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SECURITIES AND EXCHANGE COMMISSION  
[Release No. 34-82678; File No. SR-ICEEU-2018-002]

Self-Regulatory Organizations; ICE Clear Europe Limited; Notice of Filing of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice Relating to Amendments to the ICE Clear Europe Limited CDS Procedures, CDS Risk Policy, and CDS Risk Model Description  
February 9, 2018.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 6, 2018, ICE Clear Europe Limited (“ICE Clear Europe”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule changes described in Items I, II, and III below, which Items have been prepared primarily by ICE Clear Europe. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

ICE Clear Europe Limited proposes to modify certain provisions of its CDS Procedures to support clearing of a new single-name CDS transaction type and to modify its CDS Risk Policy and CDS Risk Model Description to enhance risk management relating to CDS involving European banks.

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

In its filing with the Commission, ICE Clear Europe included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. ICE Clear Europe has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Clearing Agency's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

ICE Clear Europe proposes to modify certain provisions of its CDS Procedures to support clearing of a new single-name CDS transaction type. ICE Clear Europe also proposes to amend its CDS Risk Policy and CDS Risk Model Description to better address certain risks associated with CDS referencing European banks relating to the issuance of new debt structures by those banks. These revisions do not involve any changes to the ICE Clear Europe Clearing Rules.

Proposed Amendments to the CDS Procedures

The purpose of the proposed changes to the CDS Procedures is to support clearing of a new single-name CDS transaction type: Standard European Senior Non-Preferred Financial Corporate. ICE Clear Europe understands that market participants generally propose to commence trading of this transaction type as of March 20, 2018, and relevant standard documentation for the transaction type has recently been published by the International Swaps and Derivatives Association, Inc. ("ISDA"). Transactions under such standard documentation, will be generally similar to Standard European Financial Corporate transactions currently cleared by the Clearing House, but will have a reference

obligation that will be subordinated to other senior obligations, but will rank senior to so-called “tier 2” obligations that are subordinated for purposes of European Union bank regulatory capital requirements. ICE Clear Europe proposes amending its CDS Procedures to provide for the clearance of contracts referencing this new transaction type. ICE Clear Europe believes the addition of these contracts will benefit the market for credit default swaps by providing market participants the benefits of clearing, including reduction in counterparty risk and safeguarding of margin assets pursuant to Clearing House Rules.

Specifically, ICE Clear Europe proposes amending Paragraph 4.3(c)(ii) of the CDS Procedures to reference Standard European Senior Non-Preferred Financial Corporate as a transaction type eligible to be submitted for clearing. Similarly, Paragraph 11.3(i) is amended in the definition of ‘Non-STEC Single Name Contract’ to include Standard European Senior Non-Preferred Financial Corporate in the list of types of Reference Entities eligible to be cleared by ICE Clear Europe. ICE Clear Europe also proposes amending the definition of ‘Single Name Contract Reference Obligations’ in Paragraph 11.3(j) to remove a requirement that the relevant obligation must be a “senior level” obligation, and add instead that the obligation be of the applicable seniority level for the terms of the contract (to accommodate the seniority level of Senior Non-Preferred transactions, as discussed above).

#### Proposed Amendments to the CDS Risk Model Description

ICE Clear Europe’s risk management methodology incorporates considerations of idiosyncratic credit events and the associated potential losses. These credit event losses are termed Loss-Given-Default (“LGD”). In order to support clearing of the new

transaction type, ICE Clear Europe proposes certain LGD enhancements to its risk model. A description of these changes is set forth below.

ICE Clear Europe first proposes Risk Factor (“RF”) level LGD enhancements. These proposed RF level enhancements are designed to better capture the LGD risk associated with the issuance of new debt structures by European banks, and provide a consistent recovery rate scenario approach to different sub-factors.

Under ICE Clear Europe’s risk model, every Single Name (“SN”) reference entity is deemed an RF. Each combination of definition, doc-clause, tier and currency for a given SN RF determines a SN Risk Sub-Factor (“RSF”). Currently, ICE Clear Europe measures losses associated with credit events (“LGD”) by means of a stress-based approach, which utilizes three recovery rate (“RR”) scenarios: minimum RR, expected RR, and maximum RR. Outright and index-derived RSF exposures are combined at each RR scenario.

The results of these RR scenarios are used as an input into the Profit/Loss-Given Default (“P/LGD”) calculations at both the RSF and RF levels. For each RSF, P/LGD is calculated as the worst credit event outcome, and for each RF, P/LGD is calculated as the sum of the worst credit outcomes per RSF. These final P/LGD results are used as part of the determination of risk requirements.

ICE Clear Europe proposes enhancements to the RF level LGD calculation. Specifically, ICE Clear Europe proposes a change to the calculation by incorporating a more consistent approach in the calculation of the P/LGD by using the same RR scenarios applied to the different RSFs which form part of the considered RF.

For each RF, ICE Clear Europe will continue to calculate an “extreme outcome” as the sum of the worst RSF P/LGDs across all scenarios. ICE Clear Europe will also, for each RF, calculate an “expected outcome” as the worst sum of all the RSF P/LGDs across all of the same scenarios. Under the proposed approach, ICE Clear Europe will then combine the results of the “extreme outcome” calculation and the “expected outcome” calculation to compute the total LGD for each RF.

ICE Clear Europe also proposes to expand its LGD analysis to Risk Factor Groups (“RFG”). Under the proposed changes, a collection of related RFs will form a RFG. These related RFs will be defined as a RFG based on either 1) having a common majority parental sovereign ownership (e.g. quasi-sovereigns and sovereigns), or 2) being a majority owned subsidiary of a common parent entity according to the Bloomberg Related Securities Analysis. A RFG can consist of only one RF. This change will better capture the risk exposure dynamics of related RFs, and will allow ICE Clear Europe the ability to provide limited LGD benefits across RFs with opposite exposures, as well as allow for the ability to capture accumulation of directional exposure for related RFs.

Under the proposed approach, the total quantity LGD will be calculated on a RFG level, and account for the exposure due to credit events associated with the reference entities within a given RFG. If a RFG contains only one RF, the LGD will continue to be computed as the risk exposure due to a credit event for a given underlying reference entity. Under the proposed approach, ICE Clear Europe will sum the P/LGDs for each RF in a given RFG, with limited offsets in the event RFs exhibit positive PLGD. Using the results of the above calculation, ICE Clear Europe will obtain the RFG level LGD. The

proposed approach also includes a calculation which allows for the RFG level LGD to be attributed to each RF within the considered RFG.

ICE Clear Europe proposes changes to the ‘Loss Given Default Risk Analysis’ section of the CDS Risk Model Description Document to reflect the described RF and RFG LGD calculation changes. ICE Clear Europe also proposes conforming changes to other sections of the CDS Risk Model Description to incorporate these methodology changes and reflect the RFG analysis.

ICE Clear Europe proposes a revision to the ‘Uncollateralized Loss Given Default’ calculation in order to incorporate the RFG level LGD attribution calculation mentioned above.

ICE Clear Europe proposes changes to the ‘Idiosyncratic Jump-to-Default Requirements’ section of the CDS Risk Model Description document. Currently, the portfolio Jump to Default (“JTD”) approach collateralizes the worst uncollateralized LGD (“ULGD”) exposure among all RFs. Under the proposed approach, the portfolio JTD approach will collateralize, through the portfolio JTD IM requirement that accounts for the RFG-specific LGD collateralization, the worst ULGD exposure among all RFGs. The ULGD exposure for a given RFG will be calculated as a sum of the associated RF ULGDs.

ICE Clear Europe also proposes minor edits to the ‘SWWR’ (Specific Wrong Way Risk) and ‘GWWR’ (General Wrong Way Risk) sections to update language and calculation descriptions to accommodate the introduction of the RFG to the ‘Idiosyncratic Jump-to-Default Requirements’ section.

ICE Clear Europe proposes changes to the ‘Guaranty Fund Methodology’ section. ICE Clear Europe’s risk management approach establishes GF to provide for the mutualization of losses under extreme credit market scenarios. Specifically, the ICE Clear Europe GF is designed to provide adequate funds to cover losses associated with the default of the two Clearing Member (“CM”) affiliate groups that would potentially cause the largest aggregate credit exposure to ICE Clear Europe under extreme, but plausible market conditions. ICE Clear Europe’s current GF methodology includes, among other assumptions and adverse market conditions, the assumption that up to three credit events, different from the ones associated with CMs, occur during the established risk horizon. ICE Clear Europe proposes expanding this analysis to the RFG level. Under this proposed approach, it will be assumed that credit events associated with up to three RFGs, different from the ones associated with the CMs and the RFs that are in the RFGs as the CMs, occur during the established risk horizon. As such, the uncollateralized losses, used in the Guaranty Fund analysis, reflect the proposed expansion to the RFG level.

ICE Clear Europe also proposes clarifications to the calculation for the Specific Wrong Way Risk component of the Guaranty Fund. Currently, for a given CM, the Specific Wrong Way Risk component is based on self-referencing positions arising from one or more RFs; ICE Clear Europe proposes clarifying this analysis to be based on the RFG level.

The amendments to the CDS Risk Model Description also contain typographical corrections and similar technical corrections and clarifications.

Proposed Amendments to the CDS Risk Policy

ICE Clear Europe also proposes conforming changes to the CDS Risk Policy consistent with those described above.

Specifically, the definition of a Risk Sub-Factor is proposed to be amended that it will be defined as a specific combination of SN, tier and currency (as well as documentation clause), where the union of all Risk Sub-Factors that share the same underlying SN forms a SN Risk Factor.

The CDS Risk Policy is also being amended such that instead of the worst SN, the worst LGD associated with a Risk Factor Group (“RFG”), will be selected to establish the portfolio JTD requirement. The amendments also clarify that a Risk Factor Group is a set of Risk Factors related by a common parental ownership.

With respect to the guaranty fund calculation, provisions in respect of two uncollateralized LGD relating to the guaranty fund calculation is being amended such that instead of the GF LGD being estimated for every SN based on the total portfolio positions in the SNs, the GF LGD will be estimated for every RFG based on the total portfolio positions in the SNs belonging to the same RFG.

The amendments to the CDS Risk Policy also contain typographical corrections and similar technical corrections and clarifications.

(b) Statutory Basis

Section 17A(b)(3)(F) of the Act<sup>3</sup> requires, among other things, that the rules of a clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions, and to the extent applicable, derivative agreements, contracts and transactions and to comply with the provisions of the Act and the rules and

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<sup>3</sup> 15 U.S.C. 78q-1(b)(3)(F).



regulations thereunder. ICE Clear Europe believes that the proposed rule changes are consistent with the requirements of the Act and the rules and regulations thereunder applicable to ICE Clear Europe, in particular, to Section 17(A)(b)(3)(F),<sup>4</sup> because ICE Clear Europe believes that the proposed rule changes will promote the prompt and accurate clearance and settlement of securities transactions, derivatives agreements, contracts, and transactions.

In regards to the proposed amendments to the Procedures, contracts referencing the Standard European Senior Non-Preferred Financial Corporate transaction type are similar to the Non-STEC Single Name contracts currently cleared by ICE Clear Europe, and will be cleared pursuant to ICE Clear Europe's existing clearing arrangements and related financial safeguards, protections and risk management procedures (with the modifications to the CDS Risk Policy and CDS Risk Model Description discussed herein). Clearing of these contracts will allow market participants an increased ability to manage risk and will ensure the safeguarding of related margin assets pursuant to Clearing House Rules. ICE Clear Europe believes that acceptance of these contracts, on the terms and conditions set out in the Rules, is consistent with the prompt and accurate clearance of and settlement of securities transactions and derivative agreements, contracts and transactions cleared by ICE Clear Europe, the safeguarding of securities and funds in the custody or control of ICE Clear Europe, and the protection of investors and the public interest, within the meaning of Section 17A(b)(3)(F) of the Act.<sup>5</sup>

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<sup>4</sup> Id.

<sup>5</sup> 15 U.S.C. 78q-1(b)(3)(F).

Clearing of contracts referencing the Standard European Senior Non-Preferred Financial Corporate transaction type will also satisfy the requirements of Rule 17Ad-22.<sup>6</sup> In particular, in terms of financial resources, ICE Clear Europe will apply its existing initial margin methodology to the contracts (with the modifications to the CDS Risk Policy and CDS Risk Model Description discussed herein). ICE Clear Europe believes that this model (as proposed to be amended) will provide sufficient initial margin requirements to cover its credit exposure to its Clearing Members from clearing such contracts, consistent with the requirements of Rule 17Ad-22(b)(2) and (e)(6).<sup>7</sup> In addition, ICE Clear Europe believes its Guaranty Fund, under its methodology as proposed to be revised, will, together with the required initial margin, provide sufficient financial resources to support the clearing of the contracts consistent with the requirements of Rule 17Ad-22(b)(3) and (e)(4).<sup>8</sup> ICE Clear Europe also believes that its existing operational and managerial resources will be sufficient for clearing of the contracts, consistent with the requirements of Rule 17Ad-22(e)(17),<sup>9</sup> as the new contracts are substantially the same from an operational perspective as existing contracts. Similarly, ICE Clear Europe will use its existing settlement procedures and account structures for the new contracts, consistent with the requirements of Rule 17Ad-22(e)(8), (9) and (10)<sup>10</sup>, as to the finality and accuracy of its daily settlement process and

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<sup>6</sup> 17 CFR 240.17Ad-22.

<sup>7</sup> 17 CFR 240.17Ad-22(b)(2) and (e)(6).

<sup>8</sup> 17 CFR 240.17Ad-22(b)(3) and (e)(4).

<sup>9</sup> 17 CFR 240.17Ad-22(e)(17).

<sup>10</sup> 17 CFR 240.17Ad-22(e)(8), (9) and (10).

addressing the risks associated with physical deliveries. ICE Clear Europe determined to accept the contracts for clearing in accordance with its governance process, consistent with the requirements of Rule 17Ad-22(e)(2).<sup>11</sup> Finally, ICE Clear Europe will apply its existing default management policies and procedures for the contracts. ICE Clear Europe believes that these procedures allow for it to take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of Clearing Member insolvencies or defaults in respect of the additional single names, in accordance with Rule 17Ad-22(e)(13).<sup>12</sup>

With regards to the LGD enhancements, the proposed risk model revisions enhance ICE Clear Europe's risk methodology and are expected to impose more conservative requirements, which would enhance the financial resources available to ICE Clear Europe and thereby facilitate its ability to promptly and accurately clear and settle its cleared CDS contracts. In addition, the proposed revisions are consistent with the relevant requirements of Rule 17Ad-22.<sup>13</sup> In particular, the LGD related amendments will enhance the financial resources available to the Clearing House, and continue to ensure that ICE Clear Europe maintains sufficient financial resources to withstand a default by the two Clearing Member families to which it has the largest aggregate exposure in extreme, but plausible market conditions, and are therefore reasonably designed to meet

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<sup>11</sup> 17 CFR 240.17Ad-22(e)(2).

<sup>12</sup> 17 CFR 240.17Ad-22(e)(13).

<sup>13</sup> 17 C.F.R. §240.17Ad-22.

the margin and financial resource requirements of Rule 17Ad-22(b)(2-3) and (e)(4) and (e)(6).<sup>14</sup>

(B) Clearing Agency's Statement on Burden on Competition

ICE Clear Europe does not believe the proposed rule changes would have any impact, or impose any burden, on competition not necessary or appropriate in furtherance of the purpose of the Act. Contracts referencing the Standard European Senior Non-Preferred Financial Corporate transaction type will be available to all ICE Clear Europe participants for clearing. The clearing of these contracts by ICE Clear Europe does not preclude the offering of the contracts for clearing by other market participants.

Additionally, the LGD enhancements apply uniformly across all Clearing Members.

Therefore, ICE Clear Europe does not believe the proposed rule changes impose any burden on competition that is inappropriate in furtherance of the purposes of the Act.

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

Written comments relating to the proposed amendments have not been solicited or received by ICE Clear Europe. ICE Clear Europe will notify the Commission of any comments received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

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<sup>14</sup> 17 C.F.R. §240.17Ad-22(b)(2-3) and (e)(4) and (e)(6).

- (A) by order approve or disapprove the proposed rule change or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

The proposal shall not take effect until all regulatory actions required with respect to the proposal are completed.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, security-based swap submission or advance notice is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-ICEEU-2018-002 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-1090.

All submissions should refer to File Number SR-ICEEU-2018-002. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent

amendments, all written statements with respect to the proposed rule change, security-based swap submission or advance notice that are filed with the Commission, and all written communications relating to the proposed rule change, security-based swap submission or advance notice between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, N.E., Washington, D.C. 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filings will also be available for inspection and copying at the principal office of ICE Clear Europe and on ICE Clear Europe's website at <https://www.theice.com/clear-europe/regulation#rule-filing>.

All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-ICEEU-2018-002 and should be submitted on or before [INSERT DATE 21 DAYS FROM PUBLICATION IN THE FEDERAL REGISTER].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>15</sup>

Eduardo A. Aleman,  
Assistant Secretary.

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<sup>15</sup> 17 CFR 200.30-3(a)(12).

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