April 15, 2016

Brent J. Fields, Secretary
Securities and Exchange Commission
100 F. Street, NW
Washington, DC 20549

Re: Release No. IC-31933; File No. S7-24-15; “Use of Derivatives by Registered Investment Companies and Business Development Companies”

Dear Mr. Fields:

Intercontinental Exchange, Inc. (“ICE”) appreciates the opportunity to comment on the proposed rule filing (“Proposal”). In summary, ICE believes that regulators, fund managers and investors will benefit most if the SEC considers modifying the aspects of the proposal mentioned below in a way that aligns them more consistently with other federal government valuation and risk measurement rules.

Background

As the owner and operator of SuperDerivatives, Inc. and Interactive Data Holdings Corp (“IDC”), the bulk of our comments below are focused from the lens of the Proposal’s potential impact on the process of providing valuations of assets that are used to establish a fund’s Net Asset Value (“NAV”). In addition, as the operator of the largest listing exchange for exchange traded funds (“ETFs”), NYSE Arca Equities, Inc., we also want to raise the awareness of the Commission that the Proposal treats all funds equally without recognition that not all funds have the same construct. Specifically, in light of the unique disclosure requirements applicable to ETFs, we believe the Commission should consider whether the Proposal should be more carefully tailored to apply only to certain funds.

Value at Risk (“VaR”) Models and Considerations

The Proposal strives to provide guidance on the use of different valuation methodologies for purposes of determining the risk of a fund’s portfolio. As described in the Proposal, there are potential shortfalls with certain value-at-risk (“VaR”) methodologies that use a “relative” measure of risk which benchmarks against the risk of a fund’s portfolio as a whole, rather than the risk of the individual derivatives positions in a fund’s portfolio. ICE appreciates the Commission’s view that the use of an overly broad relative VaR methodology could result in inadvertent limitations on risk or volatility in a fund’s portfolio that may be inconsistent with the intent of the Investment Company Act of 1940. ICE maintains, however, that relative VaR methodologies on the

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whole serve as an appropriate measurement of the aggregate exposure of derivative holdings as compared to the rest of the fund’s portfolio. By exploring a distribution of scenarios and their outcomes on the portfolio, VaR and related methodologies are widely used by professional fund managers and investors to understand the risks in portfolios. While any single summary statistic cannot describe all possible risks associated with a portfolio, VaR approaches, and more importantly, their limitations, are well understood in the asset management industry. Indeed, IDC’s BondEdge analytics software currently supports aspects of VaR calculations, and it is currently enhancing existing software to support functionality more closely aligned with the Proposal. We strongly believe that the Commission should be more flexible in providing options to funds using a VaR or other risk methodologies under the risk-based portfolio limit in the Proposal and align the Proposal more closely with valuation requirements applied in other contexts, such as those by banking regulators. For example, as noted in the Proposal, the Basel Committee on Bank Supervision is standardizing market risk measurements for covered banks by moving towards an Expected Shortfall methodology and allowing different approaches from VaR to attempt to better capture tail risks and exposures.2

If a reliance on a prescriptive type of VaR model under the risk-based portfolio limit remains the focus of the Commission in any approved rule, we agree with the approach taken to require a minimum of three years of data for developing a historical simulation. For example, we have been working with numerous Comprehensive Capital Analysis and Review (CCAR) banks to support their internal Pre-provision net revenue (PPNR) and loss provisioning models with historical data. Although many of the banks ask that we use five or more years of data, analysis indicates that three years of historical data is sufficient in calculating a historical simulation while preserving the right to expand the time horizon if necessary.

Notional Amount Methodology

The Proposal seeks to establish a methodology for calculating notional amount of the fund’s leverage under the exposure-based portfolio limit. In establishing the requirements for the notional exposure calculation, the Commission rightly distinguishes various types of derivatives transactions in terms of structure and payout timing. Specifically, with respect to transactions that fall within the Commission’s definition of a “complex derivative,” the Proposal articulates a carve-out for derivatives for which payout is non-linear, including standard put or call options. We believe that the notional exposure calculation methodology for complex derivatives transactions should be refined further to consider certain specific examples before finalizing the rule to avoid any unintended consequences.

By way of example, the Proposal specifies that for a standard put or call option “the market value of the underlying asset multiplied by its delta, serves as an appropriate measure of a fund’s exposure...because it generally would result in a notional amount that reflects the market value of an equivalent position in the underlying reference asset for the derivatives transaction”.3 Assume, however, that a fund writes a deep out-of-the-money put option on a portfolio position. This derivative would not meaningfully contribute to notional exposure limit since it has a very low delta. Now assume that the market moves sharply lower, such that the notional balance of the instrument is more significant relative to the fund’s derivatives positions. Under the proposed rule, if a position which was suitably positioned for by the fund drove the notional leverage amount

2 See Proposal at footnote 272.
3 See Proposal at Page 77.
above 150%, the fund would be prevented from adding new derivatives positions at the exact time that it might make the most sense for the fund to recalibrate its hedging strategy to protect the investors in the fund. We encourage the Commission to consider examples such as this as it configures the various provisions for calculating the exposure-based portfolio limit.

**Qualifying Coverage Assets and the Risk-Based Coverage Amount**

The Proposal also notes that in certain situations, qualifying coverage assets are limited to cash and cash equivalent instruments to ensure that they are “extremely liquid and may be less likely to experience volatility in price or decline in value in times of stress.” To provide consistency from a valuations perspective, as well as an investor perspective, we recommend that the SEC consider aligning its approach with that taken by other Federal regulators which, to address concerns similar to the SEC’s, specify what constitutes a “high-quality liquid asset” (i.e. HQLA). Among other criteria, the bank regulations specify a maximum allowable 30-calendar day price drop to be considered eligible as HQLA, tiers instruments into 3 levels (i.e. Level 1, 2A or 2B), and requires an instrument-by-instrument analysis to demonstrate the “liquid and readily marketable” standard. These rules allow for only high-quality and liquid instruments to be considered in the numerator of the Liquidity Coverage Ratio (“LCR), and has the benefit of already being under understood by investors and regulators as a reliable source of liquidity even during periods of stress.

We also believe the Commission could expand the universe of potentially eligible qualifying coverage assets for funds, thus reducing the operational burdens, while still responsibly ensuring only the most liquid instruments are eligible coverage assets. For existing regulations, IDC has created a service which identifies the magnitude and timing of every instrument’s most significant 30-calendar day price drop which can be an easy means for funds to comply with the LCR rules.

In addition, it would be helpful if the Commission provided examples that can be used to assist the industry in ensuring that both practitioners and regulators have the same understanding of the requirements. For example, in a situation where a fund has a swap with mark-to-market gains, although it is clear that "the mark-to-market coverage amount would be equal to zero," it is not as obvious whether those gains constitute a buffer that can be factored in to the risk-based coverage amount, or if the fund must assume the contract’s market value is zero.

With regards to financial commitment obligations, the qualifying coverage assets is allowed to include any liquid instrument that can easily be converted to cash in a term that is less than when the obligation is expected to come due, with certain limitations. We believe that the Commission should explicitly align this portion of the requirement with SEC Proposed Rule 22e-4 and that the number of days to liquidate the instrument for the purpose of the proposal, should it be approved, should suffice as the appropriate comparison to the tenor of the obligation.

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4 See Proposal at Page 154
5 The Office of the Comptroller of the Currency, Federal Reserve System and Federal Deposit Insurance Corporation have adopted rules which use an alternative approach to what is proposed by the SEC. See: https://www.federalregister.gov/articles/2014/10/10/2014-22520/liquidity-coverage-ratio-liquidity-risk-measurement-standards
6 See Proposal at footnote 333.
Stress Testing

With specific regards to stress testing, we believe that funds could benefit from further Commission guidance with respect to the magnitude of the expected stress. The proposal specifies that “the fund's adviser would use a stressed VaR model to estimate the potential loss the fund could incur, at a given confidence level, under stressed conditions.” Our communication with funds indicates that some funds would benefit from further guidance. This guidance would better align with some stress testing requirements under the Dodd-Frank Act which specifies the minimum set of factors to consider and supplies forecasts of these factors for a baseline, adverse and severely adverse scenario.

Effects on Pricing and Fair Valuation Determinations

The Proposal states “to the extent that a reduction in the use of derivatives adversely affects pricing efficiency or transparency, it may become more difficult for a fund (or its third-party pricing service) and its board of directors to determine fair values where necessary.” As a leading pricing provider, we appreciate that transparent price discovery has a positive impact on the quality of an evaluated price and leads to a valuations environment driven by observable market data. However, in the absence of transparent pricing data, IDC has developed methodologies that efficiently leverage observable market data and apply that data to areas of the market that are less observable. If the Commission is interested in hearing more about these methodologies, we are happy to be a resource as you finalize the Proposal.

Thank you again for the ability to comment, we appreciate the work the staff has completed in issuing the Proposal and we welcome the opportunity to discuss any of these issues further.

Sincerely,

Brendon J. Weiss
Co-Head, Government Affairs

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8 See Proposal at page 170.
9 See Proposal at page 287.