

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-68938; File No. SR-ICC-2012-23)

February 15, 2013

Self-Regulatory Organizations; ICE Clear Credit LLC; Order Approving Proposed Rule Change to Add Rules Related to the Clearing of iTraxx Europe Index CDS

I. Introduction

On December 6, 2012, ICE Clear Credit LLC (“ICC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change (SR-ICC-2012-23) 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> The proposed rule change was published for comment in the Federal Register on December 26, 2012.<sup>3</sup> On February 8, 2013, the Commission extended the time within which to take action of the proposed rule change to March 26, 2013.<sup>4</sup> The Commission received no comment letters regarding the proposal. For the reasons discussed below, the Commission is granting approval of the proposed rule change.

II. Description of the Proposed Rule Change

The purpose of the proposed rule change is to adopt new rules that will provide the basis for ICC to clear additional credit default swap contracts. ICC is proposing, as described in further detail below, to amend Chapters 8, 20, and 26 and Schedule 401 and Schedule 502 of its rules, as well as make corresponding changes to the applicable ICC Policies and Procedures to provide for the clearance of iTraxx Europe Index CDS (“iTraxx Contracts”). The iTraxx

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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> Securities Exchange Act Release No. 68481 (Dec. 19, 2012), 77 FR 76109 (Dec. 26, 2012).

<sup>4</sup> Securities Exchange Act Release No. 68882 (Feb. 8, 2013), 78 FR 10646 (Feb. 14, 2013).

Contracts reference the iTraxx Europe index, the current series of which consists of 125 European corporate reference entities. iTraxx Contracts, consistent with market convention and widely used standard terms documentation, can be triggered by credit events for failure to pay, bankruptcy and restructuring. iTraxx Contracts will be denominated in Euro.

ICC proposes to amend Chapter 8 of its rules to provide for an additional Guaranty Fund Contribution by those Clearing Participants that present Specific Wrong Way Risk (i.e., the risk that arises from the fact that iTraxx Contracts include, in part, the names of certain Clearing Participants or Clearing Participant affiliates). In a default scenario, if the defaulting Clearing Participant has funded a Specific Wrong Way Risk Contribution, the Specific Wrong Way Risk Contributions of all contributing Clearing Participants would be used immediately following the defaulting Clearing Participant's funds to cure deficits related to the default.

ICC proposes to amend Chapter 20 of its rules, concerning CDS generally, to remove definitions that are included in Chapter 26E of the rules, as well as to include the Specific Wrong Way Risk Guaranty Fund Contribution, as appropriate, as a portion of Clearing Participant funds.

ICC proposes to amend Section 26E of its rules to include certain additional provisions relevant to the treatment of restructuring credit events under iTraxx Contracts and standard single-name CDS Contracts referencing European corporate reference entities ("European SN Contracts"). In addition, ICC proposes to make conforming changes in Section 26E of the Rules (the CDS Restructuring Rules), principally to address the particular restructuring terms that apply to iTraxx Contracts and European SN Contracts. Specifically, ICC proposes to modify the notice delivery procedures in Rule 26E-104 to include "notices to exercise movement option" under the Modified Restructuring Maturity Limitation and Conditionally Transferable Obligation terms under the ISDA Credit Derivatives Definitions ("Mod Mod R terms"). In addition, the

definition of “Triggered Restructuring CDS Contract” has been modified to reflect that under Mod Mod R terms a CDS contract may be triggered in part following a restructuring credit event.

ICC also proposes to add Section 26F to provide for the clearance of the iTraxx Contracts. Rule 26F-102 (Definitions) sets forth the definitions used for the iTraxx Contract Rules. An “Eligible iTraxx Europe Untranching Index” is defined as “each particular series and version of an iTraxx Europe index or sub-index, as published by the iTraxx Untranching Publisher, included from time to time in the List of Eligible iTraxx Untranching Indexes,” which is a list maintained, updated and published by the ICC Board of Managers or its designee, containing certain specified information with respect to each index. “iTraxx Europe Untranching Terms Supplement” refers to the market standard form of documentation used for credit default swaps on the iTraxx Europe index, which is incorporated by reference into the contract specifications in Chapter 26F. ICEE has stated that the remaining definitions are substantially the same as the definitions found in ICC Section 26A and Section 26C, other than certain conforming changes.

Rules 26F-309 (Acceptance of iTraxx Europe Untranching Contracts by ICE Clear Credit), 26F-315 (Terms of the Cleared iTraxx Europe Untranching Contract), and 26F-316 (Updating Index Version of Fungible Contracts After a Credit Event or a Succession Event; Updating Relevant Untranching Standard Terms Supplement) reflect or incorporate the basic contract specifications for iTraxx Contracts. In addition to various non-substantive conforming changes, proposed Rule 26F-317 (Terms of iTraxx Europe Untranching Contracts) differs from

the corresponding Rule 26A-317 for CDX.NA Contracts to reflect the fact that restructuring is a credit event for the iTraxx Contract.<sup>5</sup>

In connection with clearing iTraxx Contracts, ICC will update Schedule 401 of its Rules (Eligible Collateral & Thresholds), as applicable, with respect to Initial Margin and Guaranty Fund liquidity requirements for Non-Client and Client-Related positions for both US Dollar and Euro denominated products.

ICC will also update Schedule 502 of its Rules (Cleared Products List) to include the following iTraxx Contracts: Markit iTraxx Europe Main Series 18 with a 5-year maturity, maturing on December 20, 2017; Markit iTraxx Europe Main Series 18 with a 10-year maturity, maturing on December 20, 2022; Markit iTraxx Europe Main Series 17 with a 5-year maturity, maturing on June 20, 2017; Markit iTraxx Europe Main Series 17 with a 10-year maturity, maturing on June 20, 2022; Markit iTraxx Europe Main Series 16 with a 5-year maturity, maturing on December 20, 2016; Markit iTraxx Europe Main Series 16 with a 10-year maturity, maturing on December 20, 2021; Markit iTraxx Europe Main Series 15 with a 5-year maturity, maturing on June 20, 2016; Markit iTraxx Europe Main Series 15 with a 10-year maturity, maturing on June 20, 2021; Markit iTraxx Europe Main Series 14 with a 5-year maturity, maturing on December 20, 2015; Markit iTraxx Europe Main Series 14 with a 10-year maturity,

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<sup>5</sup> The provisions dealing with the “spin-out” of a single name CDS following a restructuring credit event for a component of the iTraxx Europe index are part of the iTraxx Europe Untranchured Standard Terms Supplement (Nov. 2009 edition), which is incorporated into the contract specifications for cleared iTraxx Europe contracts through proposed ICC Rule 26F-315(c). Specifically, Section 7.3(b) of the Supplement addresses the removal of the restructured reference entity from the index and continuation of that component as a separate contract. (Proposed ICC Rule 26F-317(h) clarifies the treatment of the reference obligation for that separate cleared contract.) This is part of the basic standard terms of the iTraxx Europe contract and operates the same way in both the cleared and uncleared contexts (much like other aspects of the market standard terms supplements and/or ISDA Credit Derivatives Definitions on which other cleared and uncleared CDS trade).

maturing on December 20, 2020; Markit iTraxx Europe Main Series 13 with a 5-year maturity, maturing on June, 20, 2015; Markit iTraxx Europe Main Series 13 with a 10-year maturity, maturing on June, 20, 2020; Markit iTraxx Europe Main Series 12 with a 5-year maturity, maturing on December 20, 2014; Markit iTraxx Europe Main Series 12 with a 10-year maturity, maturing on December 20, 2019; Markit iTraxx Europe Main Series 11 with a 5-year maturity, maturing on June 20, 2014; Markit iTraxx Europe Main Series 11 with a 10-year maturity, maturing on June 20, 2019; Markit iTraxx Europe Main Series 10 with a 5-year maturity, maturing on December 20, 2013; Markit iTraxx Europe Main Series 10 with a 10-year maturity, maturing on December 20, 2018; Markit iTraxx Europe Main Series 9 with a 5-year maturity, maturing on June 20, 2013; Markit iTraxx Europe Main Series 9 with a 10-year maturity, maturing on June 20, 2018; Markit iTraxx Europe Main Series 8 with a 5-year maturity, maturing on December 20, 2012; Markit iTraxx Europe Main Series 8 with a 10-year maturity, maturing on December 20, 2017; Markit iTraxx Europe Main Series 7 with a 10-year maturity, maturing June 20, 2017; Markit iTraxx Crossover Series 18 with a 5-year maturity, maturing on December 20, 2017; Markit iTraxx Crossover Series 17 with a 5-year maturity, maturing on June 20, 2017; Markit iTraxx Crossover Series 16 with a 5-year maturity, maturing on December 20, 2016; Markit iTraxx Crossover Series 15 with a 5-year maturity, maturing on June 20, 2016; Markit iTraxx Crossover Series 14 with a 5-year maturity, maturing on December 20, 2015; Markit iTraxx Crossover Series 13 with a 5-year maturity, maturing on June, 20, 2015; Markit iTraxx Crossover Series 12 with a 5-year maturity, maturing on December 20, 2014; Markit iTraxx Crossover Series 11 with a 5-year maturity, maturing on June 20, 2014; Markit iTraxx Crossover Series 10 with a 5-year maturity, maturing on December 20, 2013; Markit iTraxx Crossover Series 9 with a 5-year maturity, maturing on June 20, 2013; Markit iTraxx HiVol

Series 18 with a 5-year maturity, maturing on December 20, 2017; Markit iTraxx HiVol Series 17 with a 5-year maturity, maturing on June 20, 2017; Markit iTraxx HiVol Series 16 with a 5-year maturity, maturing on December 20, 2016; Markit iTraxx HiVol Series 15 with a 5-year maturity, maturing on June 20, 2016; Markit iTraxx HiVol Series 14 with a 5-year maturity, maturing on December 20, 2015; Markit iTraxx HiVol Series 13 with a 5-year maturity, maturing on June, 20, 2015; Markit iTraxx HiVol Series 12 with a 5-year maturity, maturing on December 20, 2014; Markit iTraxx HiVol Series 11 with a 5-year maturity, maturing on June 20, 2014; Markit iTraxx HiVol Series 10 with a 5-year maturity, maturing on December 20, 2013; Markit iTraxx HiVol Series 9 with a 5-year maturity, maturing on June 20, 2013; and Markit iTraxx HiVol Series 8 with a 5-year maturity, maturing on December 20, 2012.

ICC also updated its Policies and Procedures to provide for the clearance of iTraxx Contracts, specifically the ICC Treasury Operations Policies & Procedures, ICC Risk Management Framework and ICC End-of-Day (“EOD”) Price Discovery Policies and Procedures. Consistent with the changes to Schedule 401 of the ICC Rules, the ICC Treasury Operations Policies & Procedures have been updated to include Initial Margin and Guaranty Fund liquidity requirements for Non-Client and Client-Related positions for both US Dollar and Euro denominated products. In order to accommodate the return of funds during London banking hours, the ICC Treasury Operations Policies & Procedures have been updated to require requests for Euro withdrawals to be submitted by 9:00 AM Eastern.

The ICC Risk Management Framework has been updated to account for Euro denominated portfolios. Specifically, updates have been made to the Guaranty Fund, Initial Margin and Mark-to-Market Methodologies to address: Wrong Way Risk, Foreign Exchange Risk, Liquidity Risk, Time Zone Risk, and Operational Risk. Additionally, the Portfolio

Approach was updated to include appropriate portfolio benefits between North American CDS Indices and iTraxx Contracts. ICE Clear Credit will continue to review risk parameters with Clearing Participants through existing governance procedures and will notify Clearing Participants of any changes.<sup>6</sup>

The ICC EOD Price Discovery Policies and Procedures has been updated to provide that ICC will use ICE Clear Europe's EOD prices for iTraxx Contracts and rely on the ICE Clear Europe Firm Trade process to ensure the accuracy of price submissions. ICC will extend the risk time-horizon for iTraxx Contracts to account for the half day difference, on average, between the EOD price discovery process timings. The extended risk horizon accounts for the fact that European markets close earlier and new financial information may be reflected only in the North American instrument prices and not reflected in the iTraxx Contracts, in general.

### III. Discussion

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>7</sup> Section 17A(b)(3)(F) of the Act 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

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<sup>6</sup> Telephone conversation February 15, 2013 among Michelle Weiler, Assistant General Counsel, ICE Clear Credit; Marta Chaffee, Assistant Director, SEC; Gena Lai, Senior Special Counsel, SEC; Jennifer Ogasawara, Financial Economist, SEC; and Justin Byrne, Attorney-Advisor, SEC.

<sup>7</sup> 15 U.S.C. 78s(b)(2)(C).

transactions, as well as to assure the safeguarding of securities and funds in the custody or control of the clearing agency or for which the clearing agency is responsible.<sup>8</sup>

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a registered clearing agency. The Commission carefully considered ICC's ability to clear the iTraxx Contracts in a manner that assures the safeguarding of securities and funds which are in the custody and control of ICC or for which ICC is responsible. In addition, the Commission notes that the Commodity Futures Trading Commission has determined that iTraxx Contracts are to be subject to mandatory clearing under Section 2(h) of the Commodity Exchange Act.<sup>9</sup> ICC's clearance of iTraxx Contracts therefore will promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions.

#### IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of the Act and in particular with the requirements of Section 17A of the Act<sup>10</sup>

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<sup>8</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>9</sup> 7 U.S.C. 2(h); see also Clearing Requirement Determination Under Section 2(h) of the CEA, Final Rule, 77 FR 74283 (Dec. 13, 2012) at 74291, 74336 - 74337.

<sup>10</sup> 15 U.S.C. 78q-1.



and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>11</sup> that the proposed rule change (File No. SR-ICC-2012-23) be, and hereby is, approved.<sup>12</sup>

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>11</sup> 15 U.S.C. 78s(b)(2).

<sup>12</sup> In approving this proposed rule change the Commission has considered the proposed rule's impact of efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>13</sup> 17 CFR 200.30-3(a)(12).