

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-67650; File No. SR-CME-2012-22)

August 14, 2012

Self-Regulatory Organizations; Chicago Mercantile Exchange, Inc.; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change to Amend Rules to Facilitate Customer Portfolio Margining of Interest Rate Futures and Interest Rate Swaps

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on August 7, 2012, the Chicago Mercantile Exchange, Inc. (“CME”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule changes described in Items I and II, below, which Items have been prepared primarily by CME. The Commission is publishing this Notice and Order to solicit comments on the proposed rule changes from interested persons, and to approve the proposed rule changes on an accelerated basis.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

CME proposes to amend rules related to its interest rate swaps (“IRS”) and interest rate futures clearing offerings by establishing a portfolio margining program for customer portfolios containing IRS and interest rate futures positions. The text of the proposed rule changes is available on the CME’s website at <http://www.cmegroup.com>, at the principal office of CME, and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, CME included statements concerning the purpose of and basis for the proposed rule changes and discussed any comments it

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

received on the proposed rule changes. The text of these statements and comments may be examined at the places specified in Item III below. CME has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of these statements.³

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose of the Proposed Rule Change

CME is registered as a derivatives clearing organization with the Commodity Futures Trading Commission ("CFTC"), and currently operates a substantial business clearing both IRS and interest rate futures contracts. The changes that are the subject of this filing are proposed rules that would establish a portfolio margining program for customer portfolios containing cleared IRS and interest rate futures positions. More specifically, the proposed rule amendments consist of revisions to CME Rule 8G831 (Commingling of Eligible Futures and Swaps Positions) and certain corresponding changes to the CME IRS Clearing House Manual of Operations.

CME believes the rule changes will benefit customers and the overall derivatives markets by: (1) enabling customers who clear trades through CME to obtain the benefit of margin offsets between interest rate futures and IRS, thus reducing their trading costs and allowing for more efficient capital usage; (2) improving the efficiency and effectiveness of risk management; and (3) encouraging greater utilization of clearing, thereby facilitating systemic risk reduction.

CME notes that it has also submitted the proposed rule changes that are the subject of this filing to its primary regulator, the CFTC, in CME Submission 12-151, and

³ The Commission has modified the text of the summaries provided by CME.

is awaiting the CFTC's approval for the proposal.⁴ As described below, CME believes there is good cause for the Commission to grant approval for the proposed rule changes on an accelerated basis by August 31, 2012 to ensure the proposed rule changes can be implemented immediately when CFTC approval is obtained.

a. CME's Proposed Portfolio Margining Program for Eligible Interest Rate Futures Products and IRS; Commingling of Related Positions

CME has considerable experience clearing and managing the risks of interest rate futures, and has been clearing IRS since October 2010. CME notes that it previously implemented a portfolio margining program for interest rate futures and IRS products in proprietary or "house" accounts of clearing member firms.⁵

i. *Eligible Products*

CME's IRS offering currently includes seven currencies—*viz.*, USD, EUR, GBP, CAD, AUD, JPY, and CHF—each with varying contract attributes. CME identified the following interest rate futures that will initially be eligible for commingling with IRS in CFTC 4d(f) accounts (*i.e.*, customer cleared swaps accounts): Eurodollar Futures and Treasury Futures, including U.S. Treasury Bonds and 2-, 5- and 10-Year Treasury Notes. These particular futures products were identified as eligible for commingling based on their exposure to similar or correlated risk factors as IRS, thus allowing for margin offsets. In accordance with the proposed amendments to Rule 8G831, interest rate futures may be commingled with IRS in 4d(f) accounts only if the futures are risk reducing.

⁴ CFTC rules permit self-regulatory organizations like CME voluntarily to request approval of proposed rule changes. See 17 CFR 40.5.

⁵ See SR-CME-2012-05, Securities Exchange Act Release No. 34-66641 (Mar. 21, 2012), 77 FR 18288 (Mar. 27, 2012).

ii. *Clearing Firm Eligibility*

To be permitted to commingle interest rate futures and IRS under CME's program, a clearing firm must be a futures commission merchant ("FCM") registered with the CFTC and an IRS clearing member of CME, and it must also be a clearing member of CME, the Chicago Board of Trade ("CBOT"), or both in order to clear interest rate futures. FCM clearing members must also satisfy minimum regulatory capital requirements under applicable law (including CFTC regulations and CME/CBOT rules) and must also be in compliance with CME's operational and risk-management rules and requirements for IRS and CME/CBOT clearing members.

iii. *Margin Methodology*

Pursuant to the proposed changes to CME Rule 8G831, interest rate futures residing with IRS in CFTC 4d(f) accounts held at CME will be subject to the margin model developed by CME for IRS. This model is based on an Historical Value at Risk (HVaR) methodology with Exponentially Weighted Moving Average (EWMA) volatility forecasting. CME's margin model for IRS covers at least 99 percent of potential losses over any five-day period in a large universe of portfolios, covering 99 percent of market moves.

HVaR was selected both for its scalability across multiple currencies and its transparency to market participants: it is a standard, well understood model and is easily replicable. CME has enhanced the multi-currency HVaR model to address risks arising from rate risk and foreign exchange conversion risks. The model is designed to mitigate the rate risks created by additional currencies, correlated yield curves, and differing liquidity profiles. The model also takes into account foreign exchange conversion rates

and their implication on collateral liquidation for multi-currency losses. In addition, the HVaR model provides margin offsets for multi-currency portfolios.

iv. *Default Scenarios*

CME has considered issues involved with the default of a clearing member and/or the default by one or more of a clearing member's cleared swaps customers with a commingled account. Because the commingled positions would reside in CFTC 4d(f) accounts, these customer commingled interest rate futures and IRS (and collateral associated therewith) would be part of the customer "cleared swaps" account class under the CFTC's Part 190 Bankruptcy Rules. This means these positions would be treated in accordance with the CFTC's Part 22 regulations providing for legal segregation of customer funds with operational commingling, which become effective on November 8, 2012.

Any default by an IRS clearing member—including a default involving customer commingled positions—would also be governed by CME's rules and default management procedures for IRS (including CME Rules 8G802, 8G814, and 8G975). These rules and procedures are based on input from IRS clearing members and market participants, as well as CME's depth of default management experience from many years as a derivatives clearing house. CME's default management rules and procedures are reviewed and updated as circumstances warrant. CME Clearing makes these updates in consultation with the CME IRS Risk Committee and the CME IRS Default Management Committee.

2. Statutory Basis

CME believes the proposed rule changes are consistent with the requirements of the Act, including Section 17A,⁶ and the rules and regulations thereunder applicable to CME. CME observes that the proposed rule changes involve improvements and efficiencies that are related to CME's interest rate futures and swap product offerings for investors. Accordingly, CME believes the proposed rule changes will benefit customers in the following ways: (i) by enabling customers who clear trades through CME to obtain the benefit of margin offsets between interest rate futures and IRS, thus reducing their trading costs and allowing for more efficient capital usage; (ii) by improving the efficiency and effectiveness of risk management; and (iii) by encouraging greater utilization of clearing, thereby facilitating systemic risk reduction. CME contends that the proposed changes are designed to promote the prompt and accurate clearance and settlement of securities transactions and derivatives agreements, contracts and transactions; to assure the safeguarding of securities and funds that are in CME's custody or control; and, in general, to help to protect investors and the public interest.

Furthermore, CME points out that the proposed rule changes are limited to the clearing of futures and swaps, and thus relate solely to CME's futures and swaps clearing activities pursuant to its registration as a derivatives clearing organization under the Commodity Exchange Act ("CEA"). CME thus asserts that the proposed rule changes do not significantly affect any of CME's securities clearing operations or any related rights or obligations of CME or persons using such service. CME notes that the policies of the CEA with respect to clearing are comparable to a number of the policies underlying the

⁶ 15 U.S.C. 78q-1.

Act, such as promoting market transparency for over-the-counter derivatives markets, promoting the prompt and accurate clearance of transactions, and protecting investors and the public interest.

B. Self-Regulatory Organization's Statement on Burden on Competition

CME does not believe that the proposed rule changes will have any impact, or impose any burden, on competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

CME has not solicited, and does not intend to solicit, comments regarding these proposed rule changes. CME has not received any unsolicited written comments from interested parties.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule changes are consistent with the Act. Comments may be submitted by any of the following methods:

- Electronic comments may be submitted by using the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>), or by sending an e-mail to rule-comments@sec.gov. Please include File No. SR-CME-2012-22 on the subject line.
- Paper comments should be sent in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, D.C., 20549-0609.

All submissions should refer to File Number SR-CME-2012-22. To help the Commission process and review your comments more efficiently, please use only one

method of submission. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule changes that are filed with the Commission, and all written communications relating to the proposed rule changes between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, N.E., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filings also will be available for inspection and copying at the principal office of CME. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-CME-2012-22 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Commission's Findings and Order Granting Accelerated Approval of Proposed Rule Change

Section 19(b) of the Act⁷ directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization. The Commission concludes that the proposed rule changes are consistent with the requirements of the Act, in particular with the

⁷ 15 U.S.C. 78s(b).

requirements of Section 17A of the Act,⁸ and the rules and regulations thereunder applicable to CME. In particular, the Commission concludes that the proposed rule changes are consistent with Section 17A(b)(3)(F) of the Act,⁹ which requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of derivative agreements, contracts and transactions. It is the Commission's view that the proposed rule changes should allow CME to enhance its services in clearing IRS and interest rate futures products, thereby promoting the prompt and accurate clearance and settlement of derivative agreements, contracts and transactions.

In its filing, CME requested that the Commission approve these proposed rule changes on an accelerated basis, so they can become effective prior to August 31, 2012. CME has articulated three reasons for granting its request for accelerated approval. One, the products covered by this filing, and CME's operations as a derivatives clearing organization for such products, are regulated by the CFTC under the CEA. Two, the proposed rule changes affect the IRS swaps and interest rate futures that CME clears, and therefore relate solely to its swaps and futures clearing activities, and do not significantly relate to CME's functions as a clearing agency for security-based swaps. Three, CME believes the rules will benefit customers and the overall derivatives markets in the following ways: (i) by enabling customers who clear trades through CME to obtain the benefit of margin offsets between interest rate futures and IRS, thus reducing their trading costs and allowing for more efficient capital usage; (ii) by

⁸ 15 U.S.C. 78q-1. In approving these proposed rule changes, the Commission has considered the proposed rule changes' impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

⁹ 15 U.S.C. 78q-1(b)(3)(F).

improving the efficiency and effectiveness of risk management; and (iii) by encouraging greater utilization of clearing, thereby facilitating systemic risk reduction. CME contends that, as a result, the proposed rule changes will help to protect investors and the public interest.

The Commission concludes that there is good cause, pursuant to Section 19(b)(2) of the Act,¹⁰ for approving the proposed rule changes prior to the thirtieth day after the date of publication of notice in the Federal Register because: (i) the proposed rule changes do not significantly affect any of CME's securities clearing operations (whether in existence or contemplated by its rules) or any related rights or obligations of CME or persons using such service; and (ii) the activity relating to CME's non-security clearing operations for which CME is seeking approval is subject to regulation by another federal regulator.

¹⁰ 15 U.S.C. 78s(b)(2).

V. Conclusion

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act that the proposed rule change (SR-CME-2012-22) be, and hereby is, APPROVED on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹¹

Elizabeth M. Murphy
Secretary

¹¹ 17 CFR 200.30-3(a)(12).