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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-87804; File No. SR-ICC-2019-011]

### **Self-Regulatory Organizations; ICE Clear Credit LLC; Order Approving Proposed Rule Change Relating to the ICC Default Auction Procedures—Initial Default Auctions and the ICC Secondary Auction Procedures**

December 19, 2019

#### I. Introduction

On October 31, 2019, ICE Clear Credit LLC (“ICC”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to revise ICC’s Default Auction Procedures—Initial Default Auctions (“Initial Default Auction Procedures”) and Secondary Auction Procedures. The proposed rule change was published for comment in the Federal Register on November 18, 2019.<sup>3</sup> The Commission did not receive comments regarding the proposed rule change. For the reasons discussed below, the Commission is approving 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.

<sup>3</sup> Self-Regulatory Organizations; ICE Clear Credit LLC; Notice of Filing of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice Relating to the ICC Default Auction Procedures—Initial Default Auctions and the ICC Secondary Auction Procedures; Exchange Act Release No. 87502 (Nov. 12, 2019); 84 Fed. Reg. 63693 (Nov. 18, 2019) (“Notice”).

## II. Description of the Proposed Rule Change

To resolve a default by a Clearing Participant, ICC may auction the defaulting Clearing Participant's open CDS contracts through one or more auctions where ICC's other, non-defaulting Clearing Participants bid on the contracts.<sup>4</sup> If ICC does not auction off all of the open CDS contracts in an initial auction, ICC may conduct one or more secondary auctions to allocate the remaining open CDS contracts. ICC conducts initial auctions pursuant to its Initial Default Auction Procedures and secondary auctions pursuant to its Secondary Auction Procedures (collectively, the "Auction Procedures"). The proposed rule change would improve both the initial and secondary default auction processes by amending the Auction Procedures to (i) require that ICC use the automated Default Management System ("DMS") to communicate with Clearing Participants and that Clearing Participants use the DMS to communicate with ICC; (ii) allow for all or nothing bidding in default auctions; and (iii) update defined terms and make clarifications in light of these changes.

The proposed rule change would make substantially identical changes to both the Initial Default Auction Procedures and the Secondary Auction Procedures. Thus, for the sake of brevity, the description below refers collectively to changes to the Auction Procedures.

### A. Automated DMS

ICC's DMS is a web-based system that ICC uses to set the specifications for an auction as well as to communicate certain information to, and receive certain information from, Clearing Participants with respect to an auction. Clearing Participants bid on auctions through the DMS, and the DMS in turn controls bidding by, for example, prohibiting a Clearing Participant from

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<sup>4</sup> Capitalized terms used herein but not otherwise defined have the meanings assigned to them in the ICC Clearing Rules (the "Rules") or the Auction Procedures. The description herein is substantially excerpted from the Notice, 84 Fed. Reg. at 63693.

submitting more than one valid all-or-nothing bid, as discussed further below. Moreover, through the DMS, ICC announces winners of auctions. ICC has assigned to Clearing Participants credentials for logging into and using the DMS, and Clearing Participants have tested the DMS by using it in various default drills.

Currently, under the Auction Procedures, ICC communicates the details of an auction to Clearing Participants in writing, using a standardized form that is currently set out in Annex A of the Auction Procedures. The proposed rule change would delete Annex A in its entirety and would require that ICC communicate the details of an auction to Clearing Participants through the DMS rather than in writing. Similarly, the proposed rule change would require that ICC notify the winning bidder in an auction through the DMS, rather than by email, telephone, or in writing (which are the methods that the Auction Procedures currently require ICC to use to notify a winning bidder). Finally, the Auction Procedures allow ICC to set a minimum bid requirement for an auction, under which Clearing Participants are required to bid for a minimum notional amount of contracts. Currently ICC must communicate this minimum bid requirement to Clearing Participants through a notice, the form of which is set out in Annex B to the Auction Procedures. Under the proposed rule change, ICC would still be able to set a minimum bid requirement as before, but the proposed rule change would delete Annex B in its entirety and would require that ICC communicate the details of a minimum bid requirement to Clearing Participants through the DMS instead. Thus, the proposed rule change would give ICC the ability to communicate the details of an auction to Clearing Participants electronically, through the DMS, which is designed to help improve the speed and consistency of such communications.

The proposed rule change similarly would require that Clearing Participants communicate with ICC through the DMS rather than through written communications as

required under the current Rules. Specifically, Clearing Participants currently are required to submit bids in writing using a Bid Form. Under the proposed rule change Clearing Participants would be required to submit bids in an auction electronically through the DMS instead. This is designed to improve the speed and accuracy of such submissions.

Finally, the current Auction Procedures specify that ICC may set a minimum bid size for an auction and currently provide that any bid below the minimum bid size will be null and void. The proposed rule change would leverage the DMS to automate these existing requirements by specifying that the DMS would be designed to automatically prevent Clearing Participants from submitting bids below the minimum bid size and to render null and void any bid below the minimum bid size that the DMS accepted in error. This too is designed to help improve the speed and accuracy of bid submissions by Clearing Participants, and also to help ensure that such bid submissions are consistent with existing requirements.

B. All or Nothing Bidding

Currently, the Auction Procedures do not permit a Clearing Participant to submit an all or nothing bid. An all or nothing bid is a bid in which the Clearing Participant stipulates that, should its bid be the winning bid, the Clearing Participant will receive 100% of the contracts being auctioned or no contracts at all. The proposed rule change would revise the Auction Procedures to allow Clearing Participants to submit all or nothing bids. Specifically, a Clearing Participant could submit one all or nothing bid per auction. A Clearing Participant would do so by marking the bid as an all or nothing bid in the bid submission (which, as noted above, would be submitted electronically through the DMS). The proposed rule change would also specify that a Clearing Participant could submit in the same auction both one all or nothing bid and non-all or nothing bids (referred to in the proposed rule change as “Standard Bids”) on its own behalf or on behalf of its customers.

Under the Auction Procedures, ICC determines the auction price by ordering bids sequentially, starting with the highest bid price and ending with the lowest bid price. The price of the bid at which, along with any equal or higher bids, the sum of the notional amount of contracts being purchased equals or is greater than the notional amount of contracts that ICC is auctioning is the clearing price of the auction (the “Auction Clearing Price”). In other words, ICC proceeds down the list of bids by price, starting with the highest priced bid, and sets the Auction Clearing Price at the bid that, along with the other higher priced bids before it, allows ICC to allocate 100% of the open CDS contracts.

The Auction Procedures currently require that, in the event there are multiple bids at the Auction Clearing Price and there is a shortfall of open CDS contracts, ICC must allocate the contracts *pro rata* according to the notional amount of contracts that each winning bidder requested in its bid. As revised under the proposed rule change, the Auction Procedures would require that, where there is an all or nothing bid in the sequence of bids before the Auction Clearing Price, the price of the all or nothing bid would set the Auction Clearing Price (because that would be the highest priced bid that would allow ICC to allocate 100% of the open contracts). In that case, ICC would allocate to the all or nothing bidder 100% of the contracts even if there are Standard Bids at a higher or equal price. If there were more than one all or nothing bid at the Auction Clearing Price, then the Auction Procedures, as revised under the proposed rule change, would require that ICC allocate the portfolio equally among all the bidders submitting all or nothing bids.

The proposed rule change would update other provisions of the Auction Procedures to clarify how those provisions would apply in light of all or nothing bidding. First, the Auction Procedures currently provide that ICC may, after an initial auction, in its discretion and after

consultation with the CDS Risk Committee, determine the Auction Clearing Price for such an auction to be less than 100% of the notional amount of the contracts and declare a second auction to auction off the remaining contracts. ICC may do so if, in its reasonable determination, awarding 100% of the notional amount of the contracts would have a material impact on the amounts payable or receivable by ICC. The proposed rule change would not alter this provision but would specify that, in such a situation, ICC could disregard any all or nothing bids received in the initial auction.

Second, the proposed rule change would revise the Auction Procedures to clarify how an all or nothing bid affects the calculation of a Clearing Participant's bid price for purposes of determining the competitiveness of a Clearing Participant's bid and satisfaction of a Clearing Participant's minimum bid requirement. The competitiveness of a Clearing Participant's bid and satisfaction of a Clearing Participant's minimum bid requirement are important because under ICC Rule 802(b) and the default auction priority set out in the Auction Procedures, in the event that ICC needs to use non-defaulting Clearing Participants' contributions to the Guaranty Fund to resolve the default of a Clearing Participant, ICC uses first the contributions to the Guaranty Fund attributable to Clearing Participants that did not satisfy their minimum bid requirement (referred to as Non-Bidding Participants), followed by those that submitted less competitive bids. Currently, ICC uses the weighted average of a Clearing Participant's Standard Bids to determine bid price and thus to determine the competitiveness of a Clearing Participant's bids in an auction for these purposes. Under the updated Auction Procedures, as revised by the proposed rule change, where a Clearing Participant has submitted both an all or nothing bid and one or more Standard Bids, the Clearing Participant's bid price would be the more competitive of (1) the weighted average bid price of all valid Standard Bids made by the Clearing Participant in the

auction (weighted by the portfolio size of each such bid, and converted into USD at the relevant FX spot rate, if applicable) and (2) the price of any valid All or Nothing Bid made by the Clearing Participant in the Auction. For this purpose, the more competitive of the two would be the one that results in the best outcome for ICC; in other words, the bid under which ICC will receive the most, or pay out the least, cash in return for the auctioned contracts.

Finally, under the updated Auction Procedures, as revised by the proposed rule change, if a Clearing Participant's Standard Bids do not satisfy its minimum bid requirement, the Clearing Participant's bid price would be the price of its all or nothing bid. Where a Clearing Participant has submitted only one or more Standard Bids (and has not submitted an all or nothing bid), and that Clearing Participant's Standard Bids do not satisfy its minimum bid requirement, the Auction Procedures would treat the Clearing Participant as a Non-Bidding Participant, which, as noted above, has consequences under ICC Rule 802(b). Specifically, if ICC needs to use non-defaulting Clearing Participants' contributions to the Guaranty Fund to resolve the default of a Clearing Participant, ICC uses first the contributions to the Guaranty Fund attributable to Non-Bidding Participants.<sup>5</sup>

#### C. Updates to Defined Terms and Clarifications

Related to the changes described above, the proposed rule change would update defined terms and make an additional clarification to the Auction Procedures.

In connection with the proposed requirement that Clearing Participants submit bids through the DMS, and to better specify the meaning of the defined term, the proposed rule change would change the defined term "Closing Time" to "Bidding Close Time." The proposed

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<sup>5</sup> See ICC Rule 802(b) and the default auction priority set out in the Auction Procedures.

rule change would define the term as the bidding close time specified by ICC in the relevant auction specifications.

To distinguish all or nothing bids, the proposed rule change would add to the Auction Procedures the defined term “Standard Bid.” A Standard Bid would be a valid bid submitted by a Clearing Participant that was not an all or nothing bid.

To refer to a bid submitted through the DMS, rather than in paper through the bid form, the proposed rule change would create the defined term “Bid Submission.” The proposed rule change would define the term Bid Submission to mean a bid submitted through the DMS.

Finally, the Auction Procedures currently allow a Clearing Participant to transfer its minimum bid requirement to an affiliate that is also a Clearing Participant. The Auction Procedures specify that, in such a case, a Clearing Participant that so transfers or outsources its minimum bid requirement to an affiliate remains liable for any breach by its affiliate in respect of such Clearing Participant’s Minimum Bid Requirement. The proposed rule change would further clarify that in such a case, a Clearing Participant will take on the same position as a Senior Bidder, Split Bidder, Subordinate Bidder, or Non-Bidding Participant as the affiliate, as appropriate. This change is unrelated to the other changes discussed above, but ICC is using the proposed rule change to submit this additional clarification.

### III. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such

organization.<sup>6</sup> For the reasons given below, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act<sup>7</sup> and Rule 17Ad-22(d)(11) thereunder.<sup>8</sup>

A. Consistency with Section 17A(b)(3)(F) of the Act

Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of ICC be designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions, as well as to assure the safeguarding of securities and funds which are in the custody or control of ICC or for which it is responsible, and, in general, to protect investors and the public interest.<sup>9</sup> As discussed above, the proposed rule change would require that ICC use the DMS to communicate certain information to Clearing Participants, such as specific parameters of an auction, and would in turn, require Clearing Participants to use the DMS to communicate their bids to ICC. The DMS would also automatically reject bids that do not satisfy the minimum bid size. The Commission believes that in doing so the proposed rule change would improve the efficiency and accuracy of communications regarding default auctions, which may help to avoid delays or miscommunications that could delay the completion of an auction. Thus, in requiring use of the DMS, the Commission believes the proposed rule change would help to promote the prompt resolution of default auctions. Similarly, the Commission believes that all or nothing bidding would enhance ICC's ability to sell all of the open CDS contracts in an initial default auction by providing a means for a single bidder to take all of the contracts and requiring that ICC allocate

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<sup>6</sup> 15 U.S.C. 78s(b)(2)(C).

<sup>7</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>8</sup> 17 CFR 240.17Ad-22(d)(11).

<sup>9</sup> 15 U.S.C. 78q-1(b)(3)(F).

such contracts to that bidder if the all or nothing bid meets the Auction Clearing Price. Finally, the Commission believes that the updates to the defined terms and the clarification regarding a Clearing Participant's ability to transfer its minimum requirement to an affiliate would support and enhance ICC's ability to implement these changes.

Through default auctions, ICC allocates the open CDS contracts of a defaulting Clearing Participant to other, non-defaulting Clearing Participants. Thus, in improving the efficiency of such auctions, the Commission believes the proposed rule change would promote the prompt and accurate clearance and settlement of the CDS transactions resulting from such auctions. Moreover, the Commission believes that the default of a Clearing Participant, if not promptly resolved, could cause losses for ICC. The Commission believes the proposed rule change would help to avoid these losses by promoting the prompt resolution of default auctions, and therefore the prompt resolution of a Clearing Participant's default. Because losses resulting from the default of a Clearing Participant could disrupt ICC's ability to operate and therefore threaten ICC's access to securities and funds, the Commission believes the proposed rule change also would help to assure the safeguarding of securities and funds in ICC's custody and control. Finally, for these reasons, the Commission believes that the proposed rule change would, in general, protect investors and the public interest.

Therefore, the Commission finds that the proposed rule change would promote the prompt and accurate clearance and settlement of securities transactions, assure the safeguarding of securities and funds in ICC's custody and control, and, in general, protect investors and the public interest, consistent with the Section 17A(b)(3)(F) of the Act.<sup>10</sup>

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<sup>10</sup> 15 U.S.C. 78q-1(b)(3)(F).

B. Consistency with Rule 17Ad-22(d)(11)

Rule 17Ad-22(d)(11) requires that ICC establish, implement, maintain and enforce written policies and procedures reasonably designed to make key aspects of its default procedures publicly available and establish default procedures that ensure that ICC can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a participant default.<sup>11</sup> As discussed above, the Commission believes the proposed rule change would improve the efficiency and accuracy of communications regarding default auctions and increase the likelihood that ICC is able to allocate all open CDS contracts in an initial auction by providing a means for a single bidder to take all of the contracts up for auction. The Commission believes that these changes would help ICC to resolve defaults quickly through auctions. The Commission believes, in turn, that resolving defaults quickly through auctions would therefore help to ensure that ICC can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a Clearing Participant's default.

Therefore, for the above reasons the Commission finds that the proposed rule change is consistent with Rule 17Ad-22(d)(11).<sup>12</sup>

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<sup>11</sup> 15 U.S.C. 17Ad-22(d)(11).

<sup>12</sup> 15 U.S.C. 17Ad-22(d)(11).

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act, and in particular, with the requirements of Section 17A(b)(3)(F) of the Act<sup>13</sup> and Rule 17Ad-22(d)(11) thereunder.<sup>14</sup>

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act<sup>15</sup> that the proposed rule change (SR-ICC-2019-011), be, and hereby is, approved.<sup>16</sup>

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>17</sup>

**J. Matthew DeLesDernier,**

*Assistant Secretary.*

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<sup>13</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>14</sup> 17 CFR 240.17Ad-22(d)(11).

<sup>15</sup> 15 U.S.C. 78s(b)(2).

<sup>16</sup> In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

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

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