

October 19, 2012

VIA E-MAIL SUBMISSION

Head of Payments Policy Department  
Reserve Bank of Australia  
GPO Box 3947  
Sydney NSW 2001  
pysubmissions@rba.gov.au

Re: Consultation on New Financial Stability Standards—August 2012

Dear Head of Payments Policy Department:

CME Group Inc. (“CME Group”) appreciates the opportunity to comment on the Consultation on New Financial Stability Standards (“Consultation Paper”).<sup>1</sup>

CME Group is the parent of four Designated Contract Markets (“DCMs”): 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”). These DCMs 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’s clearing house division (“CME Clearing”) offers clearing and settlement services for exchange-traded futures contracts, as well as over-the-counter (“OTC”) derivatives transactions through CME ClearPort. CME is registered with the U.S. Commodity Futures Trading Commission (“CFTC”) as a Derivatives Clearing Organization (“DCO”) and is one of the largest central counterparty (“CCP”) clearing services in the world.

1. Cross Border CCPs – Materially Equivalent Standards

CME Group believes local financial stability standards should allow market participants to clear through both domestic and foreign CCPs and supports the Consultation Paper’s adoption of this approach. We support the efforts of the Reserve Bank of Australia (“RBA”) to adopt international recommendations and to “place reliance on a sufficiently equivalent overseas regulator in respect of assessment against those standards for which a ‘materially equivalent’ standard is explicitly applied in the overseas regulatory regime.”<sup>2</sup> Allowing foreign CCPs to be utilized for purposes of the mandatory clearing obligation is consistent with IOSCO’s February 2012 report on *Requirements for Mandatory Clearing*, which states:

Advantages of allowing the use of third country CCPs to satisfy mandatory clearing are that it could allow mandatory clearing obligations to apply to a wider range of products or currencies

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<sup>1</sup> Reserve Bank of Australia, *Consultation on New Financial Stability Standards*, (August 29, 2012).

<sup>2</sup> *Id.* at 19.

than is available within any individual jurisdiction as well as increasing consistency between regimes and reducing the potential for regulatory arbitrage. Utilising such CCPs in mandatory clearing regimes would allow authorities to decrease counterparty risk via utilisation of central clearing over and above the use of domestic CCPs. The ability of third country CCPs to provide clearing services under overseas mandatory clearing regimes may also incentivise domestic CCPs to expand the range of products they offer in order to protect and expand their market share.<sup>3</sup>

As observed in CPSS-IOSCO's May 2010 report entitled *Guidance on the application of the 2004 CPSS-IOSCO Recommendations for Central Counterparties to OTC derivatives CCPs*, "[g]reater use of CCPs for OTC derivatives will increase their systemic importance."<sup>4</sup> Successful management of systemic risk will require a regulatory regime that incorporates appropriate measures whereby more than one CCP may be utilized for purposes of the mandatory clearing obligation. As such, CME Group believes that systemic risk management can be best accomplished by allowing central clearing through both domestic and foreign CCPs.

As is discussed in the Consultation Paper, the licensing of foreign CCPs would require a 'materially equivalent' standard analysis. Rather than requiring overseas licensed CCPs to comply with potentially conflicting regulatory standards set by local regulators, the better approach is relying on the relevant regulatory regime in the CCP's home country—if it is found to provide materially equivalent obligations and protections, and to require the foreign CCPs to cooperate with local regulators by sharing information and in other ways. CME Group strongly supports this approach; the UK Financial Services Authority has utilized this approach for a number of years in connection with recognised overseas clearing houses, including CME Clearing, and recognised overseas investment exchanges.

## 2. Legal Basis

The RBA's *Attachment 2: Draft Guidance – Financial Stability Standards for Central Counterparties* ["Proposed CCP Standards"] states that:

"[a] central counterparty should be a legal entity (whose primary activity is operating the central counterparty) and one which is separate from other entities which may expose it to risks unrelated to those arising from its function as a central counterparty."<sup>5</sup>

Due to the important role that CCPs play in the global financial markets, CME Group is supportive of the goals of regulators to establish a framework through which risks to CCPs can be appropriately analyzed and limited. Further, we appreciate the flexibility provided by Proposed CCP Standard 1.1.1, where the RBA provides CCPs the opportunity to "demonstrate that any risks posed to [their] primary activity as a central counterparty are appropriately and effectively managed."<sup>6</sup> However, the Proposed Standard notes strongly imply that the best structure for a CCP is to be legally separate and distinct from other businesses and entities within the group. As a general statement, we do not support a one-size-fits-all regulatory framework that does not account for the unique legal structure and legal/regulatory framework under which each CCP operates.

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<sup>3</sup> Technical Comm. Int'l Org. Sec. Comm'ns, [IOSCO], *Requirements for Mandatory Clearing*, at 38, IOSCO Doc. OR05/12 (February 29, 2012).

<sup>4</sup> Comm. Payment and Settlement Sys. & Technical Comm. Int'l Org. Sec. Comm'ns [CPSS-IOSCO], *Guidance on the Application of the 2004 CPSS-IOSCO Recommendations for Central Counterparties to OTC Derivatives CCPs*, at 1, CPSS Doc. 89 (May 12, 2010).

<sup>5</sup> Reserve Bank of Australia, *Consultation on New Financial Stability Standards, Attachment 2: Draft Guidance – Fin. Stability Standards for Cent. Counterparties* [hereinafter *Proposed CCP Standards*], at ¶ 1.1 (August 29, 2012).

<sup>6</sup> *Proposed CCP Standards* at ¶ 1.1.1.

We believe that the best way to effectuate a proper risk management framework for CCPs is through reliance on the *Principles for Financial Market Infrastructures* (“PFMI”) issued by CPSS-IOSCO in April 2012.<sup>7</sup> More specifically, we support the idea that each financial market infrastructure should complete a resolution and recovery plan through which they “should identify scenarios that may potentially prevent [them] from being able to provide [their] critical operations and services as a going concern and assess the effectiveness of a full range of options for recovery or orderly wind down” as required by Proposed CCP Principle 3 (Framework for the comprehensive management of risks), Standard 3.3.8 (Recovery and orderly wind-down plans).<sup>8</sup> Conducting an in-depth analysis of the risk scenarios attributable to each CCP based on their operations and structure as required by the PFMI is a much better and more tailored solution to mitigating CCP risk than making a generally applicable rule that CCPs should be separate legal entities. For example, the results of the analysis required by a resolution and recovery plan may demonstrate ways that having a CCP operate in the same legal entity as an exchange (or other ancillary business) could provide beneficial access to the expertise and financial resources appurtenant to the exchange(s). Since the de facto assumption that having a CCP as separate legal entity may not bear out in all cases (which is likely why a similar proposal wasn’t included in the PFMI), we do not believe that Proposed CCP Standards 1.1 and 1.2 should be included in the finalized guidance to the FSS.

We would also like to quickly comment on Proposed CCP Standard 1.6.2, which deals with the requirement that cross border CCPs obtain an independent legal opinion for the RBA that covers “cover[s] potential conflicts of law, the enforceability of the central counterparty’s rules in all relevant jurisdictions, and the central counterparty’s ability to satisfy its regulatory obligations in all relevant jurisdictions.”<sup>9</sup> This requirement is similar to CFTC Regulation 39.27, which requires DCOs providing clearing services outside the United States to “identify and address material conflict of law issues” and “demonstrate the enforceability of its choice of law in relevant jurisdictions.”<sup>10</sup> As noted above, we believe that conducting ‘materially equivalent’ analyses of a CCP’s home regulatory framework should be used to assess whether the CCP should be granted a license/recognition in the local jurisdiction and to avoid potentially conflicting regulatory standards in the home and local jurisdiction. As such, we believe that the RBA should rely on CFTC Regulation 39.27, and other similar regulations in other jurisdictions, rather than requiring an independent legal opinion for its own benefit.

To the extent that the RBA decides to apply this requirement to cross border CCPs, we assume that it does not expect to see a voluminous legal opinion<sup>11</sup> that analyzes these issues in every jurisdiction in which a cross border CCP operates. Rather, it is our expectation that the RBA uses the word “relevant” to imply that it would expect to see legal opinions where the resulting analysis could have an impact on the ability of the cross border CCP to operate in Australia. We respectfully suggest that the RBA clarify the meaning of the word “relevant” in the context of this legal opinion requirement in the final release, especially as it applies to cross border CCPs.

### 3. Exchange Settlement Account

Proposed CCP Standard 9.1 requires CCPs deemed systemically important by the RBA with Australian dollar obligations to “settle its Australian dollar obligations across an Exchange Settlement Account held at the Reserve Bank, in its own name, or that of a related body corporate acceptable to the Reserve

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<sup>7</sup> Comm. Payment and Settlement Sys. & Technical Comm. Int’l Org. Sec. Comm’ns [CPSS-IOSCO], *Principles for Financial Market Infrastructures*, CPSS Doc. 101 (April 16, 2012)

<sup>8</sup> *Id.* at 34.

<sup>9</sup> *Proposed CCP Standards* at ¶ 1.6.2.

<sup>10</sup> 17 C.F.R. § 39.27.

<sup>11</sup> On average, the legal opinions received by CME Group when conducting this analysis have been 40+ pages. Thus a legal opinion covering every jurisdiction we operate in would be hundreds of pages long.

Bank.”<sup>12</sup> We would be happy to open an Exchange Settlement Account with the RBA but would encourage flexibility in the application of this requirement due to potential conflict with the regulations of a cross border CCP’s home regulator. For example, it is possible that CFTC Regulations 1.49 and 22.8<sup>13</sup> and the guidance contained in the CFTC’s final rule covering swaps customer collateral requirements<sup>14</sup> could present issues for DCOs seeking to hold customer swaps collateral in foreign jurisdictions.<sup>15</sup> Thus, we would suggest that the RBA be flexible in the way that cross border CCPs may meet the requirement that they open exchange settlement accounts and hold collateral in an Austraclear account.

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CME Group thanks the RBA for the opportunity to comment on this matter and we would be happy to discuss any of these issues. If you have any comments or questions, please feel free to contact me at (312) 930-3488 or Kathleen.Cronin@cmegroup.com; or Sean Downey, Director and Associate General Counsel, at (312) 930-8167 or Sean.Downey@cmegroup.com.

Sincerely,



Kathleen M. Cronin

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<sup>12</sup> *Proposed CCP Standards* at ¶ 9.1.

<sup>13</sup> 17 C.F.R. § 1.49 (providing for permissible locations of swaps customer collateral accounts); 17 C.F.R. § 22.8 (same).

<sup>14</sup> Protection of Swaps Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions, 77 Fed. Reg. 6336 (Feb. 7, 2012) (to be codified at 17 C.F.R. §§ 22, 190).

<sup>15</sup> For example, the application of Australian insolvency law to customer swaps collateral could present problems under CFTC regulations.