

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-82542; File No. SR-ICC-2018-001)

January 19, 2018

Self-Regulatory Organizations; ICE Clear Credit LLC; Notice of Filing of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice Relating to the ICC Rules, ICC Risk Management Model Description Document, ICC Risk Management Framework, ICC Stress Testing Framework, and ICC Liquidity Risk Management Framework

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934,<sup>1</sup> and Rule 19b-4,<sup>2</sup> notice is hereby given that on January 16, 2018, ICE Clear Credit LLC (“ICC”) 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 ICC. The Commission is publishing this notice to solicit comments on the proposed rule change.

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

The purpose of the proposed rule change is to make revisions to the ICC Clearing Rules (the “Rules”) to support clearing of a new transaction type. ICC also proposes related loss given default enhancements to the ICC Risk Management Model Description Document, the ICC Risk Management Framework, the ICC Stress Testing Framework, and the ICC Liquidity Risk Management Framework.

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, ICC included statements concerning the purpose of and basis for the proposed rule change, security-based swap submission, or

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

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

advance notice and discussed any comments it received on the proposed rule change, security-based swap submission, or advance notice. The text of these statements may be examined at 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, Security-Based Swap Submission, or Advance Notice

(a) Purpose

ICC proposes revisions to its Rules, Risk Management Model Description Document, Risk Management Framework, Stress Testing Framework, and Liquidity Risk Management Framework. ICC believes such revisions will facilitate the prompt and accurate clearance and settlement of securities transactions and derivative agreements, contracts, and transactions for which it is responsible. The proposed revisions are described in detail as follows.

**Proposed Amendments to the ICC Rules**

The purpose of the proposed changes to the ICC Rules is to support clearing of a new transaction type, Standard European Senior Non-Preferred Financial Corporate, which was recently published by the International Swaps and Derivatives Association, Inc. (“ISDA”). ICC proposes amending its Rules to provide for the clearance of contracts referencing this new transaction type. ICC believes the addition of these contracts will benefit the market for credit default swaps by providing market participants the benefits of clearing, including reduction in counterparty risk and safeguarding of margin assets pursuant to clearing house rules.

Specifically, ICC proposes amending Rule 26H-102 (Definitions), ‘List of Eligible Standard European Financial Corporate (“STEF”) Reference Entities’ to

include Standard European Senior Non-Preferred Financial Corporate in the list of Eligible STEFC Reference Entities to be cleared by ICC. ICC also proposes amending Rule 26H-102 (Definitions), ‘STEFC Contract Reference Obligations’ to note that in the case of a STEFC Reference Entity where the transaction type is Standard European Senior Non-Preferred Financial Corporate, the STEFC Contracts Reference Obligation shall be determined in accordance with the Additional Provisions for Senior Non-Preferred Reference Obligations, as published by ISDA. ICC also proposes conforming changes to Rule 26H-303 (STEFC Contract Adjustments) and Rule 26H-315 (Terms of the Cleared STEFC Contract), to incorporate reference to the new transaction type.

### **Proposed Loss Given Default Enhancements**

ICC’s risk management methodology incorporates considerations of idiosyncratic credit events and the associated potential losses. These credit event losses are termed Loss-Given-Default (“LGD”). In order to support clearing of the new transaction type, ICC proposes certain LGD enhancements to its risk model. A description of these changes is set forth below.

ICC first proposes Risk Factor (“RF”) level LGD enhancements. These proposed RF level enhancements are designed to better capture the LGD risk associated with the issuance of new debt structures by European banks, and provide a consistent recovery rate scenario approach to different sub-factors.

Under ICC’s risk model, every Single Name (“SN”) reference entity is deemed a RF. Each combination of definition, doc-clause, tier, and currency for a given SN RF determines a SN Risk Sub-Factor (“RSF”). Currently, ICC measures losses associated with credit events (“LGD”) by means of a stress-based approach, which utilizes three

recovery rate (“RR”) scenarios: minimum RR, expected RR, and maximum RR. Outright and index-derived RSF exposures are combined at each RR scenario.

The results of these RR scenarios are used as an input into the Profit/Loss-Given-Default (“P/LGD”) calculations at both the RSF and RF levels. For each RSF, P/LGD is calculated as the worst credit event outcome, and for each RF, P/LGD is calculated as the sum of the worst credit outcomes per RSF. These final P/LGD results are used as part of the determination of risk requirements.

ICC proposes enhancements to the RF level LGD calculation. Specifically, ICC proposes a change to the calculation by incorporating a more consistent approach in the calculation of the P/LGD by using the same RR scenarios applied to the different RSFs which part of the considered RF.

For each RF, ICC will continue to calculate an “extreme outcome” as the sum of the worst RSF P/LGDs across all scenarios. ICC will also, for each RF, calculate an “expected outcome” as the worst sum of all the RSF P/LGDs across all of the same scenarios. Under the proposed approach, ICC will then combine the results of the “extreme outcome” calculation and the “expected outcome” calculation to compute the total LGD for each RF.

ICC also proposes to expand its LGD analysis to Risk Factor Groups (“RFG”). Under the proposed changes, a collection of related RFs will form a RFG. These related RFs will be defined as a RFG based on either 1) having a common majority parental sovereign ownership (e.g. quasi-sovereigns and sovereigns), or 2) being a majority owned subsidiary of a common parent entity according to the Bloomberg Related Securities Analysis. A RFG can consist of only one RF. This change will better capture the risk

exposure dynamics of related RFs, and will allow ICC the ability to provide limited LGD benefits across RFs with opposite exposures, as well as allow for the ability to capture accumulation of directional exposure for related RFs.

Under the proposed approach, the total quantity LGD will be calculated on a RFG level, and account for the exposure due to credit events associated with the reference entities within a given RFG. If a RFG contains only one RF, the LGD will continue to be computed as the risk exposure due to a credit event for a given underlying reference entity. Under the proposed approach, ICC will sum the P/LGDs for each RF in a given RFG, with limited offsets in the event RFs exhibit positive PLGD. Using the results of the above calculation, ICC will obtain the RFG level LGD. The proposed approach also includes a calculation which allows for the RFG level LGD to be attributed to each RF within the considered RFG.

ICC proposes changes to the ‘Loss Given Default Risk Analysis’ section of the Risk Management Model Description Document to reflect the described RF and RFG LGD calculation changes. ICC also proposes conforming changes to other sections of the Risk Management Description Document to incorporate these methodology changes and reflect the RFG analysis.

ICC proposes a revision to the ‘Uncollateralized Loss Given Default’ calculation in order to incorporate the RFG level LGD attribution calculation mentioned above.

ICC proposes changes to the ‘Idiosyncratic Jump-to-Default Requirements’ section of the Risk Management Model Description document. Currently, the portfolio JTD approach collateralizes the worst uncollateralized LGD (“ULGD”) exposure among all RFs. Under the proposed approach, the portfolio JTD approach will collateralize,

through the portfolio JTD IM requirement that accounts for the RFG-specific LGD collateralization, the worst ULGD exposure among all RFGs. The ULGD exposure for a given RFG will be calculated as a sum of the associated RF ULGDs.

ICC also proposes minor edits to the ‘Portfolio Level Wrong-Way Risk and Contagion Risk Analysis’ section to update language and calculation descriptions to accommodate the introduction of the RFG to the ‘Idiosyncratic Jump-to-Default Requirements’ section.

ICC proposes changes to the ‘Guaranty Fund Methodology’ section. ICC’s risk management approach establishes GF to provide for the mutualization of losses under extreme credit market scenarios. Specifically, the ICC GF is designed to provide adequate funds to cover losses associated with the default of the two CP affiliate groups that would potentially cause the largest aggregate credit exposure to ICC under extreme but plausible market conditions. ICC’s current GF methodology includes, among other assumptions and adverse market conditions, the assumption that up to three credit events, different from the ones associated with CPs, occur during the established risk horizon. ICC proposes expanding this analysis to the RFG level. Under this proposed approach, it will be assumed that credit events associated with up to three RFGs, different from the ones associated with the CPs and the RFs that are in the RFGs as the CPs, occur during the established risk horizon. As such, the uncollateralized losses, used in the Guaranty Fund analysis, reflect the proposed expansion to the RFG level.

ICC also proposes clarifications to the calculation for the Specific Wrong Way Risk component of the Guaranty Fund. Currently, for a given CP, the Specific Wrong

Way Risk component is based on self-referencing positions arising from one or more RFGs; ICC proposes clarifying this analysis to be based on the RFG level.

ICC proposes conforming changes to its Risk Management Framework, Liquidity Risk Management Framework, and Stress Testing Framework, to reflect the LGD enhancements described above. For the Risk Management Framework, ICC proposes revisions to the 'Jump-to-Default Requirements' section to note that the worst LGD associated with a RFG is selected to establish the portfolio idiosyncratic JTD requirements. ICC also proposes revisions to the 'Guaranty Fund' section to reflect the RFG LGD enhancements related to ICC's Guaranty Fund calculation.

With regards to the Stress Testing Framework, ICC proposes changes to its stress testing methodology to be based on the reference entity group level (also referred to as the RFG level). Currently, ICC utilizes scenarios based on hypothetically constructed (forward looking) extreme but plausible market scenarios augmented with adverse credit events affecting up to two additional reference entities per CP affiliate group; ICC proposes expanding its adverse credit event analysis to include up to two additional reference entity groups. ICC also proposes that the selected RFG for stress testing purposes must contain one or more reference entities displaying 500 bps or greater 1-Y end-of-day spread level in order to be subjected to credit events. ICC also proposes changes to its reverse stress testing, general wrong way risk, and contagion stress testing analyses, to be at the RFG level. ICC proposes removing RF level references under its Recovery Rate Sensitivity analysis to be consistent with the proposed changes related to RFG.

Finally, with regards to the ICC Liquidity Risk Management Framework, ICC proposes changes to its liquidity stress testing methodology to be based on the reference entity group level (also referred to as the RFG level). Currently (consistent with the stress testing methodology), ICC utilizes scenarios based on hypothetically constructed (forward looking) extreme but plausible market scenarios augmented with adverse credit events affecting up to two additional reference entities per CP affiliate group; ICC proposes expanding its adverse credit event analysis to include up to two additional reference entity groups. Similar to the Stress Testing Framework, ICC also proposes that the selected RFG for liquidity stress testing purposes must contain one or more reference entities displaying 500 bps or greater 1-Y end-of-day spread level in order to be subjected to credit events. Finally, ICC is adding additional language to the liquidity framework detailing the rationale behind the selection of the 500 bps threshold, to be consistent with Stress Testing Framework.

(b) Statutory Basis

Section 17A(b)(3)(F) of the Act<sup>3</sup> 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 and to comply with the provisions of the Act and the rules and regulations thereunder. ICC believes that the proposed rule changes are consistent with the requirements of the Act and the rules and regulations thereunder applicable to ICC, in particular, to Section 17(A)(b)(3)(F)<sup>4</sup>, because ICC believes that the proposed rule

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

<sup>4</sup> Id.



changes will promote the prompt and accurate clearance and settlement of securities transactions, derivatives agreements, contracts, and transactions.

In regards to the proposed amendments to the ICC Rules, contracts referencing the Standard European Senior Non-Preferred Financial Corporate transaction type are similar to the STEFC contracts currently cleared by ICC, and will be cleared pursuant to ICC's existing clearing arrangements and related financial safeguards, protections and risk management procedures. Clearing of these contracts will allow market participants an increased ability to manage risk and ensure the safeguarding of margin assets pursuant to clearing house rules. ICC believes that acceptance of these contracts, on the terms and conditions set out in the Rules, is consistent with the prompt and accurate clearance of 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, and the protection of investors and the public interest, within the meaning of Section 17A(b)(3)(F) of the Act.<sup>5</sup>

Clearing of contracts referencing the Standard European Senior Non-Preferred Financial Corporate transaction type will also satisfy the requirements of Rule 17Ad-22.<sup>6</sup> In particular, in terms of financial resources, ICC will apply its existing initial margin methodology to the contracts. ICC believes that this model will provide sufficient initial margin requirements to cover its credit exposure to its clearing members from clearing such contracts, consistent with the requirements of Rule 17Ad-22(b)(2).<sup>7</sup> In addition, ICC

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<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>6</sup> 17 CFR 240.17Ad-22.

<sup>7</sup> 17 CFR 240.17Ad-22(b)(2).

believes its Guaranty Fund, under its existing methodology, will, together with the required initial margin, provide sufficient financial resources to support the clearing of the contracts consistent with the requirements of Rule 17Ad-22(b)(3).<sup>8</sup> ICC also believes that its existing operational and managerial resources will be sufficient for clearing of the contracts, consistent with the requirements of Rule 17Ad-22(d)(4),<sup>9</sup> as the new contracts are substantially the same from an operational perspective as existing contracts.

Similarly, ICC will use its existing settlement procedures and account structures for the new contracts, consistent with the requirements of Rule 17Ad-22(d)(5), (12) and (15)<sup>10</sup> as to the finality and accuracy of its daily settlement process and avoidance of the risk to ICC of settlement failures. ICC determined to accept the contracts for clearing in accordance with its governance process, which included review of the contracts and related risk management considerations by the ICC Risk Committee and approval by its Board. These governance arrangements are consistent with the requirements of Rule 17Ad-22(d)(8)<sup>11</sup>. Finally, ICC will apply its existing default management policies and procedures for the contracts. ICC believes that these procedures allow for it to take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of clearing member insolvencies or defaults in respect of the additional single names, in accordance with Rule 17Ad-22(d)(11).<sup>12</sup>

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<sup>8</sup> 17 CFR 240.17Ad-22(b)(3).

<sup>9</sup> 17 CFR 240.17Ad-22(d)(4).

<sup>10</sup> 17 CFR 240.17Ad-22(d)(5), (12) and (15).

<sup>11</sup> 17 CFR 240.17Ad-22(d)(8).

<sup>12</sup> 17 CFR 240.17Ad-22(d)(11).

With regards to the LGD enhancements, the proposed risk model revisions enhance ICC's risk methodology and are expected to impose more conservative requirements, which would enhance the financial resources available to ICC and thereby facilitate its ability to promptly and accurately clear and settle its cleared CDS contracts. In addition, the proposed revisions are consistent with the relevant requirements of Rule 17Ad-22<sup>13</sup>. In particular, the LGD related amendments will enhance the financial resources available to the clearing house, and continue to ensure that ICC maintains sufficient financial resources to withstand a default by the Clearing Participant ("CP") family to which it has the largest exposure in extreme but plausible market conditions, and are therefore reasonably designed to meet the margin and financial resource requirements of Rule 17Ad-22(b)(2-3)<sup>14</sup>.

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

ICC does not believe the proposed rule changes would have any impact, or impose any burden, on competition. Contracts referencing the Standard European Senior Non-Preferred Financial Corporate transaction type will be available to all ICC participants for clearing. The clearing of these contracts by ICC does not preclude the offering of the contracts for clearing by other market participants. Additionally, the LGD enhancements apply uniformly across all CPs. Therefore, ICC does not believe the proposed rule changes impose any burden on competition that is inappropriate in furtherance of the purposes of the Act.

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<sup>13</sup> 17 C.F.R. §240.17Ad-22.

<sup>14</sup> 17 C.F.R. §240.17Ad-22(b)(2-3).

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change , Security-Based Swap Submission, or Advance Notice 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 , Security-Based Swap Submission, or 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 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](mailto:rule-comments@sec.gov). Please include File Number SR-ICC-2018-001 on the subject line.

Paper Comments:

Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-1090.

All submissions should refer to File Number SR-ICC-2018-001. 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, N.E., Washington, D.C. 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 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-2018-001 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>15</sup>

Eduardo A. Aleman  
Assistant Secretary

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