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January 7, 2013

The Honorable Gary Gensler  
U.S. Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, NW.  
Washington,  
DC 20581

**RE: Chicago Mercantile Exchange Inc. ("CME") Submission # 12-391**

Dear Chairman Gensler:

The Global Foreign Exchange Division ("GFXD") of the Global Financial Markets Association ("GFMA") welcomes the opportunity to comment on behalf of its members on the proposal made by the Chicago Mercantile Exchange Inc. ("CME") in its amended submission # 12-391R dated December 6, 2012 (the "**Submission**"), which requests the Commission to approve of a new Chapter 10 and Rule 1001 (the "**Proposed Rule**") of the CME's Swap Data Repository ("**SDR**") rulebook.

The GFXD was formed in cooperation with the Association for Financial Markets in Europe ("AFME"), the Securities Industry and Financial Markets Association ("SIFMA") and the Asia Securities Industry and Financial Markets Association ("ASIFMA"). Its members comprise 22 global foreign exchange market participants<sup>1</sup>, collectively representing more than 90% of the foreign exchange dealer market<sup>2</sup>. Both the GFXD and its members are committed to ensuring a robust, open and fair marketplace and welcome the opportunity for continued dialogue with the Commodity Futures Trading Commission (the "**Commission**").

**Summary**

Our members believe that the Commission should not approve the Proposed Rule for multiple reasons. The intention of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank**") was to promote accountability and transparency in the derivatives market, including requiring designated clearing organizations ("**DCO**") such as the CME to "permit fair and open access"<sup>3</sup>. The Proposed Rule, which would require all swaps cleared with the CME to be reported to the CME's SDR, violates this principle on its face. Furthermore, the Commission has clearly indicated that "consistent with the principles of open access... a registered swap data repository shall not tie or bundle the offering of mandated regulatory services with other ancillary services that a swap data repository may provide to market participants."<sup>4</sup> The Proposed Rule would tie the use of the CME's clearing function to a customer's use of the CME's SDR in violation of this rule. We emphasize that the concerns raised in this letter are not exclusive to the CME and the Proposed Rule but apply generally to any DCO that seeks to require all swaps cleared with it to be reported to a specific SDR.

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<sup>1</sup> Bank of America Merrill Lynch, Bank of New York Mellon, Bank of Tokyo Mitsubishi UFJ, Barclays Capital, BNP Paribas, Citigroup, Credit Agricole, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan, Lloyds, Morgan Stanley, Nomura, Royal Bank of Canada, Royal Bank of Scotland, Société Générale, Standard Chartered Bank, State Street, UBS, and Westpac.

<sup>2</sup> According to Euromoney league tables.

<sup>3</sup> CEA section 5(b)(c)(2)(C)(iii), as amended by Dodd-Frank.

<sup>4</sup> 17 C.F.R. § 49.27(a)(2).

In the Submission, the CME claims that such concerns are irrelevant because after a swap is cleared, the CME "should be the only entity with reporting obligations for the resulting swaps"<sup>5</sup>, and the rule therefore only applies to the CME. However, swap dealers and major swap participants ("SDs/MSPs") remain obligated to report daily valuation data even if a swap is cleared with the CME<sup>6</sup>, so would be forced to report to the CME's SDR, which imposes on SDs/MSPs the additional costs of creating informational links with multiple SDRs, increases fragmentation of swap data and thereby reduces swap market transparency for regulators.

In addition, the Submission fails to address the cost concerns of the Proposed Rule that have been raised by parties such as the Depository Trust & Clearing Corporation ("DTCC")<sup>7</sup>, since various market participants have expended significant time and expense toward designing and establishing information technology systems and infrastructure to comply with rules for swap data reporting promulgated by the CFTC as well as foreign regulators. These efforts were undertaken on the assumption that the Commission would not permit DCOs to create anti-competitive standards such as the Proposed Rule.

#### **I. The Proposed Rule removes reporting party choice as to the SDR and forces SDs/MSPs to use the CME's SDR.**

The Commission's final rules on Swap Data Recordkeeping and Reporting Requirements (the "Reporting Release")<sup>8</sup> set out clear and distinct responsibilities for the reporting of swap transactions. They do so in a manner that promotes efficiency and minimizes the overall costs of regulatory reporting. The Reporting Release rightly places greater obligations on those parties that are best suited to manage them. It also sets out an important principle that "all swap data for a given swap must be reported to a single SDR, which must be the SDR to which required primary economic terms data for that swap is first reported"<sup>9</sup>. Not only does this provide regulators with better and more efficient access to swap data without the need to reconstruct a swap's lifecycle through data that is fragmented across multiple SDRs<sup>10</sup>, it is also more efficient from the perspective of the Reporting Counterparty.

Because the Commission has identified that certain parties, and in particular SDs and MSPs, have ongoing obligations to report swap continuation data, we believe it is important to give those parties the choice as to which SDR they wish to report. This allows them to choose the SDR that best suits their needs: a choice which may take in to account wider reporting responsibilities. For example, a U.S. counterparty that only trades cleared swaps may find it optimal to report all of its swap data to an SDR that is linked to a DCO (but should not have the designation forced upon it). However, many SDs/MSPs have additional regulatory concerns that would cause reporting swap data to another SDR to be more efficient, such as Part 23 reconciliation requirements or reporting obligations to foreign regulators. For example, for a swap executed between a European SD/MSP and a counterparty that is a U.S. Person, the SD/MSP will be required to report swap data in accordance with the CFTC rules as well as the European regulatory regime. A DCO's captive SDR may not meet the European regulator's requirements or may choose not to register with the European regulatory authorities (to the extent any such registration is required), so a rule that requires the SD/MSP to report swap data to the DCO's captive SDR would force the European SD/MSP to report swap data to multiple SDRs and may even be in contravention of the rules of the European regulator. However, there may be other SDRs which comply with both regulatory standards, and would therefore be far more efficient for an SD/MSP to use. Therefore, the appropriate way to satisfy reporting obligations (including obligations of foreign regulators) will be to report swap

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<sup>5</sup> See page 2 part 5) of the Submission.

<sup>6</sup> Commission Rule 45.4(b)(2)(ii).

<sup>7</sup> See the comment letter on the Proposed Rule to the CFTC from dated November 20, 2012 (the "DTCC Letter").

<sup>8</sup> See 17 CFR Part 45; RIN 3038-AD19; 77 F.R. 2136 (Jan. 13, 2012).

<sup>9</sup> See Reporting Release at 2168.

<sup>10</sup> The Commission believes that important regulatory purposes of the Dodd-Frank Act would be frustrated, and that regulators' ability to see necessary information concerning swaps could be impeded, if data concerning a given swap was spread over multiple SDRs. See Reporting Release at 2168.

data to an SDR of such party's choice – something that would not be fully taken into account in a simple cost-benefit analysis of the various swap reporting scenarios. Accordingly, we strongly believe that the counterparties to the original swap should be able to select the SDR to which the reporting is made (including for cleared swaps), as provided in the Commission's original (and now withdrawn) FAQ guidance.

In refuting the concerns raised by DTCC to the Proposed Rule, the CME ignored these important market participant concerns and relied almost exclusively on its argument that the Proposed Rule only relates to "the manner by which CME Clearing is meeting and will meet *its* regulatory reporting obligations" because the Proposed Rule, on its face, is only applicable to the CME<sup>11</sup>. However, this argument is not persuasive because it ignores the ongoing obligations of SDs/MSPs to report valuation information as well as the fact that the Reporting Release explicitly contemplates a different reporting regime.

#### A. SD/MSP Reporting Obligations

In the Submission, the CME argues that "Consistent with its role as the central counterparty, CME...should be the only entity with reporting obligations for the resulting swaps and related positions.<sup>12</sup>" However, this provision ignores the obligation of SDs/MSPs to report valuation data even for cleared swaps, as per Commission Rule 45.4(b)(2)(ii), which provides that "valuation data for the swap must be reported as follows: (i) By the derivatives clearing organization, daily; and (ii) If the reporting counterparty is a swap dealer or major swap participant, by the reporting counterparty, daily.<sup>13</sup>" This rule clearly establishes that the CME will not be the only party that is required to report swap data to the SDR with respect to cleared swaps.

The obligation of SDs/MSPs to report valuation data will entail a significant effort on their part. SDs/MSPs cannot simply rely on the valuation prepared by the DCO, but will instead apply their own calculations and methodologies to determine the correct valuation for each swap. In order to do so, SDs/MSPs will need to have full and accurate access to all data for such swap, including life cycle events that may alter their valuation of such swap. Forcing SDs/MSPs to report swap data to multiple SDRs will only exacerbate these difficulties, as they will need to reconcile the swap data in their records with swap data being reported by DCOs to multiple SDRs and also ensure that the information contained in each SDR is accurate and up to date<sup>14</sup>. Given the ongoing SD/MSP valuation reporting requirements, it would increase efficiency and decrease the likelihood of the mis-valuation of swaps if SDs/MSPs were permitted to select the SDRs to which to report their swaps data.

The CME cannot argue that this obligation is extinguished when the swap is cleared, because the Commission Rule and the Reporting Release make it clear that valuation reporting by the SD/MSP is in addition to any such reporting by the CME<sup>15</sup>. As Commission Rule 45.10 provides that all swap data for a given swap must be reported to the SDR to which the swap creation data was made, the Proposed Rule would require all SDs/MSPs to report valuation data to the CME's SDR for any swap cleared by the CME. Therefore, the CME's argument that the Proposed Rule only affects the CME's reporting obligations is simply incorrect – the direct effect of the Proposed Rule will be to require all SDs/MSPs to

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<sup>11</sup> The CME is relying on the language in the Proposed Rule that states "the Clearing House shall report", rather than a reference to all parties. Submission, Appendix A.

<sup>12</sup> See page 2 part 5) of the Submission.

<sup>13</sup> Emphasis added.

<sup>14</sup> We note that this should not be a problem for DCOs, as they will already have all relevant information for their own valuation reporting obligations because of their role in clearing the swap.

<sup>15</sup> After considering comments received, the Commission has determined that for cleared swaps where the reporting counterparty is a non-SD/MSP, a DCO's valuation is sufficient for regulatory purposes....Because prudential regulators have informed the Commission that counterparty valuations are useful for systemic risk monitoring even where valuations differ, the final rule requires SD and MSP reporting counterparties to report the daily mark for each of their swaps, on a daily basis. Reporting Release, at 2154.

report valuation data for swaps cleared by the CME to the CME's SDR. As such, the CME's contention that this rule "does not impose any condition precedent on a CME clearing member" is simply untenable.

## B. The Reporting Release

In the Reporting Release, the Commission stated that the CME had recommended that initial data reporting for cleared swaps should be made to a DCO or an SDR chosen by the DCO. However, the Commission expressly chose not to adopt such a rule, and noted that "because the final rule does not require each cleared swap to be reported to an SDR affiliated with the DCO that clears the swap, in some circumstances DCOs may incur some increased costs, relative to an environment in which all cleared swaps must be reported to a DCO–SDR."<sup>16</sup> The Commission further went on to state that:

For an off-facility, cleared swap with respect to which the reporting counterparty makes the initial PET data report, the DCO would incur incremental costs if the reporting counterparty chooses to report to an SDR other than the DCO–SDR. In this circumstance the DCO would be required to report confirmation data and continuation data to the SDR receiving the initial report, and thus to assume the costs necessary to establish connectivity to that SDR and transmit data to it.<sup>17</sup>

In both instances the Commission's language clearly indicates that in certain circumstances reporting parties other than DCOs would be permitted to select the SDRs to which their swaps should be reported, in particular if the PET data was reported by the SD/MSP to another SDR. Indeed, the Commission plainly stated that the party who makes the first swap data report for the swap "in effect choose[s] the SDR"<sup>18</sup>. However, the Proposed Rule would require the CME and SDs/MSPs to report swap data to the CME's SDR only, which expressly contradicts the Commission's language in the Reporting Release.

Furthermore, the Commission clearly did not intend to require each cleared swap to be reported to an SDR affiliated with the DCO.<sup>19</sup> The Proposed Rule would, in effect, frustrate the Commission's intent because it would permit the CME to achieve by a Commission-approved DCO rule what it could not achieve by a Commission rule. Since the Commission refused to grant the CME's request in the Reporting Release, we urge the Commission to refuse to permit it by means of a DCO rule instead.

## II. The Proposed Rule is Anti-Competitive

The Commodity Exchange Act (the "**CEA**") mandates fair and open access to clearing services,<sup>20</sup> and that an SDR "shall not [a]dopt any rule or take any action that results in any unreasonable restraint of trade; or [i]mpose any material anticompetitive burden on the trading, clearing, or reporting of transactions."<sup>21</sup> These principles are key in promoting a strong SDR market by encouraging competition. As the Commission noted in the Reporting Release:

requiring that all cleared swaps be reported only to DCOs registered as SDRs or to SDRs chosen by a DCO would create a non-level playing field for competition between DCO–SDRs and non-

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<sup>16</sup> Reporting Release at 2186.

<sup>17</sup> Reporting Release at 2187 (emphasis added). The Reporting Release does continue to state that "if the DCO chooses to register as an SDR, as explicitly permitted by the statute and anticipated by these commenters, the reporting counterparty would be able to reduce its costs by selecting the DCO–SDR as the SDR receiving the initial report, and thus avoid the need to send data separately to an SDR for regulatory reporting purposes and to a DCO for clearing purposes." However, in this context "reporting counterparty" clearly does not refer to the DCO itself, since the initial PET report referenced in the first sentence would be made by one of the original counterparties if the swap is not accepted for clearing prior to the relevant deadline.

<sup>18</sup> Reporting Release at 2168.

<sup>19</sup> See Reporting Release at 2149 .

<sup>20</sup> See CEA § 5b(c)(2)(C)(iii).

<sup>21</sup> See CEA § 21(f)(1).

DCO SDRs. The Commission also believes that it would make DCOs collectively, and could in time make a single DCO–SDR, the sole recipient of data reported concerning cleared swaps.<sup>22</sup>

Yet the Proposed Rule would create exactly such a non-level playing field for non-DCO SDRs and would allow the CME to accomplish by DCO rule a market position that the Commission rightly feared.

In addition, the Proposed Rule would create a condition precedent for the use of clearing services in violation of Commission Rule 49.27, which prohibits SDRs from tying or bundling "mandated regulatory services with other ancillary services that a swap data repository may provide to market participants". The Commission was conscious of this, confirming to Commissioner Bart Chilton that "a registered SDR, consistent with the principles of open access, shall not tie or bundle the offering of mandated regulatory services with other ancillary services that an SDR may provide to market participants."<sup>23</sup> Congress was also concerned about this issue, repeatedly expressing concern regarding the applicability of anti-bundling provisions to DCOs.<sup>24</sup> The Proposed Rule would clearly violate the Commission's rules on bundling as well as the spirit of Dodd-Frank's commitment to the efficiency and transparency of the swaps market.

The CME's proposal is also inconsistent with the approach taken to SDRs by other regulators. For example, the Committee on Payment and Settlement Systems ("CPSS") and the International Organization of Securities Commissions ("IOSCO") issued a paper in April 2012 which stated that "[A] TR [trade repository] should not engage in anti-competitive practices such as product or service tying... . A TR should also not develop closed, proprietary interfaces that result in ... barriers to entry with respect to competing service providers ... ." <sup>25</sup> (An SDR would be a trade repository for these purposes.)

In the Submission, the CME attempted to dismiss these concerns by arguing that the Proposed Rule was only relevant to the CME's reporting obligations and that the anti-competitiveness concern is "overblown"<sup>26</sup>. Neither argument is persuasive.

As already discussed above in part I.A. of this letter, the Proposed Rule would require all SDs/MSPs that clear swaps with the CME to report valuation data to the CME's SDR. Therefore, the CME's claim that the rule cannot be anti-competitive because it only clarifies how the CME will fulfill its reporting obligation is incorrect. With respect to the anti-competitive concerns, the CME observed that another leading DCO, LCH.Clearnet Limited ("**LCH**"), does not require reporting to LCH's SDR. However, if the Proposed Rule is approved, there will be nothing to prevent LCH from promulgating a similar rule. The Commission should not leave competition in the SDR market to the good graces of the DCOs.

A requirement that reporting for all swaps cleared with the CME must use the CME's SDR will ultimately tilt the SDR market against SDRs that are not affiliated with a DCO, which would discourage competition and lead to less efficiency and higher SDR prices for consumers. In addition, the Proposed Rule would bundle the CME's clearing and reporting services, in violation of the spirit of Dodd-Frank, the Commission's rules and Congressional concerns that no such bundling should occur.

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<sup>22</sup> Reporting Release, at 2149.

<sup>23</sup> Commodity Futures Trading Commission (CFTC), Open Meeting to Discuss a Final Rule on Derivatives Clearing Organization General Provisions and Core Principles; a Final Rule on Position Limits for Futures and Swaps; and a Notice of Proposed Amendment to Effective Date for Swap Regulation (Oct. 18, 2011) (colloquy between The Honorable Bart Chilton and Mr. Ananda Radhakrishnan).

<sup>24</sup> For example, Continuing Oversight of the Wall Street Reform and Consumer Protection Act: Hearing Before the Senate Comm. on Agriculture, Nutrition, and Forestry, 112th Cong. 74 (2011).

<sup>25</sup> CPSS-IOSCO, "Principle for Financial Market Infrastructures" (April 2012) Section 3.18.4; available at <http://www.bis.org/publ/cpss101a.pdf>

<sup>26</sup> Submission, pages 5-6: DTCC Argument 2: Violation of Fair and Open Access Principles and page 7: DTCC Argument 3: Violation of Anti-Competitive Provisions.

### III. The Proposed Rule would weaken reporting infrastructure and increase costs

As a result of the Proposed Rule, a swap could effectively be reported to more than one SDR, which would increase the risks of errors in reporting of data. As recognized in the Submission, immediately after executing an off-facility swap, SDs/MSPs would be required to report it to an SDR for real time reporting (Part 43) purposes and would be required to report the primary economic terms ("**PET**") data to an SDR if the swap was not accepted for clearing by the relevant deadline. There is no requirement (and there should be no requirement) that the SD/MSP make such reports to the CME's SDR. However, under the Proposed Rule, once cleared through the CME, the original swap would be extinguished, and the CME would report the swap to its SDR. This could result in the use of more than one SDR and risks fragmentation of information in the swap market, which the Commission has stated it is trying to avoid.<sup>27</sup> The Commission addressed fragmentation by requiring that all swap reporting must be made to the SDR to which the initial swap was reported. The purpose of this rule would be undermined if reporting for a swap before and after acceptance for clearing went to separate SDRs.

In addition, if SDs/MSPs are required to report swap data to each DCO's captive SDR, it will require SDs/MSPs to develop operational connections to each SDR of a DCO. This additional burden would come on top of the need to pay for the DCO's SDR either directly or by paying more generally for clearing services. Given that use of DCOs for clearing will be mandatory, the costs for using DCOs should be as low as possible and DCOs should not be permitted to effectively force SDs/MSPs to pay for additional services beyond clearing.

Finally, over the past year, many market participants have spent considerable time, effort and expense preparing to comply with the Commission's swap reporting rules. Relying on Commission Rules in Part 45 and 49, as well as the Commission guidance in the Reporting Release that it would not permit DCOs to dictate which SDRs could be used by its participants, SDs/MSPs have focused on creating reporting systems with single access points for regulatory reporting. The Proposed Rule would require SDs/MSPs to restructure the operations and plans that they have already developed for reporting.

#### Conclusion

For the reasons set forth above, we urge the Commission to reject the Proposed Rule.

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We appreciate the opportunity to share our views on the Proposed Rule. Please do not hesitate to contact me at +44 20 7743 9319 or at [jkemp@gfma.org](mailto:jkemp@gfma.org) should you wish to discuss any of the above.

Yours sincerely,



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<sup>27</sup> Reporting Release, 77 F.R. 2149.

<sup>28</sup> The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA.