



October 30, 2015

**VIA E-MAIL AND ON-LINE SUBMISSION**

Melissa D. Jurgens  
Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Centre 1155 21st Street, NW  
Washington, DC 20581

**Re: Request for Comment on Proposed Amendments to Swap Data Recordkeeping and Reporting Requirements for Cleared Swaps**

Dear Ms. Jurgens:

CME Group Inc. ("CME Group") appreciates the opportunity to comment on the Commodity Futures Trading Commission's (the "CFTC's" or "Commission's") recent notice of proposed rulemaking for swap data recordkeeping and reporting requirements for cleared swaps (the "NPR").<sup>1</sup> By way of background, CME Group is one of the world's largest and most diverse derivatives marketplaces. It operates multiple repositories<sup>2</sup> globally, including a swap data repository in the U.S., a swap execution facility ("SEF"), multiple Designated Contract Markets ("DCMs") and a derivatives clearing organization ("DCO"), which is one of the largest central counterparty clearing services in the world.

We commend the Commission for revisiting its current reporting rules and proposing changes for cleared swap transactions. The Commission has expressed an interest in making changes that would improve the efficiency of swap data collection and maintenance, enhance the quality of swap transaction data, improve the Commission's ability to utilize the data for regulatory purposes and simplify the reporting rules. These are laudable goals for any rulemaking in this area.

We are completely aligned with the view the Commission expressed in the NPR that the DCO is "in the best position" to report on "clearing swaps". We fully support the proposed amendments in the NPR that assign all reporting obligations to the DCO for clearing swaps, including all confirmation data and the daily reporting of valuation data, that provide the DCO the right to select the SDR to which it

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<sup>1</sup> See 80 Fed. Reg. 52544, Amendments to Swap Data Recordkeeping and Reporting Requirements for Cleared Swaps (Aug. 31, 2015).

<sup>2</sup> CME Inc. is provisionally registered as a US Swap Data Repository with the CFTC. It (or its affiliate) also operates trade repositories authorized to do business in Manitoba, Ontario, Quebec, the EU and Australia.

reports, that clarify the obligation to create and transmit unique swap identifiers (“USIs”), and that remove market participant obligations to report daily valuations on cleared swaps.

That said, we find the proposed amendments in large part simply codify existing practices and do not take advantage of the opportunity to do more. Clearly, cleaning up legal uncertainties created by the current rule set is an absolutely necessary step. However, the Commission could instead choose to enhance its reporting regime significantly with additional measures that would help ensure that the quality and usability of swap data provided to the Commission and public is improved in a material way.

Finally, although the Commission did seem to consider some aspects of the additional measures we are recommending, it declined to propose them based on what we believe to be a flawed cost-benefit analysis. For example, the costs borne by market participants did not appear to be properly quantified.

Our recommended approach is simple and fully meets all stated Commission goals. We have consistently called for similar approaches since Dodd-Frank gave the Commission responsibility to implement a swap data reporting regime. In essence, we believe the DCO should have all reporting obligations related to cleared swaps.<sup>3</sup> To apply this to the NPR, the Commission could add rules that require the DCO to assume all reporting obligations for original swaps and require DCOs to report to an SDR as soon as it accepts the swap for clearing. This approach is the best way for the Commission to achieve its goal of improving the efficiency of swap data collection and maintenance and at the same time would save the industry (and the staff) significant resources on an on-going basis. This approach would also by itself improve the quality and usability of data available to the public and the CFTC and would actually be easier to implement operationally than the current proposal. Furthermore, any proper cost-benefit comparison in our opinion would demonstrate that the DCO is best positioned to report on swaps that it accepts (or rejects) for clearing.

### **Data quality and usability issues won’t be adequately addressed by the proposed rules**

In the NPR preamble, the Commission identified the following goals that it considered to be critical to enable the Commission to monitor for systemic risk: (1) improve swap transaction data quality, (2) improve the Commission’s ability to utilize the data for regulatory purposes, and (3) improve the efficiency of data collection and maintenance. However, as discussed below, we do not believe the proposed rules would actually achieve those objectives.

First, although the proposed rules ratify the current market practices for DCO reporting on clearing swaps (that is, the “beta” and “gamma” swaps), they leave unchanged the role of SEFs and DCMs as the reporter of creation data for the original swaps (that is, so called “alpha swaps”). The proposed rules attempt to deal with the inherent challenges in bifurcating reporting responsibilities for alpha, beta and gamma swaps by placing new obligations on DCOs to send termination messages for alpha swaps

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<sup>3</sup> The approach would technically require amendments to Part 45, 43 and 39. The Part 45 changes described by the NPR could remain largely in place, along with new rule changes that appoint the DCO as sole reporter for swaps that are intended to be cleared, as explained more below. Corresponding changes would also need to be made to Part 43. Finally, changes would also be necessary in the Part 39 Regulations, to ensure that each DCO receives all the information it needs on incoming clearing submissions to discharge its new reporting duties.

accepted for clearing to the SDR to which the alpha swap was reported (“Initial SDR”). This change was deemed necessary because current reporting rules do not require a DCO to send a termination message to an Initial SDR.

This approach, that is, attempting to improve the reconciliation processes between SDRS holding differing parts of the alpha, beta and gamma, is an attempt to deal with longstanding and in our view unnecessary complications and retention of operational risk. We agree that fully reconciled alpha transactions would be an improvement on the current status quo. But, we do not believe that merely obligating the DCO to terminate those alpha swaps which have been accepted for clearing would do enough to achieve that intended result. Under existing rules,<sup>4</sup> which remain unchanged in the NPR, if the swap will be cleared, the reporting counterparty<sup>5</sup> is required to send to the DCO the identity of the Initial SDR and the USI of the alpha swap. It has been our experience that a reporting counterparty rarely provides the DCO with this information. This failure means the DCO cannot meet its obligations to terminate the alpha swap. Therefore it is possible, and we argue quite likely, that orphan alpha swaps will continue to persist under the changes called for in the NPR. An amendment to Part 39<sup>6</sup> requiring a clearing message to include all information needed by the DCO to make a complete Part 45 submission would minimize the existence of ‘orphan alpha’ swaps. However, this change will not, in and of itself, fully address the issue<sup>7</sup> because the DCO will still be dependent on the reporting counterparty to provide this information.

We think there’s a better, simpler way to address this particular problem. If the DCO is assigned all reporting obligations for the original and clearing swaps, it would eliminate the fractured audit trail and remove the need to perfect the unnecessary reconciliation process between SDRs for “orphan alpha” swaps. It would also streamline cleared trade reporting in the sense that hundreds of reporting counterparties would be reduced to a limited number of DCOs. Further, it would also ensure that the CFTC has access to one set of data for a cleared swap in one place. This would undoubtedly improve the

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<sup>4</sup> 17 CFR §45.10 (a)(1) and (b)(1)(iii) require a SEF/DCM and SD/MSP, respectively to transmit to the DCO the identity of the swap data repository to which primary economic terms data/swap creation data is reported by the counterparty/SEF or DCM as well as the USI.

<sup>5</sup> In the case of a reporting counterparty that is a non-SD/MSP, the SDR to which the trade is reported is responsible for creating and transmitting the USI to the DCO.

<sup>6</sup> Part 39 will need to be amended even under our proposal to make the DCO the sole reporter for swaps that are intended to be cleared. This change ensures that DCOs obtain all information required to make complete Part 45 reports that extends beyond the clearing terms (such as U.S. person status and swap dealer designation). This would create a level playing field among the DCOs in connection with obtaining this data.

<sup>7</sup> Since 17 CFTC§45.10(c)(3) requires, for off-facility swaps executed with a non-SD/MSP reporting counterparty, *“The swap data repository to which the swap is reported....shall transmit the unique swap identifier created pursuant to §45.5 to ....the derivatives clearing organization....”* the DCO would not be able to make the USI of the original swap a required field on a clearing message. This fact all but guarantees that there will be a subset of clearing messages submitted without the information necessary to terminate the alpha swap.

Commission's ability to utilize the SDR data for regulatory purposes and reduce the amount of time spent by staff reconciling the data across SDRs.<sup>8</sup>

### **SEFs/DCM alpha reporting can result in the inaccurate public reporting**

The CFTC can eliminate the dissemination of erroneous data in connection with void *ab initio* swaps<sup>9</sup>, and intended to be cleared (“ITBC”) swaps reported by SEFs and DCMs, if it delays the reporting of ITBC swaps until they are accepted or rejected for clearing and thus, legally binding. Currently, the reporting rules require SEFs and DCMs to report ITBC swaps to an SDR as soon as technologically practicable. As a result, SEFs and DCMs often report ITBC swaps to an SDR, and in turn the SDR reports the swaps to the public, before they are accepted for clearing.

However, an ITBC swap does not exist as a matter of law until all material conditions to the swap are satisfied, a legal conclusion confirmed by staff’s straight through processing guidance (“STP guidance”).<sup>10</sup> Acceptance of a swap for clearing by a DCO is a material condition of an ITBC swap. In other words, until the DCO accepts a swap for clearing, the swap does not legally exist. Thus, ITBC swaps that are reported before they are accepted by a DCO for clearing do not legally exist at the time they are reported to the public. The STP guidance further provides that if an ITBC swap is not accepted for clearing, the swap is void *ab initio*.<sup>11</sup> This leaves open the possibility that swaps that are publicly reported may later be rejected from clearing. These swaps are thus void, making the public reports misleading since the swaps never legally existed. The DCO is the first to know whether swaps are accepted for clearing and is best positioned to report accurate data on original swaps to the SDR as soon as technologically practicable, at the point in time when the DCO accepts each swap for clearing. Further, reassigning the regulatory reporting obligation on original swaps from the SEFs and DCMs to DCOs would not add more than 10 seconds to the reporting process under current STP guidance.<sup>12</sup>

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<sup>8</sup> A significant amount of CFTC resources are required to link the original swaps and clearing swaps for linked trades that are reported to multiple SDRs in connection with creating an audit trail for these swaps. The CFTC could eliminate the need for this task and save these resources by making the DCO the sole reporter for both original and clearing swaps.

<sup>9</sup> An example is where an execution platform that matches a trade (like a SEF) sends a report to an SDR for Part 43 and 45 purposes immediately after it matches the trade but prior to, or at the same time as, a swap is sent to a DCO for clearing.

<sup>10</sup> See, e.g., CFTC regulations 1.73, 1.74, 37.702(b), 38.601, and 39.12(b)(7) and September 26, 2013 Staff Guidance on Swaps Straight-Through Processing.

<sup>11</sup> Under CFTC Regulation 43.2, the term “Execution” means an agreement to the terms of a swap that legally binds the parties to such swap terms under applicable law. Parties to an ITBC swap that is rejected for clearing are not legally bound to the terms of the swap.

<sup>12</sup> During the rulemaking phase for reporting rules, the Commission grappled with the issue of how to report cleared swaps. Some commenters specifically called for the establishment of a reporting system whereby the DCO acted as sole reporter for centrally cleared swaps. However, the Commission declined to take this approach, in part, based on the following premise: “Allowing the first report of swap data concerning a swap to come from a

Furthermore, SEFs and DCMs are currently obligated to include in their Part 43 reports to SDRs certain terms that are unknown until the ITBC swaps are accepted by a DCO for clearing. Such terms include time of execution and whether a publicly reportable swap transaction will be cleared by a DCO.<sup>13</sup> The time of execution for an ITBC swap is the time at which the DCO accepts the swap for clearing.<sup>14</sup> The time of execution as well as whether the swap will be accepted for clearing is thus unknown and cannot be accurately reported prior to acceptance for clearing.

The DCO is best positioned under the current STP market structure to accurately report ITBC swaps to an SDR. The DCO is the entity that accepts each ITBC swap for clearing. The point of acceptance for clearing is the moment in time when all material terms become known and the swap becomes legally binding and therefore reportable.<sup>15</sup>

### **The Commission's cost-benefit analysis is flawed**

In the Notice of Proposed Rulemaking, the Commission discusses the cost and benefits of certain alternatives suggested by commenters in response to the 2014 request for comment<sup>16</sup>, including requiring the original and clearing swaps to be reported to the same SDR chosen by the DCO accepting the swap for clearing. The Commission's demurral in the NPR cited the fact that *"...the proposed rule more closely reflects current industry practices relative to the alternative, there would be some*

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*DCO following clearing.....would result in reporting delays that the Commission does not believe are desirable. Without reporting of primary economic terms data shortly following execution of a swap, regulators examining SDR data for regulatory purposes in many cases would not see the swap in question for hours or in some cases nearly an entire day (if initial reporting followed clearing), or even for days or weeks (if initial reporting followed full legal confirmation). This lack of complete swap data would frustrate fundamental purposes of financial reform, recognized not only by Congress in passing Dodd- Frank, but internationally."* Since that time, STP Guidance has been issued and clarified the required treatment for ITBC Swaps (which are subject to SEF or DCM Rules). STP guidance sets the timing standard for acceptance or rejection of swaps for clearing as 10 seconds or less. Thus, reassigning the regulatory reporting obligation on original swaps from the SEFs and DCMs to DCOs would not add more than 10 seconds to the reporting process. Additionally, because the original swaps do not exist until they are accepted for clearing, it is inappropriate and potentially misleading to report such swaps prior to that time.

<sup>13</sup> Included amongst the Part 43 fields is a designation of Cleared or Uncleared described in Appendix A to Part 43 as an indicator of "whether a publicly reportable swap transaction is going to be cleared by a derivatives clearing organization." A SEF or DCM will not know whether the swap "is going to be cleared" at the time it sends a Part 43 report to the SDR; an indicator of whether the swap will be cleared or uncleared can only be accurately reported once the clearing determination has been made.

<sup>14</sup> See CFTC Regulation §43.2 (defining "Execution" as "...an agreement by the parties (whether orally, in writing, electronically, or otherwise) to the terms of a swap that legally binds the parties to such swap terms under applicable law"). Because clearing is a term of the swap, execution does not occur until the trade is cleared and thus the Execution Timestamp cannot be reported accurately prior to acceptance for clearing.

<sup>15</sup> See fn 15.

<sup>16</sup> See Request for Comment Review of Swap Data Recordkeeping Requirements 79 Fed. Reg. 16689 (March 26, 2014).

*potentially significant one-time costs, including the costs of changes to existing systems, associated with changing practices to conform to the alternatives....”*

While we concede that there will be a one-time cost to reporting counterparties associated with making changes to their existing systems, these are not the only relevant costs that must be considered. The Commission fails to take into account the fact that there are recurring expenses associated with systems usage, maintenance and personnel hours required for data reporting.<sup>17</sup> Moreover, the Commission also did not consider the fees charged by the SDRs to utilize their reporting service on an ongoing basis.<sup>18</sup> These costs are now quantifiable well known and can reach in the millions annually depending on the ticket, notional volumes and maturity of the swaps. Under our recommended approach, every entity other than the DCO would not be responsible for making reports on intended to be cleared swaps and therefore would not have to incur any ongoing reporting fees. The failure to take fees charged by SDRs into account, and other related recurring expenses incurred, severely underestimates the cost borne by reporting counterparties to report ITBC swaps on a going forward basis under the Commission’s reporting rules.

Further, the Commission also seemed to reach a conclusion in its cost-benefit analysis that commenting market participants did not appear to share. The Commission, when dealing with the topic of sole DCO reporting, stated: “[a]dopting the framework suggested by commenters above could result in a disruption of industry work flows and could require significant retooling of operational and technological solutions in place designed to report swap data, all at an additional cost to market participants.” The NPR itself identified a number of prominent commenters who directly supported placing swap data reporting obligations for ITBC swaps solely on the DCO.<sup>19</sup>

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<sup>17</sup> The Commission acknowledged these costs when it adopted Part 45 initially. See Final Rule Swap Data Recordkeeping and Reporting Requirements 77 Fed. Reg. 2136 at 2182 (January 13, 2012)

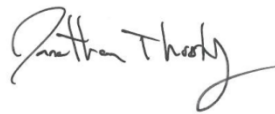
<sup>18</sup> In the cost-benefit analysis in the final rule release detailed the costs that the Commission anticipated would be incurred by reporting counterparties and registered entities in order to comply with the rules regarding creation data.....(a) significant non-recurring investments in technological systems and personnel; and (b) recurring expenses associated with systems usage and maintenance and personnel hours required for data reporting. More specifically, the Commission anticipated the following recurring costs:“(i) operational support for its OMS, including adaptation to new products, systems upgrades and ongoing maintenance; (ii) maintaining connectivity with an SDR that accepts data, including the demands on technological systems and the burden associated with the personnel hours necessary to facilitate transmission of data; and (iii) compliance with error correction procedures, including the burden associated with the personnel hours necessary to monitor and report errors. SDR fees were not included in the costs which would be borne by reporting counterparties.

<sup>19</sup> Footnote 157 of the proposed rulemaking identified the following commenters as supportive of placing the swap data reporting obligations for ITBC swaps solely on the DCO: CME, NFPEA, EEI, ICE, CEWG and NFP Electric Associations.

Swaps that are intended to be cleared should not be reported until they are accepted for clearing and thus, legally binding. In any cost-benefit comparison the DCO is best positioned to report on the swaps it accepts for clearing. If the DCO is also given the task of reporting ITBC swaps when accepted for clearing, the rest of the industry could be excused from this task, avoiding unnecessary costs and operational complexity. These costs savings will be coupled with improvements to the quality of the data available to the public and Commission and can be rapidly implemented.

We thank the Commission for initiating this important process and giving us the opportunity to comment.

Sincerely,

A handwritten signature in black ink, appearing to read "Jonathan Thursby". The signature is written in a cursive, flowing style with a long horizontal stroke at the end.

Jonathan Thursby  
President, CME SDR