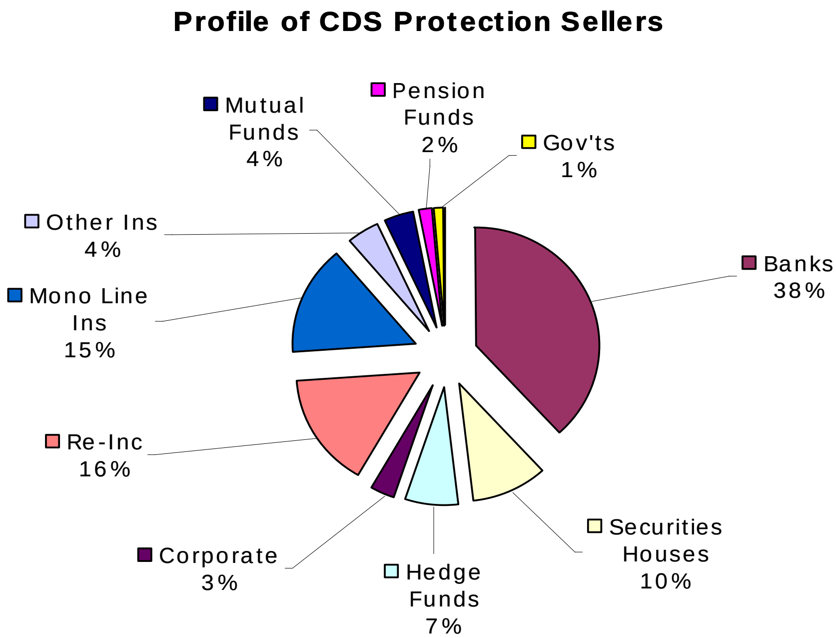



***Credit Market Participants*** - Who are the major participants in the credit default swap market? Surveys reveal that commercial banks, *i.e.*, holders of large corporate loan exposure, are the largest participants in this market. Commercial banks are more active as CDS protection buyers, but they also hold very significant positions as protection sellers. Banks often attempt to minimize a portion of their credit risk in order to preserve capital.




Source: BBA Credit Derivatives Report 2003/2004

Insurance companies, both re-insurers and other insurers, represent a growing percentage of CDS users, especially on the protection sell side. Insurance companies more often serve as CDS protection sellers because their traditional area of expertise is in analyzing and accepting risk. Hedge funds also have taken a very active role in this segment of the OTC derivatives market. Hedge funds are about twice as active on the credit protection buy side *vis-à-vis* the protection sell side.




Source: BBA Credit Derivatives Report 2003/2004

# 4. Contract Specifications for CME Credit Event Futures

## CHAPTER 455: CME Credit Event Futures

### 45500. SCOPE OF CHAPTER

This chapter is limited in application to trading in CME Credit Event Futures. The procedures for trading, clearing, settlement, and any other matters not specifically covered herein shall be governed by the rules of the Exchange.

### 45501. COMMODITY SPECIFICATIONS

CME Credit Event Futures shall be based upon specified Reference Entities as determined by the Board of Directors. The Board of Directors may determine to list multiple contracts based on a particular Reference Entity with varying terms and conditions. The following Reference Entities, and their Successor Reference Entities, have been approved by the Board of Directors as subjects of CME Credit Event Futures. Successor(s) to a Reference Entity shall be determined by the Board of Directors in accordance with Rule 45504.

| Reference Entity | Notional Value (NV) | Minimum Increment | Final Settle-ment Rate (F) | Position Limit |
|---|---|---|---|---|
| Cendant Corp. | $100,000 (USD) | 0.5 basis points ($5.00) | 50% | 5,000 contracts |
| Jones Apparel Group, Inc. | $100,000 (USD) | 0.5 basis points ($5.00) | 50% | 5,000 contracts |
| Tribune Corporation | $100,000 (USD) | 0.5 basis points ($5.00) | 50% | 5,000 contracts |
| | | | | |

### 45502. FUTURES CALL

#### 45502.A. Schedule

Futures contracts shall be scheduled for trading during such hours and delivery in such months as may be determined by the Board of Directors.

#### 45502.B. Trading Unit

CME Credit Basket Event Futures shall be based on a Notional Value and denominated in such currency as determined by the Board of Directors as depicted in Rule 45501.

#### 45502.C. Minimum Increments

CME Credit Basket Event Futures shall be traded with a minimum price increment as determined by the Board of Directors as depicted in Rule 45501. Bids and offers shall be quoted in terms of basis points of Notional Value. *E.g.,* If the minimum price increment of a contract with a Notional Value of $100,000 is established at 0.5 basis points per Rule 45501, then the minimum price increment equates to $5.00 (=0.005% x $100,000). A quotation of 405.5 basis points based on a contract with a Notional Value of $100,000 equates to $4,055.00.

### 45502.D. Position Limits

A person shall not own or control more than a specified number of contracts net long or short positions in any single contract as determined by the Board of Directors as depicted in Rule 45501.

### 45502.E. Accumulation of Positions

For the purposes of this rule, the positions of all accounts directly or indirectly owned or controlled by a person or persons, and the positions of all accounts of a person or persons acting pursuant to an expressed or implied agreement or understanding, and the positions of all accounts in which a person or persons have a proprietary or beneficial interest, shall be cumulated.

### 45502.F. Exemptions

The foregoing position limits shall not apply to (1) bona fide hedge positions meeting the requirements of Regulation 1.3(z)(1) of the CFTC and the rules of the Exchange, and (2) other positions exempted pursuant to Rule 543.

### 45502.G. Final Settlement Date

Futures trading shall terminate at 12:00 p.m. (Chicago Time) on the Final Settlement Date. The Final Settlement Date shall be the second London bank business day immediately preceding the third Wednesday of the contract expiration month.

If a Credit Event is Declared ("Declaration of Credit Event") per Rule 45503.A., on or prior to the Final Settlement Date, the CME Credit Event Futures contract in question shall be subject to Early Settlement. Trading shall terminate at the regularly scheduled termination of trading on the Early Settlement Date; or, at 12:00 noon (C.S.T.) if the Declaration of Credit Event and Early Settlement Date coincides with the regularly scheduled Final Settlement Date.

### 45502.H. Contract Modifications

Specifications shall be fixed as of the first day of trading of a contract. If any U.S. governmental agency or body issues an order, ruling, directive or law that conflicts with the requirements of these rules, such order, ruling, directive or law shall be construed to take precedence and become part of these rules, and all open and new contracts shall be subject to such government orders.

### 45503. CASH SETTLEMENT

Delivery of CME Credit Event futures shall be by cash settlement.

### 45503.A. Final Settlement Procedures

In absence of a Declaration of Credit Event, on or prior to the Final Settlement Date, the Final Settlement Price, on the Final Settlement Date, shall be 0.0 basis points and the Final Settlement Value shall be 0.00.

If, on or prior to 11:59 a.m. (C.S.T.) on the Final Settlement Date, the Exchange is in receipt of a Credit Event Notice per Rule 45503.C., the Exchange shall confirm whether such Credit Event has or has not occurred. A Credit Event Notice means a notice from an Exchange Clearing Member carrying position(s) in the CME Credit Event Futures contract in question, to the Exchange, in a form prescribed by the Exchange that describes a Credit Event that occurred prior to 11:59 a.m. (C.S.T.) on the Final Settlement Date. Such confirmation shall be by reference to at least two (2) Public Sources of Information, as defined in the INTERPRETATIONS TO CHAPTER 455. If such Credit Event is confirmed, the Exchange shall issue a Declaration of Credit Event. Final Settlement may be postponed pending Exchange confirmation of a Credit Event.

If a Credit Event is declared ("Declaration of Credit Event"), the CME Credit Event Futures contract in question shall be subject to Early Settlement. Trading shall terminate at the regularly scheduled termination of trading on the Early Settlement Date; or, at 12:00 noon (C.S.T.) if the Declaration of Credit Event coincides with the regularly schedule Final Settlement Date.

The Final Settlement Price on the Early Settlement Date shall be equal to the Final Settlement Rate (F) of the contract per Rule 45501. *E.g.,* if F is established at 45% per Rule 45502.I., the Final Settlement Price shall be 0.45 or 4,500 basis points; this equates to a Final Settlement Value of $45,000 for a contract with a Notional Value (NV) of $100,000 (= 45% of $100,000).

**45503.B. Credit Events**

Credit Event means, with respect to CME Credit Event Futures, one or more of Bankruptcy; Failure to Pay; Obligation Acceleration; Obligation Default; Repudiation/Moratorium; or, Restructuring; in accordance with the INTERPRETATIONS TO CHAPTER 455.

**45503.C. Final Mark-to-Market**

Following the determination of the Final Settlement Price, clearing members holding open positions in CME Credit Event futures at the time of termination of trading in that contract shall make payment to or receive payment from the Clearing House in accordance with normal variation margin procedures based on a settlement price equal to the Final Settlement Price.

**45504. ADJUSTMENTS TO CME CREDIT EVENT FUTURES**

Determinations as to whether and how to adjust the terms of CME Credit Event Futures to reflect events affecting Reference Entities and their Successor(s) shall be made by the Board of Directors based on its judgment as to what is appropriate for the protection of investors and the public interest, taking into account such factors as fairness to the buyers and sellers of CME Credit Event Futures on the underlying interest, the maintenance of a fair and orderly market, efficiency of settlement, and consistency of interpretation and practice in accordance with the INTERPRETATIONS TO CHAPTER 455.

Adjustments to CME Credit Event Futures may include, but are not limited to, assigning a single or multiple CME Credit Event Futures contracts based upon Successor Reference Entities in satisfaction of retiring CME Credit Event Futures; attachment of a cash payment from longs to shorts or shorts to longs as appropriate; early cash settlement of retiring CME Credit Event Futures at a fair and reasonable price; or such other provisions or combinations of provisions as deemed appropriate by the Board of Directors.

Every determination by the Board of Directors in respect of CME Credit Event Futures pursuant to this Rule shall be within the discretion of the Board of Directors and shall be conclusive and binding on all investors and not subject to review.

### 45505. FAILURE TO PERFORM

If the clearing member fails to perform all acts required by this chapter, then that clearing member shall be deemed as failing to perform which may be punishable as a major violation. The Board may also assess such penalties as it deems appropriate.

### 45506. ACTS OF GOVERNMENT, ACTS OF GOD AND OTHER EMERGENCIES

(Refer to Rule 701. – ACTS OF GOVERNMENT, ACTS OF GOD AND OTHER EMERGENCIES)

## INTERPRETATIONS TO CHAPTER 455 [1]

### I. Credit Events

Credit Event means, with respect to CME Credit Event Futures, one or more of Bankruptcy, Failure to Pay, Obligation Acceleration, Obligation Default, Repudiation/Moratorium or Restructuring. If an occurrence would otherwise constitute a Credit Event, such occurrence will constitute a Credit Event whether or not such occurrence arises directly or indirectly from, or is subject to a defense based upon: (a) any lack or alleged lack of authority or capacity of a Reference Entity to enter into any Obligation or, as applicable, an Underlying Obligor to enter into any Underlying Obligation, (b) any actual or alleged unenforceability, illegality, impossibility or invalidity with respect to any Obligation or, as applicable, any Underlying Obligation, however described, (c) any applicable law, order, regulation, decree or notice, however described, or the promulgation of, or any change in, the interpretation by any court, tribunal, regulatory authority or similar administrative or judicial body with competent or apparent jurisdiction of any applicable law, order, regulation, decree or notice, however described, or (d) the imposition of, or any change in, any exchange controls, capital restrictions or any other similar restrictions imposed by any monetary or other authority, however described.

(a) "Bankruptcy" means a Reference Entity (1) is dissolved (other than pursuant to a consolidation, amalgamation or merger); (2) becomes insolvent or is unable to pay its debts or fails or admits in writing in a judicial, regulatory or administrative proceeding or filing its inability generally to pay its debts as they become due; (3) makes a general assignment, arrangement or composition with or for the benefit of its creditors; (4) institutes or has instituted against it a proceeding seeking a judgment of insolvency or bankruptcy or any other relief under any bankruptcy or insolvency law or other similar law affecting creditors' rights, or a petition is presented for its winding-up or liquidation, and, in the case of any such proceeding or petition instituted or presented against it, such proceeding or petition (i) results in a judgment of insolvency or bankruptcy or the entry of an order for relief or the making of an order for its winding-up or liquidation or (ii) is not dismissed, discharged, stayed or restrained in each case within thirty calendar days of the institution or presentation thereof; (5) has a resolution passed for its winding-up, official management or liquidation (other than pursuant to a consolidation, amalgamation or merger); (6) seeks or becomes subject to the appointment of an administrator, provisional liquidator, conservator, receiver, trustee, custodian or other similar official for it or for all or substantially all its assets; (7) has a secured party take possession of all or substantially all its assets or has a distress, execution, attachment, sequestration or other legal process levied, enforced or sued on or against all or substantially all its assets and such secured party maintains possession, or any such process is not dismissed, discharged, stayed or restrained, in each case within thirty calendar days thereafter; or (8) causes or is subject to any event with respect to it which, under the applicable laws of any jurisdiction, has an analogous effect to any of the events specified in clauses (1) to (8) (inclusive).

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[1] The INTERPRETATIONS TO CHAPTER 455 have been adapted with the permission of International Swaps & Derivatives Association, Inc. (ISDA) from the copyrighted © 2003 "ISDA Credit Derivatives Definitions." Specifically, Sections I, II and III are adapted from Article IV of the 2003 ISDA Credit Derivatives Definitions. Section IV is adapted from Article III, Section 3.5. Section V is adapted from Article II, Section 2.25. Section VI is adapted from Article III, Section 3.6. Section VII is adapted from Article III, Section 3.7. Section VIII is adapted from Article III, Section 3.8. Section IX is adapted from Article II, Section 2.1. Section X is adapted from Article II, Section 2.2.

(b) "Obligation Acceleration" means one or more Obligations in an aggregate amount of not less than the Default Requirement have become due and payable before they would otherwise have been due and payable as a result of, or on the basis of, the occurrence of a default, event of default or other similar condition or event (however described), other than a failure to make any required payment, in respect of a Reference Entity under one or more Obligations.

(c) "Obligation Default" means one or more Obligations in an aggregate amount of not less than the Default Requirement have become capable of being declared due and payable before they would otherwise have been due and payable as a result of, or on the basis of, the occurrence of a default, event of default or other similar condition or event (however described), other than a failure to make any required payment, in respect of a Reference Entity under one or more Obligations.

(d) "Failure to Pay" means, after the expiration of any applicable Grace Period (after the satisfaction of any conditions precedent to the commencement of such Grace Period), the failure by a Reference Entity to make, when and where due, any payments in an aggregate amount of not less than the Payment Requirement under one or more Obligations, in accordance with the terms of such Obligations at the time of such failure.

(e) "Repudiation/Moratorium" means

(1) the occurrence of both of the following events: (i) an authorized officer of a Reference Entity or a Governmental Authority (x) disaffirms, disclaims, repudiates or rejects, in whole or in part, or challenges the validity of, one or more Obligations in an aggregate amount of not less than the Default Requirement or (y) declares or imposes a moratorium, standstill, roll-over or deferral, whether de facto or de jure, with respect to one or more Obligations in an aggregate amount of not less than the Default Requirement and (ii) a Failure to Pay, determined without regard to the Payment Requirement, or a Restructuring, determined without regard to the Default Requirement, with respect to any such Obligation occurs on or prior to the Repudiation/Moratorium Evaluation Date.

(2) Repudiation/Moratorium Evaluation Date. "Repudiation/Moratorium Evaluation Date" means, if a Potential Repudiation/Moratorium occurs on or prior to the Scheduled Termination Date, (i) if the Obligations to which such Potential Repudiation/Moratorium relates include Bonds, the date that is the later of (A) the date that is 60 days after the date of such Potential Repudiation/Moratorium and (B) the first payment date under any such Bond after the date of such Potential Repudiation/Moratorium (or, if later, the expiration date of any applicable Grace Period in respect of such payment date) and (ii) if the Obligations to which such Potential Repudiation/Moratorium relates do not include Bonds, the date that is 60 days after the date of such Potential Repudiation/Moratorium. If (i) the Repudiation/Moratorium Extension Condition is satisfied and (ii) an Event Determination Date in respect of that Repudiation/Moratorium does not occur during the Notice Delivery Period, the Repudiation/Moratorium Evaluation Date will be the Termination Date (even if a Repudiation/Moratorium occurs after the Scheduled Termination Date).

(3) "Potential Repudiation/Moratorium" means the occurrence of an event described in clause (i) of the definition of Repudiation/Moratorium.

(4) The "Repudiation/Moratorium Extension Condition" is satisfied by the delivery of a Repudiation/Moratorium Extension Notice and, if specified as applicable in the related Confirmation, Notice of Publicly Available Information by the Notifying Party to the Exchange that is effective during the period described in clause (a) of the definition of Notice Delivery Period.

(5) "Repudiation/Moratorium Extension Notice" means an irrevocable notice (which may be by telephone) from the Notifying Party to the Exchange that describes a Potential Repudiation/Moratorium that occurred on or after the Effective Date and on or prior to the Scheduled Termination Date. A Repudiation/Moratorium Extension Notice must contain a description in reasonable detail of the facts relevant to the determination that a Potential Repudiation/Moratorium has occurred and indicate the date of the occurrence. The Potential Repudiation/Moratorium that is the subject of the Repudiation/Moratorium Extension Notice need not be continuing on the date the Repudiation/Moratorium Extension Notice is effective.

(f) "Restructuring" means

(1) That, with respect to one or more Obligations and in relation to an aggregate amount of not less than the Default Requirement, any one or more of the following events occurs in a form that binds all holders of such Obligation, is agreed between the Reference Entity or a Governmental Authority and a sufficient number of holders of such Obligation to bind all holders of the Obligation or is announced (or otherwise decreed) by a Reference Entity or a Governmental Authority in a form that binds all holders of such Obligation, and such event is not expressly provided for under the terms of such Obligation in effect as of the later of the Trade Date and the date as of which such Obligation is issued or incurred:

(i) A reduction in the rate or amount of interest payable or the amount of scheduled interest accruals;

(ii) A reduction in the amount of principal or premium payable at maturity or at scheduled redemption dates;

(iii) A postponement or other deferral of a date or dates for either (A) the payment or accrual of interest or (B) the payment of principal or premium;

(iv) A change in the ranking in priority of payment of any Obligation, causing the Subordination of such Obligation to any other Obligation; or

(v) Any change in the currency or composition of any payment of interest or principal to any currency which is not a Permitted Currency.

"Permitted Currency" means (x) the legal tender of any Group of 7 country (or any country that becomes a member of the Group of 7 if such Group of 7 expands its membership) or (y) the legal tender of any country which, as of the date of such change, is a member of the Organization for Economic Cooperation and Development and has a local currency long-term debt rating of either AAA or higher assigned to it by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. or any successor to the rating business thereof, Aaa or higher assigned to it by Moody's Investors Service, Inc. or any successor to the rating business thereof or AAA or higher assigned to it by Fitch Ratings or any successor to the rating business thereof.

(2) Notwithstanding the provisions of Section I(f)(1) of the INTERPRETATIONS TO CHAPTER 455 none of the following shall constitute a Restructuring:

(i) The payment in euros of interest or principal in relation to an Obligation denominated in a currency of a .Member State of the European Union that adopts or has adopted the single currency in accordance with the Treaty establishing the European Community, as amended by the Treaty on European Union;

(ii) The occurrence of, agreement to or announcement of any of the events described in Section I(f)(1) (i) to (v) of the INTERPRETATIONS TO CHAPTER 455 due to an administrative adjustment, accounting adjustment or tax adjustment or other technical adjustment occurring in the ordinary course of business; and

(iii) The occurrence of, agreement to or announcement of any of the events described in Section I(f)(1) (i) to (v) of the INTERPRETATIONS TO CHAPTER 455 in circumstances where such event does not directly or indirectly result from a deterioration in the creditworthiness or financial condition of the Reference Entity.

(3) For purposes of Section I(f)(1), I(f)(2), and III of the INTERPRETATIONS TO CHAPTER 455, the term Obligation shall be deemed to include Underlying Obligations for which the Reference Entity is acting as provider of a Qualifying Affiliate Guarantee or, if All Guarantees is specified as applicable in the related Confirmation, as provider of any Qualifying Guarantee. In the case of a Qualifying Guarantee and an Underlying Obligation, references to the Reference Entity in Section I(f)(1) of the INTERPRETATIONS TO CHAPTER 455 shall be deemed to refer to the Underlying Obligor and the reference to the Reference Entity in Section I(f)(2) of the INTERPRETATIONS TO CHAPTER 455**,** shall continue to refer to the Reference Entity.

## II. Certain Definitions Relating to Credit Events.

(a) "Default Requirement" means USD 10,000,000 or its equivalent in the relevant Obligation Currency, in either case as of the occurrence of the relevant Credit Event.

(b) Governmental Authority. "Governmental Authority" means any de facto or de jure government (or any agency, instrumentality, ministry or department thereof), court, tribunal, administrative or other governmental authority or any other entity (private or public) charged with the regulation of the financial markets (including the central bank) of a Reference Entity or of the jurisdiction of organization of a Reference Entity.

(c) Obligation Currency. "Obligation Currency" means the currency or currencies in which an Obligation is denominated.

(d) Payment Requirement. "Payment Requirement" means USD 1,000,000 or its equivalent in the relevant Obligation Currency, in either case as of the occurrence of the relevant Failure to Pay or Potential Failure to Pay, as applicable.

## III. Limitation on Obligations in Connection with Credit Events.

Notwithstanding anything to the contrary Section I(f)(1) of the INTERPRETATIONS TO CHAPTER 455 the occurrence of, agreement to or announcement of any of the events described in Section I(f)(1) (i) to (v) of the INTERPRETATIONS TO CHAPTER 455 shall not be a Restructuring unless the Obligation in respect of any such events is a Multiple Holder Obligation.

"Multiple Holder Obligation" means an Obligation that (i) at the time of the event which constitutes a Restructuring Credit Event is held by more than three holders that are not Affiliates of each other and (ii) with respect to which a percentage of holders (determined pursuant to the terms of the Obligation as in effect on the date of such event) at least equal to sixty-six-and two-thirds is required to consent to the event which constitutes a Restructuring Credit Event.

## IV. Publicly Available Information

Publicly Available Information" means:

(a) Information that reasonably confirms any of the facts relevant to the determination that the Credit Event or Potential Repudiation/Moratorium, as applicable, described in a Credit Event Notice or Repudiation/Moratorium Extension Notice has occurred and which (i) has been published in or on not less than the Specified Number of Public Sources, regardless of whether the reader or user thereof pays a fee to obtain such information ; provided that, if either of the parties or any of their respective Affiliates is cited as the sole source of such information, then such information shall not be deemed to be Publicly Available Information unless such party of its Affiliate is acting in its capacity as trustee, fiscal agent, administrative agent, clearing agent or paying agent for an Obligation, (ii) is information received from or published by (A) a Reference Entity that is not a party to the relevant CME Credit Event futures contract or (B) a trustee, fiscal agent, administrative agent, clearing agent or paying agent for an Obligation, (iii) is information contained in any petition or filing where a Reference Entity institutes or has instituted against it a proceeding seeking a judgment of insolvency or bankruptcy or any other relief under any bankruptcy or insolvency law or other similar law affecting creditors' rights, or a petition is presented for its winding-up or liquidation, and, in the case of any such proceeding or petition instituted or presented against it, such proceeding or petitions (i) results in a judgment of insolvency or bankruptcy or the entry of an order for relief or the making of an order for its winding-up or liquidation or (ii) is not dismissed, discharged, stayed or restrained in each case within thirty calendar days of the institution or presentation thereof or (iv) is information contained in any order, decree, notice of filing, however described, of or filed with a court, tribunal, exchange, regulatory authority or similar administrative, regulatory or judicial bond.

(b) In the event that with respect to the CME Credit Event futures contract in which the Buyer is (i) the sole source of information in its capacity as trustee, fiscal agent, administrative agent, clearing agent or paying agent for an Obligation and (ii) a holder of the Obligation with respect to which a Credit Event has occurred, the Buyer shall be required to deliver to the Exchange a certificate signed by a Managing Director (or other substantively equivalent title) of the Buyer, which shall certify the occurrence of a Credit Event with respect to a Reference Entity.

(c) In relation to any information of the type described in paragraph (a) of "Publicly Available Information", the Exchange may assume that such information has been disclosed to it without violating any law, agreement, or understanding regarding the confidentiality of such information and that the party delivering such information has not taken any action or entered into any agreement or understanding with the Reference Entity or any Affiliate of the Reference Entity that would be breached by, or would prevent, the disclosure of such information to third parties.

(d) Publicly Available Information need not state (i) in relation to Downstream Affiliate and Voting Shares, the percentage of Voting Shares owned, directly or indirectly, by the Reference Entity and (ii) that such occurrence (A) has met the Payment Requirement or Default Requirement, (B) is the result of exceeding any applicable Grace Period or (C) has met the subjective criteria specified in certain Credit Events.

## V. Downstream Affiliate and Voting Shares

(a) "Downstream Affiliate" means an entity, at the date of the event giving rise to the Credit Event which is the subject of a Credit Event Notice, the Delivery Date or the time of identification of a Substitute Reference Obligation (if applicable), whose outstanding Voting Shares are more than 50 percent owned, directly or indirectly, by the Reference Entity.

(b) "Voting Shares" shall mean those shares or other interests that have the power to elect the board of directors or similar governing body of an entity.

## VI. Notice of Publicly Available Information

"Notice of Publicly Available Information" means an irrevocable notice for the party delivering the relevant Credit Event Notice or Repudiation/Moratorium Extension Notice to the Exchange that cites Publicly Available Information confirming the occurrence of the Credit Event or Potential Repudiation/Moratorium as applicable, described in the Credit Event Notice or Repudiation/Moratorium Extension Notice. In relation to a Repudiation/Moratorium Credit Event, the Notice of Publicly Available Information must cite Publicly Available Information confirming the occurrence of both clauses (i) and (ii) of the definition of Repudiation/Moratorium. The notice given must contain a copy, or a description in reasonable detail, or the relevant Publicly Available Information. A Notice of Publicly Available Information shall be subject to the requirement regarding notices set forth by the Exchange. If Notice of Publicly Available Information is applicable to a CME Credit Event futures contract and a Credit Event Notice or Repudiation/Moratorium Extension Notice, as applicable, contains Publicly Available Information, such Credit Event Notice or Repudiation/Moratorium Extension Notice will also be deemed to be a Notice of Publicly Available Information. Appendix A to "Interpretations & Special Notices Relating to Chapter 455" sets forth a form including the Notice of Publicly Available Information.

**VII. Public Source**

"Public Source" means a source of Publicly Available Information such as Bloomberg Service, Dow Jones Telerate Service, Reuters Monitor Rates Services, Dow Jones News Wire, Wall Street Journal, New York Times, Nihon Keizai Shinbun, Asahi Shinbun, Yomiuri Shinbun, Financial Times, La Tribune, Les Echos and The Australian financial Review (and successor publications), the main source(s) of business news in the country in which the Reference Entity is organized and any other internationally recognized published or electronically displayed news sources.

**VIII. Specified Number**

"Specified Number" means at least two Public Sources of Publicly Available information are available.

**IX. Reference Entity**

Reference Entity means the entity or entities specified as such in the related futures contract. Any Successor to a Reference Entity identified pursuant to the Section "Provisions for Determining a Successor" shall be the Reference Entity for the CME Credit Event futures contract as determined pursuant to the following section "Provisions for Determining a Successor".

**X. Provisions for Determining a Successor**

(a) "Successor" means in relation to a Reference Entity that is not a Sovereign, the entity or entities, if any, determined as set forth below:

(i) If one entity directly or indirectly succeeds to seventy-five per cent or more of the Relevant Obligations of the Reference entity by way of a Succession Event, that entity will be the sole Successor for the entire CME Credit Event futures contract.

(ii) If only one entity directly or indirectly succeeds to more than twenty-five per cent (but less than seventy-five per cent) of the Relevant Obligation of the Reference Entity by way of a Succession Event and not more than twenty-five per cent of the Relevant Obligations of the Reference Entity remain with the Reference Entity, the entity that succeeds to more than twenty-five per cent of the Relevant Obligations will be the sole Successor for the entire CME Credit Event futures

(iii) If more than one entity each directly or indirectly succeeds to more than twenty-five per cent of the Relevant Obligations of the Reference Entity by way of a Succession Event, and not more than twenty-five per cent of the Relevant Obligations of the Reference entity remain with the Reference Entity, each such entity and the Reference Entity will each be a Successor for a New CME Credit Event futures contract determined in accordance with section (e)

(iv) If one or more entities each directly or indirectly succeeds to more than twenty-five per cent of the Relevant Obligations of the Reference Entity by way of a Succession Event, and more than twenty-five per cent of the Relevant Obligations of the Reference Entity remain with the Reference Entity, each such entity and the Reference Entity will each be a Successor for a New CME Credit Event futures contract determined in accordance with Section (e).

(v) If one or more entities directly or indirectly succeed to a portion of the Relevant Obligations of the Reference entity by way of a Succession Event, but no entity succeeds to more than twenty-five per cent of the Relevant Obligations of the Reference Entity and the Reference Entity continues to exist, there will be no Successor and the Reference Entity and the CME Credit Event futures contract will not be changed in any way as a result of the Succession Event; and

(vi) If one or more entities directly or indirectly succeed to a portion of the Relevant Obligations of the Reference Entity by way of a Succession Event, but no entity succeeds to more than twenty-five per cent of the Relevant Obligations of the Reference Entity and the Reference Entity ceased to exist, the entity which succeeds to the greatest percentage of Relevant Obligations (or, if two or more entities succeed to an equal percentage of Relevant Obligations, the entity from among those entities which succeeds to the greatest percentage of obligations of the Reference Entity) will be the sole Successor.

The Board of Directors will be responsible for determining, as soon as reasonably practicable after it becomes aware of the relevant Succession Event (but no earlier than fourteen calendar days after the legally effective date of the Succession Event), and with effect from the legally effective date of the Succession Event, whether the relevant thresholds set forth above have been met, or which entity qualifies under Section (a)(vi), as applicable. In calculating the percentages used to determine whether the relevant thresholds set forth above have been met, or which entity qualifies under Section (a)(vi), as applicable, the Board of Directors shall use, in respect of each applicable Relevant Obligation listed in such calculation, the amount of the liability in respect of such Relevant Obligation listed in the Best Available Information and shall notify the Exchange of such calculation.

(b) “Succession Event” means an event such as a merger, consolidation, amalgamation, transfer of assets or liabilities, demerger, spin-off or other similar event in which one entity succeeds to the obligations of another entity, whether by operation of law or pursuant to any agreement. Notwithstanding the foregoing, “Succession Event” shall not include an event in which the holders of obligation of the Reference Entity exchange such obligations for the obligations of another entity, unless such exchange occurs in connections with a merger, consolidation, amalgamation, transfer of assets or liabilities, demerger, spin-off or other similar event.

(c) For purposes of the section “Provisions for Determining a Successor”, “succeed” means, with respect to a Reference Entity and its Relevant Obligations (or, as applicable, obligations), that a party other than such Reference Entity (i) assumes or becomes liable for such Relevant Obligations (or, as applicable, obligations) whether by operation of law or pursuant to any agreement or (ii) issues Bonds that are exchanged for Relevant Obligations (or, as applicable, obligations), and in either case such Reference Entity is no longer an obligor (primarily or secondarily) or guarantor with respect to such Relevant Obligations (or, as applicable, obligations). The determinations required pursuant to Section (a) shall be made in the case of an exchange offer, on the basis of the outstanding principal balance of Relevant Obligations tendered and accepted in the exchange and not on the basis of the outstanding principal balance of Bonds for which Relevant Obligations have been exchanged.

(d) Where pursuant to Section (a)(iii) or (iv), more than one Successor has been identified, the relevant CME Credit Event Futures contract will be divided into the same number of new CME Credit Event Futures contracts (the "New CME Credit Event Futures contracts") as there are Successors with the following terms:

(i) Each Successor will be the Reference Entity for the purposes of one of the CME Credit Event Futures contracts;

(ii) In respect of each New CME Credit Event Futures contract, the "final settlement price" will be the final settlement price of the original CME Credit Event Futures contract divided by the number of successors.

(iii) All other terms and conditions of the original CME Credit Event Futures contract will be replicated in each New CME Credit Event futures contract except to the extent that modification is required, as determined by the Board of Directors to preserve the economic effects of the original CME Credit Event futures contract in the New CME Credit Event futures contracts (considered in the aggregate).

(e) "Relevant Obligations" means the Obligations constituting Bonds and Loans of the Reference Entity outstanding immediately prior to the effective date of the Succession Event, excluding any debt obligations outstanding between the Reference Entity and any of its Affiliates as determined by the Board of Directors. The Board of Directors will determine the entity which succeeds to such Relevant Obligations on the basis of the Best Available Information. If the date on which the Best Available Information becomes available or is filed precedes the legally effective date of the relevant Succession Event, any assumptions as to the allocation of obligations between or among entities contained in the Best Available Information will be deemed to have been fulfilled as of the legally effective date of the Succession Event, whether or not this is in fact the case.

(f) "Best Available Information" means:

(i) In the case of a Reference Entity which files information with its primary securities regulator or primary stock exchange that includes unconsolidated pro forma financial information which assumes that the relevant Succession Event has occurred or which provides such information to its shareholders, creditors or other persons whose approval of the Succession Event is required, that unconsolidated, pro forma financial information and if provided subsequently to the provision of unconsolidated, pro forma financial information but before the Board of Directors makes its determination for the purposes of the Section, other relevant information that is contained in any written communication provided by the Reference Entity to its primary securities regulator, primary stock exchange, shareholders, creditors or other persons whose approval of the Succession Event is required; or

(ii) In the case of a Reference Entity which does not file with its primary securities regulators or primary stock exchange, and which does not provide to shareholders, creditors or other persons whose approval of the Succession Event is required, the information contemplated in (i) above, the best publicly available information at the disposal of the Board of Directors to allow it to make a determination for the purposes of this section.

Information which is made available more than fourteen calendar days after the legally effective date of the Succession Event shall not constitute Best Available Information.

(g) In relation to a Sovereign Reference Entity, “Successor” means any direct or indirect successor(s) to that Reference entity irrespective of whether such successor(s) assumes any of the obligations of such Reference Entity.