

Maria Zyskind
Staff Attorney

February 19, 2019

Re: Formalization of the ICC Risk Parameter Setting and Review Policy Pursuant to Section 5c(c)(1) of the Commodity Exchange Act and Commission Regulation 40.6(a)

VIA ELECTRONIC PORTAL

Mr. Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, D.C. 20581

Dear Mr. Kirkpatrick:

ICE Clear Credit LLC ("ICC") hereby submits, pursuant to Section 5c(c)(1) of the Commodity Exchange Act (the "Act") and Commodity Futures Trading Commission ("Commission") Regulation 40.6(a), a self-certification to formalize the ICC Risk Parameter Setting and Review Policy ("Risk Parameter Policy"). ICC is registered with the Commission as a derivatives clearing organization ("DCO"). ICC intends to implement the changes no sooner than the tenth business day following the filing of this submission with the Commission at its Washington, D.C. headquarters and with its Chicago regional office.

ICC proposes to formalize the Risk Parameter Policy that describes the process of setting and reviewing the risk management model ("model") core parameters and the performance of sensitivity analyses related to certain parameter settings. This submission includes a description of the Risk Parameter Policy. Certification of the Risk Parameter Policy pursuant to Section 5c(c)(1) of the Act and Commission Regulation 40.6(a) is also provided below.

Parameter Setting and Calibration

ICC's Risk Parameter Policy discusses the process of setting and reviewing the model core parameters and their underlying assumptions. The model requirements include bid/offer ("BO") requirements, large position requirements, Jump-To-Default ("JTD") requirements, interest rate ("IR") sensitivity requirements, basis risk requirements, and integrated spread response ("ISR") requirements. The parameters that are associated with the model requirements are listed in a table containing various parameter-related information, including the methods used to review parameter settings; the frequency of the reviews; and the groups involved in the review process ("reviewers"), such as the ICC Risk Management Department ("ICC Risk"), the Risk Working Group ("RWG"), or the Risk Committee. The parameters are described in more detail as follows.

The Risk Parameter Policy explains the process of setting and reviewing the liquidity charge parameters. The liquidity charge parameters are associated with BO requirements, also referred to as liquidity charges, which incorporate the transaction costs associated with liquidating the portfolio of a defaulting Clearing Participant ("CP"). With respect to index instruments, the Risk Parameter Policy specifies how ICC Risk estimates the BO Widths ("BOWs") for indices across volatile and extreme market conditions, in addition to how ICC Risk recognizes long-short benefits when computing portfolio-level index liquidity charges. In reference to single-name ("SN") instruments, the Risk Parameter Policy introduces certain parameters to incorporate a price-based BOW component and a spread-based BOW component into the liquidity charge. The Risk Parameter Policy requires ICC to estimate and review the liquidity charge

parameters at least monthly and summarizes the associated governance process, including the reviewers and any prerequisites to the implementation of parameter updates (e.g., review by the RWG or “no objection” ruling by the Risk Committee).

The Risk Parameter Policy discusses the estimation and the review of the concentration charge parameters, which are related to large position requirements. Large position requirements, also referred to as concentration charges, apply to positions that exceed a predefined notional amount threshold and increase as the amount above the threshold increases. The Risk Parameter Policy details how ICC Risk establishes series-specific or SN-specific concentration charge threshold levels for each index or SN Risk Factor (“RF”)¹, and how ICC Risk estimates concentration charge growth rates that determine how quickly concentration charges increase with position size. The Risk Parameter Policy directs ICC to estimate and review the concentration charge parameters at least monthly and provides information on the corresponding governance process, stating the reviewers and any prerequisites to implementing parameter updates.

The parameters impacting the JTD requirement are categorized as either Loss-Given-Default (“LGD”) or Wrong-Way Risk (“WWR”) parameters. ICC’s risk management methodology incorporates considerations of idiosyncratic credit events and the associated potential losses. These credit event losses are termed LGD, and the Risk Parameter Policy discusses the determination and review of the associated LGD parameters. Specifically, the Risk Parameter Policy explains how, in order to measure credit event losses, ICC Risk constructs JTD scenarios in terms of anticipated recovery rate (“RR”) levels (“RR scenarios”). The Risk Parameter Policy references RR scenarios and estimations for corporate SNs, sectors, and sovereign reference entities, and notes foreign exchange rate risk considerations with respect to sovereign reference entities. Additionally, the LGD computations at the RF Group (“RFG”)² level depend on certain RFG-related parameters, which are specified in the Risk Parameter Policy. The Risk Parameter Policy requires ICC to estimate and review the LGD parameters at least monthly and describes the associated governance process, noting the reviewers and any prerequisites to the implementation of parameter updates.

The Risk Parameter Policy details the process of setting and reviewing the WWR parameters. WWR arises when there is a strong adverse correlation between a CP’s default risk and the occurrence of large losses in a CP’s portfolio. ICC considers three types of WWR: specific WWR (“SWWR”) results from self-referencing trades; General WWR (“GWWR”) results from trades that involve RFs within the sovereign and banking sectors that are highly correlated with the CP, or with an entity that is guaranteed by, or affiliated with the CP; and Contagion WWR results from portfolio level aggregation of WWR exposure beyond a portfolio level WWR threshold. The Risk Parameter Policy contains information regarding the parameters that are used to quantify WWR dependence, compute WWR JTD requirements, and determine the level of WWR collateralization. The Risk Parameter Policy details the thresholds that are established as parameters for each RF generating WWR exposure, beyond which the increased level of WWR collateralization applies. Additionally, ICC estimates, reviews, and performs sensitivity analyses on the WWR parameters at least monthly, and the Risk Parameter Policy discusses the associated governance process, including the reviewers and any prerequisites to implementing parameter updates.

The Risk Parameter Policy contains information on the estimation and the review of the parameters that serve as inputs to the IR sensitivity requirement. The IR sensitivity requirement accounts for the risk associated with changes in the default-free discount term structure used to price CDS instruments. With respect to the IR sensitivity requirement parameters, the Risk Parameter Policy specifies how ICC Risk estimates the up and down parallel shifts for the US Dollar and Euro default-free discount term structures. The Risk Parameter Policy directs ICC to estimate and review the IR sensitivity requirement parameters at least monthly and specifies the corresponding governance process, noting the reviewers and any prerequisites to the implementation of parameter updates.

¹ ICC deems each index, sub-index, or underlying SN reference entity a separate RF.

² ICC deems a set of SN RFs related by a common parental ownership structure a RFG.

The Risk Parameter Policy discusses the setting and calibration of the parameters that are associated with the basis risk requirement. As index-derived SN positions and opposite “outright” SN positions are offset, the basis risk requirement is introduced to capture the differences between the trading characteristics of index instruments and their replicating baskets of SN constituents. In reference to the basis risk requirement parameters, the Risk Parameter Policy discusses how ICC Risk estimates the basis between index spreads for each index family and the basis attributable to the fact that the index and the SNs may have different coupons. ICC estimates and reviews the basis risk requirement parameters at least monthly, and the Risk Parameter Policy details the corresponding governance process, specifying the reviewers and any prerequisites to implementing parameter updates.

The parameters impacting the iSR requirement, which captures credit spread and RR fluctuations, are classified as either univariate or multivariate level. The standardized distributions that describe the behavior of credit spread log-returns are characterized by certain univariate level iSR parameters that are specified in the Risk Parameter Policy. Moreover, the Risk Parameter Policy discusses the estimation of the univariate level iSR parameters, including by considering time series analysis of credit spread log-returns. The Risk Parameter Policy explains how different mean absolute deviation (“MAD”) estimates are obtained for each time series. In addition, the Risk Parameter Policy references the setting of the exponentially weighted moving average (“EWMA”) decay rate (“EWMA factor”), along with the estimation of certain RF-specific parameters describing the SN RR distributions. The Risk Parameter Policy requires ICC to estimate, review, and perform sensitivity analyses on the univariate level iSR parameters at least monthly and specifies the associated governance process, including the reviewers and any prerequisites to the implementation of parameter updates.

The Risk Parameter Policy contains information regarding the process of determining and reviewing the multivariate level iSR parameters. Using a simulation framework, ICC generates spread and RR scenarios by means of copulas to connect the univariate distributions that describe spread and RR fluctuations. The Risk Parameter Policy describes the multivariate parameters that serve as inputs to the copula simulations. Namely, the Risk Parameter Policy specifies the setting of a certain parameter to reflect tail dependence, a concept indicating the probability of extreme values occurring jointly. The Risk Parameter Policy also references the estimation of the Kendall tau rank-order correlations for the copula simulations. ICC estimates and reviews the multivariate level iSR parameters at least monthly, and the Risk Parameter Policy notes the corresponding governance process, including the reviewers.

Sensitivity Analysis

The Risk Parameter Policy details the sensitivity analyses that ICC Risk performs to explore the sensitivity of the risk management system’s outputs to certain model core parameters that are calibrated on an ad-hoc basis and to alternative data analyses and parameter estimation techniques.

ICC conducts a sensitivity analysis on the univariate level iSR parameters by utilizing alternative techniques to estimate the parameters that fit the standardized distributions to the observed credit spread log-return data. The Risk Parameter Policy also considers the impact of the alternatively estimated parameters. This sensitivity analysis is reviewed with the RWG monthly and provides information if a change to the current estimation technique is considered. Further, the Risk Parameter Policy distinguishes two levels of sensitivity analyses, those that include a clearinghouse-wide portfolio impact study and those, such as this one, that do not include a portfolio impact study.

ICC performs a sensitivity analysis, which does not include a portfolio impact study, by introducing different values for the EWMA factor. The Risk Parameter Policy discusses the impact of using different values for this univariate level iSR parameter and requires ICC to review this sensitivity analysis monthly with the RWG.

Under the Risk Parameter Policy, ICC carries out a sensitivity analysis on the routinely updated parameters. The Risk Parameter Policy identifies certain parameters that are updated routinely (i.e., daily or monthly) and are subject to a sensitivity analysis with a clearinghouse-wide portfolio impact study. The Risk Parameter Policy requires that the results of the proposed parameter updates are reviewed with the

RWG prior to implementation and notes that this sensitivity analysis provides information regarding potential risk requirement changes due to routine parameter updates.

The portfolio benefits parameters are subject to a sensitivity analysis that includes a clearinghouse-wide portfolio impact study. Namely, ICC Risk estimates certain risk measures at pre-defined quantile levels by incorporating different dependence structures in order to guide ICC Risk in situations where back-testing results indicate excessive portfolio benefits. Under the Risk Parameter Policy, this sensitivity analysis is reviewed with the Risk Committee monthly.

Since the model allows the level of SWWR collateralization to be controlled by a model threshold, ICC conducts a sensitivity analysis for the SWWR threshold. ICC explores the maximum SWWR charges by requiring full collateralization of index-derived SWWR. This sensitivity analysis includes a clearinghouse-wide portfolio impact study and guides ICC Risk when there is a decision to fully collateralize SWWR. Under the Risk Parameter Policy, this sensitivity analysis is reviewed with the Risk Committee monthly.

ICC performs a sensitivity analysis on MAD levels by shifting all MAD estimates to their stress levels to provide information about the response of risk requirements to potential volatility shifts and to assess the viability of certain parameter-setting assumptions. This sensitivity analysis includes a clearinghouse-wide portfolio impact study and is reviewed monthly with the Risk Committee.

ICC Risk performs a sensitivity analysis for the Guaranty Fund (“GF”) JTD configuration. ICC’s GF model aims to establish financial resources that are sufficient to cover hypothetical losses associated with simultaneous credit events where up to five SN RFGs are impacted. In that, two of the selected SN RFGs are CP SN RFGs (i.e., Cover-2 GF sizing) and the other three SN RFGs are non-CP RFGs. ICC considers an alternative where three of the selected SN RFGs are CP SN RFGs (i.e., Cover-3 GF sizing) and the other two are non-CP SN RFGs. This sensitivity analysis includes a clearinghouse-wide portfolio impact study, provides information when a change to the GF JTD configuration is considered, and is reviewed with the Risk Committee monthly.

Core Principle Review:

ICC reviewed the DCO core principles (“Core Principles”) as set forth in the Act. During this review, ICC identified the following Core Principle as being impacted:

Financial Resources: The Risk Parameter Policy is consistent with the financial resources requirements of Core Principle B and the financial resource requirements set forth in Commission Regulation 39.33. The Risk Parameter Policy describes the process of setting and reviewing the model core parameters and the performance of sensitivity analyses related to certain parameter settings. The Risk Parameter Policy supports ICC’s ability to maintain sufficient margin requirements and enhances ICC’s approach to identifying potential weaknesses in the risk methodology by assuring the appropriateness of model core parameter settings through a regular review process involving various reviewers, thereby ensuring that ICC continues to maintain sufficient financial resources to withstand, at a minimum, a default by the two CP Affiliate Groups (“AGs”) to which it has the largest exposures in extreme but plausible market conditions, consistent with the requirements of Commission Regulation 39.33.

Risk Management: The Risk Parameter Policy is consistent with the risk management requirements of Core Principle D and the risk management requirements set forth in Commission Regulation 39.36. The Risk Parameter Policy directs ICC to estimate and review the model core parameter settings at least monthly and perform and review sensitivity analyses related to certain parameter settings monthly. Such procedures serve to promote the soundness of ICC’s risk management model and system and ensure that ICC possesses the ability to manage the risks associated with discharging its responsibilities, consistent with the risk management requirements of Core Principle D.

Amended Rules:

ICC proposes to formalize the Risk Parameter Policy. ICC has respectfully requested confidential treatment for the Risk Parameter Policy, which was submitted concurrently with this self-certification submission.

Certifications:

ICC hereby certifies that the Risk Parameter Policy complies with the Act and the regulations thereunder. There were no substantive opposing views to the changes.

ICC further certifies that, concurrent with this filing, a copy of the submission was posted on ICC's website, and may be accessed at: <https://www.theice.com/clear-credit/regulation>

ICC would be pleased to respond to any questions the Commission or the staff may have regarding this submission. Please direct any questions or requests for information to the attention of the undersigned at (312) 836-6854.

Sincerely,

A handwritten signature in cursive script that reads "Maria Zyskind".

Maria Zyskind
Staff Attorney