compliance with section 4b(a)(iv) of the Act.

Section 36.9 provides, among other things, that it shall be unlawful to cheat, defraud or deceive or attempt to cheat, defraud or deceive any other person or to willfully make any false report or statement. The Commission believes that compliance with these provisions, when combined with compliance with the other specific customer protection provisions included in section 36.3, should provide for appropriate customer protection safeguards. Rules submitted pursuant to paragraph (c) of section 36.3, which would permit customer order transactions to be executed using special execution procedures, require a specific prohibition against the improper disclosure of customer order information. Rules submitted pursuant to paragraph (d) of Rule 36.3 which would permit transactions to be executed using combined special execution and on-floor competitive procedures, require a specific prohibition against frontrunning. Further, these safeguards apply in a market already limited to specified eligible participants.

In addition, the Commission believes that it is important to provide examples of trading activity that would be permissible and activity that could constitute fraud and customer abuse in violation of section 36.9. It would be permissible to engage in anticipatory hedging. An FCM or floor broker would be allowed to cover when he took the opposite side of a customer order. It would not be permissible for an FCM or floor broker executing transactions using special execution procedures to take the opposite side of a customer order when doing so would deny the fill to another customer. For example, if an FCM or floor broker were to receive matching buy and sell orders from different customers, the FCM or floor broker should not take the opposite side of one of the customer orders if doing so would result in the inability to fill the order of the other customer. It also would continue to be impermissible for an FCM or floor broker to trade ahead of a customer order to the disadvantage of that order.65

## 7. Safe Harbor Provision

Paragraph (f) of section 36.3 enunciates the "safe harbor" provisions of the regulation. Transactions in exempt contracts executed in compliance with special execution procedures contained in exchange rules that are permitted to become effective shall not be deemed to be in violation of sections 4b(a)(iv), 4b(b) or 4c(a) of the Act or Commission Rules 1.38(a), 1.39, 155.2, 155.3 and 155.4. Transactions in exempt contracts that are not executed in compliance with such exchange rules shall be deemed to be in violation of section 36.3.

8. Procedures for Permitting Rules to Become Effective

Section 36.3 provides for expedited procedures under which section 4(c) contract market trading rules may be permitted to become effective. Pursuant to paragraphs (g) (1) and (2) of the regulation, section 4(c) contract market trading rules must be submitted to the Commission for review prior to becoming effective. Such rules may become effective ten days after receipt by the Commission unless the Commission, within that ten-day period, notifies the submitter that the proposal does not meet the conditions of this section. Pursuant to paragraph (g)(4) of section 36.3, any subsequent proposed modifications of such rules consistent with this section shall be subject to the same expedited Commission review procedures. In the event that the trading rules, or subsequent modifications thereof, are not permitted to become effective, they shall be subject to the usual rule approval procedures under section 5a(a)(12)(A) of the Act, 7 U.S.C. 7a(12), and Commission Rule 1.41(b)

Paragraph (g)(3) of section 36.3 provides for expedited review of certain large order execution procedures. If a contract market submits for review large order execution procedures for section 4(c) contracts which are substantially similar to procedures approved by the Commission pursuant to Commission Rule 1.39 for non-section 4(c) contracts, then such procedures shall be deemed effective upon Commission receipt thereof.

Proposed exchange clearing and financial integrity rules are not eligible for review under these expedited procedures and, thus, are subject to the usual rule approval procedures under section 5a(a)(12)(A) of the Act, 7 U.S.C. 7a(12), and Commission Rule 1.41(b). In addition, pursuant to paragraph (g)(5), exchanges may submit for Commission review and approval, pursuant to the usual rule approval procedures contained in section 5a(a)(12)(A) of the Act and Rule 1.41(b), other section 4(c)contract market rules which do not conform to the specific trading standards set forth in section 36.3 and which do not satisfy the requirements of the Act and Commission regulations.

## D. Listing Procedures

The proposed rules specify a 10-day notification requirement prior to listing new section 4(c) contract market transactions. Most commenters supported the proposed 10-day notification requirement. Several commenters further suggested that a 10day period should apply to all exchange-traded contracts or to certain categories of such contracts, such as financial futures and options. One commenter stated that the Commission should allow new section 4(c) contract market transactions to become effective, and to begin trading, immediately following the Commission's receipt of notice. This commenter further noted that, if the Commission thereafter determines that trading in a new section 4(c) transaction violates the listing standards in Rule 36.2, the Commission could take appropriate measures, suspending trading without a prior adjudication, pending further review.

The Commission believes that a 10day advance notification requirement is appropriate. This limited period should allow flexibility in listing new eligible products without impairing exchanges' ability to respond rapidly to market situations. The Commission will evaluate whether the notification period should be eliminated or revised, and whether the 10-day notification provision should be extended to certain non-section 4(c) contract market transactions, when it evaluates trading experience under the pilot program.

<sup>&</sup>lt;sup>65</sup> With certain exceptions, trading ahead of customer orders recently has been restricted in the OTC securities markets. On May 22, 1995, the SEC issued Securities Exchange Act Release No. 35751 (May 22, 1995), 60 FR 27997 (May 26, 1995), an order approving a proposed rule change submitted by the National Association of Securities Dealers, Inc., ("NASD") relating to limit order protection on NASDAQ. The rule change amended NASD's interpretation to Article III, Section 1 of the NASD Rules of Fair Practice. The interpretation generally provides that a member firm cannot accept a limit order in a NASDAQ security from its own customer,

or from a customer of another member, and continue to trade that security for its own account at prices that would satisfy the customer limit order without filling that order at the limit order price or at a price more favorable to the customer. Limit orders for retail customers that involve 10,000 shares or more and a value of \$100,000 or greater are exempt from this prohibition, as are limit orders of any size for institutional accounts. The NASD Rules of Fair Practice define an institutional account as an account of a bank, savings and loan association, insurance company, or registered investment company; a registered investment adviser; or any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$50 million. 'Release 34-35751''). See also NYSE Rule 92 (limiting members' trading when they hold an unexecuted customer order); NASD Schedule G, Section 4(f)(1), Trading Practices (prohibiting members from buying or selling securities while holding unexecuted market or limit orders); and CBOE Rule 6.73 (requiring a floor broker to handle an order using due diligence to execute the order at the best price available to him).