

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-89491; File No. SR-ICC-2020-010)

August 6, 2020

Self-Regulatory Organizations; ICE Clear Credit LLC; Notice of Filing of Proposed Rule Change Relating to the ICC Risk Management Model Description

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934,¹ and Rule 19b-4,² notice is hereby given that on July 29, 2020, ICE Clear Credit LLC (“ICC”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared primarily by ICC. 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

The principal purpose of the proposed rule change is to make changes to ICC’s Risk Management Model Description. These revisions do not require any changes to the ICC Clearing Rules (the “Rules”).³

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

In its filing with the Commission, ICC 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

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 Rules.

the places specified in Item IV below. ICC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.

(A) Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

ICC proposes to revise its Risk Management Model Description in connection with its proposed launch of the clearing of credit default index swaptions (“Index Swaptions”).⁴ ICC has previously filed with the Commission changes to certain other policies and procedures related to the clearing of Index Swaptions (the “Swaption Rule Filings”).⁵ As set out in the Swaption Rule Filings, ICC intends to adopt or amend certain related policies and procedures in preparation for the launch of clearing of Index Swaptions and does not intend to commence clearing of Index Swaptions until all such policies and procedures have been approved by the Commission or otherwise become effective. Accordingly, ICC proposes to make such changes to the Risk Management Model Description effective following the approval of all such policies and procedures and the completion of the ICC governance process surrounding the Index Swaptions product expansion.

As discussed in the Swaption Rule Filings, pursuant to an Index Swaption, one party (the “Swaption Buyer”) has the right (but not the obligation) to cause the other

⁴ Index Swaptions are also referred to herein and in the Risk Management Model Description as “index options” or “index CDS options”, or in similar terms.

⁵ SEC Release No. 34-87297 (Oct. 15, 2019) (approval), 84 Fed. Reg. 56270 (Oct. 21, 2019) (SR-ICC-2019-007); SEC Release No. 34-89142 (June 24, 2020) (approval), 85 Fed. Reg. 39226 (June 30, 2020) (SR-ICC-2020-002); SEC Release No. 34-89072 (June 16, 2020) (notice), 85 Fed. Reg. 37483 (June 22, 2020) (SR-ICC-2020-008).

party (the “Swaption Seller”) to enter into an index credit default swap transaction at a pre-determined strike price on a specified expiration date on specified terms. In the case of Index Swaptions that would be cleared by ICC, the underlying index credit default swap would be limited to certain CDX and iTraxx Europe index credit default swaps that are accepted for clearing by ICC, and which would be automatically cleared by ICC upon exercise of the Index Swaption by the Swaption Buyer in accordance with its terms.

The proposed changes amend the Risk Management Model Description to incorporate a stochastic implied mean absolute deviation (“MAD”) feature in connection with the proposed launch of the clearing of Index Swaptions and make certain other minor clarification changes. The proposed amendments would modify Section VII of the Risk Management Model Description to add a subsection on stochastic implied MAD modeling. In the Swaption Rule Filings, ICC proposed to modify the integrated spread response component of the margin model to incorporate an options-implied credit spread distribution, which includes a scale parameter related to the MAD implied from swaption prices (“implied MAD”).⁶ ICC proposes enhancements to its approach to feature a stochastic implied MAD, which presents a more advanced risk modeling technique for option instruments in rapidly changing market conditions and high-volatility market environments. Currently, the model assumes a static implied MAD formulation where the implied MAD scale does not change in response to the simulated underlying index levels.

Under the proposed changes, the risk methodology for clearing Index Swaptions would consider the risk arising from the joint fluctuations of the underlying index levels

⁶ SEC Release No. 34-89142 (June 24, 2020) (approval), 85 Fed. Reg. 39226 (June 30, 2020) (SR-ICC-2020-002).

and the options implied MAD scales in proposed Subsection VII.3. ICC would identify and describe the distribution that the changes of the implied MAD scales associated with each option expiry follow. ICC would also discuss and provide the rationale for its selected parameter estimation approach. Specifically, ICC would set out how the distribution parameters are estimated for a set of implied MAD changes. The proposed changes further explain how ICC models the joint fluctuations of the underlying index levels and the options implied MAD scales. Proposed Figure 12 illustrates the simulation approach and is thus intended to replace Figure 11 in Subsection VII.2.2 that ICC proposes to remove. Relatedly, in Subsection VII.5.1.1 with respect to instrument profit/loss (“P/L”) estimations for Index Swaptions, ICC proposes to add reference to notations related to the stochastic implied MAD from proposed Subsection VII.3.

ICC also proposes other minor clarification changes to the Risk Management Model Description. ICC propose to reference the clearinghouse in Subsection III.6 when describing where certain data is obtained and to abbreviate a term in Subsection VI.2. Given the addition of Subsection VII.3, ICC proposes to renumber the subsections in Section VII accordingly. ICC further proposes clarifications to a formula and its notes in Subsection VII.5.1.2 regarding risk factor P/L estimations, including with respect to the description of an alternative option position P/L computation, subsequent risk estimations and the addition of certain payments to portfolio requirements.

(b) Statutory Basis

ICC believes that the proposed rule change is consistent with the requirements of Section 17A of the Act⁷ and the regulations thereunder applicable to it, including the

⁷ 15 U.S.C. 78q-1.

applicable standards under Rule 17Ad-22.⁸ In particular, Section 17A(b)(3)(F) of the Act⁹ requires that the rule change be consistent with the prompt and accurate clearance and settlement of securities transactions and derivative agreements, contracts and transactions cleared by ICC, the safeguarding of securities and funds in the custody or control of ICC or for which it is responsible, and the protection of investors and the public interest. The proposed rule change would enable a stochastic implied MAD feature in the Risk Management Model Description in connection with the proposed launch of the clearing of Index Swaptions. In contrast to the static implied MAD formulation where the implied MAD scale does not change in response to the simulated underlying index levels, the stochastic implied MAD approach considers the joint fluctuations of the underlying index levels and the options implied MAD scales in proposed Subsection VII.3. Such feature presents a more advanced risk modeling technique for option instruments in rapidly changing market conditions and high-volatility market environments. The proposed clarification changes would further ensure readability and transparency with respect to ICC's risk methodology and practices in the Risk Management Model Description to ensure that it remains up-to-date, clear, and transparent to support the effectiveness of ICC's risk management system. ICC's view, these changes will enhance its risk model and thus enhance its ability to manage the participant default risk, including with respect to Index Swaptions. The proposed rule change is therefore consistent with the prompt and accurate clearing and settlement of the contracts cleared by ICC, including Index

⁸ 17 CFR 240.17Ad-22.

⁹ 15 U.S.C. 78q-1(b)(3)(F).

Swaptions, the safeguarding of securities and funds in the custody or control of ICC or for which it is responsible, and the protection of investors and the public interest, within the meaning of Section 17A(b)(3)(F) of the Act.¹⁰

The amendments would also satisfy relevant requirements of Rule 17Ad-22.¹¹ Rule 17Ad-22(e)(2)(i), (iii), and (v)¹² requires each covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide for governance arrangements that are clear and transparent; support the public interest requirements of Section 17A of the Act¹³ applicable to clearing agencies, and the objectives of owners and participants; and specify clear and direct lines of responsibility. ICC's Risk Management Model Description clearly assigns and documents responsibility and accountability for risk decisions and requires consultation or approval from relevant parties. ICC determined to incorporate a stochastic implied MAD feature in the Risk Management Model Description in accordance with its governance process, which included review and/or approval by the ICC Risk Committee and Board of the determination to enable the stochastic implied MAD feature of the model and the corresponding changes to the Risk Management Model Description. In ICC's view, the proposed rule change continues to ensure that ICC maintains policies and procedures that are reasonably designed to provide for clear and transparent governance arrangements

¹⁰ Id.

¹¹ 17 CFR 240.17Ad-22.

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

¹³ 15 U.S.C. 78q-1.

that support the public interest requirements of Section 17A of the Act¹⁴ applicable to clearing agencies, and the objectives of owners and participants, and specify clear and direct lines of responsibility, consistent with Rule 17Ad-22(e)(2)(i), (iii), and (v).¹⁵

Rule 17Ad-22(e)(4)(ii)¹⁶ requires each covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by maintaining additional financial resources at the minimum to enable it to cover a wide range of foreseeable stress scenarios that include, but are not limited to, the default of the two participant families that would potentially cause the largest aggregate credit exposure for the covered clearing agency in extreme but plausible market conditions. As discussed above, ICC proposes to modify the Risk Management Model Description to add a subsection on stochastic implied MAD modeling. Under the proposed changes, the risk methodology for clearing Index Swaptions would consider the risk arising from the joint fluctuations of the underlying index levels and the options implied MAD scales. ICC believes that the proposed changes support and enhance its ability to manage its financial resources as such feature presents a more advanced risk modeling technique for option instruments in rapidly changing market conditions and high-volatility market environments. Additionally, the proposed clarification changes provide further clarity and

¹⁴ Id.

¹⁵ 17 CFR 240.17Ad-22(e)(2)(i), (iii), and (v).

¹⁶ 17 CFR 240.17Ad-22(e)(4)(ii).

transparency regarding ICC's risk management practices to strengthen the documentation surrounding ICC's risk methodology, including the incorporation of a reference to the clearinghouse in Subsection III.6 when describing where certain data is obtained and the clarifications to a formula and its notes in Subsection VII.5.1.2. As such, the proposed amendments would strengthen ICC's ability to maintain its financial resources and withstand the pressures of defaults, consistent with the requirements of Rule 17Ad-22(e)(4)(ii).¹⁷

Rule 17Ad-22(e)(6)(i)¹⁸ requires each covered clearing agency to establish, implement, maintain, and enforce written policies and procedures reasonably designed to cover its credit exposures to its participants by establishing a risk-based margin system that, at a minimum, considers, and produces margin levels commensurate with, the risks and particular attributes of each relevant product, portfolio, and market. ICC proposes to modify the Initial Margin Methodology section of the Risk Management Model Description to enable a stochastic implied MAD feature of the model in connection with the clearing of Index Swaptions. As described above, this feature considers the relationship between the underlying index levels and the implied MAD scales and presents a more advanced risk modeling technique for option instruments in rapidly changing market conditions and high-volatility market environments. ICC believes that such feature enhances its margin methodology, which considers and produces margin

¹⁷ Id.

¹⁸ 17 CFR 240.17Ad-22(e)(6)(i).

levels commensurate with the risks and particular attributes of each relevant product, portfolio, and market, consistent with the requirements of Rule 17Ad-22(e)(6)(i).¹⁹

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

ICC does not believe the proposed rule change would have any impact, or impose any burden, on competition not necessary or appropriate in furtherance of the purpose of the Act. The proposed rule change would amend the Risk Management Model Description to add a subsection on stochastic implied MAD modeling in connection with the proposed launch of the clearing of Index Swaptions and make certain other minor clarification changes. The proposed rule change will apply uniformly across all market participants. ICC does not believe acceptance of Index Swaptions for clearing would adversely affect the trading markets for such contracts, and in fact acceptance of such contracts by ICC would provide market participants with the additional flexibility to have their Index Swaptions cleared. Acceptance of Index Swaptions for clearing will not, in ICC's view, adversely affect clearing of any other currently cleared product. ICC does not believe the amendments would adversely affect the ability of Participants, their customers or other market participants to continue to clear contracts, including CDS Contracts. ICC also does not believe the enhancements would adversely affect the cost of clearing or otherwise limit market participants' choices for selecting clearing services in Index Swaptions, credit default swaps or other products. Accordingly, ICC does not believe the amendments would impose any burden on competition not necessary or appropriate in furtherance of the purpose of the Act.

¹⁹ Id.

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

Written comments relating to the proposed rule change have not been solicited or received. ICC will notify the Commission of any written comments received by ICC.

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-ICC-2020-010 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-ICC-2020-010. 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 Credit and on ICE Clear Credit's website at <https://www.theice.com/clear-credit/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-ICC-2020-010 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.²⁰

J. Matthew DeLesDernier
Assistant Secretary

²⁰ 17 CFR 200.30-3(a)(12).