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SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-66941; File No. SR-CME-2012-06)

May 8, 2012

Self-Regulatory Organizations; Chicago Mercantile Exchange Inc.; Order Approving Proposed Rule Change to Amend Rules Related to Credit Default Swap Guaranty Fund Allocations, End-of-Day Pricing Procedures, Daily Submission Deadlines, Holiday Accrual Processing, and the Price Alignment Interest Payment Timeline

I. Introduction

On March 9, 2012, Chicago Mercantile Exchange (“CME”) filed with the Securities and Exchange Commission (“Commission”) proposed rule change SR-CME-2012-06 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder.² The proposed rule change was published for comment in the Federal Register on March 29, 2012.³ The Commission received no comment letters regarding this proposal. For the reasons discussion below, the Commission is granting approval of the proposed rule change.

II. Description

CME currently offers clearing services for certain credit default swap (“CDS”) index products. CME proposes to amend certain of its rules that would generally affect its CDS clearing offering and to make corresponding amendments to certain sections of its Manual of Operations for CME Cleared Credit Default Swaps (“CDS Manual”). The rule amendments would modify CME’s CDS guaranty fund allocation methodology, end-of-day pricing procedures, daily submission deadlines, holiday accrual processing, and the timeline for price alignment interest (“PAI”) payment timeline.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Release No. 34-66646 (March 22, 2012), 77 FR 19045 (March 29, 2012).

The proposed changes to text in the CME rulebook would amend current requirements found in CME Rule 8H07.1 relating to the allocation of the CDS guaranty fund requirements among CDS clearing members. Currently, CME calculates its guaranty fund monthly and proportionally allocates to each CDS clearing member a guaranty fund requirement based on the CDS clearing member's 90-day trailing average of its potential residual loss and 90-day trailing average of its gross notional open interest outstanding at CME. CME is proposing to change the measurement period from 90 days to 30 days so that a CME clearing member's CDS guaranty fund requirement more quickly react to the CDS clearing member's current activity and to align the measurement period with the frequency of CDS guaranty fund calculations.

The proposed changes to the text of the CDS Manual would modify end-of-day pricing procedures including procedures for CDS price submissions, crossing, and auction procedures that CME uses to arrive at the settlement price for CDS contracts. Currently, CME requires CDS clearing members to submit price levels for the full term structures of all indices and single-name reference entities by seniority, restructuring type, and currency eligible for clearing. If a CDS clearing member chooses to submit price levels on a cleared contract in which it does not hold open interest, CME hold that price submission as tradable if a cross occurs and the submitted instrument is selected pursuant to the auction process. However, under CME's current procedures, submitted price levels for non-cleared instruments are never actionable (i.e., tradable). CME is proposing to change it CDS Manual to require CDS clearing members to submit price levels for all cleared contracts in which they or their customers hold open interest. For indices where CDS clearing members are required to submit the full clearing eligible tenors of all indices, CME will only cross CDS clearing members on the tenors in which the CDS clearing members or their customers hold open interest. For single-name CDS, CME will

require CDS clearing members to submit mid price levels for the full term structures for the 0, 0.5-, 1-, 2-, 3-, 4-, 5-, 7- and 10-year tenors. However, CME may cross the CDS clearing members on any single-name reference entity in which the CDS clearing members or their customer(s) hold open interest irrespective of tenor.

CME is also amending its CDS Manual to change (1) the daily submission deadlines for CDS, (2) the CDS holiday accrual processing, and (3) the PAI payment timeline. With respect to operations timelines and reports, CME would move up the trade submission deadline for current day trades from 7:59 pm ET to 6:59 pm ET. With respect to position management, money calculations, and collateral, the revisions to the CDS Manual would require on bank holidays in the country of which the swap is denominated (e.g., Independence Day for U.S. Dollar denominated CDS contracts), accrual processing would be included in the processing for the next business day and would not occur on the relevant bank holiday. In addition, CME would calculate and pay PAI for CDS contracts on a daily basis as opposed to monthly.

III. Discussion

Section 19(b)(2)(C) of the Act 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.⁴ In particular, Section 17A(b)(3)(F)⁵ of the Act requires, among other things, that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible. By making CDS clearing members' guaranty fund requirements be based on relatively more recent histories, the

⁴ 15 U.S.C. 78s(b)(2)(C).

⁵ 15 U.S.C. 78q-1(B)(3)(F).

proposed amended rule governing guaranty fund allocations should improve CME's ability to react to CDS market dynamics and thereby should help CME better assure the safeguarding of securities and funds which are in its custody or control or for which it is responsible. As such, the proposed rule change is consistent with the requirements of Section 17A(b)(3)(F) of the Act. Also, the requirement that CDS clearing members submit pricing for all tenors of clearing-eligible indices and for the full term structure for single-name CDS should enhance CME's ability to derive end-of-day settlement prices. In addition, because the operational changes CME is proposing would generally require clearing members to make trade submissions more promptly, require CME to calculate price alignment more frequently, and clarify when price accrual processing occurs in the event of a bank holiday, such a change should promote the prompt and accurate clearance and settlement of securities transactions and derivative agreements, contracts, and transactions and therefore is consistent with the requirements of Section 17A(b)(3)(F) of the Act.

IV. Conclusion

On the basis of the foregoing, the Commission finds the proposal is consistent with the requirements of the Act and in particular with the requirements of 17A of the Act and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-CME-2012-06), be, and hereby is, approved.⁶

For the Commission, by the Division of Trading and markets, pursuant to delegated authority.⁷

Kevin M. O'Neill
Deputy Secretary

[FR Doc. 2012-11533 Filed 05/11/2012 at 8:45 am; Publication Date: 05/14/2012]

⁶ In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁷ 17 CFR 200.30-3(a)(12).