CME Group

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Via Electronic Mail: rule-comments@sec.gov

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Proposed SEC Rules – Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers (SEC Release No. 34-68071, 77 FR 70214)

CME Group Inc. ("CME Group") appreciates the opportunity to comment on the Securities and Exchange Commission's ("SEC" or the "Commission") proposed rulemaking regarding capital, margin, and segregation requirements for security-based swap dealers and major security-based swap participants and related capital requirements for broker-dealers (the "Rule Proposal").

CME Group is the parent of Chicago Mercantile Exchange Inc. ("CME"). CME is registered with the Commodity Futures Trading Commission ("CFTC") as a derivatives clearing organization and is one of the largest central counterparty clearing services for regulated derivatives contracts in the world. CME has also been "deemed registered" as a securities clearing agency by operation of law[1] for the limited purpose of clearing security-based swaps. CME's clearing house division ("CME Clearing") offers clearing and settlement services for exchange-traded futures contracts and for over-the-counter ("OTC") derivatives transactions including interest rate swaps, credit default swaps ("CDS"), agricultural swaps and other OTC contracts. CME Clearing plans to offer customer clearing for security-based swaps, specifically, single-name and narrow-based index.

As a general comment, we respectfully disagree with the Commission's apparent assumption that only firms registered as security-based swap dealers or dually registered as security-based swap dealers and broker-dealers will clear security-based swaps for customers. As a clearing agency, CME Clearing has to anticipate that the universe of clearing members that will clear customer trades in single name and narrow-index CDS will also include firms relying solely upon their broker-dealer registration with the SEC, as permitted under Section 3E(a) of the Exchange Act. That would be consistent with our experience with CDS clearing. Of the 12 CDS clearing members currently authorized to clear customer trades, each of which is dually-registered as a futures commission merchant and broker-dealer, only five to date have provisionally registered as swap dealers under the Commodity Exchange Act.

[1] See Section 763 of The Dodd–Frank Wall Street Reform and Consumer Protection Act.

We believe it is important for the SEC to apply uniform segregation requirements to all clearing firms that will clear customer trades in security-based swaps. Thus, we recommend that the Commission incorporate two features of proposed Rule 18a-4 into Commission Rule 15c3-3 to avoid disparate treatment of clearing members that are registered as security-based swap dealers ("SBSD Clearing Members") and those relying solely on broker-dealer registration ("BD Only Clearing Members") to clear customer security-based swap trades. Specifically, we recommend changes to Rule 15c3-3 that will permit BD Only Clearing Members to (1) post securities at a clearing agency to margin customer security-based swap without violating Rule 15c3-3's control requirements, and (2) exclude customer margin for cleared security based swaps on deposit with a clearing agency from its Reserve Formula calculation under Rule 15c3-3.

A. Fixes for Treatment of Margin Held at a Clearing Agency

Registered broker-dealers engaging in a customer securities business must comply with the SEC's current segregation rule, SEC Rule 15c3-3. This rule is designed to prevent a broker-dealer from using customer funds to finance its business. Under the Rule 15c3-3 regime, a broker-dealer must, among other things, maintain possession or control of all fully-paid or excess margin securities held for the account of customers. It also requires broker-dealers to make periodic computations to determine how much money it is holding that is either customer money or obtained from the use of customer securities; if this amount exceeds the amount that it is owed by customers or by other broker-dealers relating to customer transactions, the broker-dealer must deposit the excess into a special reserve bank account for the exclusive benefit of customers.

Section 3E permits both security-based swap dealers and broker-dealers to clear security-based swaps for customers, and imposes identical segregation requirements on each with respect to their handling of the funds of cleared security-based swap customers. The Rule Proposal includes new segregation requirements for security based swap dealers. These new requirements, found in proposed Rule 18a-4, are modeled closely on existing Rule 15c3-3 and feature similar possession and control and reserve account requirements. The new rule by its terms would apply to firms that are stand-alone security-based swap dealers and to those that are dually registered as broker-dealers and security-based swap dealers. It would not apply to firms that clear security-based swap activities but are only registered as broker-dealers (such as the BD Only Clearing Members).

1. Excess Collateral

Under new Rule 18a-4, a security-based swap dealer would be required to maintain possession and control of all excess securities collateral provided by customers. Excess securities collateral is defined by the new rule to include securities[2] carried by a security-based swap dealer for the account of a security-based swap customer that have a market value that exceeds a security-based swap dealer's current exposure to the customer, excluding (among other things) securities held by a clearing agency, but only to the extent the securities are being used to meet a margin requirement of the clearing agency resulting from a security-based swap transaction of the customer. This carve-out does not currently exist in Rule 15c3-3 and was not added to Rule 15c3-3 by the Rule Proposal.

[2] We use the term securities to also cover money market instruments, which are also covered by the definition.

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Thus, SBSD Clearing Members would be able to exclude securities held by a clearing agency to meet clearinghouse margin requirements for customer security-based swap positions from their obligations under proposed Rule 18a-4 to otherwise maintain physical possession or control of such securities. In contrast, BD Only Clearing Members may be preclude from posting any customer securities with a clearing agency to meet the clearing agency's margin requirements for cleared customer security-based swaps under the control requirements of Rule 15c3-3(b) applicable to a broker-dealer's handling of customer fully-paid and excess margin securities.

This disparity will complicate a clearing agency's operations for security-based swaps if it is permitted to hold securities as margin from SBSD Clearing Members but not from BD Only Clearing Members for cleared customer security-based swap positions. It could also unfairly result in substantially higher regulatory requirements for BD Only Clearing Members. We do not believe this result was intended. Accordingly, we ask the Commission to amend the control requirements of Rule 15c3-3 to permit broker-dealers to re-post customer securities with a clearing agency to meet the clearing agency's margin requirements with respect to cleared customer security-based swap positions.

2. Reserve Formula

The proposed formula for determining the amount that a security-based swap dealer must maintain in a special reserve account for the exclusive benefit of its security-based swap customers allows the dealer to deduct "Margin related to cleared security-based swap transactions in accounts carried for security-based swap customers required and on deposit in a qualified clearing agency account at a" Commission-registered clearing agency. In contrast, the security-based swaps activities of a BD Only Clearing Member would be covered by the reserve requirements of Commission Rule 15c3-3. The Rule 15c3-3 reserve formula does not contain a comparable deduction for margin funds deposited with a clearing agency. This could lead to higher reserve requirements for BD Only Clearing Members compared to entities conducting the same customer clearing businesses via security-based swap dealer registration. We do not see any reason for this unfair disparity and urge the Commission to add a comparable deduction to the Rule 15c3-3 reserve formula for customer margin amounts that a BD Only Clearing Member deposits with a clearing agency. Based on the current profile of our CDS clearing members, it is our expectation that most firms clearing security-based swap customer trades will choose to do so under a joint broker-dealer/futures commission merchant registration structure without an additional layer of registration as a security-based swap dealer (or swap dealer).

B. Haircuts

CME Group also urges the Commission to continue to consult with the CFTC to ensure that the regulations describing haircut requirements applicable to firms that are jointly registered as both broker-dealers and as futures commission merchants ("FCMs") are consistent. Specifically, CME Group notes that the proposed amendment to Appendix B to SEC Rule 15c3-1 pertaining to broad-based securities indices and interest rate swaps appear to contradict current CFTC Regulation 1.17(c)(5). As proposed by the Commission, the market risk haircut for proprietary positions in broad-based securities indices would be based on the SEC's proposed maturity grid, and, with respect to interest rate swaps, would be based on the haircut applicable to U.S. government obligations subject to a minimum 0.5% deduction. In contrast, CFTC Regulation 1.17(c)(5) provides that the market risk haircut for proprietary cleared OTC derivative positions is based a percentage (i.e. 100%, 150% or 200%) of the margin requirement. We encourage the Commission to work with the CFTC to ensure that the haircuts pertaining to the same products are treated identically under each agency's capital rules.

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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 312-930-3488, or via email at kathleen.cronin@cmegroup.com.

Sincerely,

Kathleen M Cronin

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cc: Chairman Elisse Walter
Commissioner Luis Aguilar
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