CME Group

September 21, 2012

VIA E-Mail Submission
Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Manitoba Securities Commission
New Brunswick Securities Commission
Ontario Securities Commission
Saskatchewan Financial Services Commission

c/o John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario
M5H 3S8

Me Anne-Marie Beaudoin, Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, Tour de la Bourse
Montréal, Québec
H4Z 1G3

Re: CSA Consultation Paper 91-406 – Derivatives: OTC Central Counterparty Clearing

Dear Members of the CSA Derivatives Committee:

CME Group Inc. ("CME Group") appreciates the opportunity to comment on the Canadian Securities Administrators ("CSA") consultation paper on OTC Central Counterparty Clearing ("Consultation Paper").

CME Group is the parent of four DCMs: the 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"). These DCMs 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's clearing house division ("CME Clearing") offers clearing and settlement services for exchange-traded futures contracts, and for over-the-counter ("OTC") derivatives transactions through CME ClearPort. CME is registered with the CFTC as a Derivatives Clearing Organization ("DCO") and is one of the largest central counterparty clearing services in the world.

20 South Wacker Drive Chicago, Illinois 60606 T 312 930 3488 F 312 930 4556 kathleen.cronin@cmegroup.com cmegroup.com

1. Foreign CCPs -- Comparability

CME Group believes that any legislative implementation of the clearing mandate should allow market participants to comply with the clearing mandate through the use of both domestic and foreign CCPs and we are supportive of the Consultation Paper's adoption of this approach. We support the efforts of the CSA Derivatives Committee ("Committee") to adopt international recommendations and to engage in a comparability analysis in evaluating foreign CCPs. Allowing foreign CCPs to be utilized for purposes of the mandatory clearing obligation is consistent with IOSCO's February 2012 report on *Requirements for Mandatory Clearing* (the "IOSCO Report"), which states:

> Advantages of allowing the use of third country CCPs to satisfy mandatory clearing are that it could allow mandatory clearing obligations to apply to a wider range of products or currencies than is available within any individual jurisdiction as well as increasing consistency between regimes and reducing the potential for regulatory arbitrage. Utilising such CCPs in mandatory clearing regimes would allow authorities to decrease counterparty risk via utilisation of central clearing over and above the use of domestic CCPs. The ability of third country CCPs to provide clearing services under overseas mandatory clearing regimes may also incentivize domestic CCPs to expand the range of products they offer in order to protect and expand their market share.[1]

As observed in CPSS-IOSCO's May 2010 report entitled *Guidance on the application of the 2004 CPSS-IOSCO Recommendations for Central Counterparties to OTC derivatives CCPs*, "[g]reater use of CCPs for OTC derivatives will increase their systemic importance."[2] Successful management of systemic risk will require a regulatory regime that incorporates appropriate measures whereby more than one CCP may be utilized for purposes of the mandatory clearing obligation. As such, CME Group believes that this can be best accomplished by allowing central clearing through both domestic and foreign CCPs.

As is discussed in the Consultation Paper, the recognition of foreign CCPs would require a "comparability" analysis -- rather than requiring overseas recognised bodies to comply with potentially conflicting regulatory standards set by the provincial regulators, the better approach would be to rely on the relevant regulatory regime in the CCP's home country, if it is found to provide comparable obligations and protections. CME Group is very supportive of this approach; the UK Financial Services Authority has utilized this approach for a number of years in connection with recognised overseas clearing houses, including CME Clearing, and recognised overseas investment exchanges.

Further, CME Group suggests that the Committee consider certain measures which would facilitate the entry of foreign CCPs into the Canadian markets. From a general perspective, the Consultation Paper is not clear on whether a CCP would be required to obtain regulatory approval and status from all Canadian securities regulators or whether a mechanism could exist whereby a CCP could deal with one designated primary jurisdiction. A system whereby a CCP would be required to get approval from each regulator would entail a significant amount of duplicative effort on the part of the CCP. We would suggest that the Committee consider the implementation of a "passporting" regime which would provide for a single approval process with one provincial regulator with automatic recognition in other jurisdictions. For this to work, however, this regime must be uniform across Canada. Subsequent to the approval process, we

[1] IOSCO Report, at 38.
[2] CPSS-IOSCO May 2010 consultative report, at 1.

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also believe that there the needs to be coordinated reporting and similar regulatory obligations imposed on CCPs across provincial regulators.

2. Suggested Revisions to Canadian Law

In the Consultation Paper, the Committee seeks comment on whether there are changes that need to be made to Canadian law to facilitate the efficiency of OTC derivatives clearing, either for a domestic or foreign CCP.

With respect to specific changes which we believe would facilitate the efficiency of clearing of derivatives, we have identified certain areas where we believe that greater clarity could be given in particular by creating greater certainty as to the finality of settlements and transfers of collateral and by ensuring unimpeded rights to deal with collateral in the event of a default. First, we believe there needs to be clarification that settlements and transfers of collateral under cleared transactions are not potentially subject to claw back risk under federal or provincial assignments and preferences legislation or fraudulent conveyance legislation. Second, we believe that there must be clearer rules on priority with respect to collateral provided to clearing members and CCPs. Current deficiencies in Canadian legislation in this regard are:

(i) the potential for some super-priority statutory liens and deemed trusts (federal and provincial) to interfere with a clearing member's or CCP's right to fully enforce its interest in collateral (e.g., s.30(7) of the Ontario Personal Property Security Act ("PPSA"); retail sales, tobacco and gasoline tax liens, Income Tax Act);

(ii) the inability to perfect a security interest in cash collateral by control or transfer of the funds to the clearing member or CCP and to be assured of priority on that basis. A regime that depends on the filing of financing statements and priority by order of registration is inadequate to the margining requirements in derivatives, futures and other cleared markets;

(iii) the definition of the term "futures intermediary" in the PPSAs should include dealers who are exempt from registration in recognition that certain future dealers may not be required to be registered in Canada (e.g., where they are dealing only with a U.S. manager acting for Canadian customers) the definition should not be restricted to those registered (or exempted) by Canadian regulators. The current definition currently only includes registered dealers; and

(iv) in Quebec, the definition of clearing agency in the Quebec Securities Transfer Act should include CCPs that are exempt from recognition in the jurisdiction.

Finally, we believe that a netting protection law (similar to section 13 of the Payment Clearing and Settlement Act) under provincial law should be enacted that would ensure enforceability notwithstanding other provincial laws such as receivership and corporate plans of arrangement under the business corporations legislation.

In general, the approach taken by the Committee and the recommendations outlined in the Consultation Paper are consistent with many of the international standards proposed or promulgated by US and European regulators. In reviewing the Consultation Paper, we have additional comments with respect to certain specific subject matter areas.

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3. Participant Eligibility

In the Consultation Paper, the Committee proposes to impose participant eligibility requirements which are objective, risk-based and justified in terms of the safety and efficiency of the CCP and the market it serves. In doing so, the Committee cites the provisions Commodity Futures Trading Commission ("CFTC" or "Commission") Regulation 39.12 as well as Core Principle C applicable to DCOs.[3]

CME Group supports the regulatory objective of participation requirements that are risk appropriate without being unnecessarily restrictive in order to promote fair and open access. Several of our prior comment letters on this topic similarly underscored the critical importance of a diversified, qualified and well-capitalized group of clearing members who play a central role in risk management and systemic-risk containment.

We continue to have concern about any rules which would impose arbitrary constraints on a CCP"s ability to establish appropriate admission and continuing eligibility standards for its clearing members. For instance, in Regulation 39.12(a)(2)(iii), the CFTC has prohibited DCOs from setting "a minimum capital requirement of more than $50 million for any person that seeks to become a clearing member in order to clear swaps." Capital requirements are just one aspect of an overall package of requirements for clearing membership, which also includes operational and risk management capabilities, product expertise and, for OTC derivatives, specific default management capabilities and demonstrated access to necessary market liquidity. Although the regulations permit a DCO to scale its risk tolerance to clearing members in proportion to their respective capital levels, this does not fully address concerns regarding clearing members" ability to fulfill their obligations to participate in auctions or allocations in the event of another clearing member's default.

In the CPSS/IOSCO April 2012 Report entitled *Principles for Financial Markets Infrastructure* ("FMIs"), the Report states that an "FMI should always consider the risks that an actual or prospective participant may pose to the FMI and other participants. Accordingly, an FMI should establish risk-related participation requirements adequate to ensure that its participants meet appropriate operational, financial and legal requirements to allow them to fulfill their obligations to the FMI, including the other participants, on a timely basis." In certain cleared swap markets where portfolio size and associated risk may be significant, clearing members may require minimum capital in excess of $50 million in order to fulfill their obligations to take an active part in the CCP's default procedures. We expect that the amount of minimum capital (as well as operational and risk management capabilities) that a CCP will require from its OTC clearing members will evolve over time as cleared OTC markets evolve. It is therefore critical for each CCP to have reasonable discretion to determine appropriate capital requirements for its clearing members, based upon its own analysis of the particular characteristics of the swaps that it clears and the participation requirements, including clearing members" obligations to take part in default proceedings. CME Group urges the Committee to refrain from imposing a "one size fits all" cap on clearing member capital requirements.

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3 Commodity Exchange Act Sec. 5b(c)(2)(C), 7 U.S.C. Sec. 7a-1(c)(2)(C).

4. Governance

In Section 8.2 of the Consultation Paper, the Committee recommends that CCPs adopt corporate governance policies to ensure an appropriate proportion of board members reflect diverse stakeholders, including clearing members and persons clearing indirectly through clearing members. It also proposes standards for independence which indicate independence from the CCP management, CCP ownership and affiliation with CCP clearing members.

We agree with an approach that adopts a flexible standard rather than one which requires compliance with a one size-fits-all approach with mandated percentages of independent and other types of directors. The regulation of the composition of the board of a CCP is of notable concern due to the level of expertise necessary to provide effective service. In its experience, CME Group has needed a certain level of flexibility to ensure that the individuals who serve on its board are properly qualified. This is particularly true in the case of board committees. Our Clearing House Risk Committee ("Risk Committee") is charged with making detailed and complicated decisions regarding risks posed to CME Clearing. An individual serving on the Risk Committee must have detailed knowledge and experience in clearing and derivatives markets in order to be qualified to make these important decisions on behalf of CME Clearing. CME Group has been well-served over time by a Risk Committee consisting of a variety of market participants. We seek expertise and balanced views on the Risk Committee such that no one perspective prevails in our decision-making process. Our Risk Committee achieves a balance in views between large and small firms, non-clearing firm audiences such as settlement bank representatives and independent parties. However, needs will evolve over time, and consequently we believe that any final rule must provide a CCP with suitable flexibility to determine composition.

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CME Group thanks the CSA Derivatives Committee for the opportunity to comment on this matter and we would be happy to discuss any of these issues. If you have any comments or questions, please feel free to contact me at (312) 930-3488 or Kathleen.Cronin@cmegroup.com; or Christopher Bowen, Managing Director, Chief Regulatory Counsel, at (212) 299-2200 or Christopher.bowen@cmegroup.com.

Sincerely,

Kathleen M Cronin

Kathleen Cronin
Senior Managing Director, General Counsel
and Corporate Secretary