TESTIMONY
OF
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EXECUTIVE CHAIRMAN
CME GROUP INC.
BEFORE THE

SUBCOMMITTEE ON
SECURITIES, INSURANCE AND INVESTMENT
OF THE
SENATE COMMITTEE ON
BANKING HOUSING AND URBAN AFFAIRS

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Chairman Reed, Ranking Member Crapo, Members of the Subcommittee, thank you for the opportunity to respond to the Subcommittee's questions respecting clearing of swap contracts. I am Terry Duffy, Executive Chairman of CME Group ("CME Group" or "CME"), which is the world's largest and most diverse derivatives marketplace. CME Group includes four separate exchanges—Chicago Mercantile Exchange Inc., the Board of Trade of the City of Chicago, Inc., the New York Mercantile Exchange, Inc. and the Commodity Exchange, Inc. (together "CME Group Exchanges"). The CME Group Exchanges offer the widest range of benchmark products available across all major asset classes, including futures and options based on interest rates, equity indexes, foreign exchange, energy, metals, agricultural commodities, and alternative investment products. CME also includes CME Clearing, a derivatives clearing organization ("DCO") and one of the largest central counterparty clearing services in the world; it provides clearing and settlement services for exchange-traded contracts, as well as for over-the-counter ("OTC") derivatives transactions through CME Clearing and CME ClearPort®.

The CME Group Exchanges serve the hedging, risk management and trading needs of our global customer base by facilitating transactions through the CME Globex® electronic trading platform, our open outcry trading facilities in New York and Chicago, as well as through privately negotiated transactions executed in compliance with the applicable Exchange rules and cleared by CME's clearing house. In addition, CME Group distributes real-time pricing and volume data through a global distribution network of approximately 500 directly connected vendor firms serving approximately 400,000 price display subscribers and hundreds of thousands of additional order entry system users. CME's proven high reliability, high availability platform coupled with robust administrative systems represent vast expertise and performance in managing market center data offerings.

The financial crisis focused well-warranted attention on the lack of regulation of OTC financial markets. We learned a number of important lessons and Congress crafted legislation designed to reduce the likelihood of a repetition of that disaster. However, it is important to emphasize that regulated futures markets and futures clearing houses operated flawlessly. Futures markets performed all of their essential functions without interruption and, despite failures of significant financial firms, our clearing house experienced no default and no customers on the futures side lost their collateral or were unable to immediately transfer positions and continue managing risk. Dodd-Frank was adopted to impose a new regulatory structure on a previously opaque and unregulated market – the OTC swaps market. It was not intended to engineer a new regulatory regime for the already robustly regulated futures markets.

For example, while Congress granted the Commodity Futures Trading Commission (“CFTC” or “Commission”) the authority to adopt rules respecting Core Principles, it did not direct it to eliminate principles-based regulation. Yet the Commission has proposed specific requirements for multiple Core Principles—almost all Core Principles in the case of designated contract markets (“DCMs”) and DCOs—which would eviscerate the principles-based regime that has fostered the ability of CFTC-regulated entities to effectively manage risk for the past decade.

We support the overarching goals of DFA to reduce systemic risk through central clearing and exchange trading of derivatives, to increase data transparency and price discovery, and to prevent fraud and market manipulation. Unfortunately, DFA left many important issues to be resolved by regulators with little or ambiguous direction and set unnecessarily tight deadlines on rulemakings by the agencies charged with implementation of the Act. We have concerns about many of these proposed rulemakings, about which we have previously provided written testimony to the Senate Banking Committee and other committees of this Congress. For purposes of this hearing, we will focus on the following five questions posed to us by this Subcommittee:

1) What issues may affect the safety and soundness of clearinghouses, and how should those issues be mitigated?

2) What are the similarities and differences with other cleared products that should be considered when establishing clearinghouses for swaps?

3) Are there unique attributes of certain asset classes that should be highlighted when considering adopting a clearing paradigm? How about unique attributes of certain market participants?

4) What best practices should be considered regarding ownership, governance, or control of derivatives clearinghouses?

5) What structural and economic barriers affect access to swap clearing? What must be done to eliminate or reduce those barriers?

Question 1. What issues may affect the safety and soundness of clearinghouses, and how should those issues be mitigated?

The safety and soundness of clearinghouses is a major focus of Dodd-Frank. The Core Principles for derivative clearing houses compel DCOs to have adequate financial resources, comprehensive risk management procedures and safeguards against system failures. In addition, Dodd-Frank includes eight additional Core Principles dealing with the safety and soundness of derivative clearing houses. Moreover, the CFTC has been granted increased power to force a derivative clearing house to alter a procedure or implement a new procedure if it is not in compliance with the Core Principles, without the procedural steps previously required. The rigid rules being proposed by the CFTC with respect to risk management are unnecessary and destructive of innovation and competition. Such a prescriptive set of requirements will force clearinghouses into a rigid methodology for managing risk and inhibit the ability of individuals best positioned to adapt risk management methodologies to changing circumstances. The end result of this would be to increase, rather than reduce risk.

CME Group appreciates the importance to the broader financial system of a regulatory regime designed to ensure that every DCO can perform its role as a central counterparty, including performance of its financial obligations during periods of market stress. In that regard, the Commission's DCO Core Principles have functioned admirably and effectively over the years, including during the 2008 financial crisis. CME Group can support regulations that enhance the Commission's existing core principle system, if they strike a responsible balance between establishing general prudential standards and prescriptive requirements.

On March 21, 2011, CME Group, by its CEO Craig Donohue, filed a detailed 17 page letter commenting on an additional set of CFTC risk management requirements for clearing houses. The letter, which will not be repeated here, may be accessed at http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=31993&SearchText=. CME's position on this issue can be summarized as follows:

> The Commission's Notice of Proposed Rulemaking addresses the critically important topic of risk management practices at DCOs. Greater use of DCOs for OTC derivatives heightens the importance of ensuring that risk management at every DCO is robust and comprehensive. The unique risk characteristics of OTC derivatives products and markets underscore the importance of DCOs retaining reasonable discretion and flexibility to adapt risk management practices as products and markets develop over time.
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> Risk management is not an assembly-line type of process that can be commoditized, codified and deployed in such a way as to ensure that risk management regimes of DCOs remain prudent and agile. Indeed, very few aspects of risk management can be standardized across all cleared markets to such an extent that a rules-based regime can describe each potential condition that can arise and the necessary actions that can and should be taken to mitigate risk. CME Group is therefore very concerned that certain provisions in the proposed regulations would diminish CME Clearing's ability to effectively manage risk by requiring each DCO to employ the same rigid, standardized risk management procedures.
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> Consistent with the CFTC's approach in a number of other rulemakings, regulations proposed in the NPR further the CFTC's retraction of the highly successful principles-based regime that has permitted U.S. futures markets to prosper as an engine of economic growth for this nation, to a restrictive, rules-based regime that will stifle growth, innovation and flexibility in risk management. As we have noted in comment letters in response to other proposals, Congress not only preserved principles-based regulation in the Dodd-Frank Act, it reinforced the vitality of that regime by expanding the list of core principles applicable to DCOs. Although DFA granted the CFTC the authority to adopt

regulations with respect to core principles, it did not direct the CFTC to eliminate principles-based regulation. Rather, DFA made clear that DCOs were granted reasonable discretion in establishing the manner in which they comply with the Core Principles.

Furthermore, certain of the proposed prescriptive regulations would impose significant costs not only on DCOs and their clearing members, but on the CFTC, with little or no corresponding regulatory benefit. In that regard, CME Group is very concerned that the CFTC has not performed the required cost/benefit analyses with respect to the rulemaking proposals in the NPR. Aside from certain information provided in connection with recordkeeping and reporting requirements, the "cost/benefit analysis" with regard to the regulations proposed in connection with the Core Principles consists of little more than the following two assertions: (1) "With respect to costs, the Commission has determined that the costs to market participants and the public if these regulations are not adopted are substantial"; and (2) "With respect to benefits, the Commission has determined that the benefits of the proposed rules are many and substantial." In requiring the CFTC to consider costs and benefits of its proposed actions, Congress requires an actual and concrete estimate of costs of agency action. The mere uncertainty of cost estimates does not excuse the CFTC from issuing such an estimate.

The performance of actual and concrete cost/benefit analyses is particularly important for any regulator proposing to adopt regulations that would increase the costs of central clearing of OTC derivatives.

One of the CFTC proposals which causes us great concern is the CFTC's proposal to establish lower financial resource requirements for non-systemically important DCOs, an approach we believe will exacerbate rather than ameliorate systemic risk. The CFTC relies on Title VIII of Dodd-Frank in proposing Regulation 39.29, which would require a DCO that is deemed systemically important (a "SIDCO") to comply with substantially different and higher financial resources requirements than any DCO that the Financial Stability Oversight Council does not designate as systemically important. As proposed, Regulation 39.29 would: (1) require a SIDCO to maintain financial resources sufficient to meet its financial obligations notwithstanding a default by the two clearing members creating its largest financial exposures; (2) limit a SIDCO's use of assessment powers to cover financial resources requirements relating to a default by the clearing member creating its second largest financial exposure; and (c) for purposes of valuing its assessment powers, require a SIDCO to apply the same 30-percent haircut and 20-percent post-haircut cap on assessments as proposed for non-systemically important DCOs in Regulation 39.11(d).

Any regulation should subject all DCOs to the same substantive financial resources requirements, and subject systemically important DCOs to more frequent stress testing and reporting requirements. We believe this approach is better designed to achieve Dodd-Franks' objectives of promoting robust risk management, promoting safety and soundness, reducing systemic risk and supporting the broader financial system.

Setting a lower bar for non-systemically important DCOs with regard to financial resources requirements (and, presumably, for certain other DCO core principles, including Core Principle D regarding risk management) would allow those DCOs to offer lower guaranty fund and margin requirements. In addition to putting SIDCOs at an unfair competitive disadvantage, this approach would likely attract additional volume to at least some non-systemically important DCOs and transform them into de facto SIDCOs. However, until such time as they were designated SIDCOs by the Council and given sufficient time to come into compliance with the higher requirements for SIDCOs, they would be operating under the lower and less costly standards for non-systemically important DCOs. This would contravene Title VIII's stated objectives of promoting robust risk management, promoting safety and soundness, reducing systemic risk and supporting the broader financial system.

CME Group therefore urges that all DCOs be subject to the same substantive financial resources requirements. We suggest that, rather than adopting Regulation 39.29 as proposed, the Commission should adopt a regulation that subjects SIDCOs to more frequent stress testing and reporting requirements than any DCOs the Council does not designate as systemically important. For example, a SIDCO might be required to conduct bi-monthly stress tests of its ability to cover its default obligations (rather than monthly stress testing, as proposed for all DCOs), and to submit to the Commission the reports required under proposed Regulation 39.11(f) on a monthly basis (rather than a quarterly basis, as proposed for all DCOs). This alternative approach comports with the Council's recent statement that systemically important financial market utilities should be "subject to enhanced examination, supervision, enforcement and reporting standards and requirements."

CME Group is a staunch supporter of robust and comprehensive risk management practices throughout the cleared derivatives markets. As further explained below, we are supportive of those aspects of the proposed regulations that seek to implement appropriate and cost-effective measures to build upon the principles-based regime the CFTC has overseen in recent years and that performed admirably during the recent financial crisis. It is that regime that should be extended to the cleared swaps markets, and not an untested rules-based regime that, at least in part, appears to be based upon arbitrary assumptions and rigid concepts about how DCOs should manage risk.

Question 2. What are the similarities and differences with other cleared products that should be considered when establishing clearinghouses for swaps?

If a swap contract and a futures contract have similar volatility and trade in a mature, liquid market, which should be the case for the major plain vanilla swaps, the considerations for clearing the contracts are identical. Thinly traded swaps present more difficult management processes, which our clearinghouse aims to overcome through its admission and risk management processes.

This similarity between swaps and futures for a large part of the OTC market counsels in favor of adopting the clearing rules that have worked so successfully in futures markets. Indeed, a focus of Dodd-Frank is to bring the OTC swaps market into a regulatory scheme similar to that which allowed the futures markets to function flawlessly throughout the financial crisis. If the CFTC and the SEC are to meet the goals of Dodd-Frank to transition from the world of unregulated, uncleared OTC trading to a world more nearly approximating the highly successful futures model clearing, they should adhere to the principles which have already proven effective in the management of risk. Instead, the proposed clearing rules require a significant, untested and costly revision of an approach that has proved successful in the futures model and require that this new model be implemented in an impossibly short time frame.

For example, it does not make sense to impose an entirely new regime for segregation of customer assets for swap clearing, which will impose significant costs on participants and undermine efficient risk mitigation, when the existing model of futures clearing has provided

100% protection against loss due to customer default. In its Advanced Notice of Proposed Rulemaking ("ANPR"), however, regarding segregation of customer funds, the Commission notes that it is considering imposing an "individual segregation" model for customer funds belonging to swaps customers. A Notice of Proposed Rulemaking on this subject is forthcoming and appears to impose a form of "individual segregation" model for swaps clearing but not for futures clearing. Such a model would impose unnecessary costs on derivatives clearing organizations ("DCOs") and customers alike. As noted in the ANPR, DCOs have long followed a model (the "baseline model") for segregation of collateral posted by customers to secure contracts cleared by a DCO whereby the collateral of multiple futures customers of a futures commission merchant ("FCM") is held together in an omnibus account. If the FCM defaults to the DCO because of the failure of a customer to meet its obligations to the FCM, the DCO is permitted (but not required), in accordance with the DCO's rules and CFTC regulations, to use the collateral of the FCM's other futures customers in the omnibus account to satisfy the FCM's net customer futures obligation to the DCO. Under the baseline model, customer collateral is kept separate from the property of FCMs and may be used exclusively to "purchase, margin, guarantee, secure, transfer, adjust or settle trades, contracts or commodity option transactions of commodity or option customers." A DCO may not use customer collateral to satisfy obligations related to an FCM's proprietary account.

In its ANPR, the Commission suggests the possibility of applying a different customer segregation model to collateral posted by swaps customers, proposing three separate models, each of which requires some form of "individual segregation" for customer cleared-swap accounts. Each of these models would severely limit the availability of other customer funds to a DCO to cure a default by an FCM based on the failure of a customer to meet its obligations to the DCO. The imposition of any of these alternative models first, is outside of the Commission's authority under DFA and second, will result in significant and unnecessary costs to DCOs as well as to customers—the very individuals such models are allegedly proposed to protect.

CME Group recognizes that effective protection of customer funds is critical to participation in the futures and swaps markets. This fact does not, however, call for a new segregation regime. The baseline model has performed this function admirably over the years, with no futures customers suffering a loss as a result of an FCM's bankruptcy or default. There is no reason to believe it will not operate as well in the swaps market. DFA did nothing to change this segregation regime as applied to futures, and as noted above, a focus of DFA is to bring the OTC swaps market into a regulatory scheme similar to that which allowed the futures markets to function flawlessly throughout the financial crisis. To this end, it is unreasonable to believe that Congress would intend to require a different scheme of segregation of customer funds and as a result, a different margining and default model than that currently used in the futures markets. Imposing such a conflicting model would complicate the function of DCOs intending to clear both futures and swaps. Indeed, the statutory language adopted in Section 724 of DFA does nothing to compel such a result.

The imposition of a different customer segregation system could undermine the intent behind DFA by imposing significantly higher costs on customers, clearing members, and DCOs intending to clear swaps and injecting moral hazard into a system at the customer and FCM levels. A change from the baseline model would interfere with marketplace and capital efficiency as DCOs may be required to increase security deposits from clearing members. That is, depending on the exact methodology employed, DCOs may be forced to ask for more capital from clearing members. Based on CME Group's initial assessments, these increases in capital requirements would be substantial. For example, CME Group's guarantee fund would need to double in size. Aside from these monetary costs, adoption of a segregation model would create moral hazard concerns at the FCM level. That is, the use of the new proposed models could create a disincentive for an FCM to offer the highest level of risk management to its customers (if the oversight and management of individual customer risk was shifted to the clearing house) and continue to carry the amount of excess capital they do today.

Imposition of the suggested systems could increase costs and decrease participation in the CFTC-regulated cleared-swaps market because customers may be unable or unwilling to satisfy resultant substantially increased margin requirements. FCMs would face a variety of increased indirect costs, such as staffing costs, new systems and compliance and legal costs and direct costs such as banking and custodial fees. FCMs would likely, in turn, pass these costs on to customers. Additionally, smaller FCMs may be forced out of business, larger FCMs may not have incentive to stay in business, and firms otherwise qualified to act as FCMs may be unwilling to do so due to the risk and cost imposed upon the FCM model by individualized segregation. This could lead to a larger concentration of customer exposures at fewer FCMs, further increases to margin and guarantee fund requirements, and further increased costs to customers. All of these consequences would lead to decreased participation in U.S. futures and swaps exchanges and result in loss of jobs in the United States.

Question 3. Are there unique attributes of certain asset classes that should be highlighted when considering adopting a clearing paradigm? How about unique attributes of certain market participants?

As noted above, a thorough understanding of the liquidity and other characteristics of the market for a swap in normal and stressed circumstances is the key to safety and soundness in clearing. Different swaps with different liquidity and other varied characteristics, put simply, carry with them different risks. Interest rate swaps based on U.S., U.K. and E.U. instruments should be easy to liquidate in the event of a default as are futures on U.S. debt or Eurodollars. Single name credit default swaps are expected to require an elaborate pre-set process and direct participation for clearing members.

These differences in swaps, as well as the simple fact that Dodd-Frank imposes a brand new clearing regime on the OTC swaps market, counsels in favor of a slow phasing-in of swap clearing. The Commission's proposed rules for mandatory clearing and trading of swaps should be revised to stage the transition from the existing market structure so that the participants may make the technical and documentary changes necessary to avoid technological and legal risks. We believe that the following template will make the transition to clearing swaps under DFA the quickest, least costly and most complete and effective.

Stage 1: Continued Voluntary Clearing

- The Commission's first action must be to avoid impairment of the current successful clearing process for swaps and swaps converted to futures.
- The Commission should promptly make the requisite finding, pursuant to Section 5c(b), that a DCO, which is clearing swaps as of the effective date of DFA, will be permitted to continue clearing swaps of the same class and will also be permitted to clear any swap that is economically equivalent to any futures contract that it was clearing prior to the DFA effective date.
- The Commission should approve the collateral and risk management practices and procedures that were in place as of the DFA effective date pending further notice. This

means that the traditional form of customer segregation must continue and any of the proposed alternatives to limit or eliminate fellow-customer risk must be delayed until all of the remaining stages for implementing mandatory clearing have been approved. DCOs must be permitted to operate pursuant to the Core Principles, as amended by DFA, during this period.

- The CFTC should also demonstrate that it will abide by its commitment to preserve the cross margining benefits currently available to the users of ClearPort. The Commission should adopt a regulation that treats any ClearPort product that is cleared as a future as of the DFA effective date, but which is subsequently cleared as a swap, as entitled to be carried in a 4d account with customer futures contracts.

Stage 2: Mandatory Clearing Of Certain Dollar Denominated Swaps

- Promptly after the effective date of DFA, the Commission should make an initial determination, pursuant to CEA section 2(h)(2)(A)(i), that all U.S. dollar denominated swaps that are structurally and economically equivalent to swaps that are being cleared by a DCO or ICE Trust as of the DFA effective date are subject to the mandatory clearing requirement. This determination, if it becomes final, will subject more than 60% of the swaps market—that has not been exempted from the defined term by the Department of Treasury—to mandatory clearing. Next, "the Commission shall provide at least a 30-day public comment period regarding any determination made under clause (i)." Section 2(h)(2)(A)(ii)
- At this point, section 2(h) provides a clear path for anyone who objects to the finding to make its views known and to invoke an additional review process by the Commission, taking into account the factors described in section 2(h). The review process should be staged so that final determinations are made first for the highest volume swaps.
- The Commission should not adopt differing start dates for different classes of traders for mandatory clearing of particular types of swaps.
- This proposal will (i) preserve customer choice in clearing, (ii) bring the largest volume of swaps into clearing houses as soon as possible, and (iii) allocate the Commission's resources in an efficient manner.

Stage 3: Reconsider and Repropose Regulations Respecting the Operation of DCOs.

- Do not deviate from the Core Principles regulatory regime without cause.
- Do not change the method of customer segregation without cause (as further discussed above).

Stage 4: Registration of SEFs.

- Finalize rules respecting the structure and operation of SEFs.
- Allow an adequate number of days for SEFs to become operational and to test connections to DCOs, SDRs and customers.
- Implement mandatory trading requirement.

Stage 5: Mandatory Clearing of Dollar Denominated Swaps Listed for Clearing Post DFA Effective Date.

Stage 6: Mandatory Clearing of Swaps Denominated in G-7 Currencies

Question 4. What best practices should be considered regarding ownership, governance, and control of derivatives clearinghouses?

The extensive rules proposed by the CFTC respecting ownership, governance and control of derivative clearing houses can and should wait until there is evidence that the specific limitations in Dodd-Frank do not adequately control the potential problem. The Core Principles for derivative clearing houses are clear, comprehensive and easily shaped and enforced by the Commission on an as necessary basis. Section 5b of the CEA specifically insures: fairness respecting participant and product eligibility, appropriate governance fitness standards, prevention of conflicts of interest and appropriate composition of governing boards. The CFTC drafted these provisions. In the event that Dodd-Frank does prove insufficient, which is highly unlikely, the Commission could consider drafting "best practices" or safe harbors for ownership, governance, and control rather than extremely prescriptive measures like those in the proposed rules.

The Commission's proposed rules regarding the mitigation of conflicts of interest in DCOs, DCMs and SEFs ("Regulated Entities") exceed its rulemaking authority under DFA and impose constraints on governance that are unrelated to the purposes of DFA or the CEA. Section 726 conditions the Commission's right to adopt rules mitigating conflicts of interest to circumstances where the Commission has made a finding that the rule is "necessary and appropriate" to "improve the governance of, or to mitigate systemic risk, promote competition, or mitigate conflicts of interest in connection with a swap dealer or major swap participant's conduct of business with, a [Regulated Entity] that clears or posts swaps or makes swaps available for trading and in which such swap dealer or major swap participant has a material debt or equity investment." The "necessary and appropriate" requirement constrains the Commission to enact rules that are narrowly-tailored to minimize their burden on the industry. The proposed rules are not narrowly-tailored but rather overbroad, outside of the authority granted to it by DFA and needlessly burdensome.

The Commission proposed governance rules and ownership limitations that affect all Regulated Entities, including those in which no swap dealer has a material debt or equity investment and those that do not even trade or clear swaps. Moreover, the governance rules proposed have nothing to do with conflicts of interest, as that term is understood in the context of corporate governance. Instead, the Commission has created a concept of "structural conflicts," which has no recognized meaning outside of the Commission's own declarations and is unrelated to "conflict of interest" as used in the CEA. The Commission proposed rules to regulate the ownership of voting interests in Regulated Entities by any member of those Regulated Entities, including members whose interests are unrelated or even contrary to the interests of the defined "enumerated entities." In addition, the Commission is attempting to impose membership condition requirements for a broad range of committees that are unrelated to the decision making to which Section 726 was directed.

The Commission's proposed rules are most notably overbroad in that they address not only ownership issues but the internal structure of public corporations governed by state law and listing requirements of SEC regulated national securities exchanges. More specifically, the proposed regulations set requirements for the composition of corporate boards, require Regulated Entities to have certain internal committees of specified compositions and even propose a new definition for a "public director." Such rules in no way relate to the conflict of interest Congress sought to address through Section 726. Moreover, these proposed rules improperly intrude into an area of traditional state sovereignty. It is well-established that matters of internal corporate governance are regulated by the states, specifically the state of incorporation. Regulators may not enact rules that intrude into traditional areas of state sovereignty unless federal law compels such an intrusion. Here, Section 726 provides no such authorization.

Perhaps most importantly, the proposed structural governance requirements cannot be "necessary and appropriate," as required by DFA, because applicable state law renders them completely unnecessary. State law imposes fiduciary duties on directors of corporations that mandate that they act in the best interests of the corporation and its shareholders—not in their own best interests or the best interests of other entities with whom they may have a relationship. As such, regardless of how a board or committee is composed, the members must act in the best interest of the exchange or clearinghouse. The Commission's concerns—that members, enumerated entities or other individuals not meeting its definition of "public director" will act in their own interests—and its proposed structural requirements are wholly unnecessary and impose additional costs on the industry—not to mention additional enforcement costs—completely needlessly.

Question 5. What structural and economic barriers affect access to swap clearing? What must be done to eliminate or reduce those barriers?

An end user of swaps with sufficient credit and resources to enter into a swap will experience no barrier to clearing under Dodd-Frank. A firm that seeks to act as a clearing member of a swaps clearing house must meet the operational and financial requirements of that clearing house, which should be set sufficiently high to meet the clearing house's obligations under Dodd-Frank's Core Principles for DCOs. Dodd-Frank's requirements regarding safety and soundness modify a clearing house's obligation to grant open access to any potential clearing member. The issues of managing a default involving an immature or illiquid swap contract require higher admission standards than for a futures clearing house.

The Commission's proposed rules regarding submissions by DCOs seeking approval to clear swaps may, however, provide a barrier to access to clearing simply because they impose extreme difficulty and expense on a DCO seeking to clear a given swap. The proposed regulations treat an application by a DCO to list a particular swap for clearing as obliging that DCO to perform due diligence and analysis for the Commission respecting a broad swath of swaps, as to which the DCO has no information and no interest in clearing. In effect, a DCO that wishes to list a new swap would be saddled with the obligation to collect and analyze significant amounts of information to enable the Commission to determine whether the swap that is the subject of the application and any other swap that is within the same “group, category, type, or class” should be subject to the mandatory clearing requirement.

The proposed regulation eliminates the possibility of a simple, speedy decision on whether a particular swap transaction can be cleared—a decision that the DFA surely intended should be made quickly in the interests of customers who seek the benefits of clearing—and forces a DCO to participate in an unwieldy, unstructured and time-consuming process to determine whether mandatory clearing is required. Regulation Section 39.5(b)(5) starkly illustrates this outcome. No application is deemed complete until all of the information that the Commission needs to make the mandatory clearing decision has been received. Completion is determined in the sole discretion of the Commission. This proposed regulation is one among several proposals that imposes costs and obligations whose effect and impact are contrary to the purposes of Title VII of DFA. The costs in terms of time and effort to secure and present the information required by the proposed regulation would be a significant disincentive to DCOs to voluntarily undertake to clear a “new” swap. This process to enable an exchange to list a swap for clearing is clearly contrary to the purposes of DFA.

Thank you for allowing us to respond to these important questions.