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OFFICE OF THE SECRETARIAT  
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May 21, 2010

Mr. David Stawick  
Office of the Secretariat  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, NW  
Washington DC 20581

**RE: Section 5c(c)(1) and Regulation Section 40.6. Certification of Amendments to October 2011 and Subsequent Live Cattle Futures Contract Months.  
CME Submission No. 10-130.**

Dear Mr. Stawick:

Chicago Mercantile Exchange Inc. ("CME" or "Exchange") has approved amendments to the following Live Cattle futures rules:

- Rule 704. APPROVED STOCKYARDS AND SLAUGHTER PLANTS FOR LIVE CATTLE
- Rule 10103.B.4.a. Par Delivery Unit
- Rule 10103.B.4.b. Weight Deviations
- Rule 10103.C.1. Conditions
- Rule 10103.C.5.h. Delivery Points and Allowances
- Rule 10104.A. Tendering a Certificate.

These amendments will be effective with the October 2011 contract month, which will be listed for trading at the start of business on Tuesday, June 1, 2010. The Exchange had temporarily postponed the listing of the October 2011 contract month pending consideration of these rule amendments, as described in CME Submission No. 10-104 dated April 19, 2010. Upon the listing of the October 2011 contract month, the normal listing schedule will resume.

The amendments are presented below, with additions underlined and deletions bracketed and overstruck.

## **Chapter 7 Delivery Facilities and Delivery Procedures**

### **704. APPROVED STOCKYARDS AND SLAUGHTER PLANTS FOR LIVE CATTLE**

Deliveries on Exchange contracts of live beef cattle can be made only at public livestock yards and slaughter plants designated and approved for delivery by the Exchange.

A public livestock yard shall not be eligible for deliveries as an approved stockyard unless it is a stockyard within the definition of the Packers and Stockyards Act, 1921 as amended, and has received notice to that effect from the Secretary of Agriculture. Approved stockyards shall be required to keep such records, make such reports and be subject to inspection and regulation by the Secretary of Agriculture, as provided in said Packers and Stockyards Act.

An approved slaughter plant shall, at a minimum, be federally inspected, slaughter primarily fed cattle in the normal course of business, have a fed cattle slaughter capacity of at least 500 head per day, have proper facilities for weighing and grading, and be located within ~~[approximately 450]~~ a 200-mile[s] radius of one or more approved stockyards.

## Chapter 101 Live Cattle Futures

### 10103. SETTLEMENT PROCEDURES

#### 10103.B. Live Graded Deliveries

4. Par Delivery and Substitutions.

- a. Par Delivery Unit. A par delivery unit is 40,000 pounds of USDA estimated Yield Grade 3, 55% Choice, 45% Select quality grade live steers, with no individual animal weighing less than 1,050 pounds or more than ~~[1,475]~~ 1,500 pounds. ~~[deliverable at par.]~~

(remainder of Rule 10103.B.4.a. unchanged)

- b. Weight Deviations. Steers weighing less than 1,050 pounds or more than ~~[1,550]~~ 1,500 pounds shall not be deliverable. ~~[Steers weighing more than 1,475 pounds but less than or equal to 1,550 pounds shall be deliverable at an adjustment equal to 950-1000 lbs Factor described in Rule 10103.A., multiplied by the average live weight of the delivery unit.]~~ The judgment of the grader as to ~~[the number of]~~ such overweight or underweight cattle ~~[in the delivery unit]~~ shall be final. ~~[and shall be so certified on the grading certificate.]~~

#### 10103.C. Carcass Graded Deliveries

1. Conditions.

A buyer assigned a Certificate of Delivery may call for delivery of the cattle to an approved slaughter plant corresponding to the stockyards designated in the Certificate, or to any other approved slaughter plant within ~~[450]~~ 200 miles of the feedlot from which the cattle originate. For the purposes of Chapter 101, a feedlot shall be defined as any location where cattle are confined to a pen and provided access to feed and water including, but not limited to, commercial feeding operations, farmer feeding operations and stockyards.

(remainder of Rule 10103.C.1. unchanged)

5. Par Delivery and Substitutions.

- h. Delivery Points and Allowances. Buyers electing carcass grading must specify an approved slaughter plant enumerated by the Exchange. Eligible slaughter plants include those enumerated for the stockyards to which the cattle were tendered, and any other approved slaughter plant that is within ~~[450]~~ 200 miles of the originating feedlot.

**10104. PROCEDURES FOR TENDER, DEMAND, RETENDER, RECLAIM, AND ASSIGNMENT OF CERTIFICATES OF DELIVERY**

**10104.A. Tendering a Certificate**

A clearing member representing a short may present a Certificate of Delivery (on a form prescribed by the Clearing House) to the Clearing House no later than 4:30 p.m. on any business day except that Certificates may not be tendered:

1. On or before the first Friday of the contract month;
2. After the third business day after expiration.

A Certificate of Delivery is a commitment to deliver cattle conforming with contract specifications at the delivery point designated in the Certificate, or at a corresponding approved slaughter plant selected by the buyer, if the Certificate is not reclaimed.

A Certificate tendered before the termination of trading requires delivery on the sixth business day that is also a delivery day following the tender of that Certificate, if the buyer elects live grading. If the buyer elects carcass grading, the Certificate requires delivery at the option of the buyer on any day the slaughter plant is in operation between the third business day and the sixth business day, inclusive, following tender of that Certificate.

A Certificate tendered on or after the day trading terminates requires delivery on the fourth business day that is also a delivery day following the tender of that Certificate, if the buyer elects live grading. If the buyer elects carcass grading, the Certificate requires delivery at the option of the buyer on the third business day or fourth business day following tender of that Certificate, or on an intervening day that the slaughter plant is in operation.

A Certificate must include the name, location, business address, and telephone number of the feedlot from which the cattle originate. A Certificate must also include: (1) the distance between the feedlot and the stockyards to which the cattle are tendered for delivery; (2) the distance between the feedlot and the approved slaughter plants corresponding to the stockyards to which the cattle are tendered for delivery; and (3) any other approved slaughter plants within ~~[450]~~ 200 miles of the feedlot and the distances to such approved slaughter plants.

(remainder of Rule 10104.A. unchanged)

**Discussion**

Changes to the Live Cattle delivery process that will result from these amendments can be summarized as follows:

- The radius for determining the corresponding CME-approved slaughter plants for each live-graded delivery point will increase from 150 miles to 200 miles;
- The maximum distance between the feedlot from which cattle originate and any other eligible CME-approved slaughter plants will increase from 150 miles to 200 miles;
- The maximum par weight for individual animals in live-graded deliveries will increase from 1,475 pounds to 1,500 pounds; and
- Individual animals in live-graded deliveries weighing more than 1,500 pounds will not be deliverable.

### Packing Plant Distances

The maximum distances between live-graded delivery points and corresponding CME-approved slaughter plants (see first bullet point above), and between originating feedlots and eligible CME-approved slaughter plants (see second bullet point above), have been set at 150 miles since the carcass-graded delivery provisions were implemented in 1995. Since that time, six of the original CME-approved slaughter facilities have permanently closed, along with a number of non-CME-approved plants, and no new plants meeting CME criteria have been constructed. As a result, cattle are being transported longer distances to the remaining packing plants, on average, and therefore an increase in the maximum distance for CME-approved plants is consistent with industry trends.

In addition, technology advances since the mid-1990s permits further refinement in the procedure used to determine the corresponding CME-approved slaughter facilities for each live-graded delivery point. At the outset, the process was simple fairly crude: a compass was used to draw a circle around the "dot" on a map for each town in which a live-graded delivery point was located, and "dots" for towns corresponding to the addresses of packing plants were judged to be inside or outside each circle. This was the best technology available at the time, but because the results were known at the time to be imprecise, the word "approximately" was included in Rule 704.

Later on, various web-based tools were used to find the "as the crow flies" distances between two locations. While this approach eliminated some measurement errors, it still assumed that all delivery facilities were located in the center of town, while in fact most livestock auctions and packing plants are located elsewhere.

With the advent of satellite imagery and GPS, it is now possible to measure these distances within .001 mile (approximately 5 feet). Using GPS coordinates for the center of the main auction building and center of the packing plant, distances for all delivery point-packing plant combinations have been calculated. A list of the CME-approved slaughter plants (based on the 16 plants currently approved through January 31, 2011) within a 200-mile radius of each delivery point is provided in Exhibit 1.

For the amendments to Rule 704, expanding the radius to 200 miles, plus the use of more precise measurements, results in 1 additional packing plant for 6 delivery points, and 2 additional packing plants for 3 delivery points; there is no change in the number of eligible packing plants for 4 delivery points. The availability of more packing plants will provide increased delivery capacity and greater flexibility for both delivering shorts and receiving longs. Similar benefits also should result from the amendments to Rules 10103.C.1, 10103.C.5.h. and 10104.A., which increase to 200 miles the maximum distance (in road miles, not "as the crow flies") between the originating feedlot and eligible slaughter plants.

### Deliverable Live Weights

In 2007, the Exchange began a series of steps to relieve market congestion by 1) permitting the delivery of heavier cattle in live-graded deliveries, and 2) eliminating inconsistencies between the live-graded and carcass-graded delivery requirements. These changes have been

extremely successful in expanding deliverable supply, streamlining the live-graded delivery process, and increasing live-graded delivery capacity. Now, after two-plus years of delivery experience since the first of these changes were implemented, a few adjustments are needed to fine-tune this process.

In CME Submission No. 07-39 dated May 17, 2007 and in CME Submission No. 07-74 dated September 6, 2007, it was assumed that discounts on various carcass weights compiled under mandatory reporting could be adjusted and used as reliable measures of market discounts on the corresponding weights of live animals. This led to the use of the 950-1000 lbs Factor, based on USDA's "5-Area Weekly Weighted Average Direct Slaughter Cattle – Premiums and Discounts" report (LM\_CT169), to discount live-graded steers weighing more than 1,475 pounds but not more than 1,550 pounds, as described in Rule 10103.B.4.b.

Since that time, the Exchange has learned that weight discounts on live animals may vary more widely, and less predictably, than weight discounts on carcasses. While there is general agreement among market participants that a live steer producing a 1,000-pound carcass will be heavily discounted in cash market transactions, there is little consensus about anything else regarding live weights and discounts. Some cattle feeders claim to have received weight discounts on cattle weighing as little as 1,450 pounds; others say they have never been discounted on individual animals until they approach 1,600 pounds; and still others report that it is a common practice for pens of cattle to be sold at an average price \$2-3 lower than the "regular" bid, in return for waiving the weight discounts on the heavier individuals (i.e., those producing carcasses weighing 1,000 pounds and up). In summary, there appears to be little uniformity in live weight discounts in the cash market, even within the same market area during the same time of the year.

A further complication is the fact that there is no live-animal equivalent to the LM\_CT169 report with information on weight discounts in the cash market for animals sold on a live basis, so it is impossible to make an objective evaluation of this issue. In fact, it was the lack of a live-animal equivalent to the LM\_CT169 report that led the Exchange to adopt these carcass weight discounts for live-graded deliveries. However, it is clear from the comments we have received that adjusted carcass weight discounts are not appropriate for use as live weight discounts, so Rule 10103.B.4.b. is being amended to eliminate all weight discounts on live-graded deliveries (see third bullet point above).

The Exchange also has observed a tendency for the distribution of delivery weights to be negatively skewed, or "lopsided" toward the right, so that a greater proportion of heavier-weight cattle are being delivered than would be expected to occur by random chance. This suggests that delivering shorts may be using the futures delivery process as a dumping ground for cattle that are subject to weight discounts in the cash market and are at, or are rapidly approaching, the level at which those discounts would apply.

For example, in October 2009 there were 709 live-graded deliveries, with an average weight of 1,413 pounds and a standard deviation of 41 pounds. The frequency distribution is presented in Exhibit 2, with an obvious rightward tilt. These data are average weights of the 709 delivery units, since individual weights on each of the 20,253 delivered head are not available. However, from the grading results we know there were 3,793 steers (18.7%) that weighed more than 1,475 pounds. Using standard statistical analysis, this is triple the 6.3% that we would

expect to exceed 1,475 pounds in a purely random distribution with these parameters. Furthermore, the probability of having 18.7% of the steers weigh more than 1,475 pounds by sheer chance is effectively zero. This finding supports the idea that most of these heavier cattle were intentionally selected for delivery.

To prevent further misuse of the futures delivery process as an alternative to normal cash market channels, the Exchange is reducing the maximum deliverable weight from 1,550 pounds to 1,500 pounds, via amendments to Rule 10103.B.4.a. and Rule 10103.B.4.b. (see fourth bullet point above). It should be noted that the Exchange considered a number of alternative solutions before taking this step: maintaining the status quo, which threatens to adversely affect contract performance; limiting the number of heavier cattle that can be delivered to some fixed number, which further complicates the delivery process and has proven unworkable in the past when used with other delivery characteristics; and developing a new schedule of discounts, which is not feasible without reliable cash market data and industry consensus on how live animals are discounted in the cash market.

Average steer carcass weights set a new record again in 2009 at 870 pounds for the week ending October 10, up 5 pounds from the previous record established in October 2008. However, an average carcass weight of 870 pounds is equivalent to a 1,381-pound live weight at the par 63% hot yield, which is well below the new 1,500-pound maximum. Using the summary statistics from the October 2009 delivery period described above, this 50-pound reduction would have reduced deliverable supply by just 1.6%, at the time of the year when weights are at their seasonal peak. At other times of the year when average weights are lower, the impact on deliverable supply will be even less.

### **Concluding Comments**

These amendments are the result of exhaustive discussions with a broad spectrum of market participants over a 6-month period, and represent the best solutions available to address these particular issues. The Exchange is committed to protecting the integrity of its contracts and meeting its obligations to maintain fair, orderly and efficient markets, and we believe these changes will enhance the ability of the Live Cattle contract to perform its vital price discovery and risk management functions.

CME certifies that this action complies with the Commodity Exchange Act and the regulations thereunder.

If you have any questions regarding this submission, please contact Paul Peterson at (312) 930-4587 or via e-mail at [paul.peterson@cmegroup.com](mailto:paul.peterson@cmegroup.com), or me at (312) 648-5422. Please refer to CME Submission No. 10-130 in all correspondence regarding this matter.

Sincerely,

/s/ Stephen M. Szarmack  
Regulatory Counsel

**EXHIBIT 1**  
**LIVE CATTLE DELIVERY POINTS AND**  
**CORRESPONDING CME-APPROVED SLAUGHTER PLANTS**

*Note: Italics indicate plants added by the change to a 200-mile radius*

**Amarillo, TX**

Cargill Meat Solutions	Friona, TX
Cargill Meat Solutions	Plainview, TX
Tyson Fresh Meats	Amarillo, TX
JBS	Cactus, TX
National Beef	Liberal, KS
<i>Tyson Fresh Meats</i>	<i>Holcomb, KS</i>

**Clovis, NM**

Cargill Meat Solutions	Friona, TX
Cargill Meat Solutions	Plainview, TX
Tyson Fresh Meats	Amarillo, TX
JBS	Cactus, TX

**Columbus, NE**

Cargill Meat Solutions	Schuyler, NE
Tyson Fresh Meats	Dakota City, NE
Tyson Fresh Meats	Lexington, NE
Tyson Fresh Meats	Denison, IA
JBS	Grand Island, NE

**Dodge City, KS**

Cargill Meat Solutions	Dodge City, KS
National Beef	Dodge City, KS
National Beef	Liberal, KS
Tyson Fresh Meats	Holcomb, KS
<i>JBS</i>	<i>Cactus, TX</i>
<i>Tyson Fresh Meats</i>	<i>Amarillo, TX</i>

**Norfolk, NE**

Cargill Meat Solutions	Schuyler, NE
Tyson Fresh Meats	Dakota City, NE
Tyson Fresh Meats	Lexington, NE
Tyson Fresh Meats	Denison, IA
JBS	Grand Island, NE
<i>PM Beef</i>	<i>Windom, MN</i>

**North Platte, NE**

Cargill Meat Solutions	Ft. Morgan, CO
Tyson Fresh Meats	Lexington, NE
JBS	Grand Island, NE
<i>Cargill Meat Solutions</i>	<i>Schuyler, NE</i>

**Ogallala, NE**

Cargill Meat Solutions	Ft. Morgan, CO
Tyson Fresh Meats	Lexington, NE
JBS	Grand Island, NE
JBS	Greeley, CO

**Pratt, KS**

Cargill Meat Solutions	Dodge City, KS
National Beef	Dodge City, KS
Tyson Fresh Meats	Holcomb, KS
National Beef	Liberal, KS

**Syracuse, KS**

Tyson Fresh Meats	Holcomb, KS
Cargill Meat Solutions	Dodge City, KS
National Beef	Dodge City, KS
JBS	Cactus, TX
National Beef	Liberal, KS
<i>Tyson Fresh Meats</i>	<i>Amarillo, TX</i>
<i>Cargill Meat Solutions</i>	<i>Ft. Morgan, CO</i>

**Texhoma, OK**

Cargill Meat Solutions	Dodge City, KS
Cargill Meat Solutions	Friona, TX
JBS	Cactus, TX
Tyson Fresh Meats	Amarillo, TX
National Beef	Dodge City, KS
Tyson Fresh Meats	Holcomb, KS
National Beef	Liberal, KS
<i>Cargill Meat Solutions</i>	<i>Plainview, TX</i>

**Tulia, TX**

Tyson Fresh Meats	Amarillo, TX
Cargill Meat Solutions	Friona, TX
Cargill Meat Solutions	Plainview, TX
JBS	Cactus, TX
<i>National Beef</i>	<i>Liberal, KS</i>



**Worthing, SD**

Cargill Meat Solutions  
Tyson Fresh Meats  
PM Beef  
Tyson Fresh Meats  
*JBS*

Schuyler, NE  
Dakota City, NE  
Windom, MN  
Denison, IA  
*Grand Island, NE*

**Wray, CO**

Cargill Meat Solutions  
JBS  
Tyson Fresh Meats  
*Cargill Meat Solutions*  
*Tyson Fresh Meats*

Ft. Morgan, CO  
Greeley, CO  
Lexington, NE  
*Dodge City, KS*  
*Holcomb, KS*

**EXHIBIT 2**  
**FREQUENCY DISTRIBUTION OF AVERAGE LIVE WEIGHTS**  
**FROM OCTOBER 2009 LIVE-GRADED DELIVERIES**

