

December 23, 2019

Mr. Christopher J. Kirkpatrick
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Self-Certification Pursuant to Commission Rule 40.6 – CDS Procedures
Amendments (ISDA Definitions)

Dear Mr. Kirkpatrick:

ICE Clear Europe Limited (“ICE Clear Europe” or the “Clearing House”), a registered derivatives clearing organization under the Commodity Exchange Act, as amended (the “Act”), hereby submits to the Commodity Futures Trading Commission (the “Commission”), pursuant to Commission Rule 40.6 for self-certification, the amendments to its CDS Procedures ¹(the “CDS Procedures”) discussed herein. The amendments are to become effective on the first business day following the tenth business day after submission, or such later date as ICE Clear Europe may determine.

Concise Explanation and Analysis

ICE Clear Europe proposes to modify certain provisions of its CDS Procedures to incorporate amendments to the industry-standard International Swaps and Derivatives Association (“ISDA”), 2014 Credit Derivatives Definitions (the “2014 Definitions”) that are being adopted in the broader CDS market to address so-called narrowly tailored credit events and related matters.

The amendments to the CDS Procedures will incorporate changes to the 2014 Definitions that are intended to address so-called “narrowly tailored credit events”. In the wake of certain credit events and potential credit events in the CDS market in recent years, the International Swaps and Derivatives Association, Inc. (“ISDA”), in consultation with market participants, has developed and published the 2019 Narrowly Tailored Credit Event Supplement to the 2014 ISDA Credit Derivatives Definitions (the

¹ Capitalized terms used but not defined herein have the meanings specified in the ICE Clear Europe Rules or CDS Procedures.

“NTCE Supplement”).² The NTCE Supplement, if applied to a CDS transaction, effects two principal changes to the 2014 Definitions: (1) a change to the definition of the “Failure to Pay” credit event designed to exclude certain narrowly tailored credit events and (2) a change to the process for determining the Outstanding Principal Balance of an obligation to address certain obligations of a reference entity that were issued at a discount.

As described by ISDA in the attached guidance to the NTCE Supplement, the supplement was published in light of concerns among market participants and regulators about “instances of (CDS) market participants entering into arrangements with corporations that are narrowly tailored to trigger a credit event for CDS contracts while minimizing the impact on the corporation, in order to increase payment to the buyers of CDS protection.”³ ISDA has expressed concern that “narrowly tailored defaults . . . could negatively impact the efficiency, reliability and fairness of the overall CDS market.” Regulators have also expressed concern with narrowly tailored or manufactured credit events, including a joint statement by the heads of the Commission, the Securities and Exchange Commission and the UK Financial Conduct Authority that such strategies “may adversely affect the integrity, confidence and reputation of the credit derivatives markets, as well as markets more generally. These opportunistic strategies raise various issues under securities, derivatives, conduct and antifraud laws, as well as policy concerns.”⁴

With respect to the Failure to Pay credit event, the NTCE Supplement adopts a concept of a “Credit Deterioration Requirement.” If applicable, this requirement will provide that a failure of a reference entity to make a payment on an obligation will not constitute a Failure to Pay Credit Event if the failure “does not directly or indirectly either result from, or result in, a deterioration in the creditworthiness or financial condition” of the reference entity. As such, a “narrowly tailored” or “manufactured” failure to pay, which does not reflect or result in a credit deterioration, would not constitute a Credit Event for CDS Contracts that incorporate the NTCE Supplement and apply the Credit Deterioration Requirement. The NTCE Supplement also includes guidance as to factors relevant to the determination of whether credit deterioration has occurred. That determination would, under the 2014 Definitions, in the ordinary course be made by the relevant Credit Derivatives Determinations Committee. The NTCE Supplement also amends the method of calculating the Outstanding Principal Balance of obligations. The amendments are intended to address a potential scenario where a corporation agrees to issue a bond at a substantial discount to its principal amount, where the bond could be delivered in settlement of a CDS at its full principal amount. Under the 2014 Definitions, the Quantum of the Claim (which is used to determine the Outstanding Principal Balance used in calculating settlement obligations) is determined taking into account any applicable laws insofar as they reduce the size of the claim to reflect the original issue price or accrued value of the obligation. The NTCE Supplement clarifies

² The NTCE Supplement is published on the ISDA website at <https://www.isda.org/a/KDqME/Final-NTCE-Supplement.pdf>.

³ NTCE Supplement, Guidance on the interpretation of the definition of “Failure to Pay”.

⁴ Securities and Exchange Commission, Commodity Futures Trading Commission and UK Financial Conduct Authority, Joint Statement on Opportunistic Strategies in the Credit Derivatives Markets (June 24, 2019); see also Update to June 2019 Joint CFTC-SEC-FCA Statement on Opportunistic Strategies in the Credit Derivatives Market (Sept. 19, 2019).

that the applicable laws to be With respect to the Failure to Pay credit event, the NTCE Supplement adopts a concept of a “Credit Deterioration Requirement.” If applicable, this requirement will provide that a failure of a reference entity to make a payment on an obligation will not constitute a Failure to Pay Credit Event if the failure “does not directly or indirectly either result from, or result in, a deterioration in the creditworthiness or financial condition” of the reference entity. As such, a “narrowly tailored” or “manufactured” failure to pay, which does not reflect or result in a credit deterioration, would not constitute a Credit Event for CDS Contracts that incorporate the NTCE Supplement and apply the Credit Deterioration Requirement. The NTCE Supplement also includes guidance as to factors relevant to the determination of whether credit deterioration has occurred. That determination would, under the 2014 Definitions, in the ordinary course be made by the relevant Credit Derivatives Determinations Committee.

The NTCE Supplement also amends the method of calculating the Outstanding Principal Balance of obligations. The amendments are intended to address a potential scenario where a corporation agrees to issue a bond at a substantial discount to its principal amount, where the bond could be delivered in settlement of a CDS at its full principal amount. Under the 2014 Definitions, the Quantum of the Claim (which is used to determine the Outstanding Principal Balance used in calculating settlement obligations) is determined taking into account any applicable laws insofar as they reduce the size of the claim to reflect the original issue price or accrued value of the obligation. The NTCE Supplement clarifies that the applicable laws to be considered include any bankruptcy or insolvency law or other law affecting creditors’ rights to which the relevant obligation is or may become subject. In addition, the NTCE Supplement includes the concept of “Fallback Discounting,” which if designated to be applicable, provides a method for discounting the Quantum of the Claim (where it is not otherwise reduced under applicable law or pursuant to its own terms) of an obligation that is issued at less than 95% of its principal amount, based on straight-line interpolation between the issue price and the principal amount.

ICE Clear Europe has been advised that CDS market participants are expected to commence transacting in CDS incorporating the NTCE Supplement (with Credit Deterioration Requirement and Fallback Discounting applicable) on or about January 27, 2020. In addition, ISDA has published, and opened for adherence, an NTCE Protocol pursuant to which parties may, on a multilateral basis, agree to amend outstanding, non-cleared CDS transactions to incorporate the NTCE Supplement. The amendments made by the NTCE Protocol are also expected to have an implementation date of on or about January 27, 2020. Adherence to the protocol will thus make existing transactions fungible with transactions on the new terms. Accordingly, ICE Clear Europe is proposing to amend its CDS Procedures for relevant products to incorporate the NTCE Supplement, both for new and existing cleared transactions. For this purpose, the proposed ICE Clear Europe amendments would apply to all cleared CDS contracts with corporate (i.e., non-sovereign) reference entities, consistent with the NTCE Protocol and the expected approach for new CDS transactions. ICE Clear Europe proposes to make such changes effective by the industry implementation date.

Specifically, ICE Clear Europe would amend paragraph 1 of the CDS Procedures to include new definitions for “2019 NTCE Protocol”, “2019 NTCE Supplement” and “NTCE Protocol Effective Date”, which will be the date of implementation of the

amendment. The NTCE Protocol Effective Date will be January 27, 2020 (or such later date as designated by ICE Clear Europe by Circular). ICE Clear Europe would renumber the remaining provisions of paragraph 1 of the CDS Procedures accordingly.

ICE Clear Europe would further amend relevant subparts of the CDS Procedures to implement the NTCE Supplement for 2014-type CDS Contracts cleared by ICE Clear Europe. In this regard, in paragraph 8(c) of the CDS Procedures, a new subparagraph (iii) would be added to provide that for 2014-type CDS Contracts in effect as of the NTCE Protocol Effective Date or cleared one or after that date, the Applicable Credit Derivatives Definitions include the 2019 NTCE Supplement. Certain other amendments would apply to index CDS transactions and certain other amendments would apply to single-name CDS transactions.

For index CDS transactions, for iTraxx Europe transactions, in paragraph 9 of the CDS Procedures, the definitions of iTraxx Terms Supplement and iTraxx Legacy Terms Supplement would be amended to include the new standard terms supplement and confirmations for such transactions, which incorporate the NTCE Supplement (or any electronic equivalent thereto or other applicable document specified by the Clearing House). Pursuant to paragraphs 9.2 and 9.3, the applicable new documentation would apply to iTraxx Contracts submitted for clearing on or after the NTCE Protocol Effective Date. Conforming changes to other provisions to include references to such definitions would be made. In addition, a new paragraph 9.8 would be added to provide that existing open positions in iTraxx Contracts that are 2014-type CDS Contracts or that include a Component Transaction that is a 2014-type CDS Contract, would be amended, as of the NTCE Protocol Effective Date, to reference the applicable new standard terms supplement and confirmation in lieu of the standard terms supplement and confirmation previously in effect. This will have the effect of converting existing iTraxx Contracts to reference the new standard terms incorporating the NTCE Supplement, such that they will be fungible with new iTraxx Contracts, which will also reference the new standard terms supplement and confirmation.

Substantially similar changes for CDX.NA Contracts would be made in paragraph 10 of the CDS Procedures.

In the case of Single Name Contracts, the CDS Procedures would be amended by adding a new paragraph 11.8, which provides that existing open positions in all Single Name Contracts (other than Single Name Contracts for which the Relevant Transaction Type is "Standard Western European Sovereign") that are 2014-type CDS Contracts would be amended, effective as of the NTCE Protocol Effective Date, to reference the new relevant ISDA physical settlement matrix, to be published as of the NTCE Protocol Effective Date. The amendments will have the effect of converting existing Single Name Contracts to reference the updated physical settlement matrix, such that they will be fungible with new Single Name Contracts, which will also reference that matrix. The amendments would also provide that the amendments would be effective regardless of whether any transaction record in the Deriv/SERV warehouse is updated to reflect the change. Conforming changes would be made throughout paragraph 11 to reflect this change.

Compliance with the Act and CFTC Regulations

The rule amendments are potentially relevant to the following core principle: (C) Participant and product eligibility, (D) Risk management and (O) Legal Risk Considerations, and the applicable regulations of the Commission thereunder.

- *Participant and product eligibility.* ICE Clear Europe believes that the proposed amendments to the CDS Procedures are consistent with the participant and product eligibility requirements of Core Principle C and Commission Rule 39.12. The amendments incorporate changes to the standard terms of CDS Contracts that are being widely adopted by market participants to address potential concerns that have arisen with so-called narrowly tailored credit events.
- *Risk Management.* ICE Clear Europe believes that the proposed amendments to CDS Procedures are consistent with the risk management requirements of Core Principle D. ICEU believes the amendments, by implementing the NTCE Supplement for existing and new CDS Contracts, will be consistent with, and eliminate basis risk as compared to, changes being made in the uncleared CDS markets. The changes will also ensure the fungibility of new and existing contracts in light of the NTCE Supplement amendments, which will facilitate ongoing risk management by the clearing house and market participants. As a result, in ICEU's view, the amendments continue to ensure that ICEU possesses the ability to manage the risks associated with discharging its responsibilities and are consistent with Core Principle D and Commission Rule 39.13.
- *Legal Risk Considerations.* ICE Clear Europe believes that the proposed amendments to the CDS Procedures facilitate its ability to operate pursuant to an enforceable legal framework as references to ISDA will be updated to incorporate changes to the standard terms of CDS Contracts that are being widely adopted by market participants to address potential concerns that have arisen with so-called narrowly tailored credit events. As a result, in ICE Clear Europe's view, the amendments are consistent with the requirements of Core Principle O and Commission Rule 39.27.

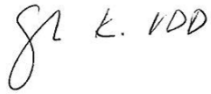
ICE Clear Europe hereby certifies that the amendments comply with the Act and the Commission's regulations thereunder.

ICE Clear Europe has received no substantive opposing views in relation to the proposed rule amendments.

ICE Clear Europe has posted a notice of pending certification and a copy of this submission on its website concurrent with the filing of this submission.

If you or your staff should have any questions or comments or require further information regarding this submission, please do not hesitate to contact the undersigned at carolyn.vandendaelen@theice.com or +44 20 7429 4515.

Very truly yours,

A handwritten signature in black ink, appearing to read 'C. L. VDD'.

Carolyn Van den Daelen
Head of Regulation & Compliance