CME Group

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July 1, 2011

VIA ELECTRONIC MAIL

David Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
secretary@cftc.gov

Re: Comments on Proposed Order regarding Effective Date for Swap Regulation

Dear Mr. Stawick:

CME Group Inc. ("CME Group")[1], on behalf of its four designated contract markets ("Exchanges" or "DCMs"), appreciates the opportunity to provide the Commodity Futures Trading Commission ("CFTC" or "Commission") with its comments on the Commission's proposed order (the "Proposed Order")[2] regarding the effective dates of various key provisions under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or "DFA"). We support the overarching goals of Dodd-Frank to reduce systemic risk through central clearing and exchange trading of derivatives, to increase data transparency and price discovery and to prevent fraud and market manipulation. Unfortunately, as the Commission is aware, Dodd-Frank left many important issues to be resolved by the regulators with little or ambiguous direction and set unnecessarily tight deadlines on rulemakings by the agencies charged with implementation of the Act.

The Commission has not been able to satisfy the arbitrary and tight deadlines set by Congress for many of the rulemakings contemplated by DFA. Significantly, the Commission has not yet adopted final rules for product or entity definitions – including rules further defining "swap." In the absence of a final definitional rulemakings by July 16, 2011, we believe that there will be great legal uncertainty for the markets. Because the market needs legal certainty akin to that provided by the Commodity Futures

[1] CME Group, the world's largest and most diverse derivatives marketplace, consists of four separate Exchanges: the Chicago Mercantile Exchange, Inc. ("CME"), the Board of Trade of the City of Chicago, Inc. ("CBOT"), the New York Mercantile Exchange, Inc. ("NYMEX") and the Commodity Exchange, Inc. ("COMEX"). These Exchanges offer the widest range of benchmark products available across all major asset classes, including futures and options based on interest rates, equity indexes, foreign exchange, energy, metals, agricultural commodities and alternative investment products.

CME also includes CME Clearing, one of the largest central counterparty clearing services in the world, which provides clearing and settlement services for exchange-traded contracts, as well as for over-the-counter derivatives transactions through CME ClearPort®.

The CME Group Exchanges serve the hedging, risk management and trading needs of our global customer base by facilitating transactions through the CME Globex® electronic trading platform, our open outcry trading facilities in New York and Chicago, as well as through privately negotiated transactions.

[2] 76 Fed. Reg. 35372 (June 17, 2011).

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Modernization Act of 2000 ("CFMA") to operate without disruption until the Commission completes its rulemaking tasks under DFA, we generally support the Proposed Order. We agree with Commissioner Sommers that the Commission's objective "should be to craft relief that is not confusing or convoluted, and that clearly allows swap market participants to continue operating as they are today and have been since 2000."[3] We believe that the Proposed Order could be enhanced in this regard. To this end, as discussed in more detail below, we recommend that the Commission clarify certain ambiguities raised by the Proposed Order and grant additional relief to enhance legal certainty.

I. Background

The Proposed Order divides the provisions of Dodd-Frank into four categories. Category 1 provisions, which explicitly require a final rulemaking from the Commission in order to become effective, do not take effect on July 16. Category 2 provisions take effect on July 16, but, to the extent that they rely on Category 1 provisions, have no legal effect. Included in Category 3 are statutory provisions in the existing Commodity Exchange Act ("CEA") that are repealed on July 16. The provisions in Category 4 will take effect on July 16. The Commission has published lists reflecting its views as to which provisions fall into Categories 1, 3 and 4; the Commission has not published such a list of Category 2 provisions. With the exception of Category 4 provisions, the Proposed Order would exempt market participants from compliance with these individual provisions of DFA until the earlier of December 31, 2011 or a final rule implementing such provisions.

We agree with Commissioners Sommers and O'Malia that the relief contained in the Proposed Order is not ideal. In particular, the expiration of exemptive relief on December 31, 2011 – less than 6 months from the date of any final order – is likely to require similar Commission action again just a few months from now in order to avoid plaguing the markets with the legal uncertainty the Commission aims to avoid with the Proposed Order. In addition to recommending that the exemptive relief expire on the sooner of July 16, 2012 or final, effective rules governing the provision at issue, we recommend that the Commission: (i) interpret Section 754 of Dodd-Frank to include Category 2 provisions, thereby treating Category 1 and 2 provisions the same under the Proposed Order; (ii) provide 4(c) relief to Exempt Commercial Markets ("ECMs") and Exempt Boards of Trade ("EBOTs") that begin operating on or after July 16; and (iii) confirm that additional exemptive relief is not needed for a DCM to list swaps for trading on or after July 16 so long as those products are regulated as futures products and market participants trading those products are regulated as futures market participants.

II. Detailed Comments

A. <u>Category 1&2 Provisions</u>

Section 754 of Dodd-Frank provides that, unless otherwise provided, the provisions of Title VII shall take effect "on the later of 360 days after the date of the enactment . . . or, to the extent that a provision of this subtitle requires a rulemaking, not less than 60 days after publication of the final rule or regulation implementing such provision." Certain provisions of Dodd-Frank contain language expressly requiring a rulemaking; the Commission has characterized these provisions as Category 1 provisions. Other provisions require a rulemaking because they reference a term that is required to be further defined by Commission rulemaking; the Commission has characterized these as Category 2 provisions. Both "require a rulemaking" within the meaning of Section 754.

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[3] Opening Statement of Commissioner Sommers, Open Meeting to Consider Effective Dates of Provisions in the Dodd-Frank Act (June 14, 2011), available at **http://www.cftc.gov/PressRoom/SpeechesTestimony/sommersstatement061411.html**.

Without final rulemakings addressing terms that require further definition by Commission rulemaking, it is impossible to interpret Category 2 provisions or to decipher market participants' obligations thereunder. Moreover, the Commission's Proposed Order as it relates to Category 2 provisions is unnecessarily complicated, creating ambiguity as to which provisions fall within Category 2 and when these provisions will become effective. The Commission has failed to provide the public with a list of provisions that it considers to be within Category 2. Instead, it leaves to the public guesswork to figure out which provisions fall within Category 2. Further, to add to the ambiguity, it appears that the Commission contemplates that sub-provisions under the same statutory section may fall within different Categories, resulting in different effective dates and different legal treatment. The proposed approach does not work and rather than clarifying for market participants their obligations under DFA as of July 16, it is a catalyst for confusion. We submit that the Commission could enhance legal certainty by simply providing that, as with Category 1 provisions, Category 2 provisions do not take effect until the Commission finalizes and makes effective the required definitional rulemakings.

B. Category 3 Provisions

The Commission lists as Category 3 provisions Sections 2(d), 2(e), 2(g), 2(h) and 5d of the current CEA. Collectively, these provisions have provided legal certainty to the over-the-counter ("OTC") market since the passage of the CFMA in 2000. Specifically, each provision sets forth an exemption or exclusion which, if satisfied, removes the transactions and the respective market participants from most provisions of the CEA and the CFTC's regulations. CFMA also provided that contracts executed pursuant to one of these exemptions or exclusions could not be held to be unenforceable as an illegal off-exchange futures contract pursuant to CEA Section 4(a). The repeal of these exemptions and exclusions is effective on July 16.

To avoid disruption to the OTC market after July 16, the Proposed Order provides the following with respect to these provisions. First, the Proposed Order clarifies that Part 35 of the Commission's regulations is unaffected by Dodd-Frank, and therefore transactions or contracts that meet Part 35 will continue to receive the exemptive relief provided for therein. Second, because Part 35 is not broad enough to provide the market with the scope of relief needed to operate without disruption after July 16, the Commission is proposing to use its authority under CEA Section 4(c) to grant temporary exemptive relief to transactions in exempt or excluded commodities (and any person or entity offering or entering into such transactions) from the CEA (other than the anti-fraud and anti-manipulation provision identified in the Proposed Order) that would otherwise comply with Part 35, notwithstanding that:

- the transaction may be executed on a multilateral transaction execution facility;
- the transaction may be cleared;
- persons offering or entering into the transaction may be eligible contract participants ("ECPs") as defined in the CEA prior to July 16;
- the transaction may be part of a fungible class of agreements that are standardized as to their material economic terms; and/or
- no more than one of the parties to the transaction is entering into the transaction in conjunction with its line of business, but is neither an ECP nor an eligible swap participant ("ESP"), and the transaction was not and is not marketed to the public.

In other words, so long as a transaction falls within Sections 2(d), 2(e), 2(g), 2(h) and 5d of the current CEA, the transaction will continue to be generally exempt from the CEA and the Commission's regulations until the sooner of December 31, 2011 or the repeal or replacement of Part 35 (or Part 32, where applicable). However, market participants may only rely on this relief to operate an ECM or an EBOT, which currently are governed by provisions in Sections 2(d) and 2(h) of the CEA, <u>if they are operating an ECM or EBOT on or before July 15, 2011</u>.

We support the Commission's efforts to provide temporary exemptive relief to the OTC market to allow it to continue operating without disruption until such time as the Commission has finalized the necessary rules for this market to operate under the provisions of DFA. The Commission's Proposed Order, in this regard, in our view is not as expansive as it needs to be to protect all markets and market participants. Specifically, the requirement that ECMs and EBOTs must be operational on or before July 15 in order to operate after July 16 unnecessarily constrains market participants from making changes to their existing business models after July 15 to come into compliance with provisions of DFA that will become effective after July 16 and any final rules that will become effective after July 16. For example, many voice-brokers in the energy space do not operate ECMs today. However, in order to continue doing business in compliance with the provision in Dodd-Frank requiring that swaps subject to the clearing mandate be traded on a DCM or swap execution facility ("SEF"), these voice-brokers may need to change their current business model. Voice-brokers will not know what will be required of SEFs in terms of operational and technological capabilities, self-regulatory obligations, capital requirements or access requirements and which products will be required to be traded on a SEF, and it would be unfair to require these market participants to embark on the process of altering their business model in the absence of clear guidance from the Commission as to what will ultimately be required of them. Accordingly, we recommend that the Commission modify the Proposed Order to afford market participants the ability to begin operating an ECM or EBOT after July 15. We can think of no harm resulting from extending the Commission's exemptive relief in this regard and believes that it would lessen the potential disruption in the marketplace; in fact, by extending the exemption, the Commission could be increasing the pool of potential SEFs once the Commission has finalized rules and made clear to market participants the regulatory requirements applicable to this new class of registered entity.

C. Category 4 Provisions

We support the Commission's Proposed Order as it relates to Category 4 provisions. Specifically, the Commission correctly notes that Category 4 provisions are self-effectuating and do not require a rulemaking or other relief from the Commission or staff in order for market participants to comply with the provisions as written. Notably, included within Category 4 are the core principles for DCMs and derivatives clearing organizations (DCOs). The Commission's determination that these provisions are self-effectuating and do not require rulemakings in order for DCMs or DCOs to comply with their statutory obligations is consistent with Congress's determination to maintain principles-based regulation for the U.S. derivatives market and to grant these self-regulatory organizations reasonable discretion in establishing the manner in which they comply with the core principles. In other words, DCMs and DCOs do not need a detailed, prescriptive set of rules to determine how to satisfy their statutory mandate.

At the Commission's Open Meeting on June 14, 2011 regarding the Proposed Order, Commissioner O'Malia asked whether the Proposed Order addressed the trading of swaps on a DCM. In response to this question, the CFTC's General Counsel stated that this was a "good question" and that the Commission was seeking guidance in comment period on whether the Commission should grant full exemptive relief for DCMs that would like to list swaps for trading. We submit that full exemptive relief is not necessary for DCMs that list swaps for trading on or after July 16 so long as those swaps are regulated as futures contracts and market participants comply with the obligations that would be imposed if trading futures contracts.

Indeed, nothing in the CEA prohibits a DCM from listing swaps for trading today. In fact, the current DCM core principles contemplate simply that the board of trade will list "contracts" for trading. *See e.g.,* Core Principle 2 (DCM shall establish rules governing the terms and conditions of "any contracts to be traded on the contract market"); Core Principle 3 (DCM shall list only "contracts that are not readily susceptible to manipulation"); and Core Principle 7 (DCM shall make available to market authorities, market participants, and the public accurate information concerning "the terms and conditions of the contracts"). The amendments made to the CEA, including DCM core principles, by Dodd-Frank do not change this analysis. To be sure, there is no provision in Dodd-Frank that could be viewed as an enabling provision granting DCMs a new right to list swaps for trading. Moreover, the above-referenced core principles remain unchanged. Therefore, the Commission should confirm that exemptive relief is not needed for a DCM to list swaps for trading on July 16 so long as those products and market participants trading those

products are regulated as futures products and those participants are regulated as futures market participants.[4]

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CME Group thanks the Commission for the opportunity to comment on this matter. We would be happy to discuss any of these issues with Commission staff. If you have any comments or questions, please feel free to contact me at (312) 930-8275 or **Craig.Donohue@cmegroup.com**, or Christal Lint, Director, Associate General Counsel at (312) 930-4527 or **Christal.Lint@cmegroup.com**.

Sincerely,

Craig S. Donohue

Craig S. Donohue

cc: Chairman Gary Gensler
Commissioner Michael Dunn
Commissioner Bart Chilton
Commissioner Jill Sommers
Commissioner Scott O'Malia

[4] To the extent that the Commission determines that exemptive relief is necessary for DCMs to list swaps for trading on July 16, the Commission should use its 4(c) exemptive authority to provide such relief. Using the Commission's exemptive authority in this manner would reduce systemic risk, enhance transparency in the swaps market and bring such markets under the full scope of the Commission's oversight. No regulatory or public purpose is served by requiring these markets to continue operating under the existing exemptions and exclusions in the CEA with virtually no oversight by the Commission or any other regulatory agency. In fact, this would run counter to the objectives of DFA.