

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-81186; File No. SR-ICC-2017-006)

July 21, 2017

Self-Regulatory Organizations; ICE Clear Credit LLC; Order Approving Proposed Rule Change Relating to ICC's End-of-Day Price Discovery Policies and Procedures

I. Introduction

On May 25, 2017, ICE Clear Credit LLC ("ICC" or "ICE Clear Credit") filed with the Securities and Exchange Commission ("Commission"), 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> a proposed rule change (SR-ICC-2017-006) to amend ICC's End-of-Day Price Discovery Policies and Procedures ("Pricing Policy") to implement an automated bid-offer width scaling methodology as part of its end-of-day pricing process. The proposed rule change was published for comment in the Federal Register on June 15, 2017.<sup>3</sup> The Commission did not receive comments regarding the proposed changes. For the reasons discussed below, the Commission is approving the proposed rule change.

II. Description of the Proposed Rule Change

Bid-offer width ("BOW") is one input in ICC's end-of-day price discovery process used to determine end-of-day price levels for ICC's cleared products. ICC derives the BOW used in its end-of-day price discovery process for each clearing-eligible instrument from BOW information supplied by its Clearing Participants. Currently, ICC determines the end-of-day BOW for index products by comparing BOW data received

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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> Securities Exchange Act Release No. 34-80895 (June 9, 2017), 82 FR 27539 (June 15, 2017) (SR-ICC-2017-006) ("Notice").

from Clearing Participants to three pre-defined BOWs. The three pre-defined BOWs are progressively larger, such that the smallest BOW (“Regime 1”) is associated with normal market conditions; the next largest BOW (“Regime 2”) is associated with market conditions experiencing some measure of volatility; and the largest BOW (“Regime 3”) is associated with more extreme market conditions. ICC selects as the end-of-day BOW (“EOD BOW”) for an index product the pre-defined BOW that is most representative of the BOWs obtained from Clearing Participants based on ICC’s methodology. For single-name instruments, ICC determines the EOD BOW by using intraday BOW data received from Clearing Participants and then applies various scaling factors to arrive at an EOD BOW based on ICC’s methodology. The EOD BOWs are used for mark-to-market and risk management purposes.

As currently constituted, ICC’s procedures allow its Risk Department to override the EOD BOW based on the Risk Department’s review and monitoring of market conditions. ICC represents that during periods of high market volatility, a significant number of BOW adjustments may need to be made, and that, if needed, such adjustments are determined and input manually.<sup>4</sup> ICC believes that this manual intervention, which takes place in a short time period, is a potential source of operational risk.<sup>5</sup>

In order to reduce this operational risk, ICC proposes to replace the manual BOW adjustment process in the Pricing Policy with an algorithm that will automatically execute the widening of selected BOWs based on the dispersion of intraday mid-level quotes, an indicator of the day’s volatility.

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<sup>4</sup> Notice, 82 FR at 27540.

<sup>5</sup> Id.

To effectuate this automatic BOW-widening process, ICC proposed to introduce a new metric, a “Variability Level,” designed to measure the movement of intraday bid-offer mid-levels relative to the existing pre-defined BOWs described above. Under the proposed changes, where the intraday BOW mid-level falls above or below the prior day’s end-of-day level by more than one pre-defined BOW, the Variability Level will be determined by a formula that takes the maximum deviation of the time series of intraday BOW mid-levels from the prior day’s end-of-day level and divides it by the pre-defined BOW. Where the intraday BOW mid-level falls within one pre-defined BOW of the prior day’s end-of-day level, the Variability Level would be set to 1.0, if the range of intraday mid-levels is less than the pre-defined BOW. If the range is greater than the pre-defined BOW, the Variability Level would be set to 1.2. Variability Levels are calculated for the on-the-run instrument in each index family.<sup>6</sup>

Once Variability Levels are calculated, ICC proposed to convert Variability Levels into Variability Bands, which correspond to a range of Variability Levels. Once Variability Levels and Variability Bands have been determined, ICC proposed to create market groups and assign each index instrument to one of these market groups. For example, the CDX.NA.IG and CDX.NA.HY would be assigned to the North American group. After assigning each index instrument to a market group, ICC would use the largest Variability Band of any instrument within a market group as the Variability Band for that market group as a whole. ICC refers to this Variability Band as the “Market-Proxy Variability Band.”<sup>7</sup> The proposed automated BOW algorithm would then adjust

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<sup>6</sup> Id.

<sup>7</sup> Id.

the EOD BOW (Regime 1, 2, or 3) for the market group as a whole by one regime (moving from Regime 1 to Regime 2, or from Regime 2 to Regime 3) or two regimes (from Regime 1 to Regime 3), with higher Market-Proxy Variability Bands resulting in a two-regime adjustment, and smaller Market-Proxy Variability Bands resulting in a one-regime adjustment, or no adjustment.<sup>8</sup>

For single-name instruments, ICC proposes to introduce a new scaling factor that would be applied, along with other scaling factors used in the current process, to the EOD BOW, as calculated based on BOW data received from participants. The Variability Scaling Factor for single-name instruments would depend on the Market-Proxy Variability Band for the market to which each single-name instrument is assigned. A higher Market-Proxy Variability Band will result in a larger scaling factor being applied.<sup>9</sup>

In addition to proposing to automate the process for increasing selected BOWs, ICC also proposed to remove a footnote from its Pricing Policy that set forth details of an intraday filtering algorithm that was planned but never implemented. Also, ICC proposed to correct inaccurate references in the Pricing Policy.<sup>10</sup>

### III. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act directs the Commission to approve a propose rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder

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<sup>8</sup> Id.

<sup>9</sup> Id.

<sup>10</sup> Id. at 27540-41.

applicable to such organization.<sup>11</sup> Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of a registered 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.<sup>12</sup> Rule 17Ad-22(d)(4) requires, in relevant part, that a registered clearing agency shall establish, implement, maintain, and enforce written policies and procedures reasonably designed to identify sources of operational risk and minimize them through the development of appropriate systems, controls, and procedures; and implement systems that are reliable, resilient and secure, and have adequate, scalable capacity.<sup>13</sup>

The Commission finds that the proposed rule change, which modifies ICC's Pricing Policy to implement an automated process for widening the EOD BOW for index and single-name instruments is consistent with Section 17A of the Act and Rule 17Ad-22 thereunder. By automating the process for widening the EOD BOWs when necessary, the Commission believes that ICC will likely reduce the risk of error or delay in the end-of-day pricing process in connection with a potentially significant number of adjustments to BOWs that would need to be made manually and in a short period of time absent the proposed changes. Since the end-of-day BOW is an input in ICC's end-of-day price discovery process, the Commission believes that the proposed rule changes will likely enhance the speed and accuracy of that process, thereby promoting the prompt clearance

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<sup>11</sup> 15 U.S.C. 78s(b)(2)(C).

<sup>12</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>13</sup> 17 CFR 240.17Ad-22(d)(4).

and settlement of derivative agreements, contracts and transactions, consistent with Section 17A(b)(3)(F) of the Act.

For similar reasons, the Commission finds that the proposed rule changes are also consistent with Rule 17Ad-22(d)(4) in that they are designed to reduce operational risk. Specifically, the proposed rule changes are intended to reduce ICC's operational risk in the end-of-day pricing process by establishing an automated process that will more quickly implement the widening of BOWs, if appropriate, based on a set of well-defined criteria. As a result, the risk of error that accompanies manual observation of market conditions and manual input of a potentially significant amount of adjustments in a small period of time during volatile market conditions is significantly reduced. Therefore, the Commission finds that the proposed rule changes are consistent with the requirements of Rule 17Ad-22(d)(4) that the registered clearing agencies establish, implement, maintain, and enforce written policies and procedures reasonably designed to identify sources of operational risk and minimize them through the development of appropriate systems, controls, and procedures; and implement systems that are reliable, resilient and secure, and have adequate, scalable capacity.

IV. Conclusion

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act that the proposed rule change (SR-ICC-2017-006) be, and hereby is, approved.<sup>14</sup>

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.<sup>15</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>14</sup> In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>15</sup> 17 CFR 200.30-3(a)(12).