

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-94280; File No. SR-ICEEU-2022-004)

February 18, 2022

Self-Regulatory Organizations; ICE Clear Europe Limited; Notice of Filing of Proposed Rule Change Relating to Amendments to the ICE Clear Europe CDS Clearing Stress Testing Policy and CDS Clearing Back-Testing Policy

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on February 10, 2022, ICE Clear Europe Limited (“ICE Clear Europe” or the “Clearing House”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule changes described in Items I, II and III below, which Items have been prepared primarily 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

ICE Clear Europe proposes to modify certain provisions of its CDS Clearing Stress Testing Policy (“CDS Stress-Testing Policy”) and CDS Clearing Back-Testing Policy (“CDS Back-Testing Policy”) to make certain clarifications and updates.³

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Capitalized terms used but not defined herein have the meanings specified in the ICE Clear Europe Clearing Rules and the CDS Clearing Stress Testing Policy and the CDS Clearing Back-Testing Policy (as applicable).

II. Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

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 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

(a) Purpose

ICE Clear Europe is proposing to [sic] its CDS Back-Testing Policy and its CDS Stress-Testing Policy to describe more fully certain existing Clearing House practices, as discussed herein.

CDS Back-Testing Policy

The amendments to the CDS Back-Testing Policy would generally clarify the types of back-testing the Clearing House performs of its CDS risk models. The amendments would also make minor terminology updates to conform uses of defined terms, make typographical corrections throughout the document, and add and/or update section names and numbering to improve organization and readability.

The general discussion of the Clearing House's Back-testing approach would be amended to add a new paragraph which would specify that the Clearing House conducts several types of back-tests described in the CDS Back-Testing Policy and that the Clearing House adopts all the available reliable and validated data for each back-test in

order to assess the model performance over a long period in which stressed market conditions and idiosyncratic events are likely to have occurred.

A new section would be added (and numbering would be updated accordingly) to describe the use of overlapping and non-overlapping data in the back-testing of the CDS risk model performed by the Clearing House. The section would state explicitly that using non-overlapping back-testing for static portfolios is the preferred approach because the CDS risk model is designed to cover a multi-days risk horizon, but that the lack of sufficiently long data sets may limit the use of the approach. Overlapping back-testing is used in order for the Clearing House to have a statistically significant sample, but the count of exceedances is artificially duplicated. The amendments also would discuss the ways the Clearing House addresses the problem of time dependent observations.

The discussion of the implementation of the Basel Traffic Light System (BTLS) would be updated to state explicitly that one of the main assumptions of BTLS is that excessive losses are time independent. The amendments would describe how, because multi-horizon overlapping back-testing is time dependent, the problem would be addressed by correcting the number of consecutive exceedances within the risk time horizon.

The discussion of Multi-horizon back testing (renamed Multi-days horizon back-testing) would clarify that the observed loss is calculated as the minimum NAV change over 5 days for house accounts. Further clarificatory updates that would be made include specifying that shortfall is also known as “back-test exceedances” and that unrealized loss is also known as “worst N-days P&L”. These updates would be made throughout the CDS Back-Testing Policy in order to be more descriptive and improve readability. The

amendments would further reflect that the Clearing House's use of the worst N-days P&L may lead to multiple consecutive back-test exceedances following one large market move in the overlapping back-testing approach.

The discussion of detailed daily back-testing results would be updated to include further explanations of the information presented in Table 2 (Example of the minimum 5-day P/L detail for daily back-testing). Specifically, the amendments would provide that the last two examples in Table 2 shows the worst N-days P/L could be the 4-days P/L or 3-days P/L.

The section relating to back-testing the production model with Clearing Members accounts would be amended to clarify that a minimum of one year of observations is required to define the statistical significance of back-testing results.

Provisions relating to back-testing the production model with Special Strategy portfolios would be updated to describe that the set of portfolios tested include strategies like Index arbitrage portfolios with long Index and short Single Names constituent of the current Index. The strategies would refer to the main Indices where the Clearing House clears part of the underlying Single Names. Additionally, the amendments would provide that back-test results at the 99.5% quantile would be reviewed on at least a monthly basis, and that back-test results at the 99.75% quantile would be reviewed on an ad-hoc basis, when there is a large market move. A table showing portfolio reconstruction for special strategy back-testing would be removed as unnecessary detail now covered in the more general description of the special strategies.

A new section addressing stylized portfolios back-testing would be added and would provide that the Clearing Risk Department would perform back-testing on a series

of stylized portfolios when a new risk factor is introduced for clearing. Such stylized portfolios aim at replicating certain trading strategies in order to make sure that the risk related to the newly introduced risk factors can be managed through the current CDS risk model. Stylized portfolios back-testing may be carried out more frequently on the risk factors that [sic] the largest open interest at the Clearing House in order to provide further assurance regarding the CDS risk model performance. The changes reflect current back-testing practice, and are intended to more clearly document such practices in the Back-Testing Policy.

The provisions relating to univariate back-testing would be updated to provide that back-testing results at 99.5% quantile would be reviewed on at least a monthly basis by the Clearing Risk Department and reported to the Model Oversight Committee on a monthly basis, which reflects current practice. Back-testing results at 99.75% quantile would be reviewed on ad-hoc basis, when stress market conditions might cause breaches at 99.5% quantile.

CDS Stress-Testing Policy

In the CDS Stress-Testing Policy, the description of the use of Hypothetical Scenarios would be updated to clarify that forward looking credit event scenarios are based on both historically observed and hypothetical extreme but plausible market scenarios. This update is intended to more clearly reflect current stress testing practice.

(b) Statutory Basis

ICE Clear Europe believes that the amendments to the CDS Back-Testing Policy and the CDS Stress-Testing Policy are consistent with the requirements of Section 17A of

the Act⁴ and the regulations thereunder applicable to it. In particular, Section 17A(b)(3)(F) of the Act⁵ 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 or for which it is responsible, and the protection of investors and the public interest.

The amendments to the CDS Back-Testing Policy are generally designed to enhance and clarify the descriptions of back-testing performed on ICE Clear Europe CDS risk models. Although these changes are largely not intended to represent a change in current Clearing House practices, they are intended to more clearly reflect those practices and thereby enhance the ongoing implementation and monitoring of back-testing. In particular, the amendments clarify the use of overlapping and non-overlapping data sets, the back-testing of stylized portfolios when new risk factors are rolled out, assumptions around time independence of exceedances, and the review process for the 99.75% quantile back tests (including the frequency of review and the Clearing House committees responsible for review). The amendment to the CDS Stress-Testing Policy would clarify the use of hypothetical scenarios in constructing forward looking credit event scenarios in stress testing of the CDS risk model. Therefore, the amendments will help ICE Clear Europe ensure that its risk model will effectively measure credit

⁴ 15 U.S.C. 78q-1.

⁵ 15 U.S.C. 78q-1(b)(3)(F).

exposures and default risks, and thus that the Clearing House adequately maintains adequate financial resources to support its CDS operations. The amendments will therefore enhance the stability of the Clearing House and overall promote the prompt and accurate clearance and settlement of securities transactions and, derivative agreements, contracts, and transactions, and the public interest in the sound operation of clearing agencies. Accordingly, the amendments are consistent with the requirements of Section 17A(b)(3)(F).⁶ (ICE Clear Europe does not believe the amendments will affect the safeguarding of securities and funds in ICE Clear Europe’s custody or control or for which it is responsible.)

For similar reasons, the proposed amendments are also consistent with relevant requirements of Rule 17Ad-22. ICE Clear Europe believes that the proposed amendments are consistent with the relevant requirements of Rule 17Ad-22(e)(4)(vi)(A),⁷ which provides that “[e]ach covered clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonable designed to, as applicable [...] effectively identify, measure, monitor and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by [...] testing the sufficiency of its total financial resources available to meet the minimum financial resource requirements [...] by conducting stress testing of its total financial resources once each day using standard predetermined parameters and assumptions”, among other requirements. The amendments to the CDS Stress-Testing Policy clarify

⁶ 15 U.S.C. 78q-1(b)(3)(F).

⁷ 17 CFR § 240.17Ad-22.

that construction of certain forward looking stress scenarios is based on hypothetical as well as historical scenarios. As amended, the CDS Stress-Testing Policy will facilitate the ongoing stress-testing of financial resources and effective management of credit exposures to CDS Clearing Members. As such, the amendments are consistent with the requirements of Rule 17Ad-22(e)(4)(vi)-(B) [sic].⁸

Rule 17Ad-22(e)(6)(vi)⁹ provides that “[e]ach covered clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonable designed to, as applicable [...] 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 [...] is monitored [sic] 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 [its] 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 (D) reporting the

⁸ 17 CFR § 240.17Ad-22(e)(4)(vi)(A).

⁹ 17 CFR § 240.17Ad-22(e)(6)(vi).

results of its analyses ... to appropriate decision makers....”. The amendments to the CDS Back-Testing Policy will, as discussed above, enhance the framework for ICE Clear Europe to conduct back-testing of CDS risk models by more clearly addressing the use of overlapping and non-overlapping back-testing data sets, the back-testing of stylized portfolios when new risk factors are implemented, and assumptions around time independence of excessive losses, among other changes. The amendments also clarify the procedures for review of back-testing at certain quantiles (on a monthly or ad hoc basis, as appropriate). As such, ICE Clear Europe believes the amendments are consistent with the requirements of Rule 17Ad-22(e)(6)(vi).¹⁰

Rules 17Ad-22(e)(2)(i) and (v)¹¹ provides that “[e]ach covered clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonable designed to, as applicable [...] provide for governance arrangements that are clear and transparent [and] specify clear and direct lines of responsibility”. As described herein, references to the roles of certain committees and departments with respect to reviews and approvals throughout the CDS Back-Testing Policy have been updated to reflect existing practice with respect to the roles of groups. As such, the amendments provide additional clarity with respect to Clearing House governance and lines of responsibility consistent with Rules 17Ad-22(e)(2)(i) and (v).¹²

¹⁰ 17 CFR § 240.17Ad-22(e)(6)(vi).

¹¹ 17 CFR 240.17 Ad-22(e)(2)(i) and (v).

¹² 17 CFR 240.17 Ad-22(e)(2)(i) and (v).

(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. In general, the amendments are intended to provide clarifications and additional details where necessary in order to reflect existing practices for CDS stress-testing and back-testing and are not intended to impose new requirements on Clearing Members. The terms of cleared CDS contracts and of clearing are not otherwise changing. As such, the amendments will apply to all CDS Clearing Members and are unlikely, in ICE Clear Europe's view, to materially affect the cost of clearing for CDS products or affect access to clearing for CDS products at ICE Clear Europe or the market for cleared services generally. To the extent the changes could lead to changes in margin rates, based on the results of stress-testing and/or back-testing, ICE Clear Europe believes any such changes would be designed to appropriately reflect its credit risk from CDS Clearing Members with respect to cleared positions. 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 written comments received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change 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 such 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 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. Please include File Number SR-ICEEU-2022-004 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-2022-004. 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 that are filed with the Commission, and all written communications relating to the proposed rule change 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 am and 3:00 pm. 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-2022-004 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.¹³

J. Matthew DeLesDernier
Assistant Secretary

¹³ 17 CFR 200.30-3(a)(12).