

February 22, 2012

BY ELECTRONIC SUBMISSION AND OVERNIGHT DELIVERY

Mr. David Stawick
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: **Mandatory Clearing Determination for Pre-Enactment Swaps and Swaps Cleared as of February 1, 2012, CME Submission No. 12-053**

Dear Mr. Stawick:

This is in response to Sarah Josephson's letter of February 1, 2012 to Kim Taylor, president of the clearing house division of Chicago Mercantile Exchange Inc. ("CME Clearing"), with respect to the CFTC's mandatory clearing determinations. Among other things, the letter requests derivatives clearing organizations ("DCOs") to agree to further extend the deadline for a determination by the CFTC on pre-enactment swaps until the review process outlined in Regulation 39.5(b) is completed. CME Clearing agrees to such an extension, per the CFTC's request.

For the sake of clarity, we thought it best to identify those pre-enactment swaps that CME Clearing continued to accept for clearing as of February 1, 2012 (the relevant date specified in Ms. Josephson's letter for purposes of this submission). Those "swaps" (utilizing the CFTC's proposed definition of that term) consist of the following:

- Credit Default Swaps ("CDS"): CDX Indices (IG 12 and IG 13, 5-year tenors)
- Denatured Fuel Ethanol Forward Month Swaps, and Cash-Settled Options on those swaps
- Freight Route Forwards
- Grain Calendar Swaps (corn, soybean and wheat)
- Equity Index Swaps:
 - S&P GSCI Excess Return ("ER") Index Swaps and Index Forwards
 - S&P GSCI Gold ER Index Swaps and Crude Oil ER Index Swaps
 - S&P GSCI ER Index Forward Swaps (2-Month and 3-Month)
 - Dow Jones-UBS Commodity Index Swaps
 - Dow-Jones Index Forward Swaps (2-Month and 3-Month)

Since the date of enactment of the Dodd-Frank Act, CME Clearing began clearing other CDS CDX Indices, and we are seeking a mandatory clearing determination for CDX North American Investment Grade series 9 and forward (including all future on-the-runs), and High Yield series 11 and forward (including all future on-the-runs). Also since Dodd-Frank was enacted, CME Clearing began clearing certain interest rate swaps (IRS). We are seeking a mandatory clearing determination for all non-option interest rate swaps denominated in a currency cleared by any qualified DCO.¹ Also included in this submission are Fertilizer Swaps, which CME Clearing accepted for clearing as of February 1, 2012, but not as of the enactment date of the Dodd-Frank Act.

In addition, as of February 1, 2012, but not as of the date of enactment of the Dodd-Frank Act, CME Clearing listed for clearing 38 OTC FX products that fall within the CFTC proposed definition of "swap". We are not seeking a mandatory clearing determination for these products, some of which we understand Treasury may exempt from a central-clearing requirement under its Dodd-Frank authority. For these reasons, CME's OTC FX products are not part of this submission.

Pursuant to Regulation 39.5(b)(3)(i), we hereby state that CME Clearing is eligible to accept each swap and each group, category, type and class of swaps that is the subject of this submission. If the CFTC determines that each such swap and group, category, type and class of swap is required to be cleared, CME Clearing will be able to maintain compliance with the 15 DCO core principles set forth in section 5b(c)(2) of the Commodity Exchange Act, and the regulations promulgated thereunder. In accordance with Regulation 39.5(b)(3)(ii)-(viii), we are providing the following information in support of this submission:

39.5(b)(3)(ii)(A): Outstanding Notional Exposures, Trading Liquidity and Pricing Data

We have enclosed an Excel spreadsheet with information regarding the relevant products' outstanding notional exposures, trading liquidity and pricing data (as applicable) at CME Clearing, as of February 1, 2012. This document has been marked for Confidential Treatment.²

39.5(b)(3)(ii)(B): Rule Framework, Capacity, Operational Expertise and Resources, Credit Support Infrastructure

In general, the rule framework for the products that are the subject of this submission can be found in the rule books of CME, the Chicago Board of Trade ("CBOT") for Grain Calendar and Ethanol Swaps, and the New York Mercantile Exchange ("NYMEX") for Freight Route Forwards. Each of these rule books is available at <http://www.cmegroup.com/market-regulation/rulebook/index.html>.

Attached is a product-specifications document that describes each "swap" that is part of this submission. The document includes links to pertinent product chapters in the CME, CBOT and NYMEX rule books.³ Also relevant to the rule framework are three CME Clearing House Manuals (one for CDS, one for IRS, and one for all remaining products), copies of which are enclosed and which have been designated for

¹ We believe that the CFTC should clarify that any swap (or group, category, type or class of swap) subject to mandatory clearing based on a submission made by one DCO may be cleared by any other qualified DCO. The legislative intent of the Dodd-Frank Act and the open-access provisions therein are strong authority for the proposition that any swap determined to be subject to mandatory clearing may be cleared by any qualified DCO.

² For purposes of this submission, we have separated the documents that are marked for Confidential Treatment from those that are not so marked.

³ To utilize the links in the attached document, place your cursor over the underlined link and press the Control button on your computer. This will turn the cursor into a hand icon and activate the link.

Confidential Treatment.⁴ The enclosed document entitled *CME Clearing Financial Safeguards* contains information regarding CME Clearing's capacity, expertise, resources and financial safeguards system.

39.5(b)(3)(ii)(C): Effect on Mitigation of Systemic Risk

While markets in certain OTC derivatives asset classes continued to function well during the recent financial crisis, the crisis demonstrated the potential for systemic risk arising from the interconnectedness of OTC derivatives market participants and the limited transparency of bilateral counterparty relationships. To help mitigate systemic risk in the OTC derivatives markets, the G-20 Leaders agreed that all standardized OTC derivatives contracts should be cleared through central counterparties by the end of 2012. One of the key goals of the Dodd-Frank Act is the reduction of systemic risk through the use of central clearing for OTC derivatives.

As a central counterparty, CME Clearing interposes itself between counterparties to the swaps (and other derivatives products) that it clears, becoming the buyer to every seller and the seller to every buyer. For each swap that it clears, CME Clearing provides all clearing house services, including a mark-to-market function, on a daily basis. Depending upon the particular asset class, CME Clearing may standardize contract-critical dates (e.g., start dates, last trade dates, expiry dates) and other contract terms. This may enable customers who hold positions to liquidate or to adjust positions simply by buying back or selling the relevant contracts. The associated benefits are considerable:

- *Centralized clearing.* Clearing OTC swaps through CME Clearing allows market participants to free up counterparty credit lines. The daily mark-to-market process employed by CME Clearing enhances customer risk management.
- *Operational efficiencies.* Centralized clearing of swaps reduces operational burdens in several ways. Standardization and centralized clearing enables consolidation of collateral management and cash flows and eliminates the need for novations or tear-ups.
- *Ease of position adjustment.* In non-cleared markets, the only means to completely eliminate the risk of a swap is to (i) enter into a tear-up agreement with the swap counterparty, or (ii) enter into a novation (i.e., find another entity willing to assume its side of the swap). In either case, the tear-up or the novation must be approved by the bilateral swap counterparty. For most asset classes, central clearing may be used to offset by a contra trade.

As further described in the enclosed document entitled *CME Clearing Financial Safeguards*, and as reflected in the enclosed Clearing House Manuals, CME Clearing has the necessary resources available to clear the swaps that are the subject of this submission. With respect to margining in particular, please see Chapter 7 of the IRS Manual and the CDS Manual, and the enclosed document entitled *CME SPAN* (the margin methodology utilized for our Grain Calendar Swaps, Ethanol Swaps, Equity Index Swaps, Freight Route Forwards and Fertilizer Swaps). With regard to the size of the OTC markets for the products that are the subject of this submission, please see the enclosed copy of Table 19 (Amounts of outstanding OTC derivatives) from the BIS Quarterly Review, December 2011.

39.5(b)(3)(ii)(D): Effect on Competition – Fees and Charges

We have enclosed documents regarding fees and charges for the "swaps" that are the subject of this submission.

⁴ Portions of the CME, CBOT and NYMEX rule books, and the enclosed Clearing House Manuals, will be revised, as necessary and appropriate, to comply with new CFTC DCO regulations that go into effect on May 7 and November 8, 2012.

39.5(b)(3)(ii)(E): Reasonable Legal Certainty in DCO or Clearing Member Insolvency

The bankruptcy of a DCO would be governed by subchapter IV of Chapter 7 of the U.S. Bankruptcy Code (11 U.S.C. §§ 761-767), and by the CFTC's Part 190 bankruptcy regulations. Also relevant in the event that CME were to enter into bankruptcy proceedings is CME Rule 818 (Close-Out Netting), a copy of which is enclosed.

The bankruptcy of a clearing member that is a U.S. futures commission merchant ("FCM") would be governed by subchapter IV of Chapter 7 of the U.S. Bankruptcy Code (11 U.S.C. §§ 761-767) and the CFTC's Part 190 bankruptcy regulations. If an FCM is also registered as a broker-dealer, certain aspects of its insolvency proceeding may also be governed by the Securities Investor Protection Act. For further details regarding the legal certainty provided under the relevant U.S. insolvency laws, please see pages 17-18 of the enclosed *CME Clearing Financial Safeguards* document.

39.5(b)(3)(iii): Product Specifications

With regard to product specifications for the "swaps" that are included in this submission, please see the attached product-specifications document and the enclosed Clearing House Manuals, including but not limited to, in the CDS Manual, Chapter 4 Appendix 1 – Cleared CDS Trade Confirmation, and Chapter 9, Credit Event/Succession Event Processing, and in the IRS Manual, Chapter 4 Appendix 1 – Cleared IRS Trade Processing.

39.5(b)(3)(iv): Participant Eligibility Standards

We have enclosed a *Summary of Requirements* for clearing membership, and the *CME Handbook for OTC Clearing Membership*. In addition, please see CME Rule 8F004 (OTC Clearing Member Obligations), 8G04 (IRS Clearing Member Obligations) and 8H04 (CDS Clearing Member Obligations). Certain of these rules and requirements will be revised, as necessary and appropriate, to comply with new CFTC regulations regarding Participant and Product Eligibility, which go into effect on May 7, 2012.

39.5(b)(3)(v): Pricing Sources, Models and Procedures

We have enclosed documents concerning settlement procedures for certain swaps that are the subject of this submission. Please also see Chapter VII (Daily Settlements and Asset Management) of the Clearing House Manual of Operations, and Chapter 8 (End of Day Valuations) of the CDS and IRS Manuals. In addition, we have enclosed a copy of a services agreement between CME and Credit Market Analysis Ltd. relating to CME's CDS products, which has been marked for Confidential Treatment.

39.5(b)(3)(vi): Risk Management Procedures

We have enclosed documents concerning CME Clearing's risk management procedures, which have been marked for Confidential Treatment. In addition, please refer to the Clearing House Manual of Operations, including but not limited to Chapters VI (Performance Bonds/Margin) and VII (Daily Settlements and Asset Management); the CDS Manual, including but not limited to Chapters 7 (CDS Margining), 8 (End of Day Valuations), 10 (Guaranty Fund Calculation) and 11 (CDS Default Management); and the IRS Manual, including but not limited to Chapters 7 (Interest Rates Margining), 8 (End of Day Valuations), 9 (Financial Safeguards – Guaranty Fund Calculation) and 11 (Interest Rate Swaps Default Management). Certain of these materials will be revised, as necessary and appropriate, to comply with new CFTC regulations regarding Risk Management, which go into effect on May 7, 2012.

39.5(b)(3)(vii): Applicable Rules, Manuals, Policies and Procedures

Links to applicable rule books are included in this submission, and copies of Clearing House Manuals and relevant policies and procedures are enclosed.

Mr. David Stawick

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39.5(b)(3)(viii): Notice of Submission

Notice of this submission (without enclosures, many of which have been designated for Confidential Treatment) has been concurrently posted on CME's web site at <http://www.cmegroup.com/market-regulation/rule-filings.html>.

Because of the large volume of enclosures with this letter, we are sending you a copy of the letter with a complete set of the enclosures via overnight courier. Should you have any questions regarding this submission, or if any additional information is required, please contact me at (312) 338-2483 or via e-mail at lisa.dunsky@cmegroup.com.

Sincerely,



Lisa Dunsky
Director and Associate General Counsel

Enclosures

cc: Sarah Josephson (by e-mail and overnight courier, w/ encl.)