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March 6, 2007

VIA ELECTRONIC DELIVERY

Ms. Jennifer Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave., N.W.
Washington DC 20551

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corp.
550 17th Street, NW
Washington, DC 20429

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

Public Information Room
Office of the Comptroller of the Currency
Independence Square
250 E Street, NW
Washington, DC 20519

Re: Notice of Proposed Rulemaking; Risk-Based Capital Standards: Advanced Capital Adequacy Framework," 71 Fed. Reg. 55830

Dear Ladies and Gentlemen:

The Chicago Mercantile Exchange Inc. ("CME") welcomes the opportunity to comment upon the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision and Office of the Comptroller of the Currency's (collectively, the "Agencies") jointly issued Notice of Proposed Rulemaking regarding Risk-Based Capital Standards: Advanced Capital Adequacy Framework (the "NPR").

CME is currently the largest futures exchange in the United States. As an international marketplace, CME brings together buyers and sellers on its CME Globex® electronic trading platform and trading floors. CME offers futures and options on futures primarily in four product areas: interest rates, stock indexes, foreign exchange and commodities. CME is also the largest derivatives clearing organization in the world. In 2006, the CME Clearing House cleared more than 1.3 billion contracts, which represents 90% of all futures and options contracts traded on U.S. designated contract markets. While maintaining an average of \$40 billion of performance bond collateral, we move \$1.5 billion to \$3 billion in daily settlement variation payments among market participants. We believe that CME's substantial experience and leadership in clearing and risk management will benefit the Agencies' review of the matters set forth in the NPR.

In the NPR, the Agencies request public comment on the implementation of new risk-based capital requirements in the U.S. for large, internationally active banking organizations. In particular, the NPR details the Agencies' plans for implementing the Basel Committee on



Banking Supervision's (BCBS) new capital accord (Basel II). As discussed more fully below, CME strongly supports the Agencies' proposal to accord a 0% risk-weighting to collateral held on deposit at a qualifying clearing house.

Under current U.S. banking capital adequacy guidelines, cash and cash equivalent collateral deposited by a U.S. bank or its consolidated affiliates with a clearing house is subject to a 100% risk-weighting for credit risk when determining the bank's capital adequacy ratios. (Presently, affiliates of three of the largest banks in the U.S. are clearing members of CME: Citigroup Global Markets, J.P. Morgan Futures and Bank of America Securities.) CME believes that the current capital adequacy treatment relating to U.S. bank deposits is onerous and outdated. We thus applaud the Agencies' proposal to accord a 0% risk-weighting to such deposits.

As set forth in the NPR:

A [bank] may attribute an EAD (*exposure at default*) of zero to: (A) Derivative contracts that are publicly traded on an exchange that requires the daily receipt and payment of cash-variation margin; (B) Derivative contracts and repo-type transactions that are outstanding with a qualifying central counterparty (but not for those transactions that a qualifying central counterparty has rejected); and (C) Credit risk exposures to a qualifying central counterparty in the form of clearing deposits and posted collateral that arise from transactions described in paragraph (d)(6)(ii)(B) of this section.

The NPR defines a "qualifying central counterparty" as a counterparty (e.g., a clearing house) that: (i) facilitates trades between counterparties in one or more financial markets by either guaranteeing trades or novating contracts; (ii) requires all participants in its arrangements to be fully collateralized on a daily basis; and (iii) the is in sound financial condition and is subject to effective oversight by a national supervisory authority.

CME strongly urges the Agencies to allow, as set forth in the NPR, a 0% risk-weighting on collateral held by a clearing house acting as a qualifying central counterparty. Such adoption is consistent with the treatment on collateral of our broker-dealer and futures commission merchant clearing members whose regulators have long recognized the protections and capital efficiencies that a clearing house guarantee provides.

Moreover, we believe that the proposal is warranted in light of the comprehensive financial safeguard systems at clearinghouses such as CME. The goal of CME's Financial Safeguard System, which benefits and protects our clearing members and their customers, is to prevent the accumulation of losses, ensure sufficient resources are available to cover future obligations and promptly detect financial and operational weaknesses.

CME's risk management and financial surveillance procedures include:

- **Mark-to-the-Market/Cash Variation.** All positions are marked to the market twice daily (or more often in times of extreme price volatility) and mark-to-market gains/losses are paid from/to CME's Clearing House; thus removing debt obligations among all clearing members as they occur.



- Collection of Performance Bond. All clearing members must deposit acceptable collateral with CME's Clearing House to meet performance bond requirements. Performance bond is a good faith deposit which guarantee performance on positions. Such requirements are established by CME and are calculated twice daily by the CME-developed Standard Portfolio Analysis of Risk™ (SPAN®) based on historical price volatilities, current and anticipated market conditions and other relevant information.
- Real-Time Position and Price Monitoring. The Risk Management Department of CME's Clearing House monitors intra-day price movements and assesses the impact of these changes on the positions of its clearing members (or their customers) and conducts stress testing on a daily basis.
- Concentration Margining. CME's Clearing House may charge clearing members an additional performance bond requirement if its potential market exposure becomes large relative to its financial resources.
- Clearing Member Risk Reviews. CME's Clearing House periodically reviews its clearing member's financial, operational and risk management procedures and capabilities to evaluate how well each firm's procedures and capabilities correspond to its business.
- Financial Surveillance of Clearing Members. Clearing members must maintain capital at levels as required by Securities and Exchange Commission or Commodity Futures Trading Commission ("CFTC") regulations and/or Exchange rules. The financial condition of clearing members is continuously monitored as is its internal controls, risk management policies and back office operations.

Presently, CME's Financial Safeguard System has resources in excess of \$4.0 billion. A detailed summary of CME's Financial Safeguard System is available at: <http://www.cme.com/clearing/set/fs/finsafsys10241.html>

Moreover, as a Derivatives Clearing Organization ("DCO") regulated by the CFTC, CME is required to adhere to a comprehensive set of DCO Core Principals, which include a requirement to:

- have adequate financial, operational and managerial resources.
- manage its risks through the use of appropriate risk management tools and procedures.
- have the ability to complete settlements in a timely manner.
- have standards, rules, procedures or programs designed to:
 - protect and ensure the safety of member collateral and funds;
 - ensure the daily processing, clearing and settlement of transactions in the event of an emergency;
 - allow for efficient, fair and safe management in the event of a clearing member's insolvency or default; and
 - ensure its systems function properly and have adequate capacity and security.

As part of its oversight of CME's Clearing House, the CFTC reviews the Clearing House's operations to ensure that the Clearing House adheres to the Core Principals.



For all of the foregoing reasons, CME urges the Agencies to recognize the risk-reduction benefits that a clearing house provides and adopt the 0% risk-weighting for clearing house collateral.

If you have questions concerning this letter, please contact Anne Bagan, Director, Audit Department, at (312) 930-3140 or abagan@cme.com.

Sincerely,

A handwritten signature in black ink, appearing to be the name of Anne Bagan, written in a cursive style.