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COMISIÓN NACIONAL DEL MERCADO DE VALORES
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REGISTRO DE SALIDA
Nº 2011150221

Ms.Nathalie Radhakrishman
US Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, D.C. 20581 -
UNITED STATES OF AMERICA

8th November 2011

Subject: Joint CFTC and SEC letter on swap and clearinghouse regulation

Dear Ms Radhakrishman,

I refer to the joint letter received from your Commission and from the SEC in August 2011 as well as to the call received from your Commission asking for our reply.

We apology for giving you our answer to the questions with some delay. Additionally, I would appreciate if you could give a copy of this reply to our colleagues from the SEC.

Should you have any further queries about the information attached, I would appreciate if you could get in touch directly to Mr Miguel Ángel Herrero, Senior Officer at Secondary Markets directorate in the CNMV. Contact details from him are the following: e-mail address maha@cnmv.es; phone + 34 91 585 4117.

Yours sincerely,

Antonio Mas
International Relations Director

Enc.-

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RESPONSE TO THE CONSULTATION ON OTC DERIVATIVES CLEARING

With reference to the CFTC questionnaire on OTC derivatives and, in particular, to your particular interest in understanding some issues on the clearing of energy swaps in Spain, you will find below some information on this regard. I hope you will find them convenient for the CFTC's purposes. Concerning the generic questions on the status of the derivatives regulation the CFTC's questionnaire is also interested in, please, note that Spain has not accomplished any individual measures with regard to the commitments of the G-20 on OTC derivatives, since a harmonised approach is going to be followed within the European Union.

According this approach, some measures are going to be introduced in two pieces of EU legislation: the Regulation on OTC derivative transactions, central counterparties and trade repositories (European Market Infrastructures Regulation, EMIR) and the MiFID review. The former includes all measures related to central clearing, reporting obligation and the regulation of market infrastructures, while the latter will tackle all issues referring to trading.

EMIR is already being discussed in the co-decision process, further the publication of the Commission's proposal on September 2010, and it is expected to be approved by the end of this year. On the other hand, the MiFID review has been published recently in order to be properly discussed by the European Institutions. For a complete reference to the content of new EMIR, please, check:

http://ec.europa.eu/internal_market/financial-markets/derivatives/index_en.htm

http://www.europarl.europa.eu/oeil/FindByProcnum.do?lang=en&procnum=COD/2010/0250

SPECIFIC ANSWERS ON ENERGY SWAPS:

As a short background before entering in the details of the energy swap clearing, let me provide you of some information on the activities and regulatory status of MEFF.

MEFF is an official secondary market and clearing house regulated by Spanish laws and under the supervision of the Spanish National Securities Market Commission. MEFF offers trading and central counterparty services for futures and options on IBEX-35 and on stocks. Likewise, MEFF offers central counterparty services for repos on Spanish Public Debt and energy derivatives.

The method in which MEFF clears electricity swaps.

Once a trade has been registered an open position is created. Each open position must fulfil a series of rules:

Trades with opposite sign for the same contract are netted regarding the open position; for example, the purchase of two Base Calendar 2012 futures and the sale of three futures from the same contract leave an open position of one future contract sold from Base Calendar 2012. Moreover, the purchase of two Base Calendar 2012 swap and the sale of three swap from the same contract leave an open position of one swap contract sold from Base Calendar 2012.

In segregated clients accounts, which have a "gross record", different trades for the same contract are not netted; following the previous example, the purchase of two Base Calendar 2012 futures and the sale of three futures from the same contract leave an open position of two futures purchased and three sold from Base Calendar 2012. Although clearing occurs at the open position level, trades are live until the expiration date. To cover the risk of these positions, margins are requested to ensure that the member is able to cover the settlements resulting from its trading.

Margins can be posted:

a) As cash in Euros credited by the Clearing Member or its Payment Agent to MEFF's Account on the TARGET2 platform. This cash amount will be immediately invested as an overnight buy and sell back repo in MEFF's securities account with the Spanish CSD.

b) By a pledge of securities, in accordance with the criteria set out in the Circular of MEFF on Margin collateral in the form of securities, or the circular which replaces it.

c) By a free of payment transfer of securities, effected by the Clearing Member to MEFF's securities account with Iberclear or with Cleastream (Luxembourgian branch), in accordance with the criteria set out in Circulars on Margin collateral in the form of securities in IBERCLEAR and Margin collateral in the form of securities in CLEARSTREAM, or those circulars which may replace them.

By means of a first demand guarantee, exclusively under the conditions and for the types of guarantees as laid down in the Circular of MEFF related to Posting of Margins.

The assets accepted can be modified in accordance with the relevant Circular.

MEFF also establish risk limits to the clearing activity of their clearing members. There is a single limit with three components: intraday risk limit, intraday risk limit stress test and margin call.

Intraday risk limit

This is recalculated every fifteen minutes for all accounts with open positions which have been operative during the session. Its purpose is to control the intraday risk by increasing position and price variation from the last settlement made at the relevant market price when the risk analysis is made.

Margins required in real-time – Margins posted in T + Variation Margin

Intraday risk limit stress test

This is done at the end of the session. Its purpose is to avoid that in case of an extreme price variation in the following session (margin call), the amount of additional margin required by MEFF could exceed 20% of the clearing member's shareholders equity. Two calculations are done: a bearish price scenario and a bullish price scenario and the clearing member worst scenario is selected.

Simulated margins – Margins posted in T+1 + Simulated variation margin.

Margin call

Its purpose is to restore the Clearing House with the necessary initial margins and the settlements which have been generated during the session for those accounts having to pay the Clearing House due to its net result in situations of extreme price movements. A single calculation is done and the scenario is determined by the specified price movement.

Simulated margins – Margins posted + Simulated variation margin.

The intraday risk limit consists on the individual guarantee calculated for limits, plus the extraordinary margin, plus a shareholder's equity percentage of the Clearing Member, and will be limited depending on its solvency. If the intraday risk is greater than the limit, the Clearing House will require additional individual guarantee to the affected clearing members. Clearing members must post the required individual guarantee within the time stipulated by Circular.

Apart from margins (see also the answer to the next question), as an addition security tier, MEFF imposes the obligation for each clearing member to contribute with a fixed amount to the energy contract group default fund: this will depend on the type of Member.

This is a joint liability guarantee. It will be used only to cover the default of another clearing member in case all other margins from the clearing member plus the MEFF margins are not sufficient to cover the obligation.

On a monthly basis, MEFF runs a stress test, comparing the risk in stress test situations for each clearing member with the energy contract group default fund. In accordance with the corresponding MEFF Circular an additional individual margin will be requested to the Clearing Member, if necessary.

<u>How does it determine initial and variation margin for the electricity swaps</u>?

Margins are requested to ensure that the member is able to cover the settlements resulting from its trading. The margins to be deposited by members and the risk calculations are determined for each group of contracts. MEFF currently has two contract groups: the financial group and the energy group.

Margins are managed under the "cross default" principle for members and the "no contamination" principle between contract groups. This means that if a member enters in default, in accordance with the "cross default" principle it does so in all contract groups (financial and energy) and the cost of the overall close must be covered by the member's individual guarantees, regardless the contract group the default corresponds to.

Nevertheless, MEFF's specific margins and those posted collectively by the members for each contract group follow the principle of "no contamination", meaning that if a clearing member is only active in the financial sector, it will not be exposed to potential losses as a result of the default of another clearing member in the energy sector and vice versa.

There are four basic components to the system of margins: initial margins, individual member's guarantees, MEFF guarantees and a contribution to the default fund by the members.

Initial margin:

This is calculated for each account. The initial margin is posted in MEFF for all the open accounts in the central register. Regarding the client's accounts in the second-tier register, the clients post the required margin in the Member. This margin covers the risk of each position under extreme but plausible conditions.

How to calculate the initial margin:

There are 4 margin classes: i) Base short term (daily and weekly contracts); ii) Peak short term; iii) Base annual, quarterly and monthly contracts iv) Peak annual, quarterly and monthly contracts.

There are various intervals in each margin class. Generally, the closer the delivery is, the greater the initial margin due to upper price volatility will be. For margin classes with daily and weekly products there are 4 margin intervals or fluctuations, depending on the time until the expiration of the contract. For margin classes with the rest of products there are 5 margin intervals or fluctuations, depending on the time until the expiration of the contract.

Various opposing contracts within a margin class are offset: for example, a long March base contract with a short quarterly base contract. The offset hours are calculated and the time-spread margin is applied in the same margin class; hours not offset have the full margin applied to them. The time-spread margin is applied within each contract group and is the maximum between a fixed amount and the difference in price of the contracts.

If there is more than one pair of contracts to be offset, priority is given to the pair of contracts with the same expiration date. In this case, the contract types with the greater number of hours are first offset. If there are contracts with a different expiration date, priority is given to the expiration pair having the closest expiration dates to each other, since they are the most closely correlated. If there is more than one pair and the time period between their expiration of the same pair is the same between pairs the expiration date which is furthest is first dealt.

There are compensations between base products and peak products, but there are no compensations between delivery and non-delivery. The margin credit or discount is calculated taking the minimum fluctuation of each group as a reference.

Contracts which do not have a daily variation margin (swaps) are also subject to mark to market adjustment margin. In other words, these contracts have not had a daily variation margin but the market value of these contracts has varied with regard to the price that was originally contracted. For this reason, this variation margin is not settled in cash but is taken into account, to a greater or lesser extent, when calculating the initial margin

Variation Margin

Daily settlements are made using a standard multilateral settlement in the Bank of Spain TARGET-2 RTGS. The individual or general clearing member requires an account in the TARGET-2 payments module. If it does not have one it may designate a payment agent who has cash accounts in a central bank of the Eurosystem so that it can make settlements through it. The variation margin is applied for annual, quarterly, monthly and weekly future contracts.

During the life of a future contract, and up to the last day it is registered, a daily variation margin takes place, based on the difference between the settlement price and the previous settlement price (for day trades: the price of the trade, for the rest: the settlement price of the previous session). On the last day of registration, the variation margin calculation is based on the difference between the final settlement price and the last settlement price.

Settlement on expiration is made for monthly, weekly and daily swap contracts.

Settlement takes place once the contract delivery period has finalized. The settlement on expiration date is established by Circular. On the maturity date Meff will automatically generate the expiration trades (type V).

The settlement price on expiration is obtained from the simple arithmetic average of the hourly price of the daily market of all the relevant hours of the contract of the delivery period of the product. The hourly price of the daily market is that published by the Operador del Mercado Ibérico de Energía – Polo Español,S.A. (OMEL) for that specific day and time. In the event of discrepancies between the Spanish and Portuguese prices, the Spanish price will be used.

In the case of a monthly swap the settlement price on expiration will be the simple arithmetic average, with the number of decimal places stipulated in the general conditions, of the hourly price of the Spanish system of all the relevant hours of the month in question. In the event of a base monthly swap, it would be the arithmetic average of all the hours in that month.

In the case of a weekly swap the settlement price on expiration will be the simple arithmetic average, with the number of decimal places stipulated in the general conditions, of the hourly price of the Spanish system of all the relevant hours of the week in question. In the event of a base weekly swap, it would be the simple arithmetic average of all the hours in that week.

Lastly, in the case of a daily swap the settlement price on expiration will be the simple arithmetic average, with the number of decimal places stipulated in the general conditions, of the hourly price of the Spanish system of all the relevant hours of the day in question. In the event of a peak daily swap, it would be the simple arithmetic average of all the relevant hours (from 08:00 to 19:59) in that day. If the expiration date is a holiday or weekend, the settlement is generated on the next working day.

What is the volume of these swaps cleared?

Data on historical volumes can be found in:

http://www.meff.es/aspx/DerEnergia/HistoricoResumen.aspx?id=ing

Who are the clearing members?

The requirements of members are listed in the Securities Market Act, the MEFF Rule Book itself and in the MEFF General Conditions.

The Spanish Securities Market Act (Act 24/1988, 28 July) states that the following may become MEFF Members that fulfill the requisites established in the Rule Book and in the relevant Circulars:

a. Investment firms that are authorized to execute client orders or trade for their own account.

b. Spanish credit institutions.

c. Investment firms and credit institutions authorized in other Member States of the European Union that are authorized to execute client orders or trade for their own account. Membership may be attained by any of the following mechanisms:

1. Directly, by establishing branches in Spain in accordance with article 71 bis of Title V of the Act 24/1988, in the case of investment firms, or in accordance with chapter II of Title V of Act 26/1988, of 29 July, on Discipline and Intervention of Credit Institutions, in the case of credit institutions.

2. By becoming remote members of MEFF without having to be established in the Spanish State.

d. Investment firms and credit institutions authorized in a country that is not a Member state of the European Union provided that, in addition to complying with the requirements laid down in Title V of Act 24/1988 for operating in Spain, the authorization given by the authorities in the home country enables them to execute client orders or trade for their own account. The Spanish Minister of Economy and Finance may deny those entities access to Spanish markets or impose condition upon access, for prudential reasons, where Spanish entities are not given equivalent treatment in the home country or where the compliance with rules of order and discipline in the Spanish securities markets is not guaranteed.

e. Any other persons which, in the opinion of MEFF, having regarded in particular to the special market functions which such persons may fulfill:

1. Have a sufficient level of trading ability and competence.

2. Have, where applicable, adequate organizational arrangements.

3. Have sufficient resources for the role they are to perform, taking into account the different financial arrangements that MEFF may have established in order to guarantee the proper settlement of transactions.

Those entities whose principal object is to invest in organized markets and which meet the conditions as to resources and solvency established by the Rule Book may also be members, with capacity restricted exclusively to trading, either on their own account or on the account of entities of their group. In the market in futures and options with non-financial underlings, attainment of membership by entities other than those envisaged above may be determined by regulation, provided that those entities meet the specialization, professionalism and solvency requirements.

The MEFF Rule Book states that the Members will be members of MEFF and may therefore develop trading activities and counterparty activities, with the extent corresponding to the class of Member and in the terms established in the Rule Book and ancillary regulations. The MEFF Rule Book states that the General Conditions of the Contracts may set forth specific terms in connection with Members' activities, depending on the Contract to which they refer. This is done in the General Conditions of Power Contracts so that utilities can become Proprietary Non Clearing Members, specifically the Power Contracts General Conditions establish:

Entities requesting being a Proprietary Non-Clearing Member for the Contract Group of Energy Underlying Assets adhering to article 3.2 of the Rule Book must comply with the following:

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Experience and professionalism.

Prove previous use of similar products to the ones described in these General Conditions in OTC markets or familiarity with the underlying power market. Certain criteria shall be taken into account, such as the corporate mission statement of the entity, its range of activities, its capacity to access the spot market of the Underlying Asset, or participation in similar derivatives markets.

The following types of entities shall be deemed to meet this requirement:

a. Those who usually engage in the business of energy production, commercialization, brokering, distribution or strategic reserve.

b. Those entities which, being part of a group of entities that carry out any of the said activities in the previous section, have the corporate mission statement of doing business in the multilateral trade platforms which have agreements with MEFF.

c. Those entities whose corporate mission statement is doing business in the energy derivatives financial markets and whose members carry out any of the activities mentioned in previous section a) without forming a group.

d. Consumers with access to the spot market of the Underlying Asset according to the applicable legislation.

Solvency

Maintain Shareholder's equity of at least Euro 50.000, or higher amount as may be established by Circular. MEFF Rule Book establishes that membership applications shall be approved by the Board of Directors of MEFF. In order to acquire such condition, Members must apply in writing to MEFF and sign the relevant agreements with MEFF as well as any additional agreements to be signed, as the case may be, with others Members, depending on the class of Member to which they belong. Members must have and maintain the necessary technical and human resources, which are established for each class of Member by Circular.

The current list of members for the energy segment is:

	Financial Derivatives		Energy Derivatives		MEFFClear	
Company	Code	Type	Code	Type	Code	Type
ACCIONA GREEN ENERGY DEVELOPMENTS, S.L.U.			A272	MNCP		
ATLANTIC COBALT S.L.			A401	MNCP		
AUDAX ENERGIA, S.L.			A295	MNCP		
BANCO SANTANDER, S.A.	A911	MLGR	A911	MLG	A911	ML
BHF BANK AG			A259	MLG		
BNP PARIBAS COMMODITY FUTURES LIMITED			A260	MLG		
CELTICA ENERGIA S.L.			A402	MNCP		
CEPSA INTERNATIONAL BV			A273	MNCP		
DEUTSCHE BANK AG AG LONDON			A298	MN		
E.ON ENERGY TRADING SE			A275	MNCP		
EDF TRADING LIMITED			A265	MNCP		
EGL ENERGIA IBERIA, S.L.			A258	MNCP		
ENDESA GENERACION, S.A.			A261	MNCP		
ENERGYA VM GESTION DE ENERGIA S.L.U.			A264	MNCP		
FACTOR ENERGIA IBERIA, S.A.			A269	MNCP		
GALP POWER, S.A.			A276	MNCP		
GAS NATURAL, SDG, S.A.			A233	MNCP		
GEOATLANTER, S.L.			A232	MNCP		
IBERDROLA GENERACION, S.A.U.			A262	MNCP		
La Unión Electro Industrial (ENERCOOP)			A400	MNCP		
MERCURIA ENERGY TRADING, S.A.			A268	MNCP		
MORGAN STANLEY & Co. Int. Plc.	A159	MNR	A263	MN		
NEXUS ENERGIA, S.A.			A278	MNCP		
RWE SUPPLY & TRADING GMBH			A267	MNCP		

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Should you have any question, do not hesitate to contact me or Mr. Miguel Ángel Herrero Alvite (maha@cnmv.es).

Sincerely yours,

Iñigo de la Lastra
Head of Secondary Markets Department