



May 9th, 2014

The European Banking Authority

RE: Draft technical standards on the margin periods for risk used for the treatment of clearing members' exposures to clients (EBA/CP/2014/01)

Dear Sir/Madam:

CME Group Inc. ("CME Group"), on behalf of its subsidiaries, Chicago Mercantile Exchange Inc. ("CME") and CME Clearing Europe Limited ("CME Clearing Europe"), would like to express appreciation to the European Banking Authority ("EBA") for the opportunity to comment on the Consultation: Draft technical standards on the margin periods for risk used for the treatment of clearing members' exposures to clients. CME Group is the parent of Chicago Mercantile Exchange Inc. ("CME"). CME is registered with the CFTC as a derivatives clearing organization ("DCO") and is one of the largest central counterparty ("CCP") clearing services in the world. CME's clearing house division ("CME Clearing") offers clearing and settlement services for exchange-traded futures contracts, as well as over-the-counter ("OTC") derivatives transactions including interest rate swaps ("IRS") and credit default swaps ("CDS"). CME Clearing Europe is a recognized clearing house with the Bank of England and is in the process of obtaining reauthorization under the European Market Infrastructure Regulation ("EMIR"). CME Clearing Europe provides clearing services for OTC derivatives in the commodity and interest rate markets and recently began clearing exchange traded derivative ("ETD") products on behalf of the new CME Europe Limited exchange.

Our responses to the specific questions posed in the consultative document are below for your consideration.

Question 1. Respondents are invited to comment on the proposed approach.

Ideally, the margin period of risk ("MPOR") employed for regulatory capital purposes would mirror the MPOR employed by a CCP in setting margin requirements. CME recognizes that the proposed framework has similarities to this approach; however, it falls short by requiring a five business day floor applicable to all ETD products. This five day minimum is far more conservative than the requirements instituted by the European Securities and Markets Authority ("ESMA") and the U.S. Commodity and Futures Trading Commission ("CFTC"). CME has long advocated that ETD products deserve consideration separate from that of OTC derivatives because they have been proven to carry much shorter liquidation periods, and ESMA and the CFTC have recognized these reduced liquidation time frames for ETDs in establishing minimum MPOR requirements for the CCP's operating in their jurisdictions.

CME acknowledges the EBA's comments in the proposed regulatory technical standards ("RTS") that the five day minimum MPOR is a standard set by the Basel Committee on Banking Supervision ("BCBS"), further implemented in Regulation (EU) No 575/2013 ("CRR"), and that it would be outside the scope of this RTS to remove. However, we reiterate our concerns with this approach and the potential consequences this regulatory misalignment could have on the ETD markets. This standard does not



account for the long-established and demonstrated liquidity profiles of certain ETD products. Moreover, our analysis of the financial markets and discussion of capital costs and efficiencies with numerous clearing members has confirmed our initial concerns that a five-day MPOR floor that does not match the CCP MPOR for ETD products will greatly reduce incentives to take advantage of the benefits of more standardized, liquid and transparent products. We urge international standard setters to remove the explicit five-day MPOR requirement for ETD products and either lower the minimum MPOR for ETDs and other similarly transacted products or permit the utilization of the MPOR employed by the Qualifying Central Counterparty (“QCCP”) in the calculation of ETD capital exposures.

The financial markets are in a state of constant evolution, and as they become more standardized and centralized through regulatory reform efforts, liquidity and transparency will naturally increase which in turn reduces risk. The idea that increased liquidity and transparency reduces risk and shortens liquidation time frames is embedded in existing international standards and national laws that set a lower MPOR used in regulated CCP margin methodologies for ETD products. We strongly believe the Basel standards and the draft RTS on margin periods of risk for clearing members’ exposures to clients should reflect this reality.

We further elaborate on the potential consequences of inappropriate margin periods of risk for liquid, cleared products in our response to Question 3 below based on our concern that the eventual consequences of applying this standard will be borne not only by clearing members and their clients, but also the broader economy through further incentives for firms to continue to trade less liquid OTC products.

Question 2. Clearing members permitted to use the IMM approach are invited to point out the technical issues that could arise under the suggested approach.

CME has no comment in response to this question.

Question 3. Respondents are invited to provide estimates of the costs and the benefits that the methodology prescribed in these draft RTS is expected to produce with respect to the baseline scenario.

CME agrees with the draft RTS that the third option identified is the most practical and well suited solution for the ever evolving financial instruments and derivatives markets. However, CME would like to note that the potential costs and benefits discussed in section 5 of the consultative paper ignore the consequences that a higher MPOR for capital exposures relative to the CCP required MPOR will have on the ETD marketplace. CME acknowledges that these types of costs would be considered out of scope for this RTS because the CRR dictates the five business day floor; however CME believes that this issue is too important to discard.

CME has grave concerns that this regulatory misalignment on MPOR could lead to a number of perverse consequences in the ETD marketplace, including but not limited to:

- (1) Leveling the MPOR for capital purposes for ETD products and OTC cleared products, creating a theoretical margin deficit for capital purposes at the clearing member level for ETD’s only, and perversely incenting clients to continue to trade less liquid OTC products.

As an example, ETD products have transparent pricing in deep, liquid markets which turn over almost 10 times more frequently than OTC derivatives. (Source: TABB Group, *The New Global Risk Transfer Market: Transformation and the Status Quo*, August 2012). ETDs are generally more standardized than OTC cleared products, providing greater efficiency, transparency and access to price and volume information in liquidation scenarios. ETDs are efficiently liquidated and pose less risk than privately negotiated, highly customized, infrequently traded derivatives. Exchange trading and clearing of standardized products results in immediate netting of offsetting positions and thus permits swift, efficient liquidation of the portfolio. For these reasons ESMA and the CFTC have aligned their requirements separately for ETDs and OTC products, and CME believes it is unwise and highly inappropriate to place ETD products on par with that of OTC cleared products from a capital modeling standpoint in this RTS.

(2) Incent bank affiliated clearing member firms to charge clients margin based on an MPOR in excess of the CCP MPOR for all ETD products, creating unnecessary collateral charges for already collateral constrained clients seeking to enter the marketplace and thereby limiting the opportunities of clients unable to satisfy the higher collateral charges to take advantage of the risk mitigation benefits of central clearing. Subsequently, in jurisdictions with weak customer asset protection schemes, the additional customer collateral charged by the bank affiliated clearing member could be rehypothecated and used as an additional funding source for unrelated activities of those bank affiliated clearing members.

(3) Further incentivize bi-lateral, non-cleared trading where initial margin is not required to be collected. CME notes that in the recent ESMA and EBA consultation paper “Draft regulatory technical standards on risk-mitigation techniques for OTC-derivative contracts not cleared by a CCP under Article 11(15) of Regulation (EU) No 648/2012”, there is a minimum threshold of €50 million proposed under which initial margin can be agreed to not be exchanged between the parties. We note that this minimum threshold is mostly likely to be applicable to the same types of smaller clients that would potentially be unable to take advantage of the benefits of central clearing due to high collateral costs. CME believes that the combination of a five business day floor for capital modeling purposes, the €50 million initial margin threshold, and the current lack of a clearing mandate in the European region will lead to a market place where the bulk of financial derivatives remain uncleared and unmargined, directly in contrast of the G-20 commitment to move standardized OTC products into a centrally cleared environment.

The above represent only a fraction of the potential costs that the five business day minimum MPOR could have on the exchange traded derivatives market. CME asks the EBA not dismiss these concerns as out of scope and to consider these additional costs in the adoption of their final regulatory technical standards on MPOR for cleared transactions.

We strongly believe that the final regulatory technical standards should be aligned with the risk profile of derivative products to ensure banks are not subject to overly punitive capital penalties on their positions in liquid and transparent risk management products cleared at a QCCP. Over time, as more OTC products are cleared, the liquidity and transparency profile of these products may converge with



those of ETD products. In this case, the capital requirements associated with these products should also benefit from the utilization of the MPOR employed by the QCCP.

We would be happy to further discuss and clarify any of the above issues with the EBA. If you have any comments or questions regarding this submission, please feel free to contact Kim Taylor, President, CME Clearing at +1 312 930-3156 and Kim.Taylor@cmegroup.com. Alternatively, you may contact Lee Betsill, CEO, CME Clearing Europe at +44 203 379 3120 and Lee.Betsill@cmegroup.com.

Sincerely,

A handwritten signature in purple ink, appearing to read "LBetsill", with a long, sweeping flourish extending to the right.

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