



Financial Regulation Strategy

HM Treasury

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14 April 2011

Dear Sirs,

CME Group Inc. (CME Group) appreciates the opportunity to comment on HM Treasury's (HMT) Consultative paper on "A new approach to financial regulation: building a stronger system" (the Consultation).

CME group is the holding company for four futures exchanges: 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 principal regulator in the United States is the Commodity Futures Trading Commission ("CFTC").

In the United Kingdom, CME, CBOT and NYMEX are recognised overseas investment exchanges and CME Clearing is a recognised overseas clearing house, the recognitions having been granted by the Financial Services Authority ("FSA"). In addition, CME Group has a wholly owned subsidiary, CME Clearing Europe Limited, which has recently been recognised as a clearing house by the FSA.

The Institutional Structure

Markets regulation

CME Group welcomes the Consultation's statement that the Financial Conduct Authority (FCA) will contain a strong markets function. In this context, we think that it is important that legislators are mindful of the significant differences in the regulatory approach to supervising markets on the one hand and providers of retail financial services on the other.

We welcome the proposal for a Markets Panel to underpin the markets regulation function. However, we think that the integrity of the markets regulation function and its role in macro prudential and resourcing discussions should be supported by further legislative underpinning.

In particular, we would support the following:

Markets representation on the Financial Policy Committee (FPC) and the FCA's Board (in this context, we welcome the appointment of Michael Cohrs, former co-head of corporate and investment banking and member of the Group Executive Committee at Deutsche Bank as an independent member of the interim FPC and regard this type of appointment as extremely positive) ;

A requirement modelled on Schedule 1 of the Financial Services and Markets Act 2000 requiring the non-executive directors of the FCA to consider the adequacy of resourcing (i.e. by ensuring resources are utilised in the most efficient and economical manner) and operation (i.e. by ensuring the FCA is appropriately discharging its functions) of the markets function ; and

A mechanism for allocating fees raised by those institutions supervised by the FCA's Markets Division to markets regulation.

CCP regulation

CME Group understands HMT's reasons for proposing that Central Counterparty Clearing Houses (CCPs) should be regulated by the Bank of England (BoE) given their systemic importance (although we do believe this gives rise to concerns about pre and post trade regulation not being joined up - see 'Co-ordination of Supervision' below). If this route is adopted we would make the following suggestions:

Careful thought should be given to how the supervisory style of the current FSA (open, approachable staff having a broad career development path through moving jobs within a large organisation) is reflected at the BoE. We think that staff who have broad markets experience are best placed to supervise CCPs. We have concerns that CCP supervisors may no longer have the flexibility to move between supervisory areas, even within the markets area, if they are employed by separate legal entities. This will be to the detriment of markets supervision as a whole. Consequently, it is of importance that practical cooperative measures are put in place between the BoE and FCA to minimise these risks. The BoE and the FCA may wish to consider the utility of staff secondments between them as a mechanism for ensuring coordination of their respective functions.

We notice the Consultation was silent on the funding of CCP supervision at the BoE. In our view, the part of the BoE which regulates CCPs should have its own discrete budget. In this context, we do not think that any fees in relation to CCPs should be available for other purposes within the BoE. At a minimum we believe that the basis of such fees should have at least the transparency of current Financial Services Authority (FSA) charging.

Competition

CME Group welcomes the Government's proposals to enable the FCA to play a credible and effective role in competition. We would however urge legislators to take steps to ensure that the various competition authorities do not have overlapping powers. If this is not avoided, there is a danger of confusion and uncertainty as to who is responsible for what in terms of competition scrutiny. We look forward to commenting on the more detailed proposals with regard to the FCA's competition remit at a later stage.

Co-ordination of Supervision

Given the current proposals to separate trade and post-trade infrastructure, we would make the following high level observations:

In principle, we welcome the proposal that the BoE and FCA should comply with the principles set out in the Consultation in relation to the co-ordination of the Prudential Regulation Authority (PRA) and the FCA. However, we think that the smaller size of the clearing function within the BoE means that these principles should be applied proportionately and it may be that less complex co-ordination mechanics are appropriate in this case. In this context, we think that a key principle should be to avoid overlaps in or inconsistency of, the supervisory approach between the BoE in relation to CCPs and the FCA in relation to markets.

There is a separate argument in favour of having a single regulatory point of contact for all of the 'recognised' or 'regulated' entities supervised by the FCA within our group. We think that consideration should be given to including this provision on the face of the legislation, although we recognise that this may ultimately be left to the FCA to decide.

It is important that the legislation provides for adequate information gateways between the BoE and FCA to share information on entities within the group.

We note that the FCA will be the UK's 'voice' at the European Securities and Markets Authority (ESMA) and welcome the Consultation's recognition of the need to coordinate the work of individual regulators so that issues relating to CCPs are given appropriate representation by the FCA at ESMA. We regard this as of the highest importance given the proposed extent of ESMA's

powers in the latest draft of the Regulation on OTC Derivatives, Central Counterparties and Trade Repositories (EMIR). These powers cover all major aspects of clearing house risk management and client protection. We hope that careful thought will be given to reflecting this need for coordination in UK legislation.

Regulatory Change

Overriding Objective of the Bill

CME Group believes that, so far as possible, legislators should ensure the Bill is a mechanism for creating the appropriate institutional shape for the UK's regulation of financial services and markets. Doing this correctly will be a difficult, complex and lengthy process and should not be confused with the amendment of the substantive regulation of markets or CCPs.

To this end, we welcome the recognition in paragraph 2.129 of the Consultation that substantive changes to the recognition requirements for CCPs should be made as a result of EMIR. The same principle should apply to markets where changes will result from the review of the Markets in Financial Instruments Directive.

In light of the above, we would urge that the mechanics of grandfathering be kept as simple and "automatic" as possible.

Product Intervention

Whilst we welcome the recognition that product intervention is unlikely to be appropriate in relation to professional or wholesale customers, we are nonetheless concerned that the Consultation appears to envisage (at least theoretically) the possibility of product banning in the wholesale sphere with few checks and balances other than a set of principles to govern the intervention power. As a minimum we would therefore strongly suggest that:

The legislation reflects a presumption that the powers would not be used in the wholesale sphere unless specific 'triggers' have been breached; and

There is a requirement to consult on the specific ban that is being proposed if the power is ever to be used in the wholesale sphere.

Competition

We note that the FCA has a competition objective but that the PRA does not have a similar objective. If our reading of the Consultation is correct (in that Multi-lateral Trading Facilities (MTFs) will be entirely regulated by the FCA) we think the objective should be welcomed to the extent it will level the playing field between MTFs and Recognised Investment Exchanges which are providing very similar services. However, there appears to be a lacuna in the proposals in that

Banks who operate Systemic Internalisers or trading mechanisms which may not fall within the MTF or regulated market definition, e.g. some of the broker crossing systems, may not be held to the same degree of competition scrutiny as markets and MTFs. This is because they will be PRA regulated for prudential purposes and the PRA will be under no obligation to consider competition in its supervision of these types of platforms, despite the fact that they will compete directly for business with markets and MTFs.

Enforcement

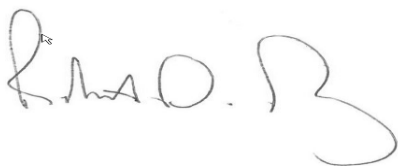
We note the intention to allow the FCA and BoE to be able to impose penalties on markets and CCPs respectively.

We are opposed to the proposal to allow early disclosure of supervisory or enforcement action (at the Warning Notice stage). There will be times when this has adverse effects on a firm's reputation long before it becomes public that a regulatory action was without merit.

We would also urge legislators to ensure that these proposals - should they progress - are not extended to early disclosure of supervisory action against markets or CCPs. We believe in the right to be able to make representations before regulatory criticism becomes public and also believe legislators should be mindful of the specific market confidence and systemic stability issues that might arise should regulatory criticism of a market or a CCP become public prior to the market or the CCP having a chance to respond.

CME Group recognises the value of the consultative process undertaken by HMT during this key time of development of the UK regulatory structure, and appreciates the opportunity to play a part in offering its views. CME Group would be delighted to discuss the proposals and views offered in this response with HMT.

Yours faithfully,

A handwritten signature in blue ink, appearing to read 'R.D. Ray', with a large, stylized flourish at the end.

Robert D. Ray
Managing Director, International Products and Services,
CME Group