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O.M.O.

March 11, 2005

Richard Shilts
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581

Re: Follow up Questions Regarding CME's Interpretation of Rule 432.D

Dear Mr. Shilts:

Your letter to CME states: "The antitrust arguments put forward by LIFFE imply that CME's Interpretation may have caused a significant entry barrier in a relevant antitrust market. These questions are designed to help determine what the relevant market is, and whether or not the rule creates a significant barrier to entry." The arguments made by LIFFE, however, are not sufficient to "imply a significant entry barrier in a relevant antitrust market." Moreover, unless a barrier to entry is the result of an unreasonable restraint of trade, it is not a matter of concern for any government agency.

CME's rule interpretation is simple and straight forward. CME's interpretation clarifies that its rule prohibiting wash trades prohibits both intra-market and inter-market wash trades. The Commodity Exchange Act ("CEA") is unequivocal: CME is obligated to adopt rules that permit it to enforce the CEA's prohibition against wash trading. CEA Section 5(d)(18) (Core Principle 18—Antitrust Considerations) provides that "**Unless necessary or appropriate to achieve the purposes of the Act** (emphasis added), the board of trade shall endeavor to avoid-(A) adopting any rules or taking any actions **that result in any unreasonable restraints of trade** (emphasis added). . . ."

I. Is the prohibition necessary and appropriate to achieve the purposes of the Act?

We believe our prohibition of illegal wash trades is necessary and appropriate to achieve the purposes of the Act. A wash trade, whether it is completed on a single exchange or across multiple exchanges is prohibited because it constitutes a sham transaction which distorts the information provided to market participants. Neither

Liffe nor the CFTC has argued that the means chosen by CME to bar inter-market wash trading is inappropriate. Unless the Commission has made findings (1) that inter-market wash trading is permissible under the Act and (2) that CME is barred from regulating such conduct in the absence of a prohibition in the Act, this inquiry should be ended. To the best of my knowledge, neither the Commission nor the staff has made a finding that inter-market wash trading is permissible. Consequently, there is no basis for your inquiry.

LIFFE ignores the introductory clause of Core Principle 18 "Unless necessary or appropriate to achieve the purposes of the Act" as well as the stated purpose of CME's Interpretation and asserts that the Interpretation operates as a prohibited restraint on competition. We believe that Liffe should first demonstrate that CME's actions are not necessary or appropriate to achieve the purposes of the Act.

II. Does the prohibition constitute an unreasonable restraint of trade?

Even if LIFFE is able to satisfy the burden of showing that CME's Interpretation is **not** necessary or appropriate to achieve the purposes of the Act, CME's action does not constitute an "unreasonable restraint of trade." Furthermore, LIFFE has provided no evidence that there has been an unreasonable restraint of trade.

Nothing in CME's Interpretation precludes any person from trading Eurodollars at LIFFE or clearing those trades at the London Clearing House. No CME rule stops CME customers from closing open positions and reestablishing them at LIFFE. LIFFE asserts that CME's Interpretation should be regarded as a refusal to permit transfer of CME's book of business to another clearing house because it requires customers to take some market risk and incur some costs to liquidate and reestablish the positions. LIFFE seems to contend that this constitutes an impermissible barrier to entry. LIFFE has cited no principle of antitrust law that requires a successful business to make it easier to transfer its open book of business to a third party (LCH) to assist a competitor (LIFFE). Failure to give up business is not a violation of the antitrust laws. The standard in the antitrust laws and the CEA is "unreasonable restraint of trade" not "refusal to assist a competitor."

An easy thought experiment may help with this analysis. First, assume that CME's rule had not been adopted in support of the CEA's prohibition against wash trades, but instead had taken the form of a naked refusal to enter into a mutual offset system with the London Clearing House or a refusal to make its contracts fungible with the contracts traded on LIFFE. It is clear that the CEA drew very narrow limits around the obligations of a DCM or DCO to enter into arrangements with other clearing houses and that there is no obligation. Congress effectively determined that such offset arrangements are not mandatory.

Second, even if the CEA offered no insight into the circumstances when clearing houses might be required to enter into cooperation or offset agreements, LIFFE has offered no evidence or argument, direct or by implication, that CME's Interpretation created any unreasonable restraint in any market, let alone a relevant antitrust market. The only cost that CME has imposed on any customer is the cost of obeying the law. Customers with positions at CME are free to execute two independent, non contingent block trades and effectively transfer those positions to LCH. LIFFE has offered no showing or cogent argument that its inability to pay customers to engage in wash trades has in any way impaired its ability to compete. It has offered no information as to the number of contracts that are likely to be transferred in the absence of the prohibition on wash trading and has offered no information or evidence as to how such presumed transfers would affect its competitive posture. LIFFE currently has an open interest of almost 200,000 Eurodollar contracts, it has made no showing that its inability to encourage wash trading has hurt its prospect of success.

The focus of your inquiry and LIFFE's arguments on a barrier to entry is misplaced. A "barrier to entry," although it makes it more difficult to enter a market, does not constitute an "unreasonable restraint of traded" and is not an antitrust violation. CME Globex is the market-leading electronic trading platform because of its breadth of products, range of functionality, global distribution, 23.5 trading hour day, reliability and capacity. Those superior features create a barrier to entry: but that barrier, no matter how high, is not an antitrust violation. I can't use my United miles on Jet Blue: this impedes Jet Blue's market entry. It does not violate the antitrust laws.

III. Questions Posed by the CFTC.

We believe that the questions you asked us to answer are premature and raise a number of serious concerns. With respect to the "switching" questions (4, 7, 8, & 9), securing the necessary data to provide an accurate response would be an enormously costly, time-consuming process. We believe it would be misleading to respond to this inquiry based on conjecture or hypothesis. We hope that you will reject any responses from others that are not clearly grounded in sound research and analysis. We previously provided substantial anecdotal evidence of massive switching between exchange markets and the OTC markets. Recent congressional testimony suggested a reversal of this business flow. We could also supply you with healthy conjecture respecting switching between Eurodollars futures and various government security futures. We are not prepared to hire the economists and conduct the research necessary to answer these questions, however, until it becomes relevant.

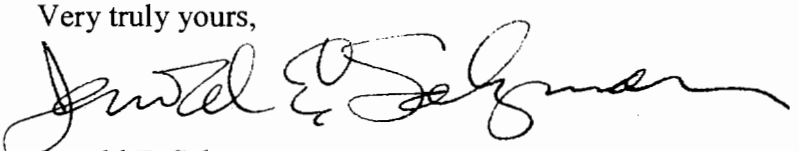
In order to accurately report on changes in user costs (question 5) over the last five years, we would need to chart, in addition to CME's transaction and clearing fees, changes in the bid/offer spread for each of 40 separate Eurodollar contracts and all the

combinations; execution, clearing and brokering fees; trader costs; error costs; communication costs, front end costs, back office costs, etc. This may not be possible to do, and even if it were possible, could not be completed prior to March 15, 2005.

Question 1's focus on floor trading is misplaced when approximately 75% of CME Eurodollar futures are traded electronically. Moreover, the wash trades that Liffe is sponsoring involve prearranged block trades, not open outcry floor trading. We do not understand Question 2. CME has not increased prices nor has it imposed a cost on moving open positions. It has confirmed its prohibition on a form of illegal conduct. Question 3 also assumes that CME has imposed a cost on moving open positions between CME and LCH. It has not. Nor do we understand your reference to "LIFFE's potentially lower costs . . ." Finally, with respect to Question 6, CME is constantly innovating with respect to its business model, product offering and technology. It is not possible to isolate improvements and enhancements made in response to the particular "competitive threat from LIFFE." CME constantly responds to competition from other futures exchanges, the OTC market.

I believe the next step should be to determine whether CME's Interpretation meets the "necessary or appropriate" test. If there is any question on that issue, we would be happy to provide you with the information necessary to satisfy your inquiry.

Very truly yours,



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JES:raf

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