



Via Portal Submission

November 1, 2019
MGEX Submission No. 19-29

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581

RE: Rule Certification Submission Pursuant to Regulation 40.6(a); Amendments to MGEX Rules

Dear Mr. Kirkpatrick:

Pursuant to Commodity Exchange Act (“CEAct”) Section 5c and Commodity Futures Trading Commission (“CFTC” or “Commission”) Regulation 40.6(a), the Minneapolis Grain Exchange, Inc. (“MGEX” or “Exchange”) hereby certifies that the new MGEX Rules attached complies with the CEAct and the Commission regulations promulgated thereunder. MGEX further certifies that the submission and pending changes to the MGEX Rules have been posted on the Exchange website at the following link: <http://www.mgex.com/regulation.html>. All capitalized terms used but not defined herein have the meanings assigned to them in the MGEX Rules.

Overview of Amendments

MGEX is a recognized third-country central counterparty (“TC-CCP”) by the European Securities and Markets Authority (“ESMA”) in accordance with Article 25 of the European Markets Infrastructure Regulation (EU) No 648/2012 (“EMIR”). In being recognized as a TC-CCP, the Exchange must meet certain equivalence conditions set forth by the European Commission’s (the “EC”) Implementing Decision (EU) 2016/377 of March 15, 2016 (the “Equivalence Decision”).

Under Article 1 of the Equivalence Decision, a DCO seeking recognition under EMIR is required to have certain internal rules and procedures that ensure initial margins are calculated and collected in accordance with the two following conditions:

- (1) that initial margins for clearing members’ proprietary positions in derivative contracts are calculated and collected using a two-day liquidation period; and

(2) that initial margin models include measures designed to mitigate the risk of procyclicality.

In addition, the DCO is required to maintain pre-funded financial resources to cover a default of at least two clearing members creating the largest exposures in extreme but plausible conditions.¹

Since the Equivalence Decision was implemented in 2016, MGEX has only cleared derivative contracts that are based on underlying agricultural products, and as a result, has been afforded an exclusion under Article 2 to the required conditions above.² However, the Exchange intends to clear a derivatives contract that is not agricultural in nature, thus necessitating the addition of MGEX Rules 2105.01., 2106.02., and 2106.03. (collectively, the “New Rules”) to meet the equivalence conditions and remain a recognized TC-CCP by ESMA.

Rule Amendments

Proprietary Account Minimum Liquidation Period

New Rule 2106.02. satisfies the first condition of Article 1 of the Equivalence Decision by ensuring performance bond requirements with respect to Clearing Member proprietary positions are calculated and collected using a liquidation period of not less than two days calculated on a net basis. This Rule does not apply to positions in agricultural commodity derivative contracts that meet the exclusion criteria of Article 2.

Measures to Mitigate Procyclicality

The addition of Rule 2106.03. requires the Clearing House to establish performance bond requirements designed to limit the likelihood of procyclicality and mitigate costly adjustments to performance bond requirements during periods of high market volatility, thus meeting the second required condition under Article 1. Likewise, this Rule does not apply to positions in agricultural contracts excluded under Article 2.

Funded Financial Resources

New Rule 2105.01. was added to fulfill the final Article 1 condition of the Equivalence Decision and requires the Clearing House to maintain funded financial resources sufficient to enable it to meet its financial obligations to Clearing Members notwithstanding a default by the two clearing members with the largest possible combined loss to the Clearing House in extreme but plausible market conditions. This Rule also clarifies that for purposes of calculating financial resources, Clearing Members under control of or under common control with another Clearing Member are to be considered a single

¹ See Article 1 of the Equivalence Decision, available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016D0377&from=EN>.

² See Article 2(1) of the Equivalence Decision, setting forth that agricultural commodity derivative contracts fulfilling certain conditions are not subject to Article 1 requirements.

Clearing Member.

DCO Core Principles

In connection with adding the New Rules, the Exchange has reviewed the core principles for derivatives clearing organizations (“DCO Core Principles”) and has determined that the amendments comply with the requirements of such principles. During the review, MGEX identified the following DCO Core Principles as potentially being impacted:

- *DCO Core Principle B – Financial Resources:* CFTC Regulation 39.33(a)(1) requires systemically important DCOs and subpart C DCOs that are systemically important in multiple jurisdictions or involved in activities with a more complex risk profile to maintain financial resources sufficient to enable it to meet its financial obligations to its clearing members notwithstanding a default by the two clearing members creating the largest combined loss to the DCO in extreme but plausible market conditions. As a subpart C DCO that does not meet the above definition, MGEX has been a “cover 1” DCO under CFTC Regulation 39.33(c)(1) rather than a “cover 2” DCO until now. With Rule 2105.01. being added to the Exchange’s Rulebook to satisfy the conditions of the EC’s Equivalence Decision, MGEX will become a “cover 2” DCO at the time these Rules are made effective. This change will also be reflected in internal policies and procedures and in MGEX’s quarterly financial resources filings with the Commission.
- *DCO Core Principle D – Risk Management:* CFTC Regulation 39.13 requires DCOs to possess certain risk management tools and procedures, including establishing risk-based initial margin requirements and minimum liquidation periods. In accordance with the Equivalence Decision, MGEX has adopted new Rule 2106.02. to ensure at least a two-day liquidation period in calculating and collected clearing member’s proprietary positions. Following the implementation of the New Rules, although MGEX’s margin methodology will remain substantially the same, MGEX will calculate and collect margin for Clearing Member proprietary accounts utilizing a two-day liquidation period for products that are not exempt under the Equivalence Decision (i.e., non-agricultural based products). If margin level increases are necessary, the Clearing House will adjust margin levels accordingly in compliance with its Rules and internal policies.

Additionally, the Exchange has created Rule 2106.03. to mitigate procyclicality pursuant to the Equivalence Decision. After implementation of the New Rules, the Clearing House will utilize selected anti-procyclicality measures to ensure MGEX remains in compliance with the requirements set forth in the New Rules.

Neither of the above new Rules apply to positions in agricultural commodity derivative contracts as excluded under Article 2 of the Equivalence Decision. As such, the anticipated impact to the Exchange or market participants with respect to agricultural-based products, including Hard Red Spring Wheat futures and options, will be minimal to none.

- *DCO Core Principle L – Public Information:* Core Principle L requires DCOs to provide market participants with sufficient information to enable them to identify and evaluate accurately the risks and costs associated with using the services of the DCO and to have clear and comprehensive rules and procedures. The Exchange Rules, as amended by the addition of the New Rules, will continue to be posted publicly on the MGEX website in satisfaction of this core principle.

Pursuant to MGEX Bylaw 204.01., the MGEX Board of Directors unanimously approved the attached amendments to the MGEX Rulebook on September 16, 2019. There were no substantive opposing views expressed by the Board of Directors, nor is the Exchange aware of any substantive opposing views with respect to this filing.

The attached amendments are to be effective on November 18, 2019. If there are any questions regarding this submission, please contact me at (612) 321-7144 or mleisen@mgex.com. Thank you for your attention to this matter.

Sincerely,

A handwritten signature in black ink that reads "Matthew Leisen". The signature is written in a cursive style with a long horizontal line extending from the end of the name.

Matthew D. Leisen
Associate Counsel, MGEX Clearing

EXHIBIT A

The following MGEX Regulations are to be amended. Additions are underlined while deletions are ~~marked through~~.

CHAPTER 21 CLEARING HOUSE RULES

- 2100.00. Requirements For Clearing
- 2100.01. Electronic Trading System Clearing
- 2100.02. Clearing Privileges
- 2100.03. Clearing Member Risk Management
- 2101.00. Settlement Banks Available For Use
- 2102.00. Acceptance Of Give-Up Trades
- 2103.00. Order Of Delivery
- 2104.00. Deadlines, Fees And Fines
- 2104.01. Clearing Fee
- 2105.00. Security Deposit
- 2105.01. Funded Financial Resources
- 2106.00. Margins
- 2106.01. Protection Of Customer Funds
- 2106.02. Proprietary Account Minimum Liquidation Period
- 2106.03. Measures to Mitigate Procyclicality
- 2107.00. Finality Of Settlement
- 2108.00. Liquidity Event
- 2108.01. Requirement To Establish Uncommitted Repurchase Agreement
- 2109.00. Clearing Member Financial Emergency
- 2109.01. Clearing Member Insolvency
- 2109.02. Protection Of Clearing House: Default By A Clearing Member
- 2109.03. Losses Borne By MGEX: Application of Funds
- 2109.04. Management of Default And Subsequent Clearing Cycles
- 2109.05. Collateral To Be Restored
- 2110.00. Clearing Members: Assessments
- 2110.01. Memberships: Special Assessments And Issuance
- 2111.00. Voluntary Contributions
- 2112.00. Haircut Settlement Cycles
- 2113.00. Cooling Off Period And Multiple Defaults
- 2114.00. Partial Tear-Ups
- 2115.00. Termination of Contracts
- 2116.00. Details of Implementation And Auctions
- 2117.00. Use Of Customer Gross Margin Files
- 2118.00. No Action; Limitation Of Liability
- 2119.00. Recovery of Loss
- 2120.00. Limited Recourse And Non-Petition
- 2121.00. Close-Out Netting And Offset

2105.01. FUNDED FINANCIAL RESOURCES.

The Clearing House will maintain funded financial resources sufficient to enable it to meet its financial obligations to Clearing Members notwithstanding a default by the two Clearing Members creating the largest combined loss to the Clearing House in extreme but plausible market conditions. If a Clearing Member controls another Clearing Member or is under common control with another Clearing Member, the affiliated Clearing Members will be considered a single Clearing Member for purposes of calculating financial resources under this Rule.

2106.02. PROPRIETARY ACCOUNT MINIMUM LIQUIDATION PERIOD.

With respect to Clearing Member proprietary positions, the Clearing House will ensure performance bond requirements are calculated and collected using a liquidation period of not less than two days calculated on a net basis. This Rule does not apply to positions in agricultural commodity derivative contracts that meet the exclusion criteria established in Article 2 of the European Commission's Implementing Decision 2016/377, dated March 15, 2016.

2106.03. MEASURES TO MITIGATE PROCYCLICALITY.

The Clearing House will establish performance bond requirements designed to limit the likelihood of procyclical changes in such requirements and mitigate costly and disruptive adjustments to performance bond requirements in periods of high market volatility. When calculating performance bond requirements, the Clearing House will include measures designed to limit procyclicality that are equivalent to at least one of the options listed in Article 1, paragraph 2(b) of the European Commission's Implementing Decision 2016/377, dated March 15, 2016. This Rule does not apply to positions in agricultural commodity derivative contracts that meet the exclusion criteria established in Article 2 of the European Commission's Implementing Decision 2016/377, dated March 15, 2016.