

May 14, 2012

**VIA ON-LINE SUBMISSION**

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

Re: Procedures To Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades (RIN 3038-AD08)

Dear Mr. Stawick:

CME Group Inc. (“CME Group”), on behalf of its four designated contract markets (“Exchanges” or “DCMs”), appreciates the opportunity to comment on the Commodity Futures Trading Commission’s (the “CFTC” or “Commission”) proposed procedures to establish appropriate minimum block sizes for large notional off-facility swaps and block trades (the “Release”).<sup>1</sup> In the Release, the Commission seeks comment on proposed rules (the “Proposed Rules”) that would implement Section 727 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”) with respect to public reporting of swap transaction data.

CME Group is the world’s largest and most diverse derivatives marketplace. CME Group includes four separate Exchanges, including 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”). The CME Group 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 includes CME Clearing, a derivatives clearing organization (“DCO”) and 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.

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<sup>1</sup> 77 Fed. Reg. 15460 (March 15, 2012).

Upon review of the proposal, the CME has significant concern on a number of points. First, we oppose the Commission's "one size fits all" approach in determining the swap block levels in the post-initial period because it neither advances the goals of Dodd-Frank nor takes into consideration the individual needs of each particular market. In the Release, the Commission is proposing to use a 67-percent notional amount calculation to determine initial block sizes for certain product classes (*i.e.*, in the interest rate and credit asset classes) and, for the post-initial period, to set appropriate minimum block sizes in these asset classes as well as in foreign exchange and for most products in the "other commodity" asset class.<sup>2</sup> The proposed notional amount calculation is intended to ensure that within a swap category, approximately two-thirds of the sum total of all notional amounts are reported on a real-time basis. As the Commission has further stated "this approach would ensure that market participants have a timely view of a substantial portion of swap transaction and pricing data to assist them in determining the competitive price for swaps within a relevant swap category."<sup>3</sup>

The 67% rule serves an arbitrary purpose and has no relationship to the explicit goals of Dodd-Frank with respect to block trading of swaps. Pursuant to the statute, the Commission is required to determine what constitutes a "large notional swap transaction" and whether public disclosure "will materially reduce market liquidity."<sup>4</sup> As is apparent from the Commission's stated purpose and its examples, it has disregarded the statutory mandate and substituted its own arbitrary purpose, *i.e.*, to real time report at least 67%, by notional value, of all swap transactions in each relevant category. This rationale has nothing to do with the size of the transaction or the impact on market liquidity. We believe that the appropriate test is one which classifies as blocks transactions that which would have a material impact on market prices if done in the public auction market. This number should be based on the usual depth of book at the time the order is to be executed. Any other approach would violate the strictures of Dodd-Frank and discredit the reputation of the CFTC as an expert regulator.

Any block level determination must take into consideration the individual needs of the particular market and should be left to each particular market operator. From a practical implementation standpoint, the Commission would be better served by retaining the ability to set block levels in the private, bilateral swaps market and deferring to the expertise of SEFs and DCMs to set the levels in their own markets. Each market has varying liquidity characteristics, including the nature and diversity of participants, which can affect the need for and size of block trades. The number of participants in these markets affects the need for, size of, and reporting requirements for blocks in swaps. All markets do not benefit from comparable liquidity and, as we have seen in our markets, certain market have benefited from the establishment of block trade levels while in other markets block trades have not been necessary. Certain markets, such as the interest rate market, have a long history with a large number of diverse participants. In contrast, many of the commodity swap markets are much less mature with less diversified and fewer participants. For these markets, real-time reporting can have a dramatic impact on their ability to lay off risk from their block transactions; consequently, the application a standard 67% notional amount is

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<sup>2</sup> 77 Fed. Reg. 15478 (March 15, 2012).

<sup>3</sup> *Id.*

<sup>4</sup> Sec. 2(a)(13)(E) of the Commodity Exchange Act, as amended by Dodd-Frank, reads, in relevant part:

"[w]ith respect to the rule providing for the public availability of transaction and pricing data for swaps described in clauses (i) and (ii) of subparagraph (C), the rule promulgated by the Commission shall contain provisions— (i) to ensure such information does not identify the participants; (ii) to specify the criteria for determining what constitutes a large notional swap transaction (block trade) for particular markets and contracts; (iii) to specify the appropriate time delay for reporting large notional swap transactions (block trades) to the public; and (iv) that take into account whether the public disclosure will materially reduce market liquidity."

entirely impractical and would make these markets more expensive for market users. Any dogmatic application of this test to other markets without significant analysis of the underlying markets serves little utility in determining truly useful block levels. Market operators, such as the CME, will have the necessary data to perform the rigorous analysis required to determine the impact of block levels on their particular market; enabling market operators to set these levels would be an effective method of effecting the goals of Dodd-Frank. From a practical standpoint, the Commission would be better served by retaining the ability to set block levels in the private, bilateral swaps market and deferring to the expertise of market operators to set the levels in their own markets.

Second, we believe that if the proposal is made applicable to trading on SEFs and DCMs, it lacks adequate regulatory context given the lack of definition surrounding various aspects of the implementation of Dodd-Frank. In our opinion, this lack of clarity precludes the ability for meaningful comment. Congress intended that, in promulgating the proposals, the Commission review the proposals to consider the benefits of market transparency and the effect that public disclosure would have on market liquidity. See CEA Section 2(a)(13)(E)(iv). It is difficult, if not impossible, to evaluate the proposal without further definition in key aspects of the rulemaking process. The rules on public reporting and trade execution (both in the swaps and the futures markets) are interrelated – as the Commission noted in its release, swap transactions exceeding a minimum block size would be exempted from the mandatory trading requirements for swaps and at this point, we do not have further clarity on how trade execution is to occur.<sup>5</sup> In this regard, the rules on swap execution facilities have yet to be finalized; there has been significant comment and as of yet no guidance on what will ultimately be an acceptable mode of trade execution on such a facility. For instance, a Request-for-Quote system which is required to be open to five participants versus one participant could significantly alter the liquidity profile of a particular market. Moreover, certain aspects of the final rules on designated contract markets, particularly Core Principle 9 [“Execution of Transactions”] and related interpretations, have far-reaching implications on both the trading of swaps and the movement of certain transactions to a swap execution facility.<sup>6</sup> How can one determine the level of market transparency and any corresponding impact on market liquidity without having the ability to appropriately view and evaluate the regulations which create the construct for and impact the entire market? As a result, we believe that the proposed regulations should be re-proposed when we have a sufficient ability to review the related rule construct.

Thirdly, in the Release, the Commission, during the initial period, has set the appropriate minimum block sizes for certain swaps based on whether the swap is economically related to the futures markets.<sup>7</sup> As stated in the Release, the Commission has noted that this approach draws on experience of the designated contract markets (“DCMs”) in determining the potential impact on liquidity risk that enhanced transparency may cause in connection with futures contract execution and understands that DCMs have set block sizes primarily in consideration of the objectives of enhancing pre-trade price transparency and reducing liquidity risk, including for products where DCMs have not set minimum block levels.<sup>8</sup> The Commission further states that economically related swap and futures contracts are economically related for the purposes of determining an appropriate minimum block size and claims that parties would likely have an incentive to conduct regulatory arbitrage by trading swaps.<sup>9</sup> The CME agrees with this approach

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<sup>5</sup> 77 Fed. Reg. 15466, fn. 87 (March 15, 2012).

<sup>6</sup> See proposed Reg. 38.502, 75 Fed. Reg. 80616 (Dec. 22, 2010).

<sup>7</sup> See, e.g., Reg. 43.6(e)(1) [for certain foreign exchange and other commodity products].

<sup>8</sup> 77 Fed. Reg. 15486 (March 15, 2012).

<sup>9</sup> Id.

Mr. David Stawick

May 14, 2012

Page 4

and the rationale for such during this initial period; after the initial period for these product classes, however, the proposal defaults to the 67 percent rule previously discussed; as noted previously, we disagree with this "one size fits all approach" and believe that the block levels should be tailored to the needs of the particular market. Any application of the 67 percent rule on a uniform basis would not take into account any potential effect of the minimum swap block levels on the futures markets.

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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) 930-3088 or by e-mail at [Phupinder.Gill@cmegroup.com](mailto:Phupinder.Gill@cmegroup.com), or Christopher Bowen, Managing Director, Chief Regulatory Counsel, at (212) 299-2200 or via e-mail at [Christopher.Bowen@cmegroup.com](mailto:Christopher.Bowen@cmegroup.com).

Sincerely,



Phupinder S. Gill

cc: Chairman Gary Gensler  
Commissioner Bart Chilton  
Commissioner Jill Sommers  
Commissioner Scott O'Malia  
Commissioner Mark Wetjen