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OFFICE OF THE SECRETARIAT

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**RULE SELF-CERTIFICATION**

November 10, 2010

Office of the Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st St., N.W.
Washington, D.C. 20581

Re: International Derivatives Clearinghouse, LLC
Reference File: SR-IDCH-2010-09

Ladies and Gentlemen:

Pursuant to Section 40.6 of the regulations promulgated by the Commodity Futures Trading Commission (the "CFTC Rules") under the Commodity Exchange Act, as amended (the "Act"), International Derivatives Clearinghouse, LLC ("IDCH"), a derivatives clearing organization registered under the Act, hereby submits this self-certification to:

1. Amend IDCH's Risk Management Procedures to:

   (i) incorporate the payment of price alignment interest ("PAI") into Variation Performance Bond for OTC Contracts,

   (ii) amend the list of currently acceptable Collateral; and

   (iii) make other clarifying changes.

2. Issue a Notice to Members to notify Clearing Members of the changes to the Risk Management Procedures.

The intended date of implementation of this amendment is November 15, 2010 (the "Effective Date").

Currently under IDCH's Risk Management Procedures, IDCH's Risk Management Department monitors the positions held by each Clearing Member throughout the day, and officially revalues such positions twice a day. The revaluation process relies on the construction of a blended interest rate curve to generate discount factors for any point along the curve. The resulting net present value of the cash flows determines the value, or mark-to-market, of the interest rate swap or interest rate swap future. Variation Performance Bond is calculated using the same revaluation for both classes of Clearing Members: Exchange Clearing Members and OTC Clearing Members.

Beginning on the Effective Date, in order to more accurately reflect the current practice in the over-the-counter interest rate swap market, IDCH will apply a price alignment interest (PAI) adjustment for OTC Contracts cleared by OTC Clearing Members. The calculation used to define PAI will be set forth in the Risk Management Procedures and in the attached Notice to Members.

Currently, IDCH's list of acceptable Collateral includes USD Cash, USD Treasury Securities and US Agency Debt Securities, Mortgage Backed Securities Guaranteed by US Agencies, and non-US Government Securities. Pursuant to IDCH's Rules 608 and 609 (Cash and Non-Cash Performance Bond Deposits), upon approval of IDCH's Risk Committee, IDCH can expand the types of cash and non-cash Performance Bond deposits that are accepted by IDCH.

Beginning on the Effective Date, IDCH will accept foreign cash as acceptable Collateral, consisting of cash denominated in Canadian dollars, Euros, Japanese Yen, Pound Sterling and Swiss Francs, subject to a minimum 5% haircut based on the market value or such larger haircuts as determined by IDCH. Also, on such date, IDCH will accept foreign sovereign debt as acceptable Collateral, consisting of bills, notes and bonds that have a time to maturity of 10 years or less issued by Canada, France, Germany and Great Britain denominated in either the issuers' home country or US dollars subject to such haircuts based on the market value that shall be determined by IDCH from time-to-time. Clearing Members will be permitted to satisfy up to 25% of their Performance Bond requirement with foreign sovereign debt.

The text of the proposed amendments (showing deletions and additions) are attached hereto. There were no opposing views among IDCH's Board of Directors, Clearing Members or market participants. IDCH hereby certifies that this amendment to the IDCH Risk Management Procedures comply with the Act and the CFTC Rules.

Regards,

Michael Dundon

Michael Dundon
Chief Risk Officer

Attachment

cc: Ananda Radhakrishnan
Nancy Schnabel
Robert Wasserman

**International Derivatives Clearinghouse, LLC**
**Reference File: SR-IDCH-2010-09**
**Amendment to Risk Management Procedures**

## VARIATION PERFORMANCE BOND

Throughout the trading day, but officially twice daily, the Risk Management Department revalues the positions held by each Clearing Member. The revaluation process relies on the construction of a blended interest rate curve to generate discount factors for any point along the curve. The resulting net present value of the cash flows (fixed side and floating side in the case of an interest rate swap future) determines the value, or mark-to-market of the interest rate swap future. The Clearinghouse debits the Clearing Member's designated bank cash account to realize (collect) any losses during the trading day. Prior day gains in value are paid once per day in the first (morning) banking process.

The blended yield curve is constructed by bootstrapping a set of quoted benchmark rates and various financial contract prices to create zero coupon discount factor curves. The bootstrapping process begins with the shortest term swap future contract and steps through them all in ascending order of maturity. At every step, discount factors from the preceding swap future contracts are used to determine the discount factor for the current one. The curve generation process strips each swap future contract into its individual cash flows and then prices it using zero coupon pricing.

The Clearinghouse uses the following elements to construct its revaluation curve:

- Deposit Rates
- Forward Rate Agreement Rates
- Swap market rates

A document describing the methodology for generating the curve is made available to the Clearing Members. The current and historic curve data are available to Clearing Members on the password protected "SwapDrop" section of the Clearinghouse Website. As new products are added, the revaluation curve methodology will be reviewed for its applicability and suitability to the risks taken by the Clearinghouse.

Variation margin is calculated using the same revaluation for both classes of Clearing Members: Exchange Clearing Members and OTC Clearing Members. However, in order to more accurately reflect the current practice in the over-the-counter interest rate swap market, the Clearinghouse applies a Price Alignment Interest (PAI) adjustment for those transactions cleared by OTC Clearing Members in the OTC account class. The PAI adjustment is calculated using the following formula:

**PAI = -1* (mtmPrevClose * overnightIndexRate * overnightPeriod / dayCount)**

Where:

- mtmPrevClose = Aggregate MTM for the account at the previous close based on the IDCG Official EOD Curve
- overnightIndexRate = Index rate for the payment currency for current business date (USD: US Fed Funds O/N)
- overnightPeriod = (followingBusinessDate - businessDateToday) in calendar days
- dayCount = Denominator of day count convention for currency (USD: 360)

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**PERFORMANCE BOND COLLATERAL**

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***Current Acceptable Collateral***

The acceptable forms of collateral for the Clearinghouse will be determined by the Risk Management Department, approved by the Chief Executive Officer, and published on the Clearinghouse website. The Clearinghouse reserves the right not to accept or to discontinue to accept any of the following forms of acceptable collateral. The acceptable forms of collateral are limited to:

1. USD Cash: Clearing members can satisfy up to 100% of their Performance Bond requirement with USD Cash;

2. Foreign Cash: Permissible foreign cash shall include Canadian Dollars, Euro, Japanese Yen, Pound Sterling and Swiss Francs subject to a minimum 5% haircut based on the market value or such larger haircuts as determined by the Clearinghouse. Clearing members can satisfy up to 100% of their Performance Bond requirement with Foreign Cash;

3. USD Treasury Bills, Notes and Bonds ("US Treasury Securities") that have a time to maturity of 10 years or less subject to such haircuts based on the market value that shall be determined by the Clearinghouse from time-to-time;

4. Foreign Sovereign Debt: Bills, Notes and Bonds that have a time to maturity of 10 years or less issued by Canada, France, Germany and Great Britain denominated in either the issuers home currency or US Dollars subject to such haircuts based on the market value that shall be determined by the Clearinghouse from time-to-time. Clearing members can satisfy up to 25% of their Performance Bond requirement with Foreign Sovereign Debt;

5. US Agency Debt Securities which shall include bills, notes and bonds directly issued by Fannie Mae, Freddie Mac, the Federal Home Loan Bank and the Federal Farm Credit Bank that have a time to maturity of 10 years or less subject to such haircuts that shall be determined by the Clearinghouse from time-to-time;

<u>6.</u> Mortgage Backed Securities ("MBS") Guaranteed by US Agencies that have a remaining time to maturity of 10 years or less. All MBS will be subject to a minimum 10% haircut based on the market value <u>or such larger haircuts as determined by the Clearinghouse</u>~~, as solely determined by IDCH~~ and shall be limited to the following MBS:

a. Fannie Mae Megas and MBS that are guaranteed by Fannie Mae:
b. Freddie Mac Gold PCs and Giants that are guaranteed by Freddie Mac: and,
c. Ginnie Mae I and Ginnie II that are guaranteed by Ginnie Mae:

Clearing members can satisfy up to 25% of their Performance Bond requirement with securities issued or guaranteed by a single US Agency issuer. When calculating the 25% concentration limit all securities issued and guaranteed by the US Agency will be applied to the 25% concentration limit.

This concentration limitation shall be separately applied to the Clearing Member's House Performance Bond requirement, the Clearing Member's CFTC Customer Segregated Performance Bond requirement and the Clearing Member's OTC Customer Sequestered Performance Bond requirement.

<u>7.</u> Non-US Government Securities

The Clearinghouse will accept the following Non-US Government Securities as acceptable Performance Bond Collateral;

a. Municipal Securities that are general obligations of any State or any political subdivision of the United States;
b. Certificate and Time Deposits ("Bank Deposits") issued by a bank as defined in section 3(a) (6) of the Securities Exchange Act of 1934, or a domestic branch of a foreign bank that carries deposits insured by the Federal Deposit Insurance Corporation and there is secondary market for the Bank Deposits and the Bank Deposits are settled via the Depository Trust & Clearing Corporation ("DTCC").
c. Commercial paper with a time to maturity of 270 days or less;
d. Corporate Debt Securities that are senior debt including notes, bonds, debentures, demand instruments and asset backed securities; and
e. Sovereign Debt Securities that are general obligations of Australia, ~~Canada, France, Germany,~~ Japan, the Netherlands ~~,~~ <u>or</u> Switzerland ~~or the United Kingdom~~ and are denominated in US Dollars.

The Clearinghouse shall maintain a list of acceptable <u>Non-US Government Securities</u> ~~security~~ issuers and issues in its Security Master File ("SM<u>F</u>~~FM~~") and will provide the SM<u>F</u>~~FM~~ to the Clearinghouse's Clearing Members. The

Clearinghouse will only accept Non-US Government Securities that are listed in the SMF.

In order to be placed in the Clearinghouse's SMF, a Non-US Government Security;

a. Must have either two acceptable long-term or short-term ratings from two acceptable rating agencies. Acceptable rating agencies include Moody's, S&P and Fitch. The minimum acceptable long-term rating for Moody's is Aa3, for S&P it is AA- and for Fitch it is AA-. The minimum short-term rating for Moody's is P-1, for S&P it is A-1 and for Fitch it is F1. Securities that have the minimum rating requirement and are on "negative watch" or have one rating that meets the above cited minimum rating with the second rating below the above cited minimum rating ("split-rated securities") will not be accepted;

b. With the exception of commercial paper, securities are to have a maximum time to maturity of 5 years. Acceptable commercial paper is to have a maximum time to maturity of 270 days;

c. The security must be activity priced on Bloomberg. As defined by Securities Exchange Commission ("SEC") Rule 15c-13-1(c) 11, there must be a "Ready Market" for the securities. Ready Market is defined as a recognized established securities market in which there exists independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bone fide competitive bid and offer quotation can be determined for a particular security almost instantaneously and where payment will be received in settlement of a sale at such price within a relative short time conforming to trade custom;

d. Securities that meet the above requirement but do not pass the Clearinghouse's qualitative review shall not be acceptable;

Securities that are issued by a Clearinghouse Clearing Member or an affiliate of the Clearing Member will not be accepted.

Non-Government Securities can be removed from the SMF without notice and any removed security weill be assigned no value in satisfaction of a Clearing Member's Performance Bond requirement.

Clearing Members can satisfy up to 25% of their Performance Bond requirement with Non-Government Securities. This limitation shall be separately applied to the Clearing Member's House Performance Bond requirement, the Clearing

Member's CFTC Customer Segregated Performance Bond requirement and the Clearing Member's OTC Customer Sequestered Performance Bond requirement.

Non-Government Securities will be held in a Clearinghouse custody account at Non-Government Securities custodians selected by the Risk Management Department and approved by the Chief Executive Officer.

IDCG
INTERNATIONAL DERIVATIVES CLEARING GROUP

International Derivatives Clearing Group, LLC
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5th Floor
New York, NY 10022
212.933.9800 office
212.933.9801 fax
www.IDCG.com

IDCH Notice to Members No. 0003-10

## Notice to Members

TO: Clearing Members of the International Derivatives Clearinghouse, LLC
FROM: Risk Management Department
SUBJECT: Payment of Price Alignment Interest (PAI) into Variation Performance Bond for OTC Contracts Cleared by OTC Clearing Members

DATE: November 15, 2010

Please be advised that beginning today, in order to more accurately reflect the current practice in the over-the-counter interest rate swap market, IDCH will apply a price alignment interest (PAI) adjustment for OTC Contracts cleared by OTC Clearing Members.

The PAI adjustment is calculated using the following formula:

**PAI = -1* (mtmPrevClose * overnightIndexRate * overnightPeriod / dayCount)**

Where:

- mtmPrevClose = Aggregate MTM for the account at the previous close based on the IDCG Official EOD Curve
- overnightIndexRate = Index rate for the payment currency for current business date (USD: US Fed Funds O/N)
- overnightPeriod = (followingBusinessDate - businessDateToday) in calendar days
- dayCount = Denominator of day count convention for currency (USD: 360)

If you have any questions, please contact:

Michael Dundon 646-687-2528 Michael.Dundon@idcg.com

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IDCH Notice to Members No. 0004-10

## Notice to Members

TO: Clearing Members of the International Derivatives Clearinghouse, LLC
FROM: Risk Management and Treasury Departments
SUBJECT: Addition to List of Currently Acceptable Collateral

DATE: November 15, 2010

Please be advised that beginning today, IDCH will accept foreign cash as acceptable Collateral, consisting of cash denominated in Canadian dollars, Euros, Japanese Yen, Pound Sterling and Swiss Francs, subject to a minimum 5% haircut based on the market value or such larger haircuts as determined by IDCH. Also, beginning today, IDCH will accept foreign sovereign debt as acceptable Collateral, consisting of bills, notes and bonds that have a time to maturity of 10 years or less issued by Canada, France, Germany and Great Britain denominated in either the issuers' home country or US dollars subject to such haircuts based on the market value that shall be determined by IDCH from time-to-time. Clearing Members will be permitted to satisfy up to 25% of their Performance Bond requirement with foreign sovereign debt.

If you have any questions, please contact:

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|---|---|---|
| Michael Dundon | 646-867-2528 | Michael.Dundon@idcg.com |
| Robert Push | 646-867-2538 | Robert.Push@idcg.com |