

March 23, 2011

The Honorable Gary Gensler  
Chairman  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, N.W.  
Washington, DC 20581

**Re: CME Group Views On Proposed Sequencing for Dodd-Frank Implementation**

Dear Chairman Gensler:

We appreciate your initiative seeking input on the sequencing and timing of rulemaking under Dodd-Frank. In your recent remarks on this subject, you grouped the rulemakings into three categories, labeled “early,” “middle,” and “late.” We agree with many but not all aspects of this proposed sequencing. The following is a high level summary of our proposed sequencing, followed by a more detailed explanation. In general, we recommend that in Phase I (early), the Commission should focus on the rules that are necessary to bring the previously unregulated swaps market into a well-developed regulatory framework like that which exists today for the U.S. futures markets. The regulatory framework for increasing transparency and reducing systemic risk in OTC derivatives was the central focus of the Dodd-Frank Act and a key issue in the economic and financial crisis. This set of major rulemaking represents the largest amount of change for the industry and cannot be satisfactorily addressed in a timely manner if key elements of the regulatory framework for swaps clearing are not determined until the middle or late stages of the rulemaking process. As such, it should have the highest priority.

Phase II should deal with the so-called “exchange-trading” requirements for swaps, including the definition and requirements for swap execution facilities, business conduct standards for swap dealers and requirements for swap data repositories. While we support efforts to increase transparency, we believe the so-called “exchange-trading” requirements and definitions and requirements for swaps trading on swap execution facilities and DCMs is less critical in time priority than the clearing mandate and related clearing rules.

In contrast to the foregoing, the exchange-traded derivatives markets operated flawlessly and the proposed rules affecting DCMs and position limits represent incremental changes to an already robust and well-developed regulatory scheme that has been in place for many decades. We recommend that the Commission leave for Phase III (late) or later those rulemakings that deal with DCMs and position limits.

## PHASE I (EARLY)

- 1. Product Definitions.** Product definitions need to be finalized before July 15 because the exemptions contained in the Commodity Exchange Act (CEA) that permit the OTC swaps market to operate today will be repealed as of July 15, e.g., CEA Section 2(h) pursuant to Dodd Frank. In our view it is essential that this rulemaking be proposed in the very near future and finalized and made effective no later than July 15, 2011 in order to avoid reintroducing legal uncertainty for market participants – a problem that was solved by Congress more than a decade ago when its adopted the Commodity Futures Modernization Act of 2000. Additionally, clarifying the definition of “swap” is necessary in order to provide meaning to other rulemakings, in particular those related to registration and regulation of market participants and reporting and recordkeeping rules. Indeed, without a clear definition of “swap,” market participants will not know whether they are subject to certain regulations or what their obligations under those regulations are. The lack of certainty regarding the product definition hinders the ability of market participants to provide meaningful comment on the related rulemakings.
- 2. Rules Governing Swaps Subject to the Clearing Mandate.** The rules relating to the clearing mandate should be finalized in the early phase. In terms of industry readiness for this transition, it is worth noting a recent comprehensive study by UBS (March 10, 2011) of OTC derivatives market participants to gauge the readiness on the buy side for this transition. Their study found that firms are increasingly preparing to clear OTC derivatives, reporting that 73% of firms are already clearing or preparing to clear, 71% expect to begin clearing within 12 months, and 82% expect the majority of their OTC business will be cleared within two years.

As discussed earlier, the reduction of systemic risk in OTC markets is predicated on a complete versus partial regulatory framework for swaps clearing. Among the numerous issues raised by the proposed rules is how to implement this mandate most efficiently. We believe the best approach would be to adopt them on a class-by-class basis, rather than a product-by-product basis. It is critical that the clearing mandate apply simultaneously to dealer-to-customer and dealer-to-dealer trades in order to ensure a level playing field environment for all market participants. We would also urge the Commission to give priority to approving classes of U.S. dollar denominated swaps given the significant percentage of transactions therein made by U.S. customers, swap dealers and major swap participants. In addition, we believe the Commission should determine in Phase I the scope of the end user exemption from the end user clearing requirement, the rules governing the segregation of collateral associated with swap positions and the bankruptcy rules that would govern in the event of clearing member or DCO insolvency, and rules pertaining to DCO conflicts of interest and core principle obligations, as well as margin and capital requirements and rules pertaining to cross margining. Given preliminary industry estimates that capital and margin requirements for swaps clearing could range from several hundred billion to potentially a trillion dollars, the margin, capital and cross margining rules are critical to ensure that its proposals are economically justified.

3. **Rules Governing New Rules/New Contracts for Clearing Houses and Exchanges.** We agree with the Chairman that the Part 40 rules are among the most important rules to finalize, in particular, as they relate to clearing houses as these are the rules that clearing houses must comply with when submitting rules to the Commission that would govern swaps they accept for clearing voluntarily. We recommend that the Commission clarify that clearing houses can begin clearing immediately upon self-certification of those products that they can adequately price from a risk perspective so long as the certifications comply with pre-established certification requirements.
4. **Reporting Rules.** We agree that swap reporting rules must be finalized before the Commission can adopt other of its proposed rules, such as position limits. We would add that, not only do these rules need to be finalized and effective, but the Commission needs to be able to analyze data collected pursuant to these rules before promulgating certain other rules, including position limits rules.
5. **Anti-Disruptive Trade Practices/Anti-Manipulation Authority.** To the extent that the Commission contemplates adopting final rules that would expand the scope of its current authority in terms of conduct that would be unlawful, we agree that the Commission should adopt final rules as soon as possible so that market participants will have certainty as to what type of conduct is permissible. Similarly, we believe that the Commission also must adopt final rules related to its new anti-disruptive trading practice authority no later than July 15. At a minimum, the Commission must adopt rules clarifying the scope of the conduct expressly prohibited by the CEA, *i.e.*, violating bids and offers, demonstrating intentional or reckless disregard for the orderly execution of transactions during the closing period, or spoofing.

## PHASE II (MIDDLE)

1. **Swap Data Repository and Swap Execution Facility Rules.** With respect to these rules, significant lead time before the effective date is necessary to allow market participants adequate time to develop/make changes to their technology or otherwise modify their operations in order to comply with the Commission's final rules. More importantly, there are material technology issues that need to be ironed out amongst market participants. Additionally, we recommend that real time reporting and block trading rules be adopted in tandem with the swap data repository and swap execution facility rules. These rules are intertwined and collectively will comprise the rules governing the execution of and related reporting of swaps. The infrastructure created by market participants to address each of these rules individually likely will be shaped by other rules mentioned in this middle group.
2. **Business Conduct Standards for Swap Dealers and Major Swap Participants.** Rulemakings addressing topics such as trading documentation, confirmation, portfolio reconciliation and compression requirements, recordkeeping, conflicts of interest and risk management should be

implemented in conjunction with the swap execution and reporting related rules. It would also be appropriate to adopt at this time rules governing segregation requirements for uncleared swaps.

### PHASE III (LATE)

1. **Rules Governing Futures Markets.** To the extent that the Commission believes that new rules are necessary and appropriate in light of Title VII, those rules should be addressed after the Commission has finalized all rules necessary to bringing the previously unregulated swaps market into the fold of a well-established regulatory regime.
2. **Position Limits.** Aside from the rulemaking being unnecessary generally or unnecessary for establishing a regulatory framework for the swaps market specifically, we believe that the Commission needs to collect and analyze relevant swap data in order to set and enforce any limits, which information it does not have access to at this time.

As always, we greatly appreciate your consideration of our views and would be happy to answer any questions you may have regarding our sequencing recommendations. We believe our recommendations will enhance the implementation process by ensuring a complete understanding of the rules pertaining to swap clearing in Phase I, a complete understanding of swap trading and reporting requirements in Phase II and a better opportunity to formulate the Commission's position limits proposals in Phase III based on the framework and data that will be completed during Phases I and II.

Sincerely,



Executive Chairman



Chief Executive Officer