

SUBMISSION COVER SHEET

Registered Entity Identifier Code (optional): 13-565R Date: December 18, 2013

IMPORTANT: CHECK BOX IF CONFIDENTIAL TREATMENT IS REQUESTED.

ORGANIZATION

CME/CBOT/NYMEX

FILING AS A:

DCM

SEF

DCO

SDR

ECM/SPDC

TYPE OF FILING

- **Rules and Rule Amendments**

Certification under § 40.6 (a) or § 41.24 (a)

"Non-Material Agricultural Rule Change" under § 40.4 (b)(5)

Notification under § 40.6 (d)

Request for Approval under § 40.4 (a) or § 40.5 (a)

Advance Notice of SIDCO Rule Change under § 40.10 (a)

- **Products**

Certification under § 39.5(b), § 40.2 (a), or § 41.23 (a)

Swap Class Certification under § 40.2 (d)

Request for Approval under § 40.3 (a)

Novel Derivative Product Notification under § 40.12 (a)

RULE NUMBERS

CME/CBOT/NYMEX RULE 822 (Liquidity Rules)

DESCRIPTION

REVISED – Adoption of new rules for liquidity risk management.

December 18, 2013

VIA E-MAIL

Ms. Melissa Jurgens
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

**RE: REVISED – CFTC Regulation 40.10(a) Advance Notice – CME/CBOT/NYMEX
Rules for Liquidity Risk Management
CME/CBOT/NYMEX Submission No. 13-565R**

Dear Ms. Jurgens:

Chicago Mercantile Exchange Inc. (“CME”), the Board of Trade of the City of Chicago, Inc. (“CBOT”), and New York Mercantile Exchange, Inc. (“NYMEX”) (collectively, the “Exchanges”) pursuant to Commodity Futures Trading Commission (“CFTC” or “Commission”) Regulation 40.10(a) submit this advance notice of proposed rules relating to liquidity risk management to comply with recently finalized Regulations 39.33 and 39.35. The new rules will be effective on February 17, ~~2013~~ 2014 or the earliest possible date the Commission authorizes implementation of these rules and the Exchanges receive all regulatory approvals.

Please note that CME/CBOT/NYMEX Submission No. 13-565R simply revises a typographical error in the above paragraph which makes an incorrect reference to the year 2013 instead of 2014. The new rules will have an effective date of February 17, 2014.

On December 2, 2013, the Commission adopted final regulations to establish additional standards for compliance with the derivatives clearing organization (“DCO”) core principles set forth in the Commodity Exchange Act (“CEA”) for systemically important DCOs (“SIDCOs”) and DCOs that elect to opt-in to the SIDCO regulatory requirements (“SIDCO Rules”) ¹. Regulation 39.33(c) established enhanced liquidity standards for SIDCOs. Regulation 39.33(c)(1)(i) requires SIDCOs to maintain eligible liquidity resources that, “at a minimum, will enable it to meet its intraday, same-day, and multiday obligations to perform settlements, as defined in § 39.14(a)(1), with a high degree of confidence under a wide range of stress scenarios that should include, but not be limited to, a default by the clearing member creating the largest aggregate liquidity obligation for the [SIDCO]...in extreme but plausible market conditions.” 39.33(c)(3) establishes qualifying liquidity resources as follows:

- “(3) *Qualifying liquidity resources.* (i) Only the following liquidity resources are eligible for the purpose of meeting the requirement of paragraph (c)(1) of this section:
- (A) Cash in the currency of the requisite obligations, held either at the central bank of issue or at a creditworthy commercial bank;
 - (B) Committed lines of credit;
 - (C) Committed foreign exchange swaps;
 - (D) Committed repurchase agreements; or
 - (E) (1) Highly marketable collateral, including high quality, liquid, general obligations of a sovereign nation.

¹ Additionally, the Commission noted in Regulation 39.40 that these standards are consistent with the Principles for Financial Market Infrastructures (“PFMIs”) published by the Committee on Payment and Settlement Systems and the Board of the International Organization of Securities Commissions (“CPSS-IOSCO”).

(2) The assets described in paragraph (c)(3)(i)(E)(1) of this section must be readily available and convertible into cash pursuant to prearranged and highly reliable funding arrangements, even in extreme but plausible market conditions.²

Additionally, the Commission finalized Regulation 39.35 in the SIDCO Rules requiring, among other things, rules to address liquidity shortfalls as follows:

“(b) *Allocation of uncovered liquidity shortfalls.* (1) Each systemically important derivatives clearing organization and subpart C derivatives clearing organization shall establish rules and/or procedures that enable it promptly to meet all of its settlement obligations, on a same day and, as appropriate, intraday and multiday basis, in the context of the occurrence of either or both of the following scenarios:

- (i) An individual or combined default involving one or more clearing members’ obligations to the systemically important derivatives clearing organization or subpart C derivatives clearing organization; or
 - (ii) A liquidity shortfall exceeding the financial resources of the systemically important derivatives clearing organization or subpart C derivatives clearing organization.
- (2) The rules and procedures described in paragraph (b)(1) of this section shall:
- (i) Enable the systemically important derivatives clearing organization or subpart C derivatives clearing organization promptly to meet its payment obligations in all relevant currencies;
 - (ii) Be designed to enable the systemically important derivatives clearing organization or subpart C derivatives clearing organization to avoid unwinding, revoking, or delaying the same-day settlement of payment obligations; and
 - (iii) Address the systemically important derivatives clearing organization’s or subpart C derivatives clearing organization’s process to replenish any liquidity resources it may employ during a stress event so that it can continue to operate in a safe and sound manner.”³

CME Clearing employs a sound risk-management framework for comprehensively managing liquidity risk. The framework serves to effectively measure, monitor, and manage liquidity risk on an ongoing basis. The framework includes assessment and maintenance of sufficient liquid resources to effect same-day settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios. The stress scenarios include the default of the clearing member and its affiliates that would generate the largest aggregate, with consideration of the second largest, and by currency liquidity obligation under extreme but plausible market conditions. CME Clearing manages liquidity risk through utilization of qualifying liquid resources to meet the liquidity obligation calculated under the framework. In order to augment this framework and comply with CFTC Regulations, the Exchanges are proposing to add certain requirements and/or capabilities that CME Clearing will employ in its administration of its liquidity risk program. This rules-based approach to liquidity risk management will also rely on and be augmented by CME Clearing’s collateral policy determinations, with liquidity risk management serving as a primary consideration in the enumeration of such collateral policies.

Rule 822.A.1. Substitution of Cash Guaranty Fund Deposits

Rule 822.A will establish a liquidity “waterfall” where in the event CME Clearing needs to obtain liquidity for non-cash collateral for same day settlement it will first attempt to obtain liquidity for such collateral through asset sale, any uncommitted funding arrangements, its committed lines of credit and any committed repurchase agreements. In the event CME Clearing requires further liquidity or such means were unsuccessful, CME Clearing may then declare a “Liquidity Event” and substitute any cash deposited by clearing members in satisfaction of their guaranty fund requirements up to the amount of U.S.

² 78 FR 72518

³ 78 FR 72519.

Treasuries deposited by a clearing member subject of such Liquidity Event. The amount of U.S. Treasuries substituted will be sized using the haircutted market value from the prior day's close of business utilizing a recognized third party pricing source and CME's then prevailing haircut schedule. CME Clearing will replace the cash for such substituted U.S. Treasuries within 29 days of the date of original substitution. Additionally, to ensure sufficient cash exits in a guaranty fund for the above mentioned substitution, CME Clearing may require any clearing member that is (or has an affiliate that is) a primary dealer with the Federal Reserve Bank of New York (a "Primary Dealer") to replace its non-cash guaranty fund deposits with cash upon 60 minutes notice.

Rule 822.A.2. Payment in Kind of US Treasuries for Settlement Variation Obligations

Further, pursuant to proposed Rule 822.A.2 in the event a liquidity shortfall remains after the substitution provided by Rule 822.A.1, CME Clearing may satisfy a settlement variation obligation to a clearing member that is (or has an affiliate that is) a Primary Dealer with U.S. Treasuries using a valuation based on the prior day's closing prices with prevailing CME haircuts applied. The amount of settlement variation that can be satisfied in this manner will be subject to a limit equal to the receiving clearing member's guaranty fund requirement at such time. Any firm receiving U.S. Treasuries under Rule 822.A.2 may notify CME Clearing that it desires to return such U.S. Treasuries in exchange for the original cash payment on the next business day.

Rule 822.B Payment in Kind For Portfolio Auction, Sale or Transfer

As part of its default management practices, CME Clearing will conduct an auction, sale or transfer of defaulted member positions and will compensate or receive payment from the winner/transferee of such positions based on bids received during the terms of the related default management action. Traditionally the compensation is denominated in cash. The Exchanges are proposing Rule 822.B to provide CME Clearing the option to include as part of the terms of an auction, sale or transfer the ability to satisfy any payment owed to a winner of an auction, sale or transfer with Federal Reserve discount window eligible securities with a market value (determined by the Clearing House as of the prior day's close of business utilizing a recognized third party pricing source) equal to the amount of such payment obligation. Any such option would be included as part of the terms of the auction, sale or transfer in advance of bidding so that bidding firms can provide pricing information taking the payment in kind possibility into account.

Rule 901.Q. Requirement to Establish Uncommitted Repo; Rule 901.R. Discount Window Access

Finally, the Exchanges are proposing two new rules to assist with its liquidity risk management. Proposed Rule 901.Q will require each clearing member that is a primary dealer or has a primary dealer affiliate to enter into (or arrange for such affiliate to enter into) a master repurchase agreement with CME on terms substantially similar to those set out by the Clearing House. Consistent with CFTC Regulation 39.33(c)(3) CME Clearing accepts certain highly marketable collateral to satisfy performance bond and guaranty fund obligations. CME Clearing currently utilizes prearranged master repurchase agreements that are highly reliable as required by paragraph 39.33(c)(3)(i)(E)(1) of the CFTC regulations. In order to ensure a diverse group of repo counterparties available to CME Clearing in times of market stress, the Exchanges are requiring that any clearing member that is a primary dealer or has a primary dealer affiliate to enter into (or arrange for such affiliate to enter into) a master repurchase agreement with CME on terms substantially similar to those set out by the Clearing House. Rule 901.R will require clearing members to inform the Clearing House whether it or one of its Affiliates has access to the Federal Reserve discount window and will notify the Clearing House if such access has been suspended, revoked, removed, terminated or otherwise limited in any way.

The text of the proposed rules is attached as Exhibit 1 and underscored.

The Exchanges request that the Commission expedite review of these rules as these proposed rules are required to satisfy Commission regulations and would materially decrease the risks presented by the SIDCO as described by the Commission in the SIDCO Rules. The Exchanges request that the Commission authorize implementation of these new rules pursuant to Regulation 40.10(g) on December 31, 2013 or as soon as practicable thereafter to assist with its compliance with the effective date of the rules and of the implementation date of international capital regulations.

The Exchanges reviewed the derivatives clearing organization core principles ("Core Principles") as set forth in the Commodity Exchange Act ("CEA"). During the review, the Exchanges identified the following Core Principles as potentially being impacted:

- Financial Resources: The proposed rules are designed to comply with the Commission's recently finalized SIDCO Rules, specifically (i) Regulation 39.33 requiring SIDCOs to maintain sufficient liquidity resources to meet its intraday, same-day, and multiday obligations to perform settlements with a high degree of confidence under a wide range of stress scenarios that should include, but not be limited to, a default by the clearing member creating the largest aggregate liquidity obligation for the [SIDCO]...in extreme but plausible market conditions and (ii) Regulation 39.35 requiring SIDCOs to establish rules and/or procedures to enable the SIDCO to meet its settlement obligations in light of a liquidity shortfall exceeding its financial resources. The proposed rules enhance CME Clearing's existing liquidity framework by providing additional liquidity resources, a framework for establishment of additional highly reliable prearranged funding arrangements and payment in kind of Federal Reserve eligible securities in the event the liquidity resources are insufficient
- Default Rules and Procedures: The proposed rules, specifically Rules 822.A.2 and 822.B, in addition to providing additional are designed to address liquidity shortfall scenarios as required under recently finalized CFTC Regulation 39.35.

Notice of this submission has been concurrently posted on CME Group's website at <http://www.cmegroup.com/market-regulation/rule-filings.html>.

The Exchanges certify these changes comply with the Act and regulations thereunder. There were no substantive opposing views to this action.

If you require any additional information regarding this submission, please contact Tim Doar at 312-930-3162 or via e-mail at Tim.Doar@cmegroup.com, or contact me at 212-299-2228 or Jason.Silverstein@cmegroup.com. Please reference our CME/CBOT/NYMEX Submission No. 13-565R in any related correspondence.

Sincerely,

/s/ Jason Silverstein
Executive Director & Associate General Counsel

cc: Board of Governors of the Federal Reserve System

Attachment: Exhibit 1

EXHIBIT 1

Proposed new CME/CBOT/NYMEX RULE 822. Liquidity Risk Management.

In order to satisfy CFTC Regulations and prudential liquidity standards, the Clearing House is establishing the following rules:

A. **Liquidity Rules.** In the event the Clearing House needs liquidity for non-cash collateral of a clearing member or its customers for same day settlement, the Clearing House will first attempt to obtain liquidity for such collateral through asset sale, any uncommitted funding arrangements, its committed lines of credit and any committed repurchase agreements. In the event the Clearing House is unable to obtain same day settlement through such means, the Clearing House may declare the occurrence of a Liquidity Event and in its sole discretion may take the following actions in the following order to secure same day liquidity for such assets as follows:

1. **Substitution of Guaranty Fund Cash.**

a. The Clearing House may substitute any cash deposited by a clearing member in a guaranty fund with U.S Treasuries deposited as performance bond or guaranty fund by a clearing member that is the subject of such Liquidity Event in an amount of assets with haircutted market value (determined by the Clearing House as of the prior day's close of business utilizing a recognized third party pricing source) equal to the amount of cash substituted. Any assets transferred by this rule shall be applied as guaranty fund deposit of any such clearing member whose cash was substituted and will be allocated pro rata among any clearing members with cash deposits. For any substitution of US Treasuries for cash in the guaranty fund, the Clearing House will replace the cash within 29 days of the date of the substitution.

b. In order to ensure the Clearing House can obtain sufficient cash from the guaranty fund pursuant 1.a. above, the Clearing House may notify any clearing member that is a primary dealer or has a primary dealer affiliate to replace its non-cash guaranty fund assets with cash within 60 minutes from the time of notification. To the extent that a clearing member(s) fails to provide cash within 60 minutes or the request occurs after 3 PM Central time, the Clearing House may debit cash from that clearing member's account in the amount of the clearing member's non-cash guaranty fund assets.

2. **Payment in Kind for Settlement Variation Obligations.** The Clearing House may satisfy settlement variation obligations to any clearing member that is a primary dealer or has a primary dealer affiliate, up to the amount of that clearing member's guaranty fund contribution, with US Treasuries valued based on the prior day's closing prices with prevailing CME haircuts applied. To the extent that the Clearing House pays its settlement variation obligations in US Treasuries, if the receiving clearing firm notifies the Clearing House on a same day basis that it will return the securities to the Clearing House on the next business day, then the Clearing House will pay cash equal to the original value of the Clearing House's settlement variation obligation on the next business day.

B. Payment in Kind For Portfolio Auction, Sale or Transfer. In accordance with the terms of any auction, sale or transfer of a defaulted or suspended clearing member's or customer portfolio for which a payment is owed by the Clearing House to an auction winner, purchaser or transferee, in lieu of satisfying such payment with cash, the Clearing House may satisfy any payment owed to such persons by transferring Federal Reserve discount window eligible securities with a market value (determined by the Clearing House as of the prior day's close of business utilizing a recognized third party pricing source) equal to the amount of such obligation.

Proposed new CME/CBOT/NYMEX DEFINITION

"Liquidity Event" shall mean the Clearing House requires liquidity (1) to satisfy obligations of a defaulted or suspended Clearing Member, (2) to satisfy obligations associated with the transfer of account(s) of a defaulted or suspended Clearing Member and (3) as a result of a liquidity constraint or default by a depository or settlement bank.

Proposed new CME/CBOT/NYMEX Rule 901.Q. Requirement to Establish Uncommitted Repo.

Each clearing member that is a primary dealer or has a primary dealer affiliate shall enter into (or arrange for such affiliate to enter into) a master repurchase agreement with CME on terms substantially similar to those set out by the Clearing House.

Proposed new CME/CBOT/NYMEX Rule 901.R. Discount Window Access.

Each Clearing Member will inform the Clearing House whether it or one of its Affiliates has access to the Federal Reserve discount window and will notify the Clearing House if such access has been suspended, revoked, removed, terminated or otherwise limited in any way.