

Maria Alarcon
Staff Attorney

June 18, 2020

Re: Formalization of ICC Exercise Procedures and Updates to ICC Rules Pursuant to Section 5c(c)(1) of the Commodity Exchange Act and Commission Regulation 40.6(a)

VIA ELECTRONIC PORTAL

Mr. Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, D.C. 20581

Dear Mr. Kirkpatrick:

ICE Clear Credit LLC (“ICC”) hereby submits, pursuant to Section 5c(c)(1) of the Commodity Exchange Act (the “Act”) and Commodity Futures Trading Commission (“Commission”) Regulation 40.6(a), a self-certification to formalize the ICC Exercise Procedures and to amend the ICC Clearing Rules (the “Rules”).¹ ICC is registered with the Commission as a derivatives clearing organization (“DCO”). ICC intends to implement the changes no sooner than the tenth business day following the filing of this submission with the Commission at its Washington, D.C. headquarters and with its Chicago regional office.

ICC proposes to formalize the Exercise Procedures and to make a related change to the Rules in connection with its proposed launch of the clearing of credit default index swaptions (“Index Swaptions”). This submission includes a description of the Exercise Procedures as well as the amendment to the ICC Rules. Certification of the Exercise Procedures and the change to the ICC Rules pursuant to Section 5c(c)(1) of the Act and Commission Regulation 40.6(a) is also provided below.

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”).² As set out in the Swaption Rule Filings, ICC intends to adopt certain related policies and procedures in preparation for the launch of clearing of Index Swaptions, including those set out in this filing, and does not intend to commence clearing of Index Swaptions until ICC is permitted under Commission regulation to implement the changes described in all such policies and procedures. As such, ICC proposes to formalize the Exercise Procedures and make the related change to the Rules effective only after ICC is permitted under Commission regulation to implement the changes described in all such policies and procedures and ICC completes its 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 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

¹ Capitalized terms used but not defined herein have the meanings specified in the Rules.

² Submission Number 1907-1516-4754-53, dated July 15, 2019; Submission Number 2001-1415-3739-55, dated January 14, 2020.

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.

I. Exercise Procedures

The Exercise Procedures are intended to supplement the provisions of Subchapter 26R of the Rules³ 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.

In paragraph 1 of the Exercise Procedures, ICC proposes to set out key definitions used for the exercise of Index Swaptions. Key defined terms would include the Exercise Period, which would be 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 document would define the circumstances that constitute the failure of the Exercise System (“Exercise System Failure”) which is the electronic system established by ICC for exercise. The Exercising Party would mean (i) with respect to an Index Swaption carried in the house account of a Participant as Swaption Buyer, such Participant, and (ii) with respect to an Index Swaption carried in the client origin account of a Participant for a Non-Participant Party as Swaption Buyer, such Non-Participant Party.

ICC proposes to describe the exercise and assignment process in paragraph 2 of the Exercise Procedures. In paragraph 2.1, ICC states that exercise notices would be delivered in accordance with the ICC Rules and the Exercise Procedures and specifically references Subchapter 26R of the Rules related to Index Swaptions.

Paragraph 2.2 of the proposed Exercise Procedures would address the procedures for exercise and assignment of Index Swaptions. The document sets forth ICC’s process of netting all open positions in such expiring Index Swaption, which takes place on the business day prior to the expiration date of an Index Swaption and applies to house and client origin accounts. To exercise an Index Swaption, the Exercising Party would deliver an exercise notice to ICC during the Exercise Period specifying the notional amount being exercised (“Exercised Notional Amount”). ICC may also establish a Pre-Exercise Notification Period during which an Exercising Party may submit, modify, and/or withdraw preliminary exercise notices. The submission of an exercise notice during the Exercise Period will be irrevocable and binding on the Exercising Party and, once validated by ICC, will be accepted by ICC and binding on ICC and the Exercising Party (and, in the case of a Non-Participant Party, its Participant). If ICC rejects an exercise notice as not valid, as described in the Exercise Procedures, it will inform the submitting party, who may resubmit a corrected notice within the Exercise Period. For informational purposes only, within the Exercise Period, ICC may estimate and provide the notional amount that it will assign to each open position in an Index Swaption of a Swaption Seller. Moreover, if an Exercising Party did not submit an exercise notice but submitted a preliminary exercise notice in respect of such Index Swaption that was not withdrawn, the Exercising Party will be deemed to have submitted an exercise notice with the Exercised Notional Amount specified under such preliminary notice. After the Exercise Period ends, ICC will determine final assignments to open positions in Index Swaptions of Swaption Sellers and notify Participants as described in the Exercise Procedures.

The proposed Exercise Procedures would address limitations and clarifications regarding the exercise process. Paragraph 2.3 sets out certain limitations, including limitations that ICC may impose during the Exercise Period and limitations as to the responsibility for any failure to exercise an Index Swaption. Paragraph 2.4 further clarifies the party that is entitled to exercise. A Participant is not entitled to provide a preliminary exercise notice or exercise notice on behalf of Non-Participant Parties for which it carries Index Swaptions. A Non-Participant Party will only be permitted to exercise an Index Swaption in a portfolio belonging to the Non-Participant Party. Additionally, under paragraph 2.4, a Participant may make certain elections as a result of a default or termination event with respect to a Non-Participant Party

³ Subchapter 26R of the Rules was proposed in the Swaption Rule Filings. Submission Number 1907-1516-4754-53, dated July 15, 2019.

for which it carries an Index Swaption, and is required to obtain the agreement of each Non-Participant Party for which it carries an open position in Index Swaptions to the provisions of the Rules and Exercise Procedures applicable to Index Swaptions.

The proposed Exercise Procedures would describe the Exercise System and provide the steps that ICC would follow in case of technical issues. Paragraph 2.5 explains the Electronic Notice Process which is the process for the electronic delivery and assignment of exercise notices or preliminary exercise notices through the Exercise System. Exercise notices would only be submitted through the Exercise System pursuant to the Electronic Notice Process, unless otherwise determined by ICC pursuant to paragraph 2.6. Namely, in the event of an Exercise System Failure affecting an Exercise Period, paragraph 2.6 provides ICC with the following options: (i) cancel and reschedule the Exercise Period, (ii) determine that automatic exercise will apply; and/or (iii) take such other action as ICC determines appropriate to permit Exercising Parties to submit exercise notices and to permit ICC to assign such notices. Paragraph 2.7 would address the situation where an Exercising Party is affected by a significant communications or information technology failure making it impossible or impractical to deliver all, or substantially all, of its exercise notices in accordance with the Electronic Notice Process during the Exercise Period (“Party Communication Failure”). Paragraph 2.8 would address the situation where Index Swaptions will be automatically exercised on the expiration date due to an Exercise System Failure.

II. Rule Amendments

ICC proposes to amend ICC Rule 304 related to offsets to incorporate a reference to the Exercise Procedures. Specifically, ICC proposes a change to ICC Rule 304(a) to clarify that netting of applicable offsetting positions in Index Swaptions would be subject to any provisions in the Exercise Procedures.

Core Principle Review:

ICC reviewed the DCO core principles (“Core Principles”) as set forth in the Act. During this review, ICC identified the following Core Principles as being impacted:

Risk Management: The Exercise Procedures and the change to the ICC Rules are consistent with the risk management requirements of Core Principle D. As discussed above, the Exercise Procedures would provide further detail as to the manner in which Index Swaptions may be exercised by Swaption Buyers and the manner in which ICC will assign such exercises to Swaption Sellers. Moreover, ICC sets out procedures in the document that are designed to protect users in the event of technical issues or technology failures, including circumstances where there is an Exercise System Failure and Party Communication Failure. The 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 related update to Rule 304(a) clarifies that netting of applicable offsetting positions in Index Swaptions would be subject to any provisions in the Exercise Procedures. ICC believes that the Exercise Procedures and the revision to the ICC Rules would thus ensure that ICC possesses the ability to manage the risks associated with discharging its responsibilities.

System Safeguards: The Exercise Procedures and the update to the ICC Rules are consistent with the system safeguards requirements of Core Principle I. The Exercise Procedures would allow ICC to manage the operational risks associated with the exercise and assignment process by establishing procedures for the exercise and assignment of Index Swaptions, which would allow ICC to identify and minimize sources of operational risks. The amendment to the Rules further incorporates reference to the Exercise Procedures into Rule 304(a). The Exercise Procedures include procedures for validating and rejecting exercise notices and procedures for exercise in the event of technical issues or technology failures. Such procedures are designed to provide sound alternatives in the case of technical issues and help mitigate the impact from technical issues to ensure that the system is reliable, secure and has adequate scalable capacity.

Public Information: The Exercise Procedures and the amendment to the ICC Rules are consistent with the public information requirements of Core Principle L. The ICC Rules are currently publically available

and the Exercise Procedures would be publically available, thus enabling market participants to identify and evaluate any risk and costs associated with using ICC's services.

Legal Risk: The Exercise Procedures and the change to the ICC Rules are consistent with the requirements of Core Principle R and Commission Regulation 39.27. The Exercise Procedures are intended to supplement the provisions of Subchapter 26R of the Rules with respect to Index Swaptions and would further ensure that ICC's Rules clearly reflect the terms and conditions applicable to Index Swaptions. The revision to the Rules consists of an update to Rule 304(a) to clarify that netting of applicable offsetting positions in Index Swaptions would be subject to any provisions in the Exercise Procedures. ICC does not believe that these changes will adversely impact its ability to comply with any Core Principles or Commission regulations.

Amended Rules:

ICC proposes to formalize the ICC Exercise Procedures and to amend the ICC Rules.

Annexed as Exhibits hereto are the following:

- A. Proposed ICC Exercise Procedures
- B. Proposed amendments to the ICC Rules

Certifications:

ICC hereby certifies that the ICC Exercise Procedures and the amendment to the ICC Rules comply with the Act and the regulations thereunder. There were no substantive opposing views to these changes.

ICC further certifies that, concurrent with this filing, a copy of the submission was posted on ICC's website, and may be accessed at: <https://www.theice.com/clear-credit/regulation>

ICC would be pleased to respond to any questions the Commission or the staff may have regarding this submission. Please direct any questions or requests for information to the attention of the undersigned at (312) 836-6854.

Sincerely,



Maria Alarcon
Staff Attorney