



Maria Alarcon
Staff Attorney

December 2, 2021

Re: Updates to ICC Rules and ICC Exercise Procedures 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 of changes to the ICC Clearing Rules (the “Rules”) and Exercise Procedures¹ in connection with the clearing of credit default index swaptions (“Index Swaptions”).² 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 revising the Rules and the Exercise Procedures related to the clearing of Index Swaptions.³ This submission includes a description of the changes to the Rules and the Exercise Procedures. Certification of the changes pursuant to Section 5c(c)(1) of the Act and Commission Regulation 40.6(a) is also provided below.

The proposed changes to the ICC Rules and Exercise Procedures enhance the restructuring component of iTraxx Index Swaptions and include other clarifications or updates, including with respect to fallback measures in the Exercise Procedures. The proposed revisions are described in detail as follows.

I. Rule Amendments

The proposed amendments revise Rule 26R-319, which addresses procedures for settlement of an exercised Index Swaption. ICC proposes clarifications to Rule 26R-319(b), under which additional settlements may be required. The proposed changes add a parenthetical with an exception and specify that

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

² Index Swaptions are also referred to in ICC’s policies and procedures as “index options” or “index CDS options”, or in similar terms.

³ 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.



clause (i) regarding the settlement of amounts owed is subject to any modification with respect to fixed rate payments or accrual rebates as specified by ICC Circular.

ICC proposes to revise Rule 26R-319(c) to amend the restructuring component of iTraxx Index Swaptions. Currently, the iTraxx Index Swaption delivers a single name position in addition to the re-versioned underlying index. For bilateral iTraxx Index Swaptions, counterparties to Index Swaption contracts on the restructured single name decide what the Index Swaption will deliver in the future if exercised/assigned: single name physical position, buyer triggered auction cash payment, or seller triggered auction cash payment. Following the changes, the cleared iTraxx Index Swaption would deliver a blend of all three outcomes such that the cleared instrument would more closely replicate the payout of the bilateral instrument.

Namely, under the amendments, the blended deliverables apply for iTraxx Index Swaption expiries on or after the auction settlement date, such that the Index Swaption delivers a re-versioned underlying index plus a blend of cash payment and single name. In subsection (c), ICC proposes minor updates in introducing Existing Restructuring as a defined term. Clause (ii) continues to discuss the Underlying New Trade that comes into effect⁴ and includes a reference to new clause (v). Clause (iii) would be amended and divided into two clauses. Amended clause (iii) discusses the treatment of the Underlying New Trade described in clause (ii) if the expiration date occurs prior to commencement of the CEN Triggering Period (as defined in the Restructuring Procedures)⁵ for the Existing Restructuring. New clause (iv) discusses the treatment of the Underlying New Trade described in clause (ii) if the expiration date occurs on or following the commencement of such period but prior to the auction settlement date.

Proposed clause (v) sets out the framework for the blended deliverables and would be applicable if the expiration date occurs on or following the auction settlement date. The proposed language requires ICC to (1) determine the extent to which positions in relevant single name contracts of the relevant tenor referencing the reference entity subject to the Existing Restructuring are settled; (2) determine, if applicable, a cash settlement amount with respect to the corresponding portion of the notional amount of the Index Swaption applicable to such reference entity; and (3) with respect to the remaining portion of such notional amount, an Underlying New Trade to come into effect. Additional specifications with respect to the Underlying New Trade and a reference to the Exercise Procedures or other applicable procedures are included.

II. Exercise Procedures Amendments

The Exercise Procedures supplement the provisions of Subchapter 26R of the Rules with respect to Index Swaptions. The proposed amendments define Minimum Intrinsic Value in paragraph 1 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 may 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. ICC would incorporate this term in respect of fallback provisions described in paragraphs 2.2(e)(ii) and 2.8. Specifically, ICC would take into account any applicable Minimum Intrinsic Value as part of its procedures for the pre-exercise notification period (during which preliminary exercise notices can be submitted, modified, and/or withdrawn) in paragraph 2.2(e)(ii) and for automatic exercise in paragraph 2.8. The proposed changes further specify that an “in the money” determination will be based on intrinsic value. In general, if intrinsic value is greater than the Minimum Intrinsic Value, the position will be exercised.

⁴ 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.

⁵ ICC Restructuring Procedures available at:
https://www.theice.com/publicdocs/clear_credit/ICE_Clear_Credit_Restructuring_Procedures.pdf.



ICC proposes paragraph 3, which would apply in connection with Rule 26R-319(c)(v) where an Existing Restructuring has occurred with respect to a reference entity underlying an exercised Index Swaption and the Index Swaption expiration date occurs on or following the auction settlement date. Paragraph 3 provisions may be modified or supplemented pursuant to ICC Circular, as specified in paragraph 3.1.

Paragraph 3.2 would set out the determination of settled portions. The proposed changes define Relevant CDS Transactions as single name contracts in the relevant reference entity cleared at ICC and such others as ICC may specify by Circular. ICC would determine the portion of the aggregate notional amount of Relevant CDS Transactions for which an eligible party timely delivered a credit event notice (“Triggered Portion”) and the portion as to which no such notice was timely delivered (“Untriggered Portion”). With respect to the Triggered Portion, paragraph 3.2 defines the Buyer and Seller Triggered Portions as the portions for which the protection buyer or seller delivered certain notices (i.e., prevailing credit event notice, prevailing notice to exercise movement option). The portion for which a movement option was applicable but for which neither protection buyer nor seller delivered a notice to exercise would be the Unmoved Portion, and together with the Untriggered Portion, the Untriggered/Unmoved Portion. ICC may establish by Circular a threshold pertaining to the Untriggered/Unmoved Portion under paragraph 3.2. This paragraph also sets out how the Buyer Triggered, Seller Triggered and Untriggered/Unmoved Portions are defined as percentages, namely the Buyer Triggered, Seller Triggered, and Untriggered/Unmoved Percentages.

Paragraph 3.3 would discuss settlement in respect of an exercised Index Swaption to which Rule 26R-319(c)(v) applies. Subsection (a) sets forth ICC’s determination of the cash settlement amount owed pursuant to Rule 26R-319(c)(v)(2). ICC would sum the settlement amounts in cash applicable to the Buyer and Seller Triggered Portions, which would be calculated based on the Relevant Notional Amount (i.e., the notional amount under the Index Swaption applicable to such reference entity) multiplied by the Buyer and Seller Triggered Percentages. The cash settlement amount may be adjusted to take into account applicable fixed payments and accrual rebates as specified by ICC Circular. Under subsection (b), the notional amount of the Underlying New Trade established under Rule 26R-319(c)(ii) and (v)(3) would be the Relevant Notional Amount multiplied by the Untriggered/Unmoved Percentage.

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 amendments to the Rules and the Exercise Procedures are consistent with the risk management requirements of Core Principle D. The changes support the clearing of Index Swaptions by ICC, including by enhancing the restructuring component of iTraxx Index Swaptions and making other clarifications or updates, to ensure that the Rules and Exercise Procedures clearly and accurately reflect the requirements and procedures applicable to iTraxx Index Swaptions and Index Swaptions more generally. The changes enhance the restructuring component such that the cleared instrument more closely replicates the payout of bilateral instruments, which would provide additional consistency to market participants. ICC believes that the proposed revisions would continue to ensure that ICC possesses the ability to manage the risks associated with discharging its responsibilities.

Settlement Procedures: The amendments to the Rules and the Exercise Procedures are consistent with the requirements of Core Principle E and Commission Regulation 39.14. The Rules continue to clearly set out the procedures for settlement of Index Swaptions on exercise. Moreover, the amended Exercise Procedures clearly set out procedures associated with the determination of the cash settlement amount owed pursuant to Rule 26R-319(c)(v)(2) and the notional amount of the Underlying New Trade established under Rule 26R-319(c)(ii) and (v)(3). The Rules and Exercise Procedures continue to enable ICC to identify and manage the risks of settlement of Index Swaptions on exercise.



System Safeguards: The amendments to the Rules and the Exercise Procedures are consistent with the system safeguards requirements of Core Principle I. The enhanced restructuring component avoids introducing unnecessary complexity or operational risk. Moreover, the Exercise Procedures 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 and including fallback measures, which help mitigate the impact from operational or technical issues. ICC's procedures continue to help mitigate the impact from technical issues to ensure that the system is reliable, secure and has adequate scalable capacity.

Public Information: The changes to the Rules and the Exercise Procedures are consistent with the public information requirements of Core Principle L. The Rules and the Exercise Procedures are currently publicly available on ICC's website, thus enabling market participants to identify and evaluate any risk and costs associated with using ICC's services.

Legal Risk: The changes to the Rules and the Exercise Procedures are consistent with the requirements of Core Principle R and Commission Regulation 39.27. The Exercise Procedures supplement the provisions of Subchapter 26R of the Rules with respect to Index Swaptions and further ensure that ICC's Rules clearly reflect the terms and conditions applicable to Index Swaptions. The proposed changes would continue to support the legal basis for ICC's clearance of Index Swaptions and operation of the exercise and assignment process.

Amended Rules:

The proposed changes consist of amendments to the Rules and the Exercise Procedures.

Annexed as Exhibits hereto are the following:

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

Certifications:

ICC hereby certifies that the changes comply with the Act and the regulations thereunder. There were no substantive opposing views to the 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,

A handwritten signature in black ink that reads "Maria Alarcon". The signature is written in a cursive, flowing style.

Maria Alarcon
Staff Attorney