

# SUBMISSION COVER SHEET

Registered Entity Identifier Code (optional)

Date: 09/29/2013

**IMPORTANT: CHECK BOX IF CONFIDENTIAL TREATMENT IS REQUESTED.**

## ORGANIZATION

GFI Swaps Exchange LLC

## 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)
- Made Available To Trade Determination under § 40.5 or § 40.6
- Advance Notice of SIDCO Rule Change under § 40.10 (a)

### • Products

- Certification under § 40.2 (a) or § 41.23 (a)
- Submission under § 39.5
- Swap Class Certification under § 40.2 (d)
- Request for Approval under § 40.3 (a)
- Novel Derivative Product Notification under § 40.12 (a)

## RULE NUMBERS

N/A

## DESCRIPTION

Self-Certification of a Class of Credit Options and Exotic Options



September 29, 2013

**BY ELECTRONIC MAIL: [submissions@cftc.gov](mailto:submissions@cftc.gov)**

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

**Re: Commission Regulations 40.2(a) and 40.2(d) –  
Class Certification of Credit Options and Exotic Options**

Dear Ms. Jurgens:

GFI Swaps Exchange LLC (“GFI”) hereby notifies the Commodity Futures Trading Commission (the “Commission”), pursuant to Commission Regulations 40.2(a) and 40.2(d), that it is certifying a class of credit options and exotic options (“Options”) iTraxx Europe Index, MCDX Index, North American CDX Index, municipal bonds, corporate debt, sovereign debt and structured credit default swaps (each, an “Underlying”) for trading on GFI’s electronic trading platform (the “Trading Platform”).

GFI will list the class of Options no earlier than October 2, 2013.

This submission letter contains the following attachments:

- The submission cover sheet.
- Attached as Exhibit A, a concise explanation and analysis of Options.
- Attached as Exhibit B, a copy of the Options Rules, which will be published as contract specifications on GFI’s website in accordance with GFI Rule 1101.
- Attached as Exhibit C, a concise explanation and analysis of the products’ compliance with applicable provisions of the Commodity Exchange Act (the “CEA”), including the Core Principles, and the Commission’s Regulations thereunder.

As required by Commission Regulation 40.2(d)(1), GFI hereby certifies that:

- (i) That each particular swap within the certified class of swaps is based upon an “excluded commodity” specified in Regulation 40.2(d)(1);
- (ii) That each particular swap within the certified class of swaps is based upon an excluded commodity with an identical pricing source, formula, procedure, and methodology for calculating reference prices and payment obligations;



(iii) That the pricing source, formula, procedure, and methodology for calculating reference prices and payment obligations in each particular swap within the certified class of swaps is identical to a pricing source, formula, procedure, and methodology for calculating reference prices and payment obligations in a product previously submitted to the Commission and certified or approved pursuant to Regulation 40.2 or Regulation 40.3; and

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(iv) That each particular swap within the certified class of swaps is based upon an excluded commodity involving an identical currency or identical currencies.

GFI certifies that each Option complies with the CEA and Commission Regulations thereunder. GFI additionally certifies that it has concurrently posted a copy of this submission letter and attachments hereto on GFI's website.

\* \* \*

In the event that you have questions, please contact the undersigned at (212) 968-2982 or [daniel.glatter@gfigroup.com](mailto:daniel.glatter@gfigroup.com).

Sincerely,

A handwritten signature in black ink, appearing to read 'Daniel E. Glatter', written in a cursive style with a large, sweeping flourish at the end.

Daniel E. Glatter



## Exhibit A

Below is a concise explanation and analysis of the Options:

Credit options are options on various underlying instruments relating to credit that give the holder the right, but not the obligation, to engage in a swap. Exotic options are options that have complex terms relating to the determination of payoff upon exercise of the option. Exotic options sometimes also include non-standard underlying instruments.

A credit default swap is a derivative transaction that allows for one party to transfer to another party for an agreed period of time the credit risk associated with a single reference entity, a group of several reference entities or an index of reference entities (an "Index CDS"). In each CDS, one party (the "Buyer") pays a cash premium (the "Premium") to the other party (the "Seller") to purchase credit protection against the occurrence of an adverse event (a "Credit Event") with respect to the reference entity or entities. The most common Credit Events are bankruptcy, failure to pay obligations and restructuring of obligations. The credit protection can relate to a specific type of obligation or all obligations of a reference entity and is expressed in terms of a notional amount of the relevant obligations. Selling credit protection is economically equivalent to owning the relevant obligations. Buying credit protection is economically equivalent to selling those obligations short.

If a Credit Event occurs before the maturity date of a CDS, the Seller must make a payment to the Buyer in accordance with the settlement terms of the CDS. In general, there are two ways to settle a CDS, with the choice being made at the initiation of the contract: physical settlement and cash settlement. Physical settlement requires the Buyer to deliver the notional amount of deliverable obligations of the reference entity to the Seller in return for the notional amount paid in cash. In cash settlement, a cash payment is made by the Seller to the Buyer equal to par minus the recovery rate of the reference asset, with recovery rate being calculated by referencing dealer quotes or observable market prices over some period after default has occurred. Market practice for CDS has become more uniform since 2009 under the auspices of the International Swaps and Derivatives Association, Inc. so that cash settlement is now the norm, Credit Events are determined by committees made up of market practitioners and settlement prices for obligations are determined by standardized auctions.

Index CDS are swaps with highly standardized market terms. The North American CDX Indices are owned and administered by Markit Group Limited. The various North American Corporate Credit Indices contain North American and Emerging Market corporate reference entities.

### North American CDX Index

The North American CDX Index family includes the following indices: North American Investment Grade CDX Index ("IG CDX"), which contains 125 North American corporate reference entities; North American High Yield CDX Index ("HY CDX"), which contains 100 North American corporate reference entities; and Emerging Market CDX Index ("EM CDX"), which contains 40 emerging market nation corporate reference entities.



## **iTraxx Index**

The Markit iTraxx Asian indices comprise of Markit iTraxx Asia ex-Japan index (a 50 equally-weighted investment grade CDS index of Asian entities), a Markit iTraxx Australia index (25 equally-weighted Australian entities) and a Markit iTraxx Japan index (50 equally-weighted CDS of Japanese entities). The iTraxx Europe Index family includes the following indices: iTraxx Europe, which is composed of 125 liquid European corporate reference entities with investment grade credit ratings that trade in the CDS market; iTraxx Europe Crossover, which is composed of up to 50 European corporate reference entities with non-investment grade credit ratings that trade in the CDS market; iTraxx Europe HiVol, which contains 30 of the widest spread non-financial corporate reference entities from Europe, Asia and emerging markets; iTraxx Europe Senior Financials, which is composed of the 25 corporate financial entities from the Markit iTraxx Europe index referencing senior debt; and iTraxx Europe Subordinated Financials, which is composed of the 25 corporate financial entities from the Markit iTraxx Europe index referencing subordinated debt.

The indices in the Markit iTraxx SovX family are the Markit iTraxx SovX Western Europe Index (comprising 15 names from the Eurozone region plus Denmark, Norway, Sweden and United Kingdom that trade on Western European documentation), the Markit iTraxx SovX CEEMEA Index (comprising 15 names in the Central & Eastern Europe, Middle East and African countries that trade on Emerging Markets documentation), Markit iTraxx SovX CEEMEA ex-EU (A subset of constituents of the Markit iTraxx SovX CEEMEA Index which do not form part of the European Economic area), the Markit iTraxx SovX Asia Pacific Index (comprising 10 names from the Asia and Oceania regions), the Markit SovX Latin America Index (comprising 8 names from the Latin America region), the Markit iTraxx SovX Global Liquid Investment Grade Index (comprising the most liquid high grade sovereign entities), the Markit iTraxx SovX G7 Index (comprising entities from the G7 universe) and the Markit iTraxx SovX BRIC Index (comprising the most liquid BRIC entities).

## **MCDX Index**

The Markit MCDX index has these primary characteristics: Reference Entities (50 equally-weighted reference entities), Reference Obligations, Ratings (specific ratings included in the index), Credit Events (Failure to pay; Restructuring), Recovery Rate assumptions (for upfront and unwind calculation), Roll Dates (3rd April, 3rd October), Tenor (3, 5, 10 years) and Quotation Standard (basis points).

## **Structured Credit Default Swaps**

There are several types of structured credit default swaps that are used in conjunction with exotic options. First, a “contingent CDS” is a variation on a credit default swap in which a payment is trigger upon the occurrence of a credit event and another specified event that is based on an overservable market variable. Contingent CDS can be based on a single-name security or on an index as a whole.



Second, a “first to default/Nth to default” is a credit default swap comprised of a basket of reference credits that entitles the purchaser to receive a payout when the first credit in the basket defaults. After such an event, the transaction terminates. The payout on an Nth to default is triggered when the specified number of credits in the basket have defaulted.

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Third, a “bespoke tranche” is a type of credit default swap that permits investors to gain exposure to a particular portion of the loss distribution of a specified index.

### **Debt**

Options can also be bought and sold over single-name sovereign debt, municipal bonds and corporate debt. Sovereign debt is the amount of money that any given country’s government has borrowed, typically issue das bonds denominated in a reserve currency. Municipal bonds are bonds issued by a local government, or their agencies. Corporate debt is generally bonds issued by a corporation. Corporate bonds are usually issued by a company to raise capital and generally have a maturity date of at least one year or longer from the issue date.

## Exhibit B

# GFI Contract Specifications

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### Swap Specifications Pursuant to Rule 1101

(i) Options that are not subject to mandatory clearing but which are accepted by a Clearing Organization and which are offered for trading on the SEF as Permitted Transactions may be submitted voluntarily by the parties for clearing.

(ii) Options not accepted by a Clearing Organization for clearing may be listed for trading on or subject to the Rules of the SEF as Permitted Transactions.

(iii) The terms and conditions of the options offered for trading as Permitted Transactions on the SEF incorporate by reference such credit and other terms as the parties may establish through their pre-existing bi-lateral agreement.

(iv) The Options listed for trading by the SEF have the following specifications:

Contract Overview	An agreement to buy or sell the right to engage in a swap on a basket of liquid North American, European or Asian based entities.
Option Trade Date	As agreed by the counterparties.
Option Seller	As agreed by the counterparties.
Option Buyer	As agreed by the counterparties.
Premium	As agreed by the counterparties.
Strike Price	As agreed by the counterparties.
Expiration Date	As agreed by the counterparties.
Underlying Index, Security or Debt, as applicable	iTraxx Asia Ex Japan iTraxx Australia iTraxx Japan iTraxx SovX CDX.NA MCDX Municipal bonds Sovereign debt Corporate debt Structured credit default swaps (contingent CDS, index contingent CDS, first to default Nth to Default, bespoke tranche)
Currency	USD
Quoting Convention and Minimum Increment	As agreed by the counterparties.
Minimum Size	As agreed by the counterparties.
Effective Date	The date on which the counterparties begin calculating accrued obligations such as fixed payments (i.e., start date of the swap).
Maturity Date	The final date on which the obligations no longer accrue and the final payment occurs.

Trade Types	Outrights; roll trades; curve trades.
Settlement	Contingent payment - Payments related to credit event settlement will be determined pursuant to the 2009 ISDA Credit Derivatives Determination Committees and Auction Settlement Supplement, (i.e., the Big Bang Protocol).
	Fixed Quarterly cash payments - reflected in basis points and paid by the protection buyer to the protection seller.  Upfront fee payment - The upfront fee is a portion of the payments, expressed in percentage points of the notional, which is present valued and paid immediately to the seller.
Trading Hours	00:01-24:00pm (ET), Sunday-Friday
Block Size	As set forth in Appendix F to Part 43 of the Commission Regulations.
Speculative Limits	As set in Part 151 of the CFTC Regulations.
Reportable Levels	As set in the CFTC Regulation 15.03.



## Exhibit C

GFI has determined that the Options certified herein bear upon the following Core Principles:

### **Core Principle 2 – Compliance with Rules**

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Trading in Options will be subject to the GFI Rulebook (the “Rules”), which prohibits abusive trading practices, including: acts detrimental to GFI (Rule 522) or that are inconsistent with just and equitable principles of trade (Rule 510), fraudulent acts (Rule 511), fictitious or non-competitive transactions (Rule 512), market manipulation (Rule 515), disruptive trading practices (Rule 516), misstatements (Rule 521), wash sales (Rule 531) and pre-negotiated or non-competitive trades, including money passes (Rule 533). Trading in these Swaps will also be subject to Rules relating to protection of customers. *See* Rules 525-528.

As with all Swaps listed for trading on the Trading Platform (as such terms are defined in the GFI Rulebook), trading activity in Options will be subject to monitoring and surveillance by GFI’s Market Regulation Department. GFI has the authority to exercise its investigatory and enforcement power where potential Rule violations are identified. *See* Chapter 7 of the Rules.

Pursuant to Rule 601(a)(i), each Option executed as a block trade must be for the quantity that is equal to or in excess of the applicable minimum block size for such Option set forth in Commission Regulations.

### **Core Principle 3 – Swaps Not Readily Susceptible to Manipulation**

With respect to an Option, the value of payments made pursuant to the terms of this type of swap is determined primarily by reference to the applicable Underlying (the “Reference Price”). The Reference Price is not readily susceptible to manipulation because it has the following characteristics: (i) it is derived from a cash market that has considerable depth and liquidity resulting from the involvement of numerous institutional participants; (ii) the way in which the Reference Price is calculated is well documented and well understood by swap market participants; (iii) it is commonly used in the swap markets; (iv) information about the Reference Price is publicly and readily available; (v) if the Reference Price is based on an index, the index is administered and published by a reputable organization; and (vi) the most active participants in the relevant cash market are entities that are subject to regulation.

### **Core Principle 4 – Monitoring of Trading and Trade Processing**

Chapter 5 of the Rules prohibits traders from manipulating, distorting the price of, and disrupting the cash settlement process of the Swaps. Such Rules are enforced by the Market Regulation Department.

### **Core Principle 5 – Ability to Obtain Information**

Pursuant to the Rules, GFI will have the ability and authority to obtain sufficient information for each Option to allow GFI to fully perform its operational, risk management, governance and regulatory functions and requirements under Part 37 of Commission Regulations.

## Core Principle 6 – Position Limits or Accountability

Rule 536 allows GFI to adopt position accountability levels for Required Transactions. Persons with positions in excess of position accountability levels established by GFI will be required to provide, upon request by GFI, information about their positions in excess of the relevant position accountability threshold and consent to halt any further increases in those positions. GFI's Rules relating to position limits, position accountability levels and aggregation standards are provided below:

### 535. Position Limits; Exemptions

- (a) The Company may establish position limits for one or more Swaps, and grant exemptions from position limits, in accordance with CFTC Regulations. A Person seeking an exemption from position limits must apply to the Market Regulation Department in the form and manner required by the Company.
- (b) A Person intending to exceed position limits, including limits established pursuant to a previously approved exemption, must file the required application and receive approval from the Company prior to exceeding such limits. Notwithstanding the foregoing, a Person who establishes an exemption-eligible position in excess of position limits and files the required application with the Company shall not be in violation of this rule provided the filing occurs within one Business Day after assuming the position. In the event the positions in excess of the limits are not deemed to be exemption eligible, the applicant will be in violation of speculative limits for the period of time in which the excess positions remained open.
- (c) The Company shall, on the basis of the application and any requested supplemental information, determine whether an exemption from position limits shall be granted. The Company may approve, deny, condition or limit any exemption request based on factors deemed by the Company to be relevant, including, but not limited to, the applicant's business needs and financial status, as well as whether the positions can be established and liquidated in an orderly manner. A Person that has received an exemption from position limits pursuant to this Rule 535 shall be deemed to have agreed:
- (i) to comply with all terms, conditions or limitations imposed by the Company with respect to the exemption;
  - (ii) that the Company may modify or revoke the exemption at any time;
  - (iii) to initiate and liquidate positions in an orderly manner; and
  - (iv) to promptly submit a supplemental statement to the Company whenever there is a material change to the information provided in the most recent application.
- (d) A Participant shall not be in violation of this Rule if it carries positions for its Customers in excess of the applicable position limits for such reasonable period of time as the firm may require to discover and liquidate the excess positions. For the purposes

of this Rule, a reasonable period of time shall generally not exceed one Business Day. A Customer who exceeds the position limits as a result of maintaining positions at more than one Participant shall be deemed to have waived confidentiality regarding his positions and the identity of the Clearing Firm(s) at which they are maintained. A Participant carrying such positions shall not be in violation of this Rule if, upon notification by the Company, it liquidates its pro-rata share of the position in excess of the limits or otherwise ensures the Customer is in compliance with the limits within a reasonable period of time.

- (e) Nothing in this Rule 535 shall in any way limit:
  - (i) the authority of the Company to take emergency action; or
  - (ii) the authority of the Company to review at any time any position owned or controlled by any Person and to direct that such position be reduced to the applicable position limit.
- (f) A Person who has received written authorization from the Company for an exemption from position limits must annually file an updated application on or before the date that is one year following the approval date of the most recent application. Failure to file an updated application shall result in expiration of the exemption.
- (g) No Person shall exceed position limits that may be established by the Company or the CFTC, unless an exemption is granted by the Company. Any Person making a bid or offer that would, if accepted, cause such person to exceed the applicable position limits shall be in violation of this Rule.

#### **536. Position Accountability**

- (a) The Company shall establish position accountability levels for Required Transactions unless the Company has previously established position limits pursuant to Rule 535. A Person who holds or controls aggregate positions in excess of position accountability levels shall:
  - (i) provide, in a timely manner upon request by the Company, information regarding the nature of the position, trading strategy, and hedging information, if applicable;
  - (ii) be deemed to have consented, when so ordered by the Company, not to further increase the positions which exceed such position accountability levels; and
  - (iii) initiate and/or liquidate such positions in an orderly manner.
- (b) For purposes of this Rule 536, all positions in accounts for which a Person, by power of attorney or otherwise, directly or indirectly controls trading shall be included with the positions held by such Person. The provisions of this rule shall apply to positions held by two or more Persons acting pursuant to an expressed or implied agreement or understanding, the same as if the positions were held by or the trading of the positions was controlled by a single Person.

### **537. Aggregation of Positions**

For purposes of Rule 535 and Rule 536, positions in Swaps shall be aggregated in accordance with CFTC Regulations.

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### **Core Principle 7 – Financial Integrity of Transactions**

All Swaps that are required to be cleared pursuant to Section 2(h) of the CEA or that are voluntarily cleared by the counterparties will be submitted for clearing through a DCO. *See* Rule 1002.

### **Core Principle 9 – Timely Publication of Trading Information**

In accordance with Part 16 of Commission Regulations, GFI will publish daily market volume data reports for each Swap (or class of Swap) in terms of notional value. In addition, GFI will publish for each trading day, by tenor of the Swap, the opening price and the high and low prices. GFI will publish a settlement price for each such Swap except that, in the case of swaps listed for clearing by a DCO, the applicable settlement price will be the settlement price established by the DCO and GFI's website will contain a hyperlink to the relevant settlement information. *See* Rule 407.

GFI will submit electronic reports of all primary economic terms data for each Swap to a registered swap data repository immediately following execution of such Swap. *See* Rule 528. All such reports will meet the standards set out in Commission Regulation 45.3, including the requirement to produce a unique swap identifier for each transaction. GFI will also issue confirmations of transactions pursuant to Rule 525.