

November 29, 2010

Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

**Re: Request for Order Exempting Certain Persons from Broker-Dealer  
Registration and Related Requirements, and from Clearing Agency  
Registration and Related Requirements**

Dear Ms. Murphy:

Chicago Mercantile Exchange Inc. (“CME”) requests that the Securities and Exchange Commission (“Commission”) extend the temporary exemptive order related to certain credit default swap (“CDS”) contracts to be cleared by CME that was issued by the Commission on March 30, 2010.<sup>1</sup> The current order expires on November 30, 2010.

The recent Wall Street Transparency and Accountability Act of 2010 amended the Securities Exchange Act of 1934 to include a new Section 3C.<sup>2</sup> Under this provision, CME, a derivatives clearing organization that has cleared CDS pursuant to an exemption from registration as a clearing agency before the bill’s date of enactment, will be deemed to be registered as a clearing agency for the purpose of clearing security-based swaps such as CDS as of July 16, 2011. As such, CME respectfully requests that its temporary exemptive order be extended until that time.

For purposes of this request we refer to prior petitions submitted to the Commission on December 14, 2009 (the “December 2009 Petition”) and on March 30, 2010 (the “March 2010 Petition”) (collectively the “Petitions”), which we incorporate herein by reference. CME

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<sup>1</sup> See Securities Exchange Act Release No. 34-61803 (March 30, 2010). The Commission initially granted CME a temporary exemptive order to facilitate its clearing of CDS contracts in March, 2009. See Securities Exchange Act Release No. 34-61803 (March 13, 2009). This temporary exemptive relief was further extended in December, 2009 and March, 2010. See Securities Exchange Act Release No. 34-61164 (Dec. 14, 2009) and Securities Exchange Act Release No. 34-61803 (March 30, 2010), respectively.

<sup>2</sup> See Section 763(a) of The Dodd Frank Wall Street Reform and Consumer Protection Act of 2010, adopting new 3C.(1) of the Securities Exchange Act of 1934.

represents that the statements concerning our offering set forth in the Petitions have not changed in any material respect, except as set forth below. CME also represents that its margin methodology as of the date of this letter is the same margin methodology that was in place when it submitted its March, 2010 Petition. In addition, CME represents that it has undertaken to implement policies and procedures designed to ensure compliance with the terms of the Commission exemptive order and that it will conduct an internal review related to its compliance program for its CDS business that will be overseen by CME's Audit Committee and that it will provide a report (which shall be approved by CME's Board of Directors) to the Commission of such review within 90-120 days of November 30, 2010.

### *CME's CDS Clearing Activities to Date*

CME began offering clearing services for CDS contracts on December 15, 2009. To date, CME's clearing activities for CDS have been limited to a small product set with carefully limited risk exposures. CME offers clearing for the following CDS index products: the five-year tenors for CDX Investment Grade Series 12, Series 13 Series 14 and Series 15. As of September 30, 2010, CME has cleared 82 CDS transactions, with a total notional value of \$255,000,000. As of September 30, 2010, open interest for CDS transactions cleared by CME was \$50,000,000 in notional value.

Throughout this initial limited phase, CME has continued to waive application of the forced trade process pursuant to our price quality auction methodology, and CME has not required CDS clearing members to execute any CDS transactions pursuant to this process.<sup>3</sup> However, CME has been conducting its internal review process to identify crossed bids and offers, and CME intends to fully implement the price quality auction methodology when CDS clearing services are expanded following the initial phase. This process is an important component of CME's overall settlement price determination process, and consequently CME requests that the Commission further extend the previously-granted exemption to CME from application of Sections 5 and 6 of the Exchange Act with respect to this process.

### *Anticipated Move to Single Guaranty Fund for CDS*

The CME CDS financial safeguards package is currently one part of a single guaranty fund that also accommodates CME's futures business. CME is evaluating the creation of a distinct CDS guaranty fund that would replace the complicated system of tranches that currently applies to CDS and futures clearing.<sup>4</sup> Although the new CDS guaranty fund will be segregated from the CME futures financial safeguards from an operational perspective, it will remain within the CME corporate entity at this time and subject to its oversight. CME anticipates that rule changes will be implemented at some point in the fourth quarter of 2010 or the first quarter of

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<sup>3</sup> See December Petition, p.8.

<sup>4</sup> The central purpose for moving to a separate CDS guaranty fund structure is to provide CDS clearing members with increased legal certainty in a significant default scenario.

2011 and that any CDS-specific contributions to the CDS guaranty fund would be transferred at that time.

The separate guaranty fund will be comprised of both funded and unfunded portions of roughly equal size. The total size of the package will be designed to cover the four largest net debtor profiles (based on theoretical losses). The components of the funded portion, which will be sized to cover the first and second largest potential defaults, will include, first, the defaulting CDS member's initial margin deposits, second, the defaulting CDS member's guaranty fund deposits, third, CME contributed capital (a minimum of \$50 million), and, finally, the guaranty fund deposits of other non-defaulting CDS clearing members. The unfunded portion will be based on CME's general assessment powers. These assessment powers will be designed to provide CME with the ability to cover the third and fourth largest net debtor profiles.<sup>5</sup> In the event of a CDS member default, CME will be able to access the CDS financial safeguard package as necessary. The separate guaranty fund will be implemented with limited recourse features.

We anticipate that rules implementing a separate guaranty fund for CDS will align to recently-implemented rules for cleared OTC interest rate swaps, for which CME launched clearing services on October 18, 2010.

#### *New Cleared OTC Derivatives Account Class*

When CME initially launched its CDS clearing initiative, all CDS contracts submitted to CME for clearing for the account of a clearing member's customer were required to be held in an account subject to CFTC Regulation 30.7.<sup>6</sup> On June 15, 2009, CME submitted a petition to the CFTC, pursuant to Section 4d of the Commodity Exchange Act (the "CEA"), asking for permission to hold CME-cleared customer CDS contracts and related collateral in the same account class as U.S. futures and options. In May 2010, the CFTC amended its Part 190 Bankruptcy Rules to create a new customer account class specifically for "cleared OTC derivatives",<sup>7</sup> a term defined to include contracts that are cleared by a DCO but not listed for trading on a designated contract market or derivatives transaction execution facility. This definition encompasses CME-cleared CDS.

Shortly after the CFTC amended its Part 190 Bankruptcy Rules to create the new OTC account class, CME withdrew its 4d petition for CDS. In accordance with the CFTC's new Part 190 Rules, on October 4, 2010, CME (in its capacity as a DCO) adopted substantive, pre-bankruptcy rules that apply to customer "cleared OTC derivatives" that are cleared by CME.<sup>8</sup> As of October 4, 2010, all CME-cleared customer CDS positions and related collateral previously

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<sup>5</sup> Because the new financial safeguards package will be intended to cover the four largest potential clearing member defaults, rather than a dollar amount, the rules will no longer include specific caps on assessments.

<sup>6</sup> 17 C.F.R. §30.7.

<sup>7</sup> See 75 FR 17297 (April 6, 2010).

<sup>8</sup> See CME Rules 8F100, 8F117 through 8F136 at <http://www.cmegroup.com/rulebook/CME/I/8F/>.

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held in 30.7 accounts are required to be held in Cleared OTC Derivatives Customer Sequestered Accounts.

CME rules for Cleared OTC Derivatives Customer Sequestered Accounts generally mirror CFTC regulations applicable to the customer account class for U.S. futures and options (17 C.F.R. §§ 1.20, *et seq.*). For example, CME's sequestration rules provide, among other things, that: (1) FCMs must prepare a daily Sequestration Statement which reflects the cleared OTC sequestered requirements, funds held in cleared OTC sequestered accounts, and any excess (or deficiency) of funds in Cleared OTC Derivatives Customer Sequestered Accounts; (2) funds of customers holding cleared OTC derivative positions must be held in Cleared OTC Derivatives Customer Sequestered Accounts for the benefit of cleared OTC derivative customers and may not be commingled with funds of the FCM or of other customers; and (3) an FCM may invest funds of cleared OTC derivative customers only in instruments that are allowed under CFTC Regulation 1.25, and such investments must be held in bank and safekeeping accounts of the FCM that are properly titled and for which the FCM has obtained satisfactory acknowledgement letters from the depository. One difference between the CME sequestration rules and CFTC regulations for the U.S. futures and options account class is that the required Sequestration Statement need not be prepared on a currency-by-currency basis, that is, an FCM may under CME rules convert all balances to U.S. dollars and then report those balances on the Sequestration Statement.

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If you have any questions, please feel free to contact the undersigned at 312.648.3851.

Sincerely,



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Ann K. Shuman, Managing Director and  
Deputy General Counsel  
Chicago Mercantile Exchange Inc.  
20 South Wacker Drive  
Chicago, IL 60606

cc: Mary L. Schapiro, Chairman, Securities and Exchange Commission  
Kathleen L. Casey, Commissioner, Securities and Exchange Commission  
Elisse B. Walter, Commissioner, Securities and Exchange Commission  
Luis A. Aguilar, Commissioner, Securities and Exchange Commission

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Troy A. Paredes, Commissioner, Securities and Exchange Commission  
James Brigagliano, Securities and Exchange Commission  
John Ramsay, Securities and Exchange Commission  
James Eastman, Securities and Exchange Commission  
Brian Bussey, Securities and Exchange Commission  
Joseph Kamnik, Securities and Exchange Commission  
Catherine Moore, Securities and Exchange Commission  
Kathleen Cronin, Chicago Mercantile Exchange Inc.  
Jerrold Salzman, Skadden, Arps, Slate, Meagher & Flom