I. Introduction

On November 19, 2021, ICE Clear Credit LLC (“ICC”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”), and Rule 19b-4, a proposed rule change to revise Rule 26R-319 of the ICC Clearing Rules (“Rules”) and the ICC Exercise Procedures (“Exercise Procedures”) in connection with the clearing of credit default index options (“Index Swaptions”). The proposed rule change was published for comment in the Federal Register on December 7, 2021. The Commission did not receive comments regarding the proposed rule change. For the reasons discussed below, the Commission is approving the proposed rule change.

____________________


3 Capitalized terms used but not defined herein have the meanings specified in the Rules and Exercise Procedures.

II. Description of the Proposed Rule Change

A. Background

Pursuant to an Index Swaption, one party (the “Swaption Buyer”) has the right (but not the obligation) to cause the other 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 cleared by ICC, the underlying index 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 by the Swaption Buyer in accordance with its terms.

B. Revisions to Rule 26R-319

ICC Rule 26R-319 describes what happens upon the exercise of an Index Swaption. ICC Rule 26R-319 consists of three parts: 26R-319(a), 26R-319(b), and 26R-319(c). 26R-319(a) applies when a Swaption Buyer effectively exercises an Index Swaption and the underlying index is not subject to a restructuring due to a credit event, while (b) and (c) apply when an Index Swaption is effectively exercised and the underlying index is subject to a restructuring due to a credit event.

Under 26R-319(a), upon the effective exercise of an Index Swaption, a contract in the form of the underlying index comes into effect between the Swaption Buyer and ICC and an exactly offsetting contract comes into effect between ICC and the Swaption Seller. The proposed rule change would not amend 26R-319(a).

26R-319(b) describes what happens when an Index Swaption is effectively exercised and one or more Event Determination Dates have occurred with respect to the underlying index on or prior to the Expiration Date. In that case, in addition to the new contracts that come into effect
under 26R-319(a), certain additional settlements may be required, as further described in 26R-319(b).

The proposed rule change would make two amendments to 26R-319(b). The proposed rule change would add a parenthetical to clarify that 26R-319(b) does not apply to an Event Determination Date in respect of an M(M)R Restructuring Credit Event because 26R-319(c) would apply in that case, as described below. The proposed rule change would further modify subpart (i) of 26R-319(b) by adding a note that the settlement contemplated by that subsection would be subject to any modification with respect to fixed rate payments or accrual rebates as specified by ICC by Circular.

26R-319(c) describes what happens when an Index Swaption is effectively exercised and one or more M(M)R Restructuring Credit Events have occurred with respect to the underlying index on or prior to the Expiration Date. 26R-319(c) is only applicable to iTraxx Index Swaptions. Under 26R-319(c) as currently written, upon settlement the Swaption Buyer would receive a re-versioned underlying index plus a single name CDS contract.

The proposed rule change would amend 26R-319(c) so that, in certain circumstances, the Swaption Buyer would receive a re-versioned underlying index plus a single name CDS contract and a cash payment. Settlement under 26R-319(c) as amended therefore could result in the re-versioned underlying index and a blend of single name position and cash. This settlement would be similar to what occurs when a buyer and seller settle an index swaption bilaterally. Thus, the proposed amendments would make settlement of a cleared Index Swaption at ICC similar to the settlement that occurs in the bilateral market, outside of the clearinghouse.⁵

26R-319(c) as currently written has an introductory sentence and four subparts. The proposed rule change first would revise the introductory sentence of 26R-319(c) to incorporate text currently found in subparts (ii) and (iii) of 26R-319(c). Specifically, the proposed rule change would incorporate from subpart (ii) language referring to the effective exercise of the Index Swaption and rights and obligations under 26-319(b). The proposed rule change also would incorporate from subpart (iii) language regarding the Relevant Index Swaption Untranched Terms Supplement.

Subpart (i) of 26R-319(c) as currently written is intentionally omitted. The proposed rule change would not revise subpart (i).

Under subpart (ii) as currently written, if an Index Swaption is effectively exercised, then in addition to the rights and obligations under 26R-319(b), a Contract constituting an Underlying New Trade for purposes of the Relevant Index Swaption Untranched Terms Supplement comes into effect between the exercising Swaption Buyer and ICC and an exactly offsetting Contract constituting an Underlying New Trade comes into effect between ICC and the assigned Swaption Seller. As mentioned above, the proposed rule change would move to the introductory clause of 26R-319(c) language currently found in subpart (ii), and therefore, the proposed rule change would delete this language from subpart (ii). The proposed rule change also would add a statement to subpart (ii) that it would be subject to a new subpart (v), as applicable (discussed below).

Subpart (iii) as currently written applies to two situations. First, it applies when the Expiration Date occurs prior to the commencement of the CEN Triggering Period (as defined in the Restructuring Procedures) for Open Positions in single-name Contracts referencing the relevant Reference Entity. Second, it applies when the Expiration Date occurs on or following
the commencement of the CEN Triggering Period for Open Positions in single-name Contracts referencing the relevant Reference Entity. The proposed rule change would split current subpart (iii) into a revised subpart (iii) and a new subpart (iv).

Like the current subpart (iii), revised subpart (iii) would apply when the Expiration Date occurs prior to the commencement of the CEN Triggering Period (as defined in the Restructuring Procedures) for Open Positions in single-name Contracts referencing the relevant Reference Entity. Under subpart (iii) as revised, the Underlying New Trade described in subpart (ii) would be subject to the provisions of the CDS Restructuring Rules (and may become a Triggered Restructuring CDS Transaction thereunder) in the same manner as other Open Positions in single-name Contracts referencing the relevant Reference Entity. This would be the same as currently found in subpart (iii). Moreover, the proposed rule change would delete from subpart (iii) language regarding the Relevant Index Swaption Untranched Terms Supplement, which would be moved to the introductory sentence of 26R-319(c), as described above. The proposed rule change also would add a reference to the Existing Restructuring (a termed defined in the introductory sentence of 26R-319(c)) and a reference to subpart (ii) of 26R-319(c).

New subpart (iv) generally would apply to the second situation described in current subpart (iii) – when the Expiration Date occurs on or following the commencement of the CEN Triggering Period. The proposed rule change would specify further that subpart (iv) only applies when the Expiration Date occurs on or following the commencement of the CEN Triggering Period and prior to the Auction Settlement Date. Under new subpart (iv), with respect to the Underlying New Trade described in subpart (ii), neither party would be permitted to deliver an MP Notice in respect of the Existing Restructuring for such Underlying New Trade, such Underlying New Trade could not become a Triggered Restructuring CDS Transaction with
respect to the Existing Restructuring, and no Event Determination Date or settlement would occur in respect of the Existing Restructuring for purposes of the Underlying New Trade. This language generally would be the same as currently found in subpart (iii).

New subpart (v) would apply in the situation not covered by subpart (iii) or subpart (iv) – if the Expiration Date occurs on or following the Auction Settlement Date. In that situation, ICC would: (a) determine the extent to which positions in relevant single-name CDS contracts of the relevant tenor referencing the Reference Entity subject to the Existing Restructuring are settled based on CDS auctions for particular maturity categories and (b) determine, if applicable, a cash settlement amount payable from one party to the other with respect to the corresponding portion of the notional amount of the Index Swaption applicable to such Reference Entity, with such settlement to be based on the applicable final settlement prices under such auctions. Moreover, with respect to the remaining portion of such notional amount, an Underlying New Trade would come into effect, provided that neither party would be permitted to deliver an MP Notice in respect of the Existing Restructuring for such Underlying New Trade, such Underlying New Trade could not become a Triggered Restructuring CDS Transaction with respect to the Existing Restructuring, and no Event Determination Date or settlement would occur in respect of the Existing Restructuring for purposes of the Underlying New Trade, as set forth in further detail in the ICC Exercise Procedures or other applicable ICC Procedures. Thus, this new subpart (v) would set out the framework for the blend of deliverables described above and would be applicable if the expiration date occurs on or following the Auction Settlement Date.

C. Revisions to the Exercise Procedures

The Exercise Procedures supplement the provisions of Subchapter 26R of the Rules with respect to Index Swaptions. The proposed rule change would amend the Exercise Procedures in
connection with amended 26R-319 discussed above, as well as to incorporate a new defined term, “Minimum Intrinsic Value”.

With respect to amended 26R-319, the proposed rule change would add a new paragraph 3 (Restructuring Settlement) to the Exercise Procedures. New paragraph 3 would apply in connection with 26R-319(c)(v), discussed above. Under new paragraph 3.1, however, ICC could modify or supplement these provisions pursuant to an ICC Circular.

New paragraph 3.3 (Settlement with respect to Existing Restructuring under Exercised Index Swaption) would describe how ICC would determine the amount of the cash settlement and the notional amount of the Underlying New Trade contemplated under new 26R-319(c)(v). ICC would determine these amounts using the Triggered Portion and Untriggered Portion of the aggregate notional amount of Relevant CDS Transaction. New paragraph 3.2 (Determination of Settled Portions) would describe how ICC would determine such Triggered Portion and Untriggered Portion.

With respect to the new defined term Minimum Intrinsic Value, the proposed rule change would define it as a minimum intrinsic value below which an Index Swaption position would not be identified as “in the money” for paragraph 2.2(e)(ii) or 2.8. ICC could establish a Minimum Intrinsic Value and/or permit an exercising party to specify a Minimum Intrinsic Value for its Index Swaptions for a relevant pre-exercise notification period or exercise period.

The proposed rule change would incorporate this new term into the existing fallback provisions described in paragraphs 2.2(e)(ii) and 2.8 of the Exercise Procedures. Specifically, ICC would take into account any applicable Minimum Intrinsic Value as part of its procedures for submitting preliminary exercise notices on behalf of the Exercising Party during the pre-exercise notification period (during which preliminary exercise notices can be submitted,
modified, and/or withdrawn) in paragraph 2.2(e)(ii). ICC also would take into account any applicable Minimum Intrinsic Value in determining whether an Index Swaption is “in the money” for automatic exercise during an Exercise System Failure in paragraph 2.8.

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 such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization. For the reasons discussed below, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act and Rule 17Ad-22(e)(1).

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.

As discussed above, the proposed rule change would revise Rule 26R-319 and the Exercise Procedures to allow for a settlement consisting of the re-versioned underlying index and a blend of single name position and cash, similar to settlement in the bilateral market outside of the clearinghouse. The Commission believes that increasing consistency between cleared and non-cleared transactions should in general encourage market participants to clear transactions in

---

8 17 CFR 240.17Ad-22(e)(1).
Index Swaptions. The Commission therefore believes these changes would promote the prompt and accurate clearance and settlement of such transactions.

Similarly, the Commission believes that amending the Exercise Procedures to incorporate the new defined term Minimum Intrinsic Value should encourage market participants to clear transactions in Index Swaptions. As discussed above, Minimum Intrinsic Value would be a value below which an Index Swaption position would not be identified as “in the money,” and therefore would not be exercised by ICC under paragraphs 2.2(e)(ii) and 2.8 of the Exercise Procedures. The Commission therefore believes that incorporating this new defined term could help establish a threshold below which ICC would not exercise Index Swaptions, thereby allowing Clearing Participants to better understand and anticipate when ICC would exercise their Index Swaption positions. The Commission believes that this change should in general encourage market participants to clear transactions in Index Swaptions, thereby promoting the prompt and accurate clearance and settlement of such transactions.

Moreover, the Commission believes that both sets of changes would establish clear and predictable procedures for settlement and exercise of Index Swaptions by ICC, thereby promoting ICC’s prompt and accurate clearance and settlement of such transactions. Specifically, the Commission believes the amendments to Rule 26R-319 and the Exercise Procedures would establish clear and effective procedures for ICC to use in effecting settlement with a re-versioned underlying index and a blend of single name position and cash. Similarly, the Commission believes that incorporating a Minimum Intrinsic Value below which ICC would not exercise Index Swaptions positions, in the circumstances contemplated by paragraphs 2.2(e)(ii) and 2.8 of the Exercise Procedures, would make ICC’s exercise of Index Swaptions in such situations more predictable and reliable.
Therefore, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act.\textsuperscript{10}

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

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.\textsuperscript{11} As discussed above, the Commission believes that the amendments to Rule 26R-319 and the Exercise Procedures would establish clear and effective procedures for ICC to use in effecting settlement with a re-versioned underlying index and a blend of single name position and cash, and therefore would provide a clear and transparent basis for ICC’s settlement of Index Swaptions. Moreover, the Commission believes that incorporating Minimum Intrinsic Value into paragraphs 2.2(e)(ii) and 2.8 of the Exercise Procedures would make ICC’s exercise of Index Swaptions in such circumstances more predictable and reliable, and therefore well-founded and clear.

Therefore, the Commission finds that the proposed rule change is consistent with Rule 17Ad-22(e)(1).\textsuperscript{12}


\textsuperscript{11} 17 CFR 240.17Ad-22(e)(1).

\textsuperscript{12} 17 CFR 240.17Ad-22(e)(1).
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 Section 17A(b)(3)(F) of the Act\textsuperscript{13} and Rule 17Ad-22(e)(1).\textsuperscript{14}

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act\textsuperscript{15} that the proposed rule change (SR-ICC-2021-023), be, and hereby is, approved.\textsuperscript{16}

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.\textsuperscript{17}

J. Matthew DeLesDernier
Assistant Secretary

\textsuperscript{14} 17 CFR 240.17Ad-22(e)(1).
\textsuperscript{16} 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).
\textsuperscript{17} 17 CFR 200.30-3(a)(12).