CME Group

Craig S. Donohue
Chief Executive Officer

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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: Market-Wide Circuit Breakers: Comments Regarding SR-FINRA-2011-054; SR-BATS-2011-025; SR-BYX-2011-025; SR-C2-2011-024; SR-CBOE-2011-087; SR-CHX-2011-030; SR-EDGA-2011-31; SR-EDGX-2011-30; SR-ISE-2011-61; SR-BX-2011-68; SR-PHLX-2011-129; SR-NASDAQ-2011-131; SR-NYSE-2011-48; SR-NYSEAMEX-2011-73; and SR-NYSEArca-2011-68.

CME Group Inc. ("CME Group") appreciates the opportunity to comment on the filings recently submitted by the national stock exchanges (the "Exchanges") and the Financial Industry Regulatory Authority, Inc. ("FINRA") proposing rule amendments that would revise the existing program of market-wide circuit breakers to better address circumstances of extraordinary market volatility across the securities markets.

CME Group is one of the world's largest and most diverse derivatives marketplaces. We operate four separate exchanges, including 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"). Our exchanges 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.

Included among these offerings are a number of domestic and global equity index futures and futures options on key benchmark indexes, including, for example, the S&P 500, the Dow Jones Industrial Average and the NASDAQ-100. CME Group's equity index markets trade 23¼ hours a day and serve important risk management and price discovery functions for our customers around the globe. Average daily volume across our equity index complex was 4.4 million contracts in September 2011. The E-mini S&P 500 Index futures, the world's most actively traded index futures contract, traded an average daily notional value of $193 billion during that period, and open interest in CME's suite of products linked to the S&P 500 Index stood at more than 6.5 million contracts at the end of the third quarter. CME Group's equity index markets are, of course, closely interconnected with the cash securities and related derivative markets, and because economic events tend to be most rapidly reflected in futures market prices, there are important implications for how tools such as market-wide circuit breakers are implemented in the futures market and coordinated with other related markets.

Background

The "Flash Crash" of May 6, 2010 clearly challenged confidence in the markets and prompted the industry to reevaluate the mechanisms in place to address occurrences of extreme market-wide volatility. On that day, the Dow Jones Industrial Average fell as much as 9.2% intraday, but despite the speed and scope of the market decline, the existing market-wide circuit breakers were not triggered and the pervasive assessment was that the markets were allowed to fall too far too fast. The applicable market-wide circuit breaker in effect at the time of the most dramatic price decline, which occurred shortly after 2:40 p.m. ET, was 20%, meaning that it would have taken a decline more than twice the magnitude the markets experienced that day to have triggered a halt in trading.

Since the events of that day, CME Group has strongly advocated for a reevaluation of the market-wide circuit breaker regime to promote greater investor confidence, ensure better alignment with today's market structures, and to serve as a more effective buffer against the type of macro-market price destabilization that has the potential to threaten the infrastructure of trading, clearing and credit systems. CME Group is therefore pleased with the initiative to recalibrate and better coordinate the market-wide circuit breakers and fully supports the fundamental goals of the proposed rule to promote market stability and investor confidence.

The proposed rule would revise key elements of the current system of market-wide circuit breakers by:

- reducing the trigger thresholds to 7, 13 and 20 percent from 10, 20 and 30 percent, and simplifying the schedule of times during which specific triggers are applicable;

- shortening the duration of the trading halts to 15 minutes from 30-120 minutes for any halt that does not otherwise close the market for the day; and

- using the S&P 500 Index rather than the Dow Jones Industrial Average as the pricing reference and recalculating the trigger thresholds daily instead of quarterly.

We do, however, have substantive concerns with certain aspects of the proposed rule changes which we believe should be addressed before implementing final rules. These concerns include the following:

- The failure to adequately evaluate the interaction of market-wide circuit breakers and single-security circuit breakers in a macro-market event and the corresponding risk of potential negative impacts to risk management capabilities, liquidity provision and operational capabilities;

- The proposal to apply only the Level III (20%) circuit breaker after 3:25 p.m. ET, and the implications for allowing such a significant market decline without any intervening market-wide trading halts;

- The absence of limits or circuit breakers in the securities space during afterhours trading, and the consequent lack of coordination between the securities and futures markets in this respect; and

- Calculating circuit breaker thresholds daily will create greater operational and communication challenges, and both market participants and market centers would benefit from thresholds established weekly rather than daily.

Interaction of Single-Security and Market-Wide Circuit Breakers

The pilot program of single-security circuit breakers currently in place and the proposed rules to replace that program with a combination of limit up/limit down and trading halt mechanisms for individual securities are well-meaning efforts by the securities exchanges to prevent erroneous trades and to address transitory liquidity gaps that led to gross distortions in the prices of many securities on May 6th. These price distortions resulted in more than 20,000 securities transactions being cancelled that day and many thousands more being allowed to stand at anomalous prices, both of which seriously undermined investor confidence in the integrity of the markets and compromised market participants' ability to effectively understand and manage their risk exposure. However, as noted in our previous comment letters regarding these programs, we believe the single security circuit breaker mechanisms, as implemented and proposed, result in an uncoordinated and overly complicated structure that, in a macro-liquidity event, will likely interact with the market-wide circuit breakers in ways that pose significant risk of undermining rather than promoting liquidity and thereby exacerbating rather than ameliorating market volatility.

First, in a macro-market event, multiple constituent stocks in the S&P 500 Index could be limited, halted and reopened on staggered timelines, creating complexity and confusion in understanding the index calculation and in ascertaining the true value of the index. Market participants would have no way of determining the relevance of the index values that are disseminated, and the resulting inability to discover accurate prices and perform appropriate risk management would surely impair liquidity in index-based products, including in critical benchmark products such as the E-mini S&P 500 futures. One critical lesson learned from the events of May 6th was that this kind of uncertainty leads liquidity providers to step away from the market precisely when their liquidity is most needed, and that, in turn, has the effect of exacerbating the volatility the mechanism was intended to mitigate.

Second, another key lesson of May 6th was the importance of inter-market linkages in today's markets, particularly with respect to index products, and the significant negative impacts on liquidity supply when those linkages cannot be relied upon by market participants or otherwise break down as the result of uncoordinated actions across comparable markets. In this case, single security price limits and/or trading halts would apply to ETFs that are based on equity indexes that also underlie other financial products such as equity index futures, yet the limits and halts would not be coordinated. If the SPDR S&P 500 ETF is limited or halted due to the triggering of a single-security circuit breaker while the E-mini S&P futures continues to trade in the absence of a market wide circuit breaker being triggered, demand for liquidity on the E-mini

will likely surge at the same time that liquidity providers who engage in arbitrage between the markets are pulling out of the E-mini futures. This will surely add further stress to the market during a period of turbulence and, again, will likely serve to exacerbate rather than mitigate the disruption. Therefore, we again strongly urge that the new rules provide for synchronous halting mechanisms across closely linked markets.

Third, to our knowledge, the interaction of the single-security circuit breakers and the market-wide circuit breakers has not been adequately modeled or back tested in a macro-liquidity scenario such as the type that occurred on May 6th. The impacts of the proposed structure in such a circumstance, including how the calculations of broad-based indexes would be affected, how related products will be impacted, how liquidity dynamics will be affected, and how market centers' operations will be impacted should be rigorously evaluated before proceeding. Failing to holistically examine and understand the interaction of these different volatility mechanisms prior to implementation is akin to deploying an untested trading algorithm in the marketplace. There will likely be many uncomfortable questions for regulators to answer if such testing is not responsibly performed and the supposed cure proves instead to aggravate the disease.

Simplicity, clarity and coordination are important components of any market-wide circuit breaker methodology if the objective is to minimize uncertainty, promote liquidity supply, and allow for the effective execution of the operational protocols. While we very strongly support the implementation of recalibrated market-wide circuit breakers, we believe the layers of complexity inherent in the interaction with the existing or proposed single-security circuit breakers will heighten uncertainty among market participants and undermine rather than promote liquidity during broadly volatile periods. As we have argued on many occasions in the aftermath of the "Flash Crash," transitory liquidity gaps can be ameliorated and erroneous trades prevented through automated mechanisms such as price banding, market and stop order protection points, and other volatility mitigation tools that are less disruptive than the current or proposed single security circuit breaker regime, and these types of tools will interact more effectively with market-wide circuit breakers.

Comment was solicited on the question of whether the market-wide circuit breaker should be triggered if a sufficient number of single-security circuit breakers or price limits are triggered to materially affect the calculation of the S&P 500 Index. CME Group believes that this would add even greater complexity and uncertainty given the market capitalization weighted construction of the index; again, this would likely impede rather than promote liquidity.

Comment was also solicited on whether the primary market should have a longer period (e.g., 30 minutes instead of 15 minutes) to reopen trading following a Level II market decline before trading resumes in other venues. CME Group believes that the intermediate trading halts should be as short as operationally practicable while allowing market participants sufficient time to reassess the market, evaluate risk and to have an opportunity to become aware of and respond to the significant price move. In the context of today's electronic market structure and sophisticated risk management capabilities, we believe a trading halt of15 minutes strikes the correct balance.

Lastly, the rule proposals requested comment as to whether market centers should implement rules that mandate cancellation of all pending orders, or only certain types of orders, in the event a market-wide circuit breaker is triggered. CME Group believes there is no sound basis for implementing such a rule, and we believe it would be highly disruptive to market participant operations as well as unfairly disadvantage participants who had established queue priority based on market centers' matching algorithms.

Triggering of Circuit Breakers After 3:25 p.m. ET

Under the proposed rules, the Level I (7%) and Level II (13%) circuit breakers would not apply after 3:25 p.m. ET, and, as such, there would be no circuit breaker triggered unless the S&P 500 Index fell 20% and triggered the closing of the market. While the probability of such a precipitous move within a relatively narrow time window is remote, if it were to occur, it would be extraordinarily disruptive, threaten the market's infrastructure and surely lead to substantial, and in our view, warranted criticism of the regulatory policy decisions that allowed for that scale of unimpeded market price decline to occur in such a short period of time. Additionally, as noted above, the events of May 6th reflected that the market was supremely troubled by a 9% decline without an intervening speed bump – it is not difficult to contemplate the rapid dissolution of investor confidence, not to mention the risk to the market's infrastructure, of an unencumbered 20% decline near the end of the trading day.

CME Group recommends that if the Level I circuit breaker has been triggered prior to 3:25 p.m., then only the Level III (20%) circuit breaker should apply after that time; if the Level I circuit breaker has not been triggered prior to 3:25 p.m., then the Level II circuit breaker should apply and result in the closing of the market for the balance of the session if it is triggered. This approach, in our view, strikes a more appropriate balance between responsibly protecting market stability, mitigating systemic risk and promoting investor confidence, and the desire to minimize the potential for disrupting the closing process.

The Commission also solicited comment on whether a provision should be made to hold a closing auction in the event of a Level III market decline. To do so would be inconsistent with the premise that the level of uncertainty among market participants and the risks to the market infrastructure arising from such a price move demand that the market close for the balance of the day. It is our position that holding a closing auction in a narrow time window following a 20% break in the market is an invitation for potentially greater dislocations in the market. In our view, a 20% decline is likely to be significantly disruptive on a variety of levels and the market should remain closed for the balance of the session.

Coordination of Limits During Afterhours Trading

CME Group exchanges' domestic equity indexes trade electronically throughout the 24-hour day except for the periods from 4:15 to 4:30 p.m. ET and 5:30 to 6:00 p.m. ET. Outside of regular trading hours (regular hours include the period from 9:30 a.m. to 4:15 p.m. ET), CME Group imposes upside and downside price limits of 5% - one-half the established 10% market-wide limit that is currently established on a quarterly basis. When the limit is reached, the market

does not halt, but trading may not take place at prices outside of the limits. If the market is limit offer at 9:15 a.m. ET and remains limit offer at 9:25 a.m. ET, there is a 5-minute trading halt until 9:30 a.m., during which time the exchange disseminates an indicative opening price until the market opening. The securities exchanges do not currently employ single-security circuit breakers or any other form of circuit breakers or price limits during afterhours trading, nor does the proposed regulation include any such limits or circuit breakers.

CME Group is committed to maintaining price limits during afterhours trading, as we believe it would be imprudent not to have such limits, particularly during a period in which liquidity is generally thinner. Such limits, whether established at 5% or some other appropriate level, help to preserve market stability and integrity, and those objectives remain critically important throughout the 24-hour trading cycle, rather than exclusively during regular trading hours. However, in the absence of the securities exchanges adopting a limit structure, there remains a coordination gap during the afterhours period that we believe merits further consideration.

The Commission also solicited comment on whether, in the event of a Level III circuit breaker being triggered, the markets should wait for the primary market to reopen in a particular security on the next trading day before trading in that security resumes. Given the interconnectedness of global markets today and the need to manage risk around the clock, particularly in the type of volatile conditions that would trigger a Level III circuit breaker, CME Group believes that it is appropriate to delay the opening of its markets from 4:30 p.m. until 7:00 p.m. ET, at which time the markets should be available for trading subject to the price limits that CME Group employs during the afterhours markets.

Daily Versus Weekly Thresholds

The rule proposals also recommend recalculating the trigger values daily instead of once every calendar quarter in order to ensure that the thresholds are appropriately calibrated to reflect current market conditions.

CME Group recommends that the market-wide trigger values be determined weekly rather than daily. We believe that doing so would aid market participants by ensuring continuity of thresholds throughout a particular week and minimize the need for daily recalibration of systems. Market centers would also face greater operational challenges in terms of adjusting and communicating thresholds on a daily basis rather than a weekly basis, and by moving to weekly recalibrations those adjustments could be made over the weekend while markets are closed. Additionally, given the timing of the dissemination of final daily S&P 500 Index values on which the thresholds are based, venues that offer afterhours trading would not have the final daily settlement value in time to establish the correct limits for afterhours trading.

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CME Group appreciates the opportunity to comment on the Exchanges' and FINRA's rule proposals. We are strongly supportive of retooling the current market-wide circuit breaker regime to better reflect current market structures and believe that it is a critically important action to be taken to promote market stability, protect the markets' infrastructure and sustain investor confidence. However, it is also vitally important that the program be implemented in a way that best accomplishes these objectives, and we urge the Commission to take into account our comments and those provided by other market participants. We are happy to discuss any questions concerning the comments contained in this letter and are otherwise available to assist the Commission in its efforts to enhance the stability and integrity of the markets.

Please feel free to contact me at (312) 930-8275 or via email at Craig.Donohue@cmegroup.com, Bryan Durkin, Chief Operating Officer, at (312)435-3687 or Bryan.Durkin@cmegroup.com, or Dean Payton, Deputy Chief Regulatory Officer, at (312) 435-3658 or Dean.Payton@cmegroup.com.

Sincerely,

Craig S. Donohue

cc: Chairman Mary Schapiro
Chairman Gary Gensler
Commissioner Bart Chilton
Commissioner Jill Sommers
Commissioner Scott O'Malia
Commissioner Mark Wetjen
Richard Shilts, CFTC Division of Market Oversight