

## OMB APPROVAL

OMB Number: 3235-0045  
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Required fields are shown with yellow backgrounds and asterisks.

Page 1 of \* 12

SECURITIES AND EXCHANGE COMMISSION  
 WASHINGTON, D.C. 20549  
 Form 19b-4

File No.\* SR - 2012 - \* 28

Amendment No. (req. for Amendments \*)

Proposed Rule Change by Chicago Mercantile Exchange, Inc.

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial \*



Amendment \*



Withdrawal



Section 19(b)(2) \*



Section 19(b)(3)(A) \*



Section 19(b)(3)(B) \*



Rule

Pilot



Extension of Time Period  
for Commission Action \*



Date Expires \*

19b-4(f)(1)



19b-4(f)(2)



19b-4(f)(3)



19b-4(f)(4)



19b-4(f)(5)



19b-4(f)(6)



Exhibit 2 Sent As Paper Document



Exhibit 3 Sent As Paper Document



### Description

Provide a brief description of the proposed rule change (limit 250 characters, required when Initial is checked \*).

Proposed Rule Change By Chicago Mercantile Exchange Inc. Related to the Liquidity Factor of its CDS Margin Methodology

### Contact Information

Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name \* Timothy

Last Name \* Elliott

Title \*

Executive Director and Associate General Counsel

E-mail \*

tim.elliott@cmegroup.com

Telephone \*

(312) 466-7478

Fax

### Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date 07/25/2012

By Timothy Elliott

(Name \*)

Executive Director and Associate General Counsel

(Title \*)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Timothy Elliott, tim.elliott@cmegroup.com

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

**Form 19b-4 Information (required)**

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change (required)**

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

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Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change.

(a) Pursuant to the provisions of Section 19(b)(2) of the Securities Exchange Act of 1934 (the “Act” or the “Exchange Act”)<sup>1</sup> and Rule 19b-4 thereunder<sup>2</sup>, Chicago Mercantile Exchange Inc. (“CME”) is filing with the Securities and Exchange Commission (“Commission”) a proposal to adjust the liquidity factor of its CDS margin methodology.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization.

(a) CME’s Board via delegated authority approved the proposed rule change on May 7, 2012.

(b) Please refer questions and comments on the proposed rule change to Tim Elliott, Associate General Counsel, CME Group, Inc., 20 S. Wacker Drive, Chicago, IL 60606, (312) 466-7478.

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

(a) Purpose

CME’s currently approved credit default swap margin methodology utilizes a “multi-factor” portfolio model to determine margin requirements for credit default swap (“CDS”) instruments. The model incorporates risk-based factors that are designed to represent the different risks inherent to CDS products. The factors are aggregated to determine the total

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<sup>1</sup> 15 U.S.C. 78s(b)(2).

<sup>2</sup> 17 C.F.R. 240.19b-4.

amount of margin required to protect a portfolio against exposures resulting from daily changes in CDS spreads. For both total and minimum margin calculations, CME evaluates each CDS contract held within a portfolio. These positions are distinguished by the single name of the underlying entity, the CDS tenor, the notional amount of the position, and the fixed spread or coupon rate. For consistency, margins for CDS indexes in a portfolio are handled based on the required margin for each of the underlying components of the index.

CME proposes to make an adjustment to one particular component of its current CDS margin model. The liquidity margin component of the CME CDS margin model is designed to capture the risk associated with bid/ask spreads and concentration inherent in the process of liquidating a portfolio of a CDS Clearing Member. The current methodology for the liquidity factor is a function of a portfolio's gross notional value, the current bid/ask of the 5 year tenor of the "on the run" contract, the Duration/Series/Tenor ("DST") factor, and a concentration factor based upon the gross notional for each of the CDX IG and CDX HY contracts. The total liquidity margin for a portfolio is the sum of the liquidity margins of the CDX IG and CDX HY CDS Contracts in the CDS Clearing Member portfolio.

The specific proposed change that is the subject of this filing relates only to the methodology used for the DST factor of the CDX IG and HY families. Under current methods, every DST calculation is calibrated separately for each index family. Further, the maximum DST value is used. The proposal is to change the DST factor so that it will apply to the specific series and tenor for each CDX IG and CDX HY CDS contract in a portfolio. The revision is designed to more closely align the DST factor with the liquidity profile of the CDS contracts in a portfolio.

The proposed adjustment does not require any changes to rule text in the CME rulebook and does not necessitate any changes to CME's CDS Manual of Operations. The change will be

announced to CDS market participants in an advisory notice that will be issued prior to implementation but after approval for the change is obtained from the Commission.

(b) Statutory Basis

The CME believes the proposed rule changes are consistent with the requirements of the Exchange Act including Section 17A of the Exchange Act. The enhancements to CME's current margin methodology will facilitate the prompt and accurate settlement of security-based swaps and contribute to the safeguarding of securities and funds associated with security-based swap transactions. The proposed rule changes accomplish those objectives because the changes are designed to better align the margin methodology with the liquidity profile of the instruments in the portfolio.

4. 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.

5. 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.

6. Extension of Time Period for Commission Action.

CME does not consent to an extension of the time period for Commission action on the proposed rule change.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D).

(a) Not applicable.

(b) Not applicable.

(c) Not applicable.

(d) This filing is made pursuant to paragraph Section 19(b)(2) of the Act and shall become effective upon approval by the Commission.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission.

The proposed rule change is not based on the rules of another self-regulatory organization or the Commission.

9. Exhibits

List of exhibits to be filed, as specified in Instructions C and D:

Exhibit 1 Notice of proposed rule change for publication in the Federal Register

Exhibit 2 Not applicable

Exhibit 3 Not applicable

Exhibit 4 Not applicable

Exhibit 5. Text of proposed rule change

**EXHIBIT 1**

**SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-\_\_\_\_\_; File No. SR-CME-2012-28]

**SELF-REGULATORY ORGANIZATIONS**

Proposed Rule Change By Chicago Mercantile Exchange Inc. Related to the Liquidity Factor of its CDS Margin Methodology

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Pursuant to Section 19(b)(2) 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 \_\_\_\_\_, 2012, 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 by CME.

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

CME proposes to make an adjustment to one particular component of its current CDS margin model. The text of the proposed rule change is below. Underscored text indicates additions; bracketed text indicates deletions.

The liquidity margin component of the CME CDS margin model is designed to capture the risk associated with bid/ask spreads and concentration inherent in the process of liquidating a portfolio of a CDS Clearing Member. The current methodology for the liquidity factor is a function of a portfolio’s gross notional value, the current bid/ask of the 5 year tenor of the “on the run” contract, the Duration/Series/Tenor (“DST”) factor, and a concentration factor based upon

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<sup>1</sup> 15 U.S.C. 78s(b)(2).

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

the gross notional for each of the CDX IG and CDX HY contracts. The total liquidity margin for a portfolio is the sum of the liquidity margins of the CDX IG and CDX HY CDS Contracts in the CDS Clearing Member portfolio. CME proposes to make changes to the methodology used for the DST factor of the CDX IG and HY families. Under current methods, every DST calculation is calibrated separately for each index family. Further, the maximum DST value is used. The proposal is to change the DST factor so that it will apply to the specific series and tenor for each CDX IG and CDX HY CDS contract in a portfolio. The revision is designed to more closely align the DST factor with the liquidity profile of the CDS contracts in a portfolio.

The text of the proposed rule change is available at the CME's Web site at <http://www.cmegroup.com>, at the principal office of CME, and at the Commission's Public Reference Room.

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## **II. Self-Regulatory Organizations 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.**

CME's currently approved credit default swap margin methodology utilizes a "multi-factor" portfolio model to determine margin requirements for credit default swap ("CDS")



instruments. The model incorporates risk-based factors that are designed to represent the different risks inherent to CDS products. The factors are aggregated to determine the total amount of margin required to protect a portfolio against exposures resulting from daily changes in CDS spreads. For both total and minimum margin calculations, CME evaluates each CDS contract held within a portfolio. These positions are distinguished by the single name of the underlying entity, the CDS tenor, the notional amount of the position, and the fixed spread or coupon rate. For consistency, margins for CDS indexes in a portfolio are handled based on the required margin for each of the underlying components of the index.

CME proposes to make an adjustment to one particular component of its current CDS margin model. The liquidity margin component of the CME CDS margin model is designed to capture the risk associated with bid/ask spreads and concentration inherent in the process of liquidating a portfolio of a CDS Clearing Member. The current methodology for the liquidity factor is a function of a portfolio's gross notional value, the current bid/ask of the 5 year tenor of the "on the run" contract, the Duration/Series/Tenor ("DST") factor, and a concentration factor based upon the gross notional for each of the CDX IG and CDX HY contracts. The total liquidity margin for a portfolio is the sum of the liquidity margins of the CDX IG and CDX HY CDS Contracts in the CDS Clearing Member portfolio.

The specific proposed change that is the subject of this filing relates only to the methodology used for the DST factor of the CDX IG and HY families. Under current methods, every DST calculation is calibrated separately for each index family. Further, the maximum DST value is used. The proposal is to change the DST factor so that it will apply to the specific series and tenor for each CDX IG and CDX HY CDS contract in a portfolio. The revision is designed to more closely align the DST factor with the liquidity profile of the CDS contracts in a portfolio.

The proposed adjustment does not require any changes to rule text in the CME rulebook and does not necessitate any changes to CME's CDS Manual of Operations. The change will be announced to CDS market participants in an advisory notice that will be issued prior to implementation but after approval for the change is obtained from the Commission.

The CME believes the proposed rule changes are consistent with the requirements of the Exchange Act including Section 17A of the Exchange Act. The enhancements to CME's current margin methodology will facilitate the prompt and accurate settlement of security-based swaps and contribute to the safeguarding of securities and funds associated with security-based swap transactions. The proposed rule changes accomplish those objectives because the changes are designed to better align the margin methodology with the liquidity profile of the instruments in the portfolio.

**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.

**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)(2)<sup>3</sup> of the Act and will become effective upon approval by the Commission.

#### **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 may be submitted by using the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>), or send an e-mail to [rule-comment@sec.gov](mailto:rule-comment@sec.gov). Please include File No. SR-CME-2012-28 on the subject line.
- Paper comments should be sent in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, D.C., 20549-1090.

All submissions should refer to File Number SR-CME-2012-28. 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 Web site (<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 inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at

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

the principal office of CME. 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-2012-28 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>4</sup>

Elizabeth M. Murphy

Secretary

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<sup>4</sup> 17 CFR 200.30-3(a)(12)