

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-69981; File No. SR-CME-2013-08)

July 12, 2013

Self-Regulatory Organizations; Chicago Mercantile Exchange Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Regarding Existing CDS Credit Limits

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June 28, 2013, Chicago Mercantile Exchange Inc. (“CME”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I, II and III below, which Items have been prepared primarily by CME. CME filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act<sup>3</sup> and Rule 19b-4(f)(1)<sup>4</sup> thereunder, so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The text of the proposed change is below. Underscored text indicates additions; bracketed text indicates deletions.

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TO: Clearing Member Firms; Back Office Managers

FROM: CME Clearing

DATE: June \_\_, 2013

ADVISORY #: 13-XXX

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(1).

**SUBJECT: CDS Clearing Member Risk Limits**

Effective July 15, 2013, CME Clearing will use technology automation to impose risk limits on Clearing Members for Credit Default Swap (CDS) Products. Pre-trade credit limits for CDS trade submission at the Clearing Member Firm level will now be automated. As you know, Clearing Member Firms currently have the ability to set CME-hosted credit limits for CDS on a customer account by customer account basis. With this change, CME Group will automate CDS credit limits on a Clearing Member Firm level, in addition to continuing to allow clearing member firms to maintain customer account by customer account credit limits. This is similar to the process that CME Clearing has in place for its interest rate swap offering, except this limit is based on margin.

CME Clearing will determine one maintenance margin limit for each Clearing Member Firm's customer and house origins. The utilization of this limit will be based on the same margin methodology that CME Clearing currently uses on a daily basis to calculate margin for each clearing member firm.

Please note that this limit will be a daily limit and will be based on trades executed for the **current trade date only**. In other words, the calculation is reset daily, and it does not reflect the exposure of any open trades prior to the current trade date.

Three hypothetical examples of the calculation of the utilization are outlined below:

**Trade 1:** Customer A executes a buy-protection \$100M notional CDXHY20 5yr trade with Clearing Member Firm B equivalent to \$5M in margin for the current trade date.

**Trade 2:** Customer C then executes a sell-protection \$100M notional CDXHY20 5yr trade with Clearing Member Firm B for the current trade date.

**Example 1: Credit Utilization – Same Trade Dates**

	<u>After Trade 1</u>	<u>After Trade 2</u>
<u>Clearing Member Firm B House Origin</u>	<u>\$5M</u>	<u>\$0M (offsetting)</u>
<u>Clearing Member Firm B Customer Origin</u>	<u>\$5M</u>	<u>\$0M (offsetting)</u>

Now, if the 2<sup>nd</sup> trade was executed on the **following trade date**:

**Example 2: Credit Utilization – Different Trade Dates**

	<u>After Trade 1</u>	<u>After Trade 2*</u>
<u>Clearing Member Firm B House Origin</u>	<u>\$5M</u>	<u>\$5M (not offsetting)</u>
<u>Clearing Member Firm B Customer Origin</u>	<u>\$5M</u>	<u>\$5M (not offsetting)</u>

Further, using the original 2 trades above as the base case, if the 2<sup>nd</sup> trade was now buy-protection (instead of sell-protection):

**Example 3: Credit Utilization – Same Trade Dates - Directional**

	<u>After Trade 1</u>	<u>After Trade 2**</u>
<u>Clearing Member Firm B House Origin</u>	<u>\$5M</u>	<u>\$10M</u>
<u>Clearing Member Firm B Customer Origin</u>	<u>\$5M</u>	<u>\$10M</u>

\*Assuming the margin on the buy-protection trade and sell-protection trade are equivalent

\*\*Assuming the portfolio margin of trades 1 and 2 combined is 10M

A consequence of pre-trade credit limit automation is that CDS transactions that exceed the daily limit will be rejected for clearing. We will continue to communicate via email and telephone to work with your firm if your utilizations are approaching their limits. In the future, we will provide firms with access to a separate view in RAV Manager with the ability to view your Clearing Member Firm and Origin level limits and utilizations.

If you have questions about the calculation or the specific limit in place for your Clearing Member Firm, please contact the CME Clearing Risk at [clearing.riskmanagement@cmegroup.com](mailto:clearing.riskmanagement@cmegroup.com) or 312.648.3888.

For all other questions, please contact the CME Client Services Team at [onboarding@cmegroup.com](mailto:onboarding@cmegroup.com) or 312-338-7112.

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II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose and basis for the proposed rule change and discussed any comments it

received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

On May 7, 2012, CME implemented risk limits that apply to clearing members clearing credit default swaps in compliance with CFTC Regulation 39(h)(1).<sup>5</sup> CME has been enforcing those limits manually since that date.

CME now proposes to issue a notice announcing CME's intention to begin enforcing these same limits through automated means. More specifically, the CME Clearing Advisory Notice would inform clearing members and market participants that CME Clearing will, beginning on July 15, 2013, automate the manner in which it imposes clearing member risk limits for credit default swap transactions, a process that is intended to result in a more effective and efficient imposition of clearing member risk limits for credit default swap transactions. Thus, CDS transactions that exceed the limits will now be automatically rejected for clearing based on the new pre-trade credit limit automation.

The proposed rule changes that are the subject of this filing will become immediately effective. CME notes that it has also certified the proposed rule changes that are the subject of this filing to its primary regulator, the Commodity Futures Trading Commission ("CFTC").

CME believes the proposed rule changes are consistent with the requirements of the Exchange Act including Section 17A of the Exchange Act. The proposed rule changes are designed to result in a more effective and efficient imposition of clearing member risk limits for

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<sup>5</sup> The Commission believes, and CME has confirmed, that CME intended to reference CFTC Regulation 39.13(h)(1).

credit default swap transactions, and as such are designed to promote the prompt and accurate clearance and settlement of securities transactions and derivatives agreements, contracts and transactions, and to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency and, in general, help to protect investors and the public interest. Furthermore, the proposed change does not announce new credit limits but rather new automated means of enforcing existing credit limits. As such, the proposed amendments constitute a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing CME rule. Therefore, the proposed rule change is therefore properly filed under Section 19(b)(3)(A) and Rule 19b-4(f)(1) thereunder.

B. Self-Regulatory Organization's Statement on Burden on Competition

CME does not believe that the proposed rule change will have any impact, or impose any burden, on competition. The proposed change informs market participants that CDS transactions that exceed the currently applicable credit limits will now be automatically rejected for clearing. Imposing automated means of enforcing an existing rule should not be seen to have any competitive impact.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

CME has not solicited, and does not intend to solicit, comments regarding this proposed rule change. CME has not received any unsolicited written comments from interested parties.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change has been filed pursuant to Section 19(b)(3)(A)<sup>6</sup> of the Act and paragraph (f)(1) of Rule 19b-4<sup>7</sup> thereunder and will become effective on filing. At any time

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<sup>6</sup> Supra note 3.

<sup>7</sup> Supra note 4.

within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-CME-2013-08 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-CME-2013-08. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be

available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of CME and on CME's website ([http://www.cmegroup.com/market-regulation/files/sec\\_19b-4\\_13-08.pdf](http://www.cmegroup.com/market-regulation/files/sec_19b-4_13-08.pdf)).

All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-CME-2013-08 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>8</sup>

Elizabeth M. Murphy  
Secretary

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<sup>8</sup> 17 CFR 200.30-3(a)(12).