

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-91834; File No. SR-ICC-2021-006)

May 11, 2021

Self-Regulatory Organizations; ICE Clear Credit LLC; Order Approving Proposed Rule Change Relating to the ICC Clearing Rules and ICC Exercise Procedures

I. Introduction

On March 25, 2021, ICE Clear Credit LLC (“ICC”) filed with the Securities and Exchange Commission, pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to revise the ICC Clearing Rules (the “Rules”) and the ICC Exercise Procedures (“Exercise Procedures”) in connection with the clearing of credit default index Swaptions (“Index Swaptions”).³

The proposed rule change was published for comment in the Federal Register on April 7, 2021.⁴ The Commission did not receive comments regarding the proposed rule change.

For the reasons discussed below, the Commission is approving the proposed rule change.

II. Description of the Proposed Rule Change

ICC proposes revising its Rules and Exercise Procedures related to the clearing of Index Swaptions.⁵ In the case of Index Swaptions cleared by ICC, the underlying index

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.

⁴ Self-Regulatory Organizations; ICE Clear Credit LLC; Notice of Proposed Rule Change Relating to the ICC Clearing Rules and ICC Exercise Procedures, Exchange Act Release No. 91450 (April 1, 2021), 86 Fed. Reg. 18087 (April 7, 2021) (“Notice”).

⁵ The description of the proposed rule change is excerpted from the Notice.

credit default swap is limited to certain CDX and iTraxx 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. ICC proposes minor revisions to support the clearing of Index Swaptions, including updates related to iTraxx Index Swaptions, an enhancement to the exercise and assignment process, and other clarifications.

A. Rule Amendments

The proposed amendments consist of minor revisions to Rule 26R-319, which addresses procedures for settlement of an exercised Index Swaption. Additional settlements may be required under Rule 26R-319(b) if one or more Credit Events has occurred with respect to the underlying index at or prior to the expiration date of the Index Swaption. Regarding the determination of Index Swaption settlement amounts, Rule 26R-319(b)(ii) currently contemplates the inclusion of an additional accrual-related component (“Additional Accrual”). However, ICC Circular 2020/070 describes how ICC determines settlement amounts for cleared Index Swaptions and states that, in light of industry discussions, the Additional Accrual for such transactions will be zero.

Amended Rule 26R-319(b)(ii) would omit the description of the Additional Accrual, which would be zero for settlement of Index Swaptions. The circular and presentation on the determination of Index Swaption settlement amounts would remain on ICC’s website.

Regarding iTraxx Index Swaptions, ICC proposes to amend Rule 26R-319(c), which applies in the case of a relevant M(M)R Restructuring Credit Event, which is when the restructuring of debt constitutes a credit event that triggers a CDS contract. Minor streamlining revisions to the exercise process rules include the proposed omission of paragraph (i) related to the delivery of MP Notices by Swaption Buyer and Swaption

Sellers. Further, ICC does not propose any changes to paragraph (ii), which details how an Underlying New Trade comes into effect. An Underlying New Trade remains defined in Rule 26R-102 as a new single name CDS trade that would arise upon exercise of an Index Swaption where a relevant Restructuring Credit Event, if applicable, has occurred with respect to a reference entity in the relevant index. ICC also proposes to amend paragraph (iii) and remove paragraph (iv) which currently discuss the treatment of the Underlying New Trade in respect of the Event Determination Date. Instead, amended paragraph (iii) would discuss the treatment of the Underlying New Trade depending on whether the expiration date occurred prior to, or on or following, the commencement of the Credit Event Notice Triggering Period (as defined in the Restructuring Procedures). If the expiration date occurs prior to commencement of the period, the Underlying New Trade will be subject to the provisions of the CDS Restructuring Rules in Subchapter 26E (and may become a Triggered Restructuring CDS Transaction thereunder). If the Expiration Date occurs on or following commencement of such period, neither party will be permitted to deliver an MP Notice, the Underlying New Trade cannot become a Triggered Restructuring CDS Transaction and no Event Determination Date or settlement will occur.

B. Exercise Procedures

The Exercise Procedures supplement the provisions of Subchapter 26R of the Rules with respect to Index Swaptions and provide further detail as to the manner in which Index Swaptions may be exercised by Swaption Buyers, the manner in which ICC will assign such exercises to Swaption Sellers, and certain actions that ICC may take in the event of technical issues.

The proposal would enhance the exercise and assignment process in the Exercise Procedures. Specifically, the proposal would revise the definition of Pre-Exercise Notification Period in Paragraph 1 to reference Paragraph 2.2(e) in respect of the Pre-Exercise Notification Period. Paragraph 2.2(e) describes the Pre-Exercise Notification Period during which an exercising party can submit, modify, and/or withdraw preliminary exercise notices. The Exercise Procedures allow firms to submit preliminary exercise notices such that the preliminary instructions can be used as the final exercise instructions in the event of a communications failure during the exercise window. The proposed changes would allow ICC to identify each exercising party's "in the money" Index Option open positions for the relevant expiration date and submit, on behalf of the exercising party, preliminary exercise notices for all such in "the money" positions. Such preliminary exercise notices submitted by ICC for an exercising party may be modified or withdrawn by the exercising party during the Pre-Exercise Notification Period. Additionally, the proposal would make a related change to Paragraph 2.2(i) to reference ICC's ability to submit, on behalf of an exercising party, a preliminary exercise notice.

The proposal would also update Paragraphs 2.6 and 2.8, which include procedures to address a failure of the electronic system established by ICC for exercise. In such case, Paragraph 2.6 provides ICC with several options including, canceling and rescheduling the Exercise Period (i.e., the period on the expiration date of an Index Swaption during which the Swaption Buyer may deliver an exercise notice to ICC to exercise all or part of such Index Swaption). The proposed changes would clarify that canceling and rescheduling the Exercise Period may include scheduling a new Pre-Exercise Notification Period, in which case any preliminary exercise notices and exercise

notices submitted prior will be ineffective. Paragraph 2.8 addresses the situation where ICC will automatically exercise on the expiration date each open position (of all exercising parties) in an Index Swaption that is determined by ICC to be “in the money” on such date. The proposal would include additional language relating to its determination of whether an Index Swaption is “in the money” in connection with the clearing of iTraxx Index Swaptions.

III. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to the organization.⁶ For the reasons given below, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act⁷ and Rules 17Ad-22(e)(1) and 17Ad-22(e)(17)(i) and (ii) thereunder.⁸

A. Consistency with Section 17A(b)(3)(F) of the Act

Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of ICC be designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions, to assure the safeguarding of securities and funds which are in the custody

⁶ 15 U.S.C. 78s(b)(2)(C).

⁷ 15 U.S.C. 78q-1(b)(3)(F).

⁸ 17 CFR 240.17Ad-22(e)(1), (e)(17)(i) and (ii).

or control of ICC or for which it is responsible, and, in general, to protect investors and the public interest.⁹

As discussed above, the proposed rule change would make minor revisions to the Rules for settlement of an exercised Index Swaption. Specifically, the proposal would revise Rule 26R-319(b)(ii) to remove the description of the Additional Accrual in the determination of Index Swaption settlement amounts. The Commission believes this minor revision helps to simplify ICC's settlement rules with respect to settlement of Index Swaptions, for which the Additional Accrual will be zero, which could make it easier to understand the potential Index Swaption settlement amounts easier, thereby promoting the prompt and accurate settlement of securities transactions.

Additionally, the proposal would amend ICC's Rules to omit and revise certain other information. Specifically, the proposal would amend Rule 26R-319(c), which applies in the case of a relevant M(M)R Restructuring Credit Event, by omitting a paragraph (i) related to the delivery of MP Notices by Swaption Buyers and Sellers, and removing paragraph (iv), which currently discusses the treatment of the Underlying New Trade in respect of the Event Determination Date. Instead, the proposed language in paragraph (iii) would discuss the treatment of the Underlying New Trade depending on whether the expiration date occurred prior to, or on or following, the commencement of the CEN Triggering Period. If the expiration date occurs prior to commencement of the period, the Underlying New Trade will be subject to the provisions of the CDS Restructuring Rules in Subchapter 26E. If the Expiration Date occurs on or following

⁹ 15 U.S.C. 78q-1(b)(3)(F).

commencement of such period, neither party will be permitted to deliver an MP Notice, the Underlying New Trade cannot become a Triggered Restructuring CDS Transaction and no Event Determination Date or settlement will occur. The Commission believes that this proposed revision will ensure that only trades meeting the timing of the triggering period will be settled. This, in turn, promotes accurate clearance and settlement during specified periods as well as assuring the safeguarding of securities or funds in ICC's custody or control or for which it is responsible by ensuring only appropriate securities and funds are exchanged.

Further, as noted above, the Exercise Procedures supplement the provisions of Subchapter 26R of the Rules with respect to Index Swaptions and provide further detail as to the manner in which Index Swaptions may be exercised by Swaption Buyers, the manner in which ICC will assign such exercises to Swaption Sellers, and certain actions that ICC may take in the event of technical issues. First, the definition of Pre-Exercise Notification Period has been revised to include a reference to Paragraph 2.2(e), which itself describes the Pre-Exercise Notification Period during which an exercising party can submit, modify, and/or withdraw preliminary exercise notices such that the preliminary instructions can be used as the final exercise instructions in the event of a communications failure during the exercise window. The Commission believes that this proposed change enhances the definition of this term by cross-referencing a more complete description of this period. Additionally, the proposal would revise Paragraph 2.2(e), which would allow ICC to identify each exercising party's "in the money" Index Option open positions for the relevant expiration date and submit, on behalf of the exercising party, preliminary exercise notices for all such "in the money" positions.

Further, such preliminary exercise notices submitted by ICC for an exercising party may be modified or withdrawn by the exercising party during the Pre-Exercise Notification Period. Additionally, the proposal would make a related change to Paragraph 2.2(i) to reference ICC's ability to submit, on behalf of an exercising party, a preliminary exercise notice. The Commission believes that these proposed changes to the procedures related to the pre-exercise notification period would enhance the procedures by clarifying ICC's role in identifying each Exercising Party's "in the money" Index Option Open Positions for the relevant Expiration Date and submitting preliminary notices. The Commission believes that this should help the preliminary notification process operate smoothly and ensure that the preliminary instructions can be used as the final exercise instructions in the event of a communications failure during the exercise window, thereby increasing reliability of the process and helping to ensure prompt and accurate clearance and settlement of securities upon the exercise of Index Swaptions.

The proposed rule change would further revise the Exercise Procedures to account for the Pre-Exercise Notification Period during a systems failure. Specifically, as noted above, paragraph 2.6 provides ICC with several options including canceling and rescheduling the Exercise Period in the event of an exercise systems failure. The proposed changes would clarify that canceling and rescheduling the Exercise Period may include scheduling a new Pre-Exercise Notification Period, in which case any preliminary exercise notices and exercise notices submitted prior will be ineffective. The Commission believes that this proposed change would enhance the procedures by ensuring that pre-notifications do not result in erroneous exercises when there is a

systems failure, thereby aiming to ensure accurate settlement and the safeguarding of securities and funds.

Paragraph 2.8 of the Exercise Procedures addresses the situation in which ICC will automatically exercise on the expiration date each open position in an Index Swaption that is determined by ICC to be “in the money” on such date. As noted above, the Exercise Procedures would be amended to include additional language in this paragraph relating to its determination of whether an Index Swaption is “in the money.” The Commission believes that this proposed change ensures that each of ICC’s cleared products are appropriately and accurately exercised when there has been a systems failure, which in turn supports ICC’s ability to promptly and accurately clear and settle securities transactions and safeguard securities and funds in its custody or control.

For the reasons stated above, the Commission finds that the proposed rule change should promote the prompt and accurate clearance and settlement of securities transactions and assure the safeguarding of securities and funds in ICC’s custody and control or for which it is responsible, consistent with the Section 17A(b)(3)(F) of the Act.¹⁰

B. Consistency with Rule 17Ad-22(e)(1)

Rule 17Ad-22(e)(1) requires that ICC establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for a well-founded, clear, transparent, and enforceable legal basis for each aspect of its activities in all relevant jurisdictions.¹¹ As discussed above, the proposed changes to the Rules and Procedures

¹⁰ 15 U.S.C. 78q-1(b)(3)(F).

¹¹ 17 CFR 240.17Ad-22(e)(1).

should provide clear guidance for ICC's clearance and settlement of Index Swaptions by removing from the rules the reference to the Additional Accrual in the determination of Index Swaption settlement amounts. Similarly, amending Rule 26R-319(c) as noted above, which applies in the case of a relevant M(M)R Restructuring Credit Event, should provide a clear basis for the treatment of the Underlying New Trade depending on whether the expiration date occurred prior to, or on or following, the commencement of the CEN Triggering Period.

Further, the Commission believes that in proposing changes to the procedures related to the pre-exercise notification period clarifying ICC's role in identifying each Exercising Party's "in the money" Index Option Open Positions for the relevant Expiration Date and submitting preliminary notices, the procedures would provide a clear basis for the use of the preliminary instructions such as the final exercise instructions in the event of a communications failure during the exercise window.

For these reasons, the Commission finds that the proposed rule change is consistent with Rule 17Ad-22(e)(1).¹²

C. Consistency with Rule 17Ad-22(e)(17)

Rules 17Ad-22(e)(17)(i) and (ii) require that ICC establish, implement, maintain and enforce written policies and procedures reasonably designed to, as applicable, manage its operational risks by (i) identifying the plausible sources of operational risk, both internal and external, and mitigating their impact through the use of appropriate systems, policies, procedures, and controls, and (ii) ensuring that systems have a high

¹² 17 CFR 240.17Ad-22(e)(1).

degree of security, resiliency, operational reliability, and adequate, scalable capacity.¹³

The Commission believes that by allowing ICC to identify each exercising party's "in the money" Index Option open positions for the relevant expiration date and submit preliminary exercise notices for all such in "the money" positions, ICC can mitigate the impact of a technology or communication error because they can be used as the final exercise instructions in the event of a communications failure during the exercise window. The Commission believes that such procedures should help mitigate the impact from technical issues to ensure that the system has a high degree of security, resiliency, and operational reliability. Similarly, the Commission believes that the proposed changes to the Exercise Procedures that, in the event of an exercise system failure, clarify that canceling and rescheduling the Exercise Period may include scheduling a new Pre-Exercise Notification Period, in which case any preliminary exercise notices and exercise notices submitted prior will be ineffective, enhances operational reliability of ICC's systems.

For these reasons, the Commission finds that the proposed rule change is consistent with Rule 17Ad-22(e)(17)(i) and (ii).¹⁴

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act, and in particular, with the requirements of

¹³ 17 CFR 240.17Ad-22(e)(17)(i)-(ii).

¹⁴ 17 CFR 240.17Ad-22(e)(17)(i)-(ii).

Section 17A(b)(3)(F) of the Act¹⁵ and Rules 17Ad-22(e)(1) and 17Ad-22(e)(17)(i) and (ii).¹⁶

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act¹⁷ that the proposed rule change (SR-ICC-2021-006), be, and hereby is, approved.¹⁸

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁹

J. Matthew DeLesDernier
Assistant Secretary

¹⁵ 15 U.S.C. 78q-1(b)(3)(F).

¹⁶ 17 CFR 240.17Ad-22(e)(1), (e)(17)(i) and (ii).

¹⁷ 15 U.S.C. 78s(b)(2).

¹⁸ 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).

¹⁹ 17 CFR 200.30-3(a)(12).