

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-83665; File No. SR-ICEEU-2018-009)

July 18, 2018

Self-Regulatory Organizations; ICE Clear Europe Limited; Notice of Filing of Proposed Rule Change Relating to amendments to the ICE Clear Europe CDS End-of-Day Price Discovery Policy (“Price Discovery Policy”)

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 11, 2018, ICE Clear Europe Limited (“ICE Clear Europe”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I, II and III below, which Items have been prepared by ICE Clear Europe. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change, Security-Based Swap Submission, or Advance Notice

ICE Clear Europe proposes to modify certain provisions of its Price Discovery Policy related to the bid-offer width (“BOW”) methodology for pricing single name credit default swap (“CDS”) contracts. These revisions do not require any changes to the ICE Clear Europe Clearing Rules or Procedures.<sup>3</sup>

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change, Security-Based Swap Submission or Advance Notice

In its filing with the Commission, ICE Clear Europe included statements concerning the purpose of and basis for the proposed rule change and discussed any

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> Capitalized terms used but not defined herein have the meanings specified in the ICE Clear Europe Clearing Rules.

comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. ICE Clear Europe has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change, Security-Based Swap Submission or Advance Notice

(a) Purpose

ICE Clear Europe proposes revising its Price Discovery Policy to enhance the methodology used to determine BOWs for single name CDS contracts and to make corresponding changes to related governance processes.

Each business day, ICE Clear Europe determines end-of-day ("EOD") levels for CDS Contracts through in accordance with the Price Discovery Policy, based on EOD submissions from its CDS Clearing Members. ICE Clear Europe uses these EOD levels for mark-to-market and risk management purposes. As part of this price discovery process, ICE Clear Europe determines BOWs for each CDS Contract. The BOW is intended to estimate the bid-offer width for the two-way market available for each clearing-eligible instrument at the specified determination time on each business day. The BOWs are then used in ICE Clear Europe's price discovery process as inputs in the determination of EOD levels, and other risk management matters.

The current methodology for determining BOWs for single-name CDS Contracts is based on a consensus BOW derived from observed intraday spread-quotes for the most actively traded instrument ("MATI") across the term structure and cleared coupons. The spread-based consensus BOW is multiplied by a "scrape factor" to reflect any differences

between the BOWs provided in intraday quotes and BOWs achieved in the market. ICE Clear Europe applies various factors to the consensus BOW to reflect differences in instrument liquidity at longer and shorter maturities, and at higher and lower coupons.

ICE Clear Europe is proposing to enhance the methodology for determining EOD BOWs for single name instruments. The enhancement eliminates the use of the ISDA CDS Standard Model from the computation of single name BOWs. ICE Clear Europe established its current BOW methodology at a time when it accepted submissions to its end-of-day price discovery process in both spread and price terms, at the discretion of its Clearing Members. Since that time, ICE Clear Europe has enhanced its end-of-day price discovery process to accept Single Name submissions only in price terms, eliminating the need for spread-based BOWs.<sup>4</sup> The proposed enhancement also determines BOWs consistently across single names on all reference entities, including those for which only sparse intraday data is available. The enhancement also extends the application of price-based BOW floors from the 0/3 month, 6 month and 1 year benchmark tenors to the entire set of benchmark tenors. Finally, the proposed enhancement introduces a dynamic feature that can widen BOWs in response to the observed dispersion of price-space mid-market levels submitted in the EOD price discovery process.

Under the proposed enhancement ICE Clear Europe will compute a consensus BOW for each benchmark instrument, not only for the most actively traded instrument. Rather than consensus BOWs being derived only from intraday quotes, they will be

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<sup>4</sup> ICE Clear Europe continues to use the ISDA CDS Standard Model for certain other purposes under the Price Discovery Policy in which it may convert between spread and price levels, and accordingly references to the model have been retained in the revised Price Discovery Policy notwithstanding that the model is no longer used for determining single-name BOWs.

computed as a price-based floor plus a fraction of the instrument's currently observed level, based on the average of price-space mid-market levels submitted by CDS Clearing Members as part of the EOD price discovery process. ICE Clear Europe will continue to apply various factors to the consensus BOW to reflect differences in liquidity at longer and shorter maturities and at higher and lower coupons. Under the proposed enhancement, the Clearing House will determine systematic BOWs for each benchmark instrument at the most actively traded coupon ("MATC") by applying tenor scaling factors to the corresponding consensus BOWs. These tenor scaling factors reflect the BOW of each tenor relative to the BOW of the most actively traded tenor. ICE Clear Europe will determine systematic BOWs for each benchmark instrument at other coupons by applying a combination of tenor scaling factors and coupon scaling factors to the corresponding consensus BOWs. Coupon scaling factors are an adjustment to the BOW to reflect decreased market activity at coupons larger or smaller than the MATC, and accordingly result in a wider BOW for such coupons as compared to the MATC. ICE Clear Europe will apply the appropriate Single Name variability factor resulting in the final systematic EOD BOWs based on the applicable variability band (a similar variability factor can be applied in the current approach, but on a discretionary basis). The variability factor is an additional scaling factor that widens the BOW to account for volatile or fast-moving market conditions, on the basis of a market proxy variability band that is designed to reflect observed variability levels in intraday quotes.<sup>5</sup>

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<sup>5</sup> For further discussion of the variability band approach, see Exchange Act Release No. 34-83389 (SR-ICEEU-2018-006) (June 6, 2018), 83 Fed. Reg. 27356 (June 12, 2018).

ICE Clear Europe will determine the final EOD BOW as the greater of an instrument's systematic BOW, and a dynamic BOW established for the instrument based on the dispersion of price-based mid-market EOD submissions by CDS Clearing Members for the given instrument. The amendments remove the requirement for ICE Clear Europe to provide the spread space equivalents for BOWs.

ICE Clear Europe also proposes revisions to the governance provisions of the Price Discovery Policy. Under the revisions, and consistent with the amendments to the methodology described above, the parameters used in the EOD price discovery process are established by ICE Clear Europe's clearing risk department in consultation with ICE Clear Europe's trading advisory committee, which provides additional insight into current market dynamics and conditions. The responsibilities of ICE Clear Europe's clearing risk department in this regard will include determining the price-based floors and scaling factors used to establish BOWs. (References to determination of scrape factors, which are no longer used, have been removed.)

The revised Price Discovery Policy removes a duplicative table relating to the assignment of index risk factors to market proxy groups, and updates cross-references accordingly. ICE Clear Europe also proposes a revision that trading desks at each self-clearing member are requested (but not required), to copy ICE Clear Europe on the intraday quotes they provide market participants via email.

(b) Statutory Basis

ICE Clear Europe believes that the proposed amendments are consistent with the requirements of Section 17A of the Act<sup>6</sup> and the regulations thereunder applicable to it.

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<sup>6</sup> 15 U.S.C. 78q-1.

Section 17A(b)(3)(F) of the Act<sup>7</sup> in particular requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions, the safeguarding of securities and funds in the custody or control of the clearing agency, and the protection of investors and the public interest. The proposed amendments are designed to enhance the Clearing House's Price Discovery Policy, which is necessary to determine the daily settlement prices for cleared CDS Contracts that are used in mark-to-market margin settlement and additionally are key inputs of the risk management and margin models of the Clearing House for CDS contracts. The proposed amendments in particular will update the methodology for determining BOWs, which are an important part of the determination of the EOD level. The amendments provide a more comprehensive and dynamic approach for determining BOWs for single-name CDS Contracts, that applies across all tenors of such contracts. The revised methodology takes into account both observed and submitted price levels and implements appropriate price floors and tenor, coupon and variability scaling factors that can adjust the BOW for particular instruments (including less actively traded instruments) to reflect liquidity and other market conditions. In ICE Clear Europe's view, the revised approach, together with the other aspects of the Price Discovery Policy, will facilitate more accurate determinations of EOD levels for the full range of cleared single-name instruments, and strengthen the overall EOD price discovery process. As a result, ICE Clear Europe believes that the amendments are consistent with requirements to promote prompt and accurate clearing and settlement, within the meaning of Section

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<sup>7</sup> 15 U.S.C. 78q-1(b)(3)(F).

17A(b)(3)(F).<sup>8</sup> For similar reasons, ICE Clear Europe believes that the amendments are also consistent with the risk-based margining requirements of Commission Rule 17Ad-22(e)(6),<sup>9</sup> including the requirement to use reliable sources of timely price data and

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<sup>8</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>9</sup> 17 C.F.R. 240.17Ad-22(e)(6). The rule states that “[e]ach covered clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonably designed to, as applicable:

(6) Cover, if the covered clearing agency provides central counterparty services, its credit exposures to its participants by establishing a risk-based margin system that, at a minimum:

(i) Considers, and produces margin levels commensurate with, the risks and particular attributes of each relevant product, portfolio, and market;

(ii) Marks participant positions to market and collects margin, including variation margin or equivalent charges if relevant, at least daily and includes the authority and operational capacity to make intraday margin calls in defined circumstances;

(iii) Calculates margin sufficient to cover its potential future exposure to participants in the interval between the last margin collection and the close out of positions following a participant default;

(iv) Uses reliable sources of timely price data and uses procedures and sound valuation models for addressing circumstances in which pricing data are not readily available or reliable;

(v) Uses an appropriate method for measuring credit exposure that accounts for relevant product risk factors and portfolio effects across products;

(vi) Is monitored by management on an ongoing basis and is regularly reviewed, tested, and verified by:

(A) Conducting backtests of its margin model at least once each day using standard predetermined parameters and assumptions;

(B) Conducting a sensitivity analysis of its margin model and a review of its parameters and assumptions for backtesting on at least a monthly basis, and considering modifications to ensure the backtesting practices are appropriate for determining the adequacy of the covered clearing agency's margin resources;

(C) Conducting a sensitivity analysis of its margin model and a review of its parameters and assumptions for backtesting more frequently than monthly during periods of time when the products cleared or markets served display high volatility or become less liquid, or when the size or concentration of positions held by the covered clearing agency's participants increases or decreases significantly; and

procedures and sound valuation models for addressing circumstances in which pricing data are not readily available or reliable. The enhancements discussed above will in particular take into account a broad range of observed and submitted price data and enhance the soundness of the overall methodology applied to calculating EOD pricing, through the use of tenor, coupon and variability factors to develop more accurate BOW levels for the full range of cleared instruments, including those that are less actively traded and for which direct pricing data may be less readily available. Finally, ICE Clear Europe believes that the amendments are consistent with the governance requirements of Commission Rule 17Ad-22(e)(2),<sup>10</sup> including ensuring that its written policies provide

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- (D) Reporting the results of its analyses under paragraphs (e)(6)(vi)(B) and (C) of this section to appropriate decision makers at the covered clearing agency, including but not limited to, its risk management committee or board of directors, and using these results to evaluate the adequacy of and adjust its margin methodology, model parameters, and any other relevant aspects of its credit risk management framework; and
  - (vii) Requires a model validation for the covered clearing agency's margin system and related models to be performed not less than annually, or more frequently as may be contemplated by the covered clearing agency's risk management framework established pursuant to paragraph (e)(3) of this section.”

<sup>10</sup> 17 C.F.R. 240.17Ad-22(e)(2). The rule states that “[e]ach covered clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonably designed to, as applicable:

- (2) Provide for governance arrangements that:
  - (i) Are clear and transparent;
  - (ii) Clearly prioritize the safety and efficiency of the covered clearing agency;
  - (iii) Support the public interest requirements in Section 17A of the Act ( 15 U.S.C. 78q-1) applicable to clearing agencies, and the objectives of owners and participants;
  - (iv) Establish that the board of directors and senior management have appropriate experience and skills to discharge their duties and responsibilities;
  - (v) Specify clear and direct lines of responsibility; and



for governance arrangements that specify clear and direct lines of responsibility. In this regard, the amendments update the specific responsibilities of the Clearing Risk department and the TAC in the determination of BOWs and the establishment of relevant parameters, including price-based floors and scaling factors.

(B) Clearing Agency's Statement on Burden on Competition

ICE Clear Europe does not believe the proposed rule changes would have any impact, or impose any burden, on competition not necessary or appropriate in furtherance of the purpose of the Act. The proposed changes to the Price Discovery Policy, and in particular the revised BOW methodology for Single Name instruments, will apply uniformly across all CDS Clearing Members and market participants. ICE Clear Europe does not believe the amendments will adversely affect competition among CDS Clearing Members, the cost of clearing, or the ability of market participants to clear CDS contracts generally. Similarly, the Clearing House does not believe the amendments will reduce access to clearing of CDS contracts or limit market participants' choices for clearing CDS contracts. Therefore, ICE Clear Europe does not believe the proposed rule changes impose any burden on competition that is inappropriate in furtherance of the purposes of the Act.

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments relating to the proposed amendments have not been solicited or received by ICE Clear Europe. ICE Clear Europe will notify the Commission of any comments received with respect to the proposed rule change.

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(vi) Consider the interests of participants' customers, securities issuers and holders, and other relevant stakeholders of the covered clearing agency.”

III. Date of Effectiveness of the Proposed Rule Change, Security-Based Swap Submission and Advance Notice and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the proposed rule change or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, security-based swap submission or advance notice is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-ICEEU-2018-009 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-ICEEU-2018-009. This file number should be included on the subject line if e-mail is used. To help the Commission

process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change, security-based swap submission or advance notice that are filed with the Commission, and all written communications relating to the proposed rule change, security-based swap submission or advance notice between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filings will also be available for inspection and copying at the principal office of ICE Clear Europe and on ICE Clear Europe's website at <https://www.theice.com/clear-europe/regulation>.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-ICEEU-2018-009 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>11</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>11</sup> 17 CFR 200.30-3(a)(12).