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December 21, 2011

**FOIA Confidential Treatment Request**

Assistant Secretary of the Commission for FOIA Matters  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, NW  
Washington, DC 20581

Re: FOIA Confidential Treatment Request and Detailed Written Justification –  
International Derivatives Clearinghouse, LLC Rule Certification IDCH-2011-04

Dear Secretary:

I am writing on behalf of International Derivatives Clearinghouse, LLC (the "Clearinghouse") to request confidential treatment in accordance with CFTC Regulations 40.8(c) and 145.9 for certain confidential information contained in the Clearinghouse's Rule Certification IDCH-2011-04 (the "Submission").

Specifically, the Clearinghouse is requesting confidential treatment for Confidential Appendix C to the Submission, which contains the Clearinghouse's proprietary Risk Management Procedures (the "Confidential Information"), which has been segregated and attached as Confidential Appendix C to the Submission in accordance with Commission Regulation 40.8(c)(2). In accordance with Commission Regulation 40.8(c)(3), the Submission also indicates that the Confidential Information has been segregated.

Pursuant to Commission Regulation 145.9(d), the Clearinghouse requests that confidential treatment be maintained for the Confidential Information until further notice. We also request that the Commission notify the undersigned immediately after receiving any FOIA request for the Confidential Information or any other court order, subpoena or summons for same. Finally, we request that we be notified in the event the Commission intends to disclose the Confidential Information to Congress or to any other governmental agency or unit pursuant to Section 8 of the CEA. The Clearinghouse does not waive its notification rights under Section 8(f) of the CEA with respect to any subpoena or summons for the Confidential Information.

The basis for this confidential treatment request is that disclosure of the Confidential Information would reveal confidential commercial information of the Clearinghouse relating to its risk management procedures, performance bond methodology, and curve construction methodology. This information is not made generally available to the public and has only been provided to regulators, clearing members and potential clearing members that sign a confidentiality agreement with respect to such information. The disclosure of the Confidential Information to the public would cause competitive harm to the Clearinghouse as it would allow competitors of the Clearinghouse to replicate its proprietary risk management methodologies.

The Confidential Information is therefore exempt from disclosure pursuant to Section 8 of the CEA, Section (b)(4) of the Freedom of Information Act (5 USC 552(b)(4)) (commonly referred to as "Exemption 4"), which exempts from disclosure "trade secrets and commercial or financial information obtained from a person and privileged or confidential," and Commission Regulation 145.9(d)(ii), which implements Exemption 4.

Exemption 4 is generally viewed to cover two broad categories of information in federal agency records: (1) trade secrets; and (2) information that is (a) commercial or financial, and (b) obtained from a person, and (c) privileged or confidential.

The Court of Appeals for the District of Columbia Circuit has firmly held that the terms "commercial and financial" should be given their "ordinary meanings" and has specifically rejected the argument that the term "commercial" be confined to records that "reveal basic commercial operations," holding instead that records are commercial so long as the submitter has a "commercial interest" in them.<sup>1</sup> As described above, the Clearinghouse has a "commercial interest" in the Confidential Information.

Only information "obtained from a person" is included under Exemption 4. The Clearinghouse is a person, as the term "person" includes entities such as corporations.<sup>2</sup>

There is a presumption of confidentiality for commercial information that is (1) provided voluntarily and (2) is of a kind the provider would not customarily make available to the public.<sup>3</sup> The Clearinghouse provided the Confidential Information to the Commission voluntarily in connection with the Submission in order to demonstrate to the Clearinghouse's compliance with the CEA and relevant Commission Regulations. Further, as discussed above, the Confidential Information is not customarily made available to the public by the Clearinghouse.

Notwithstanding this presumption of confidentiality, the Confidential Information still would be considered "confidential" because it is information that the Clearinghouse would not and have not disclosed to the public and its disclosure would cause substantial harm to the competitive position of the Clearinghouse.<sup>4</sup> In applying the "competitive harm" test for confidentiality, there is no requirement to demonstrate actual competitive harm.<sup>5</sup> "Actual competition and the likelihood of substantial competitive injury is all that need to be shown."<sup>6</sup> Neither the Commission nor the courts must conduct a sophisticated economic analysis to determine the likely effects of disclosure; evidence demonstrating the *potential* for economic harm is sufficient.<sup>7</sup>

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<sup>1</sup> Pub. Citizen Health Research Group v. FDA, 704 F.2d 1280, 1290 (D.C. Cir. 1983) (citing Wash. Post Co. v. HHS, 690 F.2d 252, 266 (D.C. Cir. 1982), and Bd. of Trade v. Commodity Futures Trading Comm'n, 627 F.2d 392, 403 (D.C. Cir. 1980)); accord Judicial Watch, Inc. v. United States Dep't of Energy, No. 01-0981, 2004 WL 635180, at \*24 (D.D.C. Mar. 31, 2004) (holding that reports that "constitute work done for clients" are "'commercial' in nature"), stay pending appeal on other grounds granted (May 26, 2004); Brockway v. Dep't of the Air Force, 370 F. Supp. 738, 740 (N.D. Iowa 1974) (concluding that reports generated by commercial enterprise "must generally be considered commercial information"), rev'd on other grounds, 518 F.2d 1184 (8th Cir. 1975).

<sup>2</sup> Stone v. Export-Import Bank, 552 F.2d 132 (5<sup>th</sup> Cir. 1977), cert. denied, 434 U.S. 1012 (1978).

<sup>3</sup> See Critical Mass Energy Project v. Nuclear Regulatory Commission, 975 F.2d 871, 878 (D.C. Cir. 1992) (en banc); see also Center for Auto Safety v. National Highway Traffic Safety Administration, 244 F.3d 144, 147 (D.C. Cir. 2001) (affirming continuing validity of Critical Mass and applying tests detailed in that case).

<sup>4</sup> National Parks & Conservation Association v. Morton, 478 F.2d 765 (D.C. Cir. 1974).

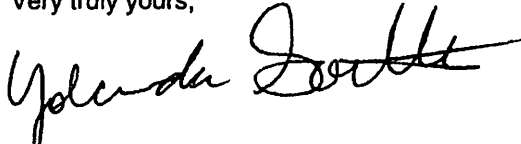
<sup>5</sup> Gulf & Western Indus., Inc. v. United States, 615 F.2d 527, 530 (D.C. Cir. 1979).

<sup>6</sup> Id.

<sup>7</sup> Utah v. Bahe et al. No. 00-4018, 2001 WL 777034, at 2 (10<sup>th</sup> Cir. July 10, 2001); Pub. Citizen Health Research Group, 704 F.2d at 1291.

For the foregoing reasons, the Clearinghouse respectfully request that the Commission staff make an initial determination to maintain the confidentiality of the Confidential Information. Please contact me at 301.978.8486 if you have any questions regarding this matter or in the event that the Confidential Information becomes subject to inquiry.

Very truly yours,

A handwritten signature in black ink, appearing to read "Yolanda Goettsch", written in a cursive style.

Yolanda M. Goettsch

cc: Ananda Radhakrishnan  
Bob Wasserman  
Garry O'Connor  
Michael Dundon

## RULE SELF-CERTIFICATION

December 21, 2011

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

Re: International Derivatives Clearinghouse, LLC  
Reference File: IDCH-2011-04

Ladies and Gentlemen:

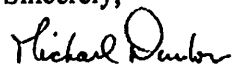
Pursuant to Section 5c(c)(1) of the Commodity Exchange Act, as amended (the "Act") and Section 40.6 of the regulations promulgated thereunder (the "CFTC Rules"), International Derivatives Clearinghouse, LLC ("IDCH"), a derivatives clearing organization registered under the Act, hereby submits this self-certification in connection with the following:

- To amend (i) Rule 101 to include swap execution facilities in the definition of Participating Trading Facility, (ii) Rule 301 to increase the minimum deposit in the Guaranty Fund for OTC Clearing Members from \$5 million to \$25 million, (iii) Rule 309 to decrease the minimum adjusted net capital requirement for OTC Clearing Members from \$300 million to \$50 million, (iv) Rule 512 to specify terms and conditions for the transfer of Customer positions from one Clearing Member to another Clearing Member, and (v) Rule 604 to amend the criteria for determining a Clearing Member to be in Default. IDCH is making these amendments to comply with the CFTC Rules that become effective on January 9, 2012.
- To adopt its Default Procedures. IDCH is adopting its Default Procedures to comply with the CFTC Rules that become effective on January 9, 2012.
- To amend its Risk Management Procedures to reflect the above rule changes and to include exhibits describing IDCH's curve construction methodology and describing IDCH's existing Historic Scenario Value-at-Risk (HS VaR) methodology for calculating Performance Bond.

The text of the proposed rule amendments (showing deletions and additions) are attached hereto as Appendix A. The IDCH Default Procedures are attached as Appendix B. The IDCH Risk Management Procedures (showing deletions and additions) are included separately as Confidential Appendix C hereto. IDCH is separately requesting confidential treatment for Confidential Appendix C.

There were no opposing views among IDCH's Board of Directors, Clearing Members or market participants. IDCH hereby certify that these rules comply with the Act and the CFTC Rules. IDCH further certifies that, concurrent with this filing, a notice of the pending certification (other than Appendix C, for which confidential treatment was requested) was posted on IDCH's website as well as a copy of the submission, which may be accessed at [http://idcg.com/pdfs/idch\\_bulletins/SR-IDCH-2011-04.pdf](http://idcg.com/pdfs/idch_bulletins/SR-IDCH-2011-04.pdf). The effective date of the rule amendments Default Procedures and amended Risk Management Procedures is January 9, 2012.

Sincerely,



Michael Dundon  
Chief Risk Officer

Attachments

**International Derivatives Clearinghouse, LLC**  
**Reference File: IDCH-2011-04**

**Appendix A**

**Rules**  
**of**  
**International Derivatives Clearinghouse, LLC**

As of January 9, 2012~~December 16, 201~~

## Chapter 1 Interpretation

### Rule 101. Definitions.

\* \* \* \* \*

“*Participating Trading Facility*” means a designated contract market, swap execution facility or foreign board of trade ~~or exempt board of trade~~ that has entered into an agreement with the Clearinghouse for the clearing of Exchange Contracts.

\* \* \* \* \*

## Chapter 3 Membership

### Rule 301. Categories of Membership

There shall be two categories of Clearing Members, Exchange Clearing Members and OTC Clearing Members, each with the following obligations and clearing privileges. A Clearing Member may be approved as both an Exchange Clearing Member and an OTC Clearing Member.

(a) Exchange Clearing Members.

(i) Each Exchange Clearing Member shall maintain a minimum deposit in the Guaranty Fund of \$2.5 million relating to its status as an Exchange Clearing Member.

(ii) An Exchange Clearing Member shall be entitled to clear Exchange Contracts through the Clearinghouse for its Proprietary Account and/or Exchange Customer Segregated Accounts, subject to the Rules.

(b) OTC Clearing Members.

(i) Each OTC Clearing Member shall maintain a minimum deposit in the Guaranty Fund of \$25.0 million relating to its status as an OTC Clearing Member.

(ii) An OTC Clearing Member shall be entitled to clear OTC Contracts through the Clearinghouse for its Proprietary Account and/or OTC Customer Segregated Accounts, subject to the Rules.

\* \* \* \* \*

### Rule 309. Capital Requirements

(c) An Exchange Clearing Member must at all times maintain adjusted net capital in excess of the greater of:



- (i) \$5,000,000;
  - (ii) Commission minimum regulatory capital requirements to the extent applicable to such Clearing Member; and
  - (iii) SEC minimum regulatory capital requirements to the extent applicable to such Clearing Member.
- (d) An OTC Clearing Member must at all times maintain adjusted net capital in excess of the greater of:
- (i) ~~\$300~~50,000,000;
  - (ii) Commission minimum regulatory capital requirements to the extent applicable to such Clearing Member; and
  - (iii) SEC minimum regulatory capital requirements to the extent applicable to such Clearing Member.
- (e) The Clearing Membership Committee may prescribe additional capital requirements with respect to any Clearing Member.

\* \* \* \* \*

## **Chapter 5**

### **Clearing of OTC Contracts**

\* \* \* \* \*

#### **Rule 512. Transfers of OTC Contracts**

- (a) An OTC Clearing Member may transfer an OTC Contract from one account carried by the Clearing Member to another account carried by the Clearing Member or to an account carried by another Clearing Member, upon written notice to the Clearinghouse in a form acceptable to the Clearinghouse, provided:
- (i) the underlying beneficial ownership in each such account remains the same;
  - (ii) an error has been made in the clearing of an OTC Contract and the error is discovered and the transfer is completed within two Business Days of the date the OTC Contract was submitted to the Clearinghouse for clearing;
  - (iii) the Clearinghouse, in its sole discretion, allows such transfer as a result of a merger or other business combination; or

(iv) the Clearinghouse, in its sole discretion, determines that such transfer is in the best interest of the Clearinghouse.

(b) The Clearinghouse shall transfer all or a portion of a Customer's OTC Contracts and related Performance Bond at the same time from one Customer Account carried by the Clearing Member to a Customer Account carried by another Clearing Member, provided:

(i) The Customer has instructed the carrying Clearing Member to make the transfer;

(ii) The Customer is not currently in default to the carrying Clearing Member;

(iii) The transferred OTC Contracts will have appropriate Performance Bond at the receiving Clearing Member;

(iv) Any remaining OTC Contracts will have appropriate Performance Bond at the carrying Clearing Member; and

(v) The receiving Clearing Member has consented to the transfer.

~~(b)(c)~~ Any such transferred OTC Contract transferred in accordance with paragraphs (a) or (b) shall be:

(i) Transferred without close-out and rebooking of the Contracts prior to transfer;

~~(i)(ii)~~ carried by the receiving Clearing Member as of the date the OTC Contract was submitted to the Clearinghouse for clearing; and

~~(i)(iii)~~ held open, or offset, as the case may be, in accordance with Rule 405.

~~(e)(d)~~ Each Clearing Member must maintain a full and complete record of all such transactions.

\* \* \* \* \*

## **Chapter 6 Settlement and Performance Bonds**

\* \* \* \* \*

### **Rule 604. Clearing Member Default**

(a) A Clearing Member ~~who (i) that fails to meet any of the Clearing Member's Obligations upon the Clearing Member's Contracts with the Clearinghouse after novation to the Clearinghouse, (ii) fails to deposit Performance Bond within one hour after demand by the Clearinghouse, (iii) that is suspended or expelled by the Clearinghouse or a Participating Trading Facility or by the Clearinghouse, (iii) that is~~

declared in default, suspended or expelled by another Derivatives Clearing Organization, clearing agency (as defined in the Securities Exchange Act of 1934, as amended), or other clearing organization, (iv) whose Settlement Bank notifies the Clearinghouse that it is ceasing to act as Settlement Bank for the Clearing Member or that the Clearing Member will not meet its Obligations, or (iv) is bankrupt or insolvent, is in Default. Upon such Default, the Clearinghouse may cause all Contracts of such Clearing Member (whether or not carried in an Exchange Customer Segregated Account as provided in Rule 412 or in an OTC Customer Segregated Account as provided in Rule 511) to be closed, netted or offset, transferred to any other Clearing Member, or otherwise resolved as deemed appropriate by the Clearinghouse and any debit balance owing to the Clearinghouse shall be immediately due and payable.

(b) In closing, netting, offsetting, transferring or otherwise resolving the Contracts of a Clearing Member as provided in paragraph (a) of this Rule, the Clearinghouse shall have the right:

(i) With respect to Exchange Contracts in an Exchange Customer Segregated Account of such Clearing Member provided for in Rule 412, to net and set off (A) any proceeds received by the Clearinghouse from the disposition of such Exchange Contract and any property or proceeds thereof deposited with or held by the Clearinghouse as Performance Bond for such account against (B) any amounts paid by the Clearinghouse in the disposition of such Exchange Contracts, including any commissions or other losses or expenses incurred in connection therewith or in connection with the liquidation of Performance Bond deposits in such account and any other amounts owed to the Clearinghouse as a result of transactions in the account or otherwise lawfully chargeable against the account;

(ii) With respect to OTC Contracts in an OTC Customer Segregated Account of such Clearing Member provided for in Rule 511, to net and set off (A) any proceeds received by the Clearinghouse from the disposition of such OTC Contract and any property or proceeds thereof deposited with or held by the Clearinghouse as Performance Bond for such account against (B) any amounts paid by the Clearinghouse in the disposition of such OTC Contracts, including any commissions or other losses or expenses incurred in connection therewith or in connection with the liquidation of Performance Bond deposits in such account and any other amounts owed to the Clearinghouse as a result of transactions in the account or otherwise lawfully chargeable against the account;

(iii) With respect to the Contracts in any other account of such Clearing Member, to net and set off (A) any proceeds by the Clearinghouse from the disposition of such Contracts, any property or proceeds thereof deposited with or held by the Clearinghouse as Performance Bond for such accounts, and any other property of the Clearing Member within the possession or control of the Clearinghouse other than property which has been identified by such Clearing Member as required to be segregated as provided for in Rule 412 or Rule 511, against (B) any amounts paid by the Clearinghouse in the disposition of such Contracts, including any commissions or other losses or expenses incurred in

connection therewith or in connection with the liquidation of Performance Bond deposits in such accounts, and any other Obligations of the Clearing Member to the Clearinghouse, including Obligations of the Clearing Member to the Clearinghouse remaining after the netting and setoffs referred to in paragraphs (b)(i) and (ii) of this Rule, and any Obligations arising from any other accounts maintained by the Clearing Member with the Clearinghouse;

(iv) To cause Contracts held in accounts of the Clearing Member that is in Default to be netted and offset against each other and, to the extent of any remaining imbalance, against the Contracts of other Clearing Members;

(v) To cause Contracts held in accounts of the Clearing Member that is in Default and of other Clearing Members to be settled at the Settlement Price for such Contracts, or at such other price or prices as the Clearinghouse may deem fair and reasonable in the circumstances; and

(vi) To defer closing or otherwise settling such Contracts if, in its discretion, it determines that the closing out of some or all of the suspended Clearing Member's Contracts would not be in the best interests of the Clearinghouse or other Clearing Members, taking into account the size and nature of the positions in question, market conditions prevailing at the time, the potential market effects of such liquidating transactions as might be directed by Clearinghouse, and such other circumstances as it deems relevant.

(c) Any Obligation of the Clearinghouse to a Clearing Member arising from a Contract or from any provision of these Rules shall be subject to all the terms of the Rules, including the setoff and other rights set forth herein. The rights of the Clearinghouse set forth herein shall be in addition to other rights that the Clearinghouse may have under applicable law and governmental regulations, other provisions of the Rules, additional agreements with the Clearing Member or any other source.

(d) If a Clearing Member remains in Default after the Clearinghouse exercises its rights under paragraphs (a) – (c) above, the following assets and proceeds will be applied to satisfy its Default, in the order of priority listed below. Each source of funds set forth below shall be completely exhausted, to the extent practicable, before the next following source is applied.

(i) First, any Performance Bond deposit of the Clearing Member; and

(ii) Second, any amounts deposited by the defaulting Clearing Member and its Affiliates that are Clearing Members into the Guaranty Fund, *provided* that if such Clearing Member is both an Exchange Clearing Member and an OTC Clearing Member (A) such Clearing Member's and its Affiliates' Guaranty Fund deposits related to its status as an Exchange Clearing Member shall first be applied to satisfy any Default related to its status as an Exchange Clearing Member and then applied to satisfy any Default related to its status as an OTC Clearing Member, and (B) such Clearing Member's and its Affiliates' Guaranty

Fund deposits related to its status as an OTC Clearing Member shall first be applied to satisfy any Default related to its status as an OTC Clearing Member and then applied to satisfy any Default related to its status as an Exchange Clearing Member.

The Clearing Member shall take no action, including but not limited to, attempting to obtain a court order, that would interfere with the ability of the Clearinghouse to so apply such assets and proceeds.

(e) If the assets and proceeds set forth in paragraph (d) above are insufficient to satisfy all of the defaulting Clearing Member's Obligations to the Clearinghouse, including all claims against the Clearinghouse by reason of novation of the Contract pursuant to Rule 402 or Rule 502, as applicable, the Clearinghouse shall nonetheless pay (including by drawing on the proceeds of any liquidity facility maintained by the Clearinghouse) all such claims, which shall be deemed a loss to it and which shall be a liability of the defaulting Clearing Member to the Clearinghouse, which the Clearinghouse may collect from any other assets of such Clearing Member or by process of law.

(f) For purposes of this Rule, each Default by a Clearing Member will be considered a separate Default event.

**International Derivatives Clearinghouse, LLC**  
**Reference File: IDCH-2011-04**

**Appendix B**

**International Derivatives Clearinghouse, LLC**  
**DEFAULT PROCEDURES**

**I. Introduction**

These Default Procedures summarize the actions that International Derivatives Clearinghouse LLC (“IDCH”) intends to take to address a Clearing Member default. Upon the actual event of default by a Clearing Member, IDCH may take such additional actions as it deems necessary for the protection of the Clearinghouse and other Clearing Members. Certain terms used but not defined herein shall have the meaning set forth in the IDCH Rulebook. The Default Procedures are intended to summarize and supplement the default rules found in the IDCH Rulebook and, in the event of a conflict between these Default Procedures and the Rulebook, the default rules will apply.

**II. Responsibilities**

The Risk Committee shall have responsibility for the implementation of these Default Procedures in the event of a Clearing Member default, and shall supervise the Chief Risk Officer, Risk Management Department and Treasury Department in the performance of their responsibilities hereunder. The Chief Risk Officer shall be the primary liaison between IDCH and the U.S. Commodity Futures Trading Commission (“CFTC”) in the event of a Clearing Member default.

**III. Declaration of a Clearing Member Default**

Pursuant to IDCH Rule 604, there are five general events that would cause a Clearing Member to be declared in default. They are:

- a. The Clearing Member fails to meet any of the Clearing Member’s financial obligations to IDCH;
- b. The Clearing Member is suspended or expelled by IDCH or a Participating Trading Facility;
- c. The Clearing Member is declared in default, suspended or expelled by another Derivatives Clearing Organization, clearing agency (as defined in the Securities Exchange Act or 1934, as amended) or other clearing organization;
- d. The Clearing Member’s Settlement Bank notifies IDCH that it is ceasing to act as Settlement Bank for the Clearing Member or that the Clearing Member will not meet its financial obligations to IDCH;
- e. The Clearing Member is bankrupt or insolvent.

The Board of Directors or the Risk Committee will determine whether a Clearing Member is in default. Upon a determination that a Clearing Member is in default, the Chief Risk Officer will notify the CFTC and the Clearing Member’s designated self-regulatory organization (if any), and

the Risk Management Department will issue a notice to Clearing Members informing them of the default.

Upon such Default, the Clearinghouse may cause all positions of the defaulting Clearing Member to be closed, netted or offset, transferred to any other Clearing Member, or otherwise resolved as deemed appropriate by the Clearinghouse and any debit balance owing to the Clearinghouse shall be immediately due and payable.

Events b. and c. are considered technical defaults while events a., d., and e. are actual defaults.

In the event of a technical default, IDCH's Risk Committee will manage the heightened risk by reducing the amount of risk that the Clearing Member poses to IDCH (reducing the Clearing Member's Total Risk Value and/or calling for greater Performance Bond), limit the Clearing Member's clearing to liquidation only or suspend the Clearing Member.

In the event of an actual default, the IDCH Risk Committee will institute its default waterfall which is described herein.

#### **IV. Default Waterfall Legal Framework**

As a CFTC-registered Derivatives Clearing Organization, IDCH is subject to the provisions of the Commodity Exchange Act and the rules and regulations of the CFTC (collectively, "CFTC Regulatory Framework"). Additionally, Subchapter IV of Chapter 7 of the US Bankruptcy Reform Act of 1978 has provisions for financial clearinghouses that exempt them from bankruptcy preference periods, providing a high level of assurance that margin collateral pledged to a clearinghouse cannot be clawed back by the estate of a bankrupt clearinghouse participant.

IDCH rules and procedures, which are subject to the CFTC Regulatory Framework, provide for the following;

- a. Once it has suspended a Clearing Member or declared a Clearing Member to be in Default, IDCH has the right to immediately begin the process of liquidating, auctioning off or neutralizing the Clearing Member's proprietary cleared portfolio.
- b. Once it has suspended a Clearing Member or declared a Clearing Member to be in Default, IDCH has the right to immediately begin the process of transferring the Clearing Member's customer cleared portfolios to either a single or multiple non-defaulting Clearing Members. If IDCH cannot transfer (in whole or in part) the customer cleared portfolio or it has determined that a transfer would not be in the best interest of the clearinghouse it can immediately begin the process of liquidating, auctioning off or neutralizing the Clearing Member's customer cleared portfolio.
- c. IDCH has unencumbered access to the defaulting Clearing Member's Guaranty Fund contribution and Performance Bond lodged with IDCH. In the event of a suspension or Default of a Clearing Member, IDCH can immediately apply the Guaranty Fund contribution and Performance Bond to satisfy any of the Clearing Member's financial



obligation to IDCH, which includes any cost associated with the liquidation, auctioning off, neutralization or transfer of a cleared portfolio; however, customer Performance Bond only may be used to satisfy an Clearing Member's obligation related to the Clearing Member's customer cleared portfolio. Any residual Guaranty Fund contribution and proprietary Performance Bond of the suspended or defaulting Clearing Member can be used to satisfy the residual obligations of the Clearing Member's customer cleared portfolio. These provisions do not permit the use of Clearing Member proprietary and customer Performance Bond to satisfy the obligations of other Clearing Members that have been suspended or are in default.

## **V. Cleared Portfolio Liquidation, Auctioning, Neutralization and Customer Transferring Procedures**

IDCH's Risk Management, Market Operations and Treasury Departments shall coordinate the liquidation or sale of the defaulting Clearing Member's positions in its Proprietary Account and the transfer of the defaulting Clearing Member's customer positions to one or more non-defaulting clearing members.

### **Transfer of Customer Positions**

The transfer of customer positions will be attempted if it has been determined solely by IDCH that the transfer is practical and does not place IDCH and its non-defaulting Clearing Members at greater risk. If IDCH has determined that a transfer of customer positions cannot be accomplished in an acceptable manner or timeframe, the customer positions shall be liquidated or auctioned.

#### **a. Customer Cleared Portfolios**

##### **Customer Positions**

- i. If positions held in a Customer Segregated Account are transferred to a single non-defaulting Clearing Member, all Performance Bond held in the Customer Segregated Account by or on behalf of the defaulting Clearing Member shall be transferred to the non-defaulting Clearing Member.

If positions held in a Customer Segregated Account are transferred to multiple non-defaulting Clearing Members, the required Performance Bond for the positions transferred shall be transferred to the non-defaulting clearing members. Excess Performance Bond shall be retained by IDCH pending instructions from the CFTC or the trustee of the defaulting Clearing Member's estate.

The Performance Bond held in a Customer Segregated Account shall be adjusted for the net Variation Settlements paid or collected. Any IDCH Advance (as

defined below) made to fund a Variation Settlement in a Customer Segregated Account shall be repaid to IDCH prior to any transfer. An IDCH Advance repayment can be made through an offset against the Performance Bond in the Customer Segregated Account.

- ii. If the positions held in a Customer Segregated positions cannot be transferred they will be liquidated or auctioned. Any remaining Performance Bond in the Customer Segregated Account remaining after the liquidation or auction, net of an IDCH Advance, shall be transferred to a special IDCH Customer Segregated Account pending instructions from the CFTC or the trustee of the defaulting Clearing Member's estate. Any negative Performance Bond balance in the Customer Segregated Account, net of an IDCH Advance, shall be added to the defaulting Clearing Member's obligations for its Proprietary Account.

b. Proprietary Cleared Portfolios

Proprietary Account Positions

- i. Any IDCH Advance made to fund Performance Bond in the defaulting Clearing Member's Proprietary Account shall be repaid to IDCH upon the liquidation or sale of the positions in the Proprietary Account. If there remains, net of the IDCH Advance, a positive cash balance in the defaulting Clearing Member's Proprietary Account, the balance shall be applied to any negative balance in the defaulting Clearing Member's Customer Segregated Account. Any remaining Performance Bond in the Proprietary Account shall be credited to an IDCH special Proprietary Account pending instructions from either the CFTC or the trustee of the defaulting Clearing Member's estate.
- ii. If the Proprietary Account has a negative balance (including any negative balance from the defaulting Clearing Member's Customer Segregated Account), the loss shall be allocated as described below.

Note: There shall be no netting of either positive or negative balances between the accounts of multiple defaulting Clearing Members. This provision applies to both Proprietary Accounts and Customer Segregated Accounts.

**VI. Collateral Management Waterfall Procedures**

In the event of a Clearing Member's actual default (i.e., failure to pay financial obligations to IDCH when due), IDCH's Treasury Department shall take the following actions:

- a. IDCH Line of Credit

IDCH's Treasury Department shall drawdown on its secured committed line of credit. The line of credit is currently at \$125 million and will be maintained at amounts based on IDCH's Risk Management Department's Stress Test. In considering the amount at which the line of credit is to be maintained, IDCH's Risk Management Department and Treasury Department will take into consideration the following:

- i. The dollar amount relationship between the Stress Test loss and IDCH Surplus Capital. Surplus Capital is defined as liquid working capital less 12-months of operating expenses. If Surplus Capital is materially larger than the Stress Test loss, a smaller line of credit will be considered. Conversely, if the Stress Test loss is materially larger than Surplus Capital, a larger line of credit will be considered.
- ii. The liquidity of the Performance Bond lodged by the Clearing Members selected for the stress test. IDCH's Performance Bond collateral rules require that 50% of a Clearing Member's Original Performance Bond requirement is satisfied through cash or highly rated and liquid sovereign debt securities that can generally be converted into cash in a single day ("Tranche 1 Margin Collateral"). The remaining composition of lodged Performance Bond can consist of corporate debt securities that have high credit ratings and can be converted into cash somewhat less quickly than highly rated and liquid sovereign debt securities ("Tranche 2 Margin Collateral"). If Tranche 1 Margin Collateral can satisfy the entire stress test loss a smaller line of credit is to be considered. If Tranche 2 Margin Collateral is needed to cure a Stress Test loss a larger line of credit will be considered.
- iii. The liquidity of all Clearing Member Performance Bond will be considered. If the majority of Original Performance Bond is Tranche 1 Margin Collateral a smaller line of credit will be considered. If 50% (the maximum) of initial margin is Tranche 2 Margin Collateral a larger line of credit will be considered.

The amount of the line of credit to be drawn during a Clearing Member default shall be no greater than the defaulting Clearing Member's Proprietary Account and Customer Segregated Account Original Performance Bond requirements and Guaranty Fund contribution. Proceeds of the draw are to be deposited in IDCH's central depository variation margin account to provide backup funding for the defaulting clearing member's unsatisfied Proprietary Account and Customer Segregated Account Variation Settlements (defined as an "IDCH Advance").

IDCH Advances shall be made while the defaulting Clearing Member's Proprietary Account positions are liquidated, auctioned or neutralized by IDCH's Risk Management Department and the defaulting clearing member's Customer Segregated Account positions are transferred to or guaranteed by a non-defaulting Clearing Member

("Counterparty Substitution") or liquidated, neutralized or auctioned. IDCH Advances shall be repaid as described herein.

b. Defaulting Clearing Members' House and Customer Initial Margin and Guaranty Fund Deposits

Upon the instruction and approval of IDCH's Chief Risk Officer, IDCH's Treasury Department is to begin the process of generating cash from the defaulting Clearing Member's Guaranty Fund contribution and Performance Bond deposits. This process can occur prior to any CFTC or court appointed trustee involvement.

- i. *Cash Guaranty Fund Contribution and Initial Margin Deposits:* All defaulting Clearing Member Guaranty Fund contributions are made in the form of cash. Additionally, Performance Bond can be satisfied through cash deposits. IDCH's Treasury Department shall convert all related investments (made by IDCH) held in the defaulting member's Guaranty Fund Account, Proprietary Account and Customer Segregated Account to cash by redeeming from all money market fund investments and selling all securities held on deposit which would be in the form of bank CDs, US Treasury Repo and US Treasury securities. Bank deposits and US Treasury Repo have maturities of no more than 90 days. US Treasury securities have maturities of no more than one year.

Proceeds from the defaulting Clearing Member's cash Performance Bond and Guaranty Fund investments are to be credited to IDCH's central depository variation margin account to fund the defaulting Clearing Member's Variation Settlements in its Proprietary Account and Customer Segregated Account.

Proceeds from the defaulting Clearing Member's Customer Segregated Account are to be transferred to IDCH's Customer Segregated Account at IDCH's central depository.

Performance Bond in the Customer Segregated Account shall only be used to fund Variation Settlements related to positions in the Customer Segregated Account of the defaulting Clearing Member.

Excess Performance Bond in the Proprietary Account and Guaranty Fund cash of a defaulting Clearing Member can be applied to satisfy Variation Settlements in the Customer Segregated Account of the defaulting Clearing Member to the extent there is a shortfall in the Customer Segregated Account of the defaulting Clearing Member.

In the event of the default of more than one Clearing Member, there shall be no netting between defaulting Clearing Members' Proprietary Accounts. For example, a post default resolution positive balance in a Proprietary Account or

Customer Segregated Account of one defaulting Clearing Member cannot be used to cover a payment in the respective Proprietary Account or Customer Segregated Account of another defaulting Clearing Member.

- ii. *Non-US Treasury Securities Lodged to Satisfy Performance Bond:* Clearing Members can satisfy their Performance Bond and Customer Segregated Account Performance Bond requirements with Government Sponsored Entity (“GSE”) debt; GSE guaranteed mortgage backed securities and certain sovereign debt and non-sovereign debt securities.

These securities are somewhat less liquid than US Treasury securities and if the defaulting Clearing Member is systemically important the default of the Clearing Member might impair the normal liquidity of these Non-US Treasury securities markets. As such, the sale of these securities shall proceed promptly after a Clearing Member default has occurred.

The timing of the sale of these securities shall be influenced by the nature of the defaulting Clearing Member’s cleared portfolio and the deposition of the defaulting Clearing Member’s Performance Bond. If IDCH’s Chief Risk Officer has determined that the cleared portfolio can be neutralized quickly with modest funding needs from Performance Bond collateral the sale of collateral will be managed accordingly thus preserving the Performance Bond collateral without a sale or a limited sale. If the Performance Bond collateral is principally cash and US Treasury securities there may be a limited sale of these other forms of collateral.

- iii. *US Treasury Securities:* Even in the event that a systemically important clearing member was to default with a knock-on effect on other markets, it is expected that US Treasury securities will be converted to cash quickly. As such, this category of collateral would be sold if IDCH’s Chief Risk Officer expected that during the unwinding of the cleared portfolio the unwinding would consume a significant portion of the Performance Bond deposit.
- iv. If Customer Segregated Account positions are subject to a Counterparty Substitution, the Performance Bond in the Customer Segregated Account will be transferred to the new Clearing Member’s Customer Segregated Account Performance Bond deposit at IDCH.

Post the default resolution; Performance Bond will be used to repay any IDCH Advance and fund any other obligation that the defaulting clearing member has to IDCH which shall include, but not be limited to, any Variation Settlement payment made, any expense incurred by IDCH to resolve the default and any fees due to IDCH from the defaulting Clearing Member. Performance Bond

balances held in the Customer Segregated Account shall only be applied against obligations due from the Customer Segregated Account. Performance Bond balances held in the defaulting clearing member's Proprietary Account shall be applied to any obligation due from the defaulting Clearing Member including any post default resolution negative net residual loss in the Customer Segregated Account.

If post default resolution there is a net positive balance in the defaulting Clearing Members Proprietary Account and/or Customer Segregated Account, the balance is to be held by IDCH pending instructions from CFTC and/or the court appointed trustee of defaulting clearing member's estate.

Note: In the event that IDCH sells or transfers the defaulting Clearing Member's positions in its Customer Segregated Account or Proprietary Account, and incurs a loss on the sale or has paid a third party a concession fee to assume the defaulting clearing member's customer and proprietary portfolios, IDCH may charge the account of the defaulting clearing member for any such loss or concession fee and such amount shall be added to the net negative liquidation amount for Clearing Member Assessment.

c. Allocation of Defaulting Clearing Members' Net Negative Liquidation

Note: Each source of funds set forth below will be completely exhausted, to the extent practicable, before the next following source is applied.

- i. The net negative liquidation of the defaulting Clearing Member first will be funded by IDCH through the application of the surplus capital of IDCH in excess of funds necessary for normal operations. IDCH currently maintains a \$50 million surplus fund. Such amounts will be deemed a liability of the defaulting Clearing Member, which IDCH may collect from other assets of the defaulting Clearing Member or by process of law. Any amounts collected from the defaulting Clearing Member shall be applied to replenish IDCH's surplus capital or repay other sources of the funds used to cover such losses.
- ii. Any amount not covered by IDCH surplus capital will be payable from the IDCH Guaranty Fund deposits of all other Clearing Members on a pro rata basis, based on each Clearing Member's average deposit in direct proportion to the total Guaranty Fund deposit requirement of each non-defaulting Clearing Member.
- iii. Any amount not covered by the Guaranty Fund deposits, will be covered first by IDCH's default insurance policy, if any such policy is maintained, then by an additional capital contribution by IDCG, if any.

- iv. Any amount not covered by default insurance or additional capital contributions will be assessed to the Clearing Members on a pro rata basis, based on each Clearing Member's average deposit in direct proportion to the total Guaranty Fund deposit requirement of each Clearing Member, subject to a cap equal to the lesser of \$30,000,000 or 40% of such Clearing Member's adjusted net capital. Clearing Member Assessments shall be payable within one day of the Clearing Member Assessment. Any remaining deficiency shall be reassessed until the deficiency has been paid or each clearing member has paid its maximum required amount.

## **VII. Testing of Default Procedures**

IDCH will conduct and document a test of its default management plan on at least an annual basis.

## **VIII. Public Access to IDCH Default Procedures**

These IDCH Default Procedures shall be amended as Clearing Members join the Clearinghouse. Detailed procedures along with committee responsibilities and roles will be dependent on the capabilities of the Clearinghouse's membership. IDCH shall post these default procedures on its website along with its rulebook.

**International Derivatives Clearinghouse, LLC**  
**Reference File: IDCH-2011-04**

**Confidential Appendix C**

**CONFIDENTIAL TREATMENT REQUESTED BY**  
**INTERNATIONAL DERIVATIVES CLEARINGHOUSE, LLC**