

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-72544; File No. SR-ICEEU-2014-10)

July 3, 2014

Self-Regulatory Organizations; ICE Clear Europe Limited; Notice of Filing of Proposed Rule Change to CDS Policies Relating to EMIR

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 June 30, 2014, 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 primarily by ICE Clear Europe. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The principal purpose of the proposed change is to amend certain of the ICE Clear Europe credit default swaps (CDS) risk policies (“Risk Policy Amendments”) in order to facilitate compliance with requirements under the European Market Infrastructure Regulation (including regulations thereunder, “EMIR”)³ that will apply to ICE Clear Europe as an authorized central counterparty.

II. Self-Regulatory Organization’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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories.

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 these statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

ICE Clear Europe submitted proposed amendments to its risk policies relating to the CDS business to facilitate compliance with requirements under EMIR, which will apply to ICE Clear Europe as an authorized central counterparty. ICE Clear Europe will be required to be in compliance with EMIR as of the time it receives authorization from the European Securities and Markets Authority. The relevant policies being modified are (i) the CDS Risk Policy (“Risk Policy”); (ii) the Risk Model Description (“Model Description”); (iii) the CDS Clearing Back-Testing Framework (“Back-Testing Framework”); (iv) the CDS Clearing Stress-Testing Framework (“Stress-Testing Framework”); and (v) the CDS Default Management Framework (“Default Management Framework”).

The changes to the Risk Policy amend the calculation of CDS initial margin requirements to comply with margin requirements under EMIR Article 41 and Article 24 of the implementing Regulatory Technical Standards.⁴ As revised, the initial margin methodology is designed to provide portfolio risk coverage against at least 5-day market realizations that would occur with probability 99.5% (previously 99.0%). In other words, the estimated requirements provide risk protection equivalent to, at least, a 5-day 99.5% Value-at-Risk measure. In addition, in order to address requirements under EMIR related to procyclicality (Article 28 of the Regulatory

⁴ Commission Delegated Regulation (EU) No. 153/2013 of 19 December 2012 Supplementing Regulation (EU) No. 648/2012 of the European Parliament and of the Council with regard to Regulatory Technical Standards on Requirements for Central Counterparties (the “Regulatory Technical Standards”).

Technical Standards) changes were made to the maximum scale used for the initial margin approach by adding a volatility scale that assigns a 25% weight to stressed period observations during the lookback period from April 2007 to the present (consistent with Article 28(b) of the Regulatory Technical Standards). The revised initial margin requirement, including certain portfolio benefit assumptions, is expected to result in more conservative initial margin requirements than under the previous approach.

Similar amendments to those described above were also made to the Model Description. Under the revised Model Description, the overall initial margin methodology, post portfolio benefits and other risk components (e.g. jump-to-default and wrong way risk), are intended to provide portfolio risk coverage against at least 5-day market realizations that would occur with probability 99.5% or higher. Conforming changes with respect to the 99.5% confidence interval were also made in the Model Description. The revised Model Description also reflects the use of stressed observations described above to limit procyclicality. The Model Description has also been revised to include the clearing house's Monte Carlo Approach for Risk Management ("MC"), which has previously been applied to Western European sovereign CDS and is proposed to be extended to all CDS.

The CDS MC approach aims to model the spread risk component of initial margin by combining individual risk factors ("RFs"), i.e., single name or index family of instruments, into a copula. Marginal distributions for individual RFs are joined together under a Student-t copula. In this way, the model preserves historical behavior of RFS and their dependencies. The value-at-risk (VaR) for the profit and loss distribution can be estimated by sampling from this copula.

The MC method offers a number of advantages over the existing scenario-based spread response method (the "Decomp SR"). The dependence structure of RFs is encoded into the

copula, as opposed to the long-short offsets algorithm used to determine portfolio benefits under the Decomp SR. The copula can also capture tail dependence, such that various extreme scenarios can be easily simulated.

The scenario-based approach of the spread risk component with its portfolio benefit assumptions is generally expected to result in a more conservative requirement when compared to the MC VaR approach for the same coverage level. In order to ensure compliance with the 99.5 confidence interval requirement for OTC derivatives under EMIR, the final spread response charge will be determined as the more conservative of the Decomp SR and the MC VaR calculated at a 99.5% confidence interval.

The CDS pricing model, used by ICE Clear Europe since the inception of clearing, has also been attached to the Risk Model Description as an annex for completeness.

With respect to the Back-Testing Framework, changes were made to implement the 99.5% confidence interval. The historical volatility calculation uses data from at the minimum the most recent year (or, if shorter, the period in which the relevant contract has been cleared). In addition, per the amendments, on at least a monthly basis, the CDS Risk Department will report the CDS back testing results and analysis to the CDS Risk Committee in order to seek their review and, if needed, their recommendations of the CDS margin model. In addition, CDS back testing results and analyses are made available to all CDS Clearing Members and clients (where known to ICE Clear Europe) for their own portfolios. Disclosed information is aggregated in a form that does not breach confidentiality. The policy also provides a framework for monitoring and remediating breaches that arise during back-testing, based on the so-called “Basel Traffic Light System”, depending on the number and magnitude of the exceedances. The

Back-Testing Framework is reviewed and approved by the CDS Risk Committee and ICE Clear Europe Board at least annually.

The Stress-Testing Framework is amended to provide further detail as to its use of daily stress testing, which allows ICE Clear Europe to discover any potential weaknesses in the risk methodologies as well as to exercise short-term measures if the tests reveal that any counterparties are inadequately collateralized. A detailed analysis of the stress testing and sensitivity testing results is performed by the CDS Risk Department at least on a monthly basis, or more frequently in stressed market conditions, to ensure the adequacy of the existing stress test scenarios and framework. The Stress-Testing Framework amendments would also add pure historical scenarios, as required under EMIR. Pure historical scenarios are applied at the single name level, using the same date across all instruments. Single-name specific stress scenarios are based on the same 5-day period when the on-the-run indices had the greatest observed related spread increases or decreases. The guaranty fund stress scenario has also been clarified, and is designed to account for: (i) the occurrence of credit events for two clearing members and three reference entities on which the defaulted clearing members sold protection, (ii) adverse contracting or widening credit spread scenarios, (iii) adverse widening of Index-single name “basis”, and (iv) adverse changes of the default-free discount terms structure. CDS stress testing results and analyses are made available to all CDS Clearing Members and clients (where known to ICE Clear Europe) for their own portfolios. Disclosed information is aggregated in a form that does not breach confidentiality. The CDS Stress Testing framework is reviewed and approved by the CDS Risk Committee and ICE Clear Europe Board at least annually.

Minor improvements have been made to the Default Management Framework. First, ICE Clear Europe will conduct a quarterly (rather than annual) review of its Default Management

Framework. Also, ICE Clear Europe will perform a mock clearing member default test at least annually.

ICE Clear Europe believes that the proposed rule change is consistent with the requirements of Section 17A of the Act⁵ and the regulations thereunder applicable to it, including the standards under Rule 17Ad-22.⁶ Section 17A(b)(3)(F) of the Act⁷ 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 proposed rule change, which is intended to ensure compliance by the clearing house with the margin and risk management requirements of EMIR, principally enhance relevant risk policies and impose more conservative initial margin requirements. As a result, ICE Clear Europe believes that the proposed rule change will contribute to the safeguarding of funds and securities associated with derivative transactions that are in the custody or control of the clearing house, as well as more generally facilitate the prompt and accurate settlement of such transactions, within the meaning of Section 17(A)(b)(3)(F).⁸ ICE Clear Europe further believes that the proposed rule change will enhance the stability of the clearing system, by reducing the risk to market participants of a default by a clearing member or other customer. In addition, the proposed change to the Risk Policy Amendments is consistent with the relevant requirements of Rule 17Ad-22.⁹ In particular, the amendments to the Risk

⁵ 15 U.S.C. 78q-1.

⁶ 17 CFR 240.17Ad-22.

⁷ 15 U.S.C. 78q-1(b)(3)(F).

⁸ 15 U.S.C. 78q-1(b)(3)(F).

⁹ 17 CFR 240.17Ad-22.

Policy and Model Description will enhance the financial resources available to the clearing house by imposing more conservative initial margin requirements for CDS, as required by EMIR and consistent with the requirements of Rule 17Ad-22(b)(2-3).¹⁰ The changes in the Default Management Policy are intended to improve on default management procedures and therefore are consistent with Rule 17Ad-22(d)(11).¹¹

For the reasons noted above, ICE Clear Europe believes that the proposed Risk Policy Amendments are consistent with the requirements of Section 17A of the Act and regulations thereunder applicable to it.

B. Self-Regulatory Organization's Statement on Burden on Competition

ICE Clear Europe does not believe the Risk Policy Amendments would have any impact, or impose any burden, on competition not necessary or appropriate in furtherance of the purposes of the Act. Although the Risk Policy Amendments may increase the costs of clearing CDS for clearing members and their customers, as a result of more conservative initial margin requirements, this change is required in order to comply with Article 41 of EMIR and implementing regulations. In addition, ICE Clear Europe believes that the revisions to the model strengthen its risk management capability and financial resources, and are therefore appropriate in furtherance of the purposes of the Act. Because these changes will apply to all clearing members that clear CDS, ICE Clear Europe does not believe the amendments will adversely affect competition among clearing members. Furthermore, since the EMIR requirements will apply to European clearing houses generally, ICE Clear Europe does not anticipate that the

¹⁰ 17 CFR 240.17Ad-22(b)(2-3).

¹¹ 17 CFR 240.17Ad-22(d)(11).

changes will adversely affect the ability of market participants to clear CDS transactions generally, reduce access to clearing generally, or limit market participants' choices for clearing derivatives. As a result, ICE Clear Europe believes that any impact on competition is appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments relating to the proposed change to the rules have not been solicited or received. ICE Clear Europe will notify the Commission of any written comments received by ICE Clear Europe.

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 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 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-2014-10 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1060.

All submissions should refer to File Number SR-ICEEU-2014-10. 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 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/notices/Notices.shtml?regulatoryFilings>.

All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-ICEEU-2014-10 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.¹²

Jill M. Peterson
Assistant Secretary

¹² 17 CFR 200.30-3(a)(12).