

GENERAL NOTICE NO: 2140



The London International Financial
Futures and Options Exchange

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BASIS TRADE FACILITY

INCLUSION OF “REPO” TRANSACTIONS AS AN ELIGIBLE CASH LEG

SIMPLIFICATION OF THE REPORTING REQUIREMENTS FOR BASIS TRADES INVOLVING CASH BONDS

Executive Summary

This General Notice informs members of:

- (a) the inclusion of “repo” trades as an eligible cash leg of a Basis Trade against STIR Futures Contracts; and*
- (b) a simplification of the submission requirements for Basis Trades involving a cash bond.*

1. “Repo” Transactions as an Eligible Cash Leg

- 1.1 The Exchange has determined to include sale and repurchase transactions (“repo” transactions) as an eligible cash leg for Basis Trades in respect of the Exchange’s STIR Futures Contracts, on and from Wednesday 11 December 2002.
- 1.2 To be acceptable as a cash leg of a Basis Trade, a repo transaction must conform to the following characteristics:
 - (a) be either a spot or forward starting repo;
 - (b) be constructed under the terms of the Bond Market Association/ISMA “Global Master Repurchase Agreement”;
 - (c) have defined start and end dates;
 - (d) not be repayable on demand;
 - (e) incorporate a defined bond which has an ISIN code;
 - (f) be traded in a permitted currency; and
 - (g) have a defined interest (repo) rate.

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- 1.3 Members are reminded that the permitted currencies in respect of Basis Trade cash legs are as follows: Euro; Sterling; US Dollar; Japanese Yen; Australian Dollar; Swiss Franc; Swedish Krona; and Danish Krone.
- 1.4 Amendments to the LIFFE CONNECT™ Trading Procedures to accommodate repo transactions as a cash leg can be found in Attachment 1 to this General Notice. These Trading Procedures describe the information which is required when a Basis Trade involving repo transactions as a cash leg is submitted to the Exchange.
- 1.5 The basis trade executing member must continue to retain information in relation to the cash leg repo transaction for three years, as described in the LIFFE CONNECT™ Trading Procedures. Where the basis trade executing member is not directly responsible for the execution of the cash leg, he must have appropriate arrangements in place with the party organising/executing the cash leg such that the relevant information can be provided promptly to the Exchange.

2. Reporting Requirements for Bonds as the Cash Leg of a Basis Trade

- 2.1 The Exchange has also resolved to simplify members' reporting requirements in respect of Basis Trades which have a bond as the cash leg.
- 2.2 At present, the executing member is required to supply details of the bond's ISIN code, the clean cash price and, in the case of deliverable bonds against bond futures, the hedge ratio methodology. With effect from Wednesday 11 December 2002, executing members will be required to supply only the following information as part of their trade submission:
 - (a) the futures contract(s) in which the BTF is being transacted;
 - (b) the delivery month(s);
 - (c) the agreed futures price(s);
 - (d) the number of Futures Contracts; and
 - (e) **a unique identifier/reference number for the cash bond transaction.**
- 2.3 The unique identifier/reference number is required to provide a cross reference to the cash transaction, in order to enable a full audit of the transaction by the Exchange.
- 2.4 Members will be required to retain the following details of the cash bond transaction for a period of three years:
 - (a) the cash bond ISIN number;
 - (b) the clean cash price;
 - (c) the hedge ratio methodology (for government bond futures contracts against deliverable bonds only);
 - (d) the coupon and maturity of the cash bond;
 - (e) the frequency of coupon payments;
 - (f) the currency of the cash bond; and
 - (g) the nominal value of the cash bond.

- 2.5 Amendments to the LIFFE CONNECT™ Trading Procedures to accommodate this change in submission requirements can also be found in Attachment 1 to this General Notice. Updated LIFFE CONNECT™ Trading Procedures will appear on the LIFFE website and in the next update of the Member Handbook in due course.

3. Further Information

- 3.1 Members seeking further information in relation to this General Notice should contact Interest Rate Product Management (+44 (0)20 7379 2222) at LIFFE.

BY ORDER OF THE BOARD

N E Carew Hunt
Market Secretary

Amendments to LIFFE CONNECT™ Trading Procedures

Additions to LIFFE CONNECT™ Trading Procedures are shown underlined.

Deletions are ~~struckthrough~~.

4.19 Basis Trading Facility

- 4.19.1 The Exchange provides a Basis Trading Facility (“BTF”) which allows members to organise and execute, subject to this Trading Procedure 4.19, transactions involving a combination of an approved basis trade instrument and an appropriate number of offsetting Futures Contracts. For the purposes of these Trading Procedures such transactions are called “basis trades”.
- 4.19.2 Any member is permitted to arrange basis trades, subject only to the member having in place arrangements for the execution of the futures leg of a basis trade via a member holding a relevant trading right (“the basis trade executing member”) to trade the basis trade Exchange Contract.
- 4.19.3 A basis trade may be organised only during the trading hours of the Futures Contract concerned, as published by the Board from time to time by General Notice.
- 4.19.4 Basis trades may be transacted only in Exchange Contracts which have been designated by the Board for that purpose. Such designations will be published, from time to time, by General Notice. Basis trades are not permitted in a delivery month of a designated contract which has never traded. The Basis Trading Facility can be used in respect of a delivery month for a Futures Contract on any trading day up to and including the business day preceding the Last Trading Day of that delivery month.
- 4.19.5 The basis trade executing member is responsible for assigning the price of the futures leg(s) of a basis trade. For the futures leg(s) to be authorised, the price(s) must be at the level trading on LIFFE CONNECT™ at the time the basis trade is submitted for execution, as specified in Trading Procedures 4.19.9 and 4.19.10, or within the high/low traded price that occurred on LIFFE CONNECT™ in the preceding thirty minutes. In the event that no trade has occurred in the relevant delivery month on that day at the time the basis trade is submitted for execution or in the preceding thirty minutes, the price of the futures leg(s) of the basis trade must be at or within the high/low traded price calculated by the Exchange maintained algorithm.

4.19.6 ~~In relation to a bond forming the cash leg of a basis trade against a government bond futures contract, a Swapnote® futures contract or one or more delivery month(s) of a short term interest rate futures contract, the basis trade executing member must provide the Exchange with the clean cash price of the bond, as specified in Trading Procedure 4.19.9. The Exchange does not require the provision of the cash price of any other type of security or OTC instrument, which may form the cash leg of a basis trade.~~ **[Deleted]**

4.19.7 The following approaches to the construction of hedge ratios for basis trades are considered acceptable:

- (a) Deliverable bonds against bond futures contracts:
A price factor or duration based method;
- (b) Other bonds against bond futures contracts:
A duration based method;
- (c) Deliverable and non-deliverable bonds against Swapnote® futures contracts or one or more delivery month(s) of a short term interest rate futures contract:
A method which is based upon the ratio of the basis point values of shifts in the yield curve of respectively the relevant cash and futures legs;
- (d) Standard plain vanilla OTC swaps against bond futures contracts, Swapnote® futures contracts of one or more delivery month(s) of a short term interest rate futures contract:
A method which is based upon the ratio of the basis point values of shifts in the yield curve of respectively the relevant cash and futures legs;
- (e) Forward Rate Agreements (FRAs) against one or more delivery month(s) of a short term interest rate futures contract:
A method which is based upon the ratio of the basis point values of shifts in the yield curve of respectively the relevant cash and futures legs;
- (f) Sale and Repurchase Agreements (Repos) against one or more delivery month(s) of a short term interest rate futures contract:
A method which is based upon the ratio of the basis point values of shifts in the yield curve of respectively the relevant cash and the futures legs;
- ~~(g)~~ European or American style OTC interest rate options (bond options, swaptions) against bond futures contracts, Swapnote® futures contracts or one or more delivery month(s) of a short term interest rate futures contract:
A method based on the relative deltas of the OTC option and futures contracts in order to achieve a delta neutral position;

- (gh) Equity securities against Universal Stock Futures Contracts:
A method based on the relative value of the equity security and the nominal underlying value of the Universal Stock Futures Contracts;
- (hi) Baskets of equity securities against equity index futures contracts:
A method based on the relative value of the basket of equity securities and the nominal underlying value of the equity index futures contracts;
- (ij) European or American style OTC equity options (stock and equity index options) against equity index futures contracts:
A method based on the relative deltas of the OTC option and futures contracts in order to achieve a delta neutral position.
- (jk) European or American style OTC or non-LIFFE exchange traded equity options against Universal Stock Futures Contracts:
A method based on the relative deltas of the OTC or exchange traded option and Universal Stock Futures Contracts in order to achieve a delta neutral position.

Where a hedge ratio differs from such methods, the member who is submitting the trade for authorisation (see Trading Procedure 4.19.8) may be required to justify the method employed.

4.19.8 When a member accepts a basis trade order, he must record the order details set out in Trading Procedure 4.19.9 – 4.19.13A and, in addition, the details prescribed by (a) – (c) below, on an order slip. Where a member employs an electronic system for order routing, such details must be recorded electronically:

- (a) time of order receipt;
- (b) identity of individual organising the basis trade; and
- (c) time stamp (at time of organisation).

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.8, must be retained by the member for a minimum period of three years.

After a basis trade has been organised the member, or where the basis trade has been organised between two members, the member who will be the seller of the futures leg of the basis trade, must execute the futures leg of the basis trade as a cross transaction, as specified in Trading Procedures 4.19.9 – 4.19.13A, or must procure that the futures leg of the basis trade is so executed by another appropriately authorised member.

4.19.9 Where a basis trade involves a government bond futures contract, a Swapnote® futures contract, or one or more delivery month(s) of a short

term interest rate futures contract against a cash bond, in respect of each basis trade, the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract(s) in which the BTF is being transacted;
- (b) delivery month(s);
- (c) agreed futures price(s);
- (d) number of Futures Contracts; and
- (e) a unique identifier/reference number for the cash bond transaction;

- ~~(e) cash bond ISIN number;~~
- ~~(f) clean cash price;~~
- ~~(g) hedge ratio methodology (for government bond futures contracts against deliverable bonds only);~~

In addition, the basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence of the following information:

- (f) cash bond ISIN number;
- (g) clean cash price;
- (h) hedge ratio methodology (for government bond futures contracts against deliverable bonds only);
- ~~(h)~~ coupon and maturity of the cash bond;
- ~~(i)~~ frequency of coupon payments;
- ~~(j)~~ currency of cash bond; and
- ~~(k)~~ nominal value of cash bond.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.9, must be retained by the member for three years. If the basis trade executing member is not directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing the cash leg such that the information in ~~(h)~~ – ~~(k)~~ above can be provided promptly to the Exchange.

4.19.10 Where a basis trade involves a government bond futures contract, a Swapnote® futures contract or one or more delivery month(s) of a short term interest rate futures contract against a plain vanilla OTC swap the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract(s) in which the BTF is being transacted;
- (b) delivery month(s);
- (c) agreed futures price(s);
- (d) number of Futures Contracts;

The basis trade executing member must also record on the basis trade registration slip the unique identifier/reference number of the swap

transaction. The basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence which contains the following information:

- (e) the cash market counterparty identifier(s) for the cash leg;
- (f) fixed rate of the swap, including accrual convention;
- (g) floating reference rate of the swap;
- (h) termination/maturity date;
- (i) effective (start) date of the swap;
- (j) next fixed and floating reset dates of the swap;
- (k) replacement/liquidation value of the swap;
- (l) frequency of payments;
- (m) currency of floating and fixed legs of the swap; and
- (n) nominal value of the swap.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.10, must be retained by the member for three years. If the basis trade executing member is not directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing that leg such that the information in (e) - (n) above can be provided promptly to the Exchange.

4.19.11 Where a basis trade involves one or more delivery month(s) of a short term interest rate futures contract against a FRA the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract(s) in which the BTF is being transacted;
- (b) delivery month(s);
- (c) agreed futures price(s);
- (d) number of Futures Contracts;

The basis trade executing member must also record on the basis trade registration slip the unique identifier/reference number of the FRA transaction. The basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence which contains the following information:

- (e) the cash market counterparty identifier(s) for the cash leg;
- (f) reference rate of the FRA;
- (g) termination/maturity date;
- (h) effective (start) date of the FRA;
- (i) replacement/liquidation value of the FRA;
- (j) currency of the FRA; and
- (k) nominal value of the FRA.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.11, must be retained by the member for three years. If the basis trade executing member is not

directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing that leg such that the information in (e) - (k) above can be provided promptly to the Exchange.

4.19.11A Where a basis trade involves one or more delivery month(s) of a short term interest rate futures contract against a Repo the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract(s) in which the BTF is being transacted;
- (b) delivery month(s);
- (c) agreed futures price(s);
- (d) number of Futures Contracts;
- (e) a unique identifier/reference number for the Repo transaction;

In addition, the basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence of the following information:

- (f) the counterparty identifier(s) for the Repo;
- (g) the coupon, maturity and ISIN code of the bond being repoed;
- (h) the nominal value and currency of the bond;
- (i) the clean price and dirty price for the opening leg of the trade;
- (j) the start and end dates for the repo; and
- (k) the repo rate.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.11 A, must be retained by the member for three years. If the basis trade executing member is not directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing the cash leg such that the information in (f) – (k) above can be provided promptly to the Exchange.

4.19.12 Where a basis trade involves equity index futures contracts against a basket of equity securities, or Universal Stock Futures Contracts against equity securities, the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract in which the BTF is being transacted;
- (b) delivery month;
- (c) agreed futures price;
- (d) number of Futures Contracts;
- (e) a unique identifier/reference number for the equity security or basket of equity securities transaction, as applicable;

In addition, the basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence of the following information:

- (f) the identity and volume traded of the equity security or each equity security comprising the basket, as applicable;
- (g) the price (including currency) at which each equity security was traded; and
- (h) any supplementary cash payment made in conjunction with the transaction.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.12, must be retained by the member for three years. If the basis trade executing member is not directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing that leg such that the information in (f) - (h) above can be provided promptly to the Exchange.

4.19.13 Where a basis trade involves a government bond futures contract, a Swapnote® futures contract, one or more delivery month(s) of a short term interest rate futures contract, a Universal Stock Futures Contract, or equity index futures contracts against an OTC option/options strategy, the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract(s) in which the BTF is being transacted;
- (b) delivery month(s);
- (c) agreed futures price(s);
- (d) number of Futures Contracts;
- (e) a unique identifier/reference number for the OTC option/options strategy transaction;

In addition, the basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence of the following information:

- (f) the price(s) (including currency) and nominal value of the OTC option/ options strategy;
- (g) the strike price(s) of the OTC option/options strategy;
- (h) class – call(s) and/or put(s);
- (i) the price(s) of the underlying instrument(s) for the OTC option/options strategy;
- (j) the time to expiration of the OTC option/options strategy; and
- (k) the delta of the OTC option/options strategy.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.13, must be retained by the member for three years. If the basis trade executing member is not directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing that leg such that the information in (f) - (k) above can be provided promptly to the Exchange.

4.19.13A Where a basis trade involves a Universal Stock Futures Contract against a non-LIFFE exchange traded option/options strategy, the following details must be submitted to the Exchange via LIFFE CONNECT™ by the basis trade executing member:

- (a) Futures Contract(s) in which the BTF is being transacted;
- (b) delivery month(s);
- (c) agreed futures price(s);
- (d) number of Futures Contracts;
- (e) a unique identifier/reference number for the exchange traded option/options strategy transaction;

In addition, the basis trade executing member must retain, in an easily accessible form that can be audited by the Exchange, documentary evidence of the following information:

- (f) the exchange on which the option contract was executed;
- (g) the price(s) (including currency) and nominal value of the exchange traded option/ options strategy;
- (h) the strike price(s) of the exchange traded option/options strategy;
- (i) class – call(s) and/or put(s);
- (j) the price(s) of the underlying instrument(s) for the exchange traded option/options strategy;
- (k) the time to expiration of the exchange traded option/options strategy; and
- (l) the delta of the exchange traded option/options strategy.

All information required to be retained by the basis trade executing member, pursuant to this Trading Procedure 4.19.13A, must be retained by the member for three years. If the basis trade executing member is not directly responsible for the execution of the cash leg of the basis trade, he must have appropriate arrangements in place with the party organising/executing that leg such that the information in (f) - (l) above can be provided promptly to the Exchange.

4.19.14 The basis trade details must be submitted to the Exchange within thirty minutes of the time at which the basis trade was organised. No basis trade can be submitted for execution later than five minutes prior to the close of trading of the Futures Contract in which the basis trade is being transacted. An exchange official will check the validity of the details submitted by the executing member. If the exchange official is satisfied that all such details are valid, he will authorise that the futures leg of the basis trade is executed. The executing member will then receive confirmation of the details of the trade.

4.19.15 [Deleted]

4.19.16 Details of the executed futures leg(s) of a basis trade will be submitted to TRS by the Trading Host.

4.19.17 Authorisation by an exchange official of a transaction does not preclude the Exchange from instigating disciplinary proceedings in the event that the transaction is subsequently found to have been made other than in compliance with Exchange Rules and Trading Procedures.

4.19.18 The following information with respect to the futures leg of a basis trade will be broadcast on LIFFE CONNECT™:

- (a) Futures Contract(s) and delivery month(s);
- (b) futures price(s); and
- (c) volume of futures traded.

In addition, these details will be distributed to Quote Vendors, marked with the trade type indicator “J”.

For each Exchange Contract, the cumulative volume of futures traded as the futures leg of basis trades/asset allocations during the day will also be published.

4.19.19 Both the long and short positions associated with the futures leg(s) of a basis trade will be entered into TRS and matched under the basis trade executing member’s mnemonic.

4.19.20 Upon request by the Market Supervision Department the basis trade executing member must produce satisfactory evidence that the basis trades have been organised in accordance with the Rules and Trading Procedures. Basis trade executing members must, therefore, be in a position to supply documentary evidence in connection with a basis trade, including, but not limited to, evidence confirming the cash leg of basis trades.

Basis trade executing members may also be required from time to time by the Market Supervision Department to request, and copy to the Exchange, confirmation of the details of the cash leg of a basis trade where another party was responsible for the execution of the cash leg.

Failure to provide satisfactory evidence in accordance with these Trading Procedures may result in the instigation of disciplinary action under Section 5 of the Rules. Sanctions available under Section 5 of the Rules include the suspension of some/all of a member’s rights.