

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-73938; File No. SR-CME-2014-19)

December 24, 2014

Self-Regulatory Organizations; Chicago Mercantile Exchange Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Regarding Certain Contractual Arrangements that Apply to its Over-the-Counter Interest Rate Swap Clearing Offering

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder² notice is hereby given that, on December 15, 2014, Chicago Mercantile Exchange Inc. (“CME”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II and III below, which Items have been prepared primarily by CME. CME filed the proposal pursuant to Section 19(b)(3)(A) of the Act,³ and Rule 19b-4(f)(4)(ii)⁴ 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

CME is proposing to make certain revenue sharing and governance changes related to certain contractual arrangements that apply to its over-the-counter interest rate swap (“OTC IRS”) clearing offering. CME entered into this arrangement (the “Agreement”) with a group of

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(4)(ii).

clearing members on June 30, 2012 and the proposed rule change has been implemented by CME since June 30, 2012.⁵

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

In its filing with the Commission, CME included statements concerning the purpose of 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. CME has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of these statements.

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

CME is registered as a derivatives clearing organization with the Commodity Futures Trading Commission ("CFTC") and operates a substantial business clearing futures and swaps contracts subject to the jurisdiction of the CFTC. CME is filing this proposed rule change with respect to the Agreement made with various third-party financial institutions (dealer founding members, "DFMs") relating to its OTC IRS clearing business. The Agreement incentivized the DFMs to support CME's initial development of its OTC IRS clearing infrastructure and is designed to ensure that the DFMs continue their demonstrated commitment to CME's ongoing IRS clearing efforts. The existing DFMs were selected based on their support in CME's development of its clearing initiative, ability to provide liquidity, their client clearing and risk management expertise, as well as their willingness to test and generally support centralized clearing in IRS Contracts on an on-going basis. CME may invite other firms to join the

⁵ Pursuant to a teleconference with CME's counsel on December 19, 2014, staff in the Division of Trading and Markets has modified this sentence to insert references to the Agreement's execution and implementation date.

Agreement in the future so long as such firms are approved by a majority of the then-existing DFMs.

In summary, under the Agreement, the DFMs that satisfy their obligations under the Agreement will receive a portion of the clearing revenues and market data revenues generated in connection with CME's clearing of certain specified IRS Contracts, will be subject to a cap on the IRS clearing fees payable to CME, and will be entitled to participate on CME's IRS advisory group. In addition, CME has agreed to minimum IRS clearing member representation on the IRS Risk Committee (the "IRS RC"). These aspects and other relevant background and context regarding the Agreement are described in greater detail below.

DFM Obligations under the Agreement

Under the Agreement, DFMs are required to (i) maintain an IRS clearing membership at CME in good standing, (ii) offer customers the ability to clear IRS Contracts at CME on a non-discriminatory basis by comparison to the terms offered for clearing of substantially similar IRS Contracts through any U.S.-based derivatives clearing organization, (iii) provide to CME certain pricing curves for daily settlement prices for IRS Contracts, and (iv) submit IRS Contracts to CME that generate specified minimum annual fees.

Economic Incentives for the DFMs under the Agreement

Under the Agreement, DFMs will pay a specified fee for each IRS Contract submitted to CME for clearing. In addition, CME and the DFMs have agreed to share certain of the adjusted gross revenues associated with CME's IRS Contracts clearing activities,⁶ including the sale of market data generated by such activities (the "Revenue Pools"). DFMs that qualify during a relevant measurement period will each receive a pro-rata share of the Revenue Pools based on

⁶ The DFM share of gross revenue is based on the number of DFMs and adjusted for applicable discounts, rebates, taxes and expenses.

volumes of IRS Contracts submitted to CME. In addition, the non-customer fees charged to each DFM for the clearing of IRS Contracts during a given measurement period will not exceed a specified annual cap.⁷

Finally, CME has agreed to offer each DFM the option of electing, in lieu of the incentives under the Agreement, any other pricing structure for the clearing of IRS Contracts that any other IRS clearing member chooses to accept from CME.

Governance Rights

In addition, CME has agreed with the DFMs that, among other things:

1. it will exercise its rights under CME's IRS RC charter⁸ so as to cause a majority of the IRS RC to be composed such that (i) employees or directors of IRS Clearing Members⁹ maintain a majority of the IRS RC (the "IRS Clearing Membership Representatives") and (ii) a majority of the IRS Clearing Membership Representatives be selected from those IRS Clearing Members that have the "n" largest average contributions to the IRS Guaranty Fund, where "n" is equal to the actual number of IRS Clearing Membership Representatives plus two (2)¹⁰;

⁷ During a December 22, 2014 teleconference with CME counsel, staff in the Division of Trading and Markets confirmed that CME has filed the following fee-related filings relating to the Agreement: Securities Exchange Act Release No. 34-66102 (Jan. 5, 2012), 77 FR 1775 (Jan. 11, 2012) (File No. SR-CME-2011-22); Securities Exchange Act Release No. 34-67036 (May 21, 2012), 77 FR 31416 (May 25, 2012) (File No. SR-CME-2012-18) and Securities Exchange Act Release No. 34-71088 (Dec. 17, 2013), 78 FR 77512 (Dec. 23, 2013) (File No. SR-CME-2013-32).

⁸ The Agreement does not amend the charter of the IRS RC.

⁹ This includes all IRS Clearing Members, not just DFMs.

¹⁰ For instance, if the actual number of IRS Clearing Membership Representatives is 5, then a majority of the IRS Clearing Membership Representatives will be selected from those IRS Clearing Members with the 7 largest average contributions to the IRS Guaranty Fund.

2. each DFM may appoint a representative (a “DFM Representative”) to participate on CME’s IRS advisory group¹¹; and

3. it will not launch any IRS Product that was not originally contemplated by the Agreement in the IRS Guaranty Fund if a majority the DFM Representatives object to such launch based on material risk management concerns that such DFM Representatives have identified and that CME is unable to reasonably mitigate.

Section 17A of the Act does not permit the rules of a clearing agency to unfairly discriminate in the admission of participants or among participants in the use of the clearing agency.¹² The rules of a clearing agency must also assure its participants are fairly represented with respect to the administration of its affairs.¹³ Further, the rules of the clearing agency must not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.¹⁴ Although the terms of the Agreement deliver certain rights to a set of participants that are not offered to others, CME believes the proposed rules are nevertheless consistent with the requirements of the Act for the following reasons.

First, the Agreement provides an enumerated group of DFMs, who are also IRS Clearing Members at CME, with economic incentives and other contractual rights that will not be afforded to other IRS Clearing Members who are not DFMs. The rationale for providing this group of DFMs with these rights is to incentivize them (i) to provide substantial support to CME

¹¹ CME’s IRS advisory group includes a representative from each of the DFMs and a representative from CME. In addition, CME may invite up to 2 non-DFM IRS clearing members that are in the top 10 contributors to the IRS Guaranty Fund and up to 3 non-IRS Clearing Members to appoint representatives to the IRS advisory group.

¹² 15 U.S.C. 78q-1(b)(3)(F).

¹³ 15 U.S.C. 78q-1(b)(3)(C).

¹⁴ 15 U.S.C. 78q-1(b)(3)(I).

in its development and structuring of its OTC IRS clearing offering and (ii) to serve as the initial set of IRS clearing members. These swap market participants invested significant time and resources to support CME staff's efforts to design, develop, and implement CME's OTC swaps clearing infrastructure and agreed to provide clearing member services for OTC IRS on an ongoing basis. Providing these rights to these participants does not constitute unfair discrimination among participants of CME because of the equity ownership-like commitments undertaken by these DFMs during CME's initial offering phase. Because the DFMs provided these equity ownership-like commitments during CME's initial offering phase, there is not unfair discrimination among participants and the Agreement should be seen to be consistent with Section 17A(b)(3)(F) of the Act.¹⁵

With respect to the governance rights provided to the DFMs, CME also believes that these should be found to be consistent with the requirements of Section 17A of the Act.¹⁶ CME recognizes that there would be reason to be concerned in circumstances where one particular member of a self-regulatory organization ("SRO") was able to acquire a controlling influence in the administration of the affairs of the SRO. Such circumstances would have the potential to jeopardize an SRO's ability to operate impartially, as a single controlling member might be tempted to exercise its controlling influence by directing the SRO to refrain from diligently surveilling the member's conduct or from punishing any conduct that violates the rules of the SRO, Commodity Exchange Act or other applicable laws. However, those types of concerns are not present with the governance incentives offered to the DFMs in the Agreement.

¹⁵ 15 U.S.C. 78q-1(b)(3)(F).

¹⁶ 15 U.S.C. 78q-1.

Further, the Agreement provides for significant market participant participation in the governance of IRS Products by specifying certain membership composition criteria for the IRS RC. These composition criteria, in general, provide assurance that the participants with the most exposure to CME's IRS clearing initiative will be represented on the IRS RC. This granting of a voice to the market participants with the greatest risk to the Clearing House for IRS products is inherently fair and consistent with Section 17A(b)(3)(C) of the Act.¹⁷ Further, these provisions also ensure that no single participant would be able to obtain a concentrated and outsized influence that would implicate the concerns outlined above nor is representation on the IRS RC based on DFM status.

Finally, the proposal will not affect any securities clearing operations of CME because CME recently filed a proposed rule change that clarified that CME has decided not to clear security-based swaps, except in a very limited set of circumstances.¹⁸ The rule filing reflecting CME's decision not to clear security-based swaps removed any ambiguity concerning CME's ability or intent to perform the functions of a clearing agency with respect to security-based swaps. Therefore, this proposal will have no effect on any securities clearing operations of CME.

For these reasons, CME submits that the specific economic incentives and contractual governance rights granted to the DFMs should be found to be reasonable and consistent with the Act. The terms of the Agreement do not constitute unfair discrimination in the admission of

¹⁷ 15 U.S.C. 78q-1(b)(3)(C).

¹⁸ See Securities Exchange Act Release No. 34-73615 (Nov. 17, 2014), 79 FR 69545 (Nov. 21, 2014) (File No. SR-CME-2014-49). The only exception is with regards to Restructuring European Single Name CDS Contracts created following the occurrence of a Restructuring Credit Event in respect of an iTraxx Component Transaction. The clearing of Restructuring European Single Name CDS Contracts will be a necessary byproduct after such time that CME begins clearing iTraxx Europe index CDS.

participants or among participants in the use of the clearing agency but rather provide reasonable incentives to support the clearing offering. The arrangements should be seen as consistent with Section 17A(b)(3)(F) of the Act,¹⁹ and should otherwise be seen to be consistent with the Act's investor protection and public interest mandates. CME submits that the proposed rule change promotes the prompt and accurate clearance and settlement of transactions, assures the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible, fosters cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, removes impediments to and perfects the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, protects investors and the public interest.

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

CME does not believe that the proposed rule change will impose any burden that is not reasonable, appropriate, or in furtherance of the Act. As discussed above, the proposed rules will provide an enumerated group of DFM firms, who are also IRS Clearing Members at CME, with economic incentives and other contractual rights that will not be afforded to other IRS Clearing Members who are not DFMs or do not become DFMs. Providing these benefits to one set of firms and not all could potentially have an impact on competition. However, CME believes any such impacts should not be seen to be unreasonable in light of the fact that these benefits were afforded in consideration of the substantial support provided to CME in the development and structuring of its OTC IRS clearing offering and the firms' agreement to serve as the initial set of clearing members.

¹⁹ 15 U.S.C. 78q-1(b)(3)(F).

Further, the changes are limited to CME's derivatives clearing business and, as such, do not affect security-based swap clearing activities of CME in any way and therefore would not impose any burden on competition that is inappropriate in furtherance of the purposes of the Act.

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 become effective upon filing pursuant to Section 19(b)(3)(A)²⁰ of the Act and Rule 19b-4(f)(4)(ii)²¹ thereunder. CME asserts that this proposal constitutes a change in an existing service of CME that (a) primarily affects the clearing operations of CME with respect to products that are not securities, including futures that are not security futures, and swaps that are not security-based swaps or mixed swaps, and forwards that are not security forwards; and (b) does not significantly affect any securities clearing operations of CME or any rights or obligations of CME with respect to securities clearing or persons using such securities-clearing service, which renders the proposed change effective upon filing. CME believes that the proposal does not significantly affect any securities clearing operations of CME because CME recently filed a rule change that clarified that CME has decided not to clear security-based swaps, except in a very limited set of circumstances.²² The rule filing reflecting CME's decision not to clear security-based swaps removed any ambiguity concerning CME's ability or intent to perform the functions of a clearing agency with respect to security-based

²⁰ 15 U.S.C. 78s(b)(3)(A).

²¹ 17 CFR 240.19b-4(f)(4)(ii).

²² See supra note 18.

swaps. Therefore, this proposal will not have an effect on any securities clearing operations of CME.

At any time 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. Please include File Number SR-CME-2014-19 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-CME-2014-19. 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 filings will also be available for inspection and copying at the principal office of CME and on CME's website at <http://www.cmegroup.com/market-regulation/rule-filings.html>.

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-2014-19 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.²³

Brent J. Fields
Secretary

²³ 17 CFR 200.30-3(a)(12).