

### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not significantly affect the protection of investors or the public interest, does not impose any significant burden on competition, and, by its terms, does not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>10</sup> and Rule 19b-4(f)(6) thereunder.<sup>11</sup>

The Exchange has requested that the Commission waive the 30-day operative delay. The Commission believes that waiver of the operative delay is consistent with the protection of investors and the public interest because such waiver will allow FINRA to more effectively carry out its enforcement activities on behalf of the Exchange. Therefore, the Commission designates the proposal operative upon filing.<sup>12</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change 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 email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NYSEAMEX-2011-93 on the subject line.

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>11</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires the Exchange to give the Commission written notice of the Exchange's intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

<sup>12</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

#### *Paper Comments*

Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090. All submissions should refer to File Number SR-NYSEAMEX-2011-93. This file number should be included on the subject line if email 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 Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change 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 Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make publicly available. All submissions should refer to File Number SR-NYSEAMEX-2011-93, and should be submitted on or before January 12, 2012.

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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### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-66001; File No. SR-ICC-2011-03]

#### **Self-Regulatory Organizations; ICE Clear Credit LLC; Order Approving Proposed Rule Change To Adopt ICC's Enhanced Margin Methodology**

December 16, 2011.

#### **I. Introduction**

On November 4, 2011, ICE Clear Credit LLC ("ICC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change SR-ICC-2011-03 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 November 10, 2011.<sup>3</sup> The Commission received three comment letters regarding the proposal.<sup>4</sup> For the reasons discussed below, the Commission is granting approval of the proposed rule change.

#### **II. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

This rule permits ICC to make certain modifications to its Risk Management Framework for clearing credit default swap ("CDS") contracts. These modifications are collectively referred to as the "Portfolio Decomposition Model." A fundamental aspect of ICC's Portfolio Decomposition Model is the recognition that CDS contracts cleared by ICC referencing broad-based securities indices are essentially compositions of specific single-name CDS contracts. Under the Portfolio Decomposition Model, ICC would, among other things, decompose CDS contracts referencing broad-based

<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. 34-65699 (November 7, 2011), 76 FR 70206 (November 10, 2011). In its filing with the Commission, ICC included statements concerning the purpose of and basis for the proposed rule change. The text of these statements is incorporated into the discussion of the proposed rule change in Section II below.

<sup>4</sup> See comment letter from Michael Hisler, Swaps & Derivatives Market Association, dated December 5, 2011 ("SDMA Letter") and comment letters from John Williams, Allen & Overy LLP, on behalf of Bank of America Merrill Lynch, Barclays Capital, BNP Paribas, Citi, Credit Suisse Securities (USA), Deutsche Bank AG, JPMorgan Chase & Co., Morgan Stanley and UBS Securities LLC, dated December 1, 2011 and December 5, 2011 ("Allen & Overy Letters"). Allen & Overy LLP's December 5, 2011 letter amended its December 1, 2011 letter, with the sole change consisting of the addition of The Goldman Sachs Group, Inc., Nomura Securities International, and The Royal Bank of Scotland plc as signatories.

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

securities indices into single-name, index-derived positions with notional amounts corresponding to their relative weight in the index.

In connection with the decomposition of CDS contracts referencing broad-based securities indices, ICC will incorporate jump-to-default risk as a component of the risk margin associated with the clearing of CDS index products. Because ICC's prior methodology did not include jump-to-default margin requirements for CDS index products, this change will result in a better measurement of the risk associated with clearing these contracts. ICC believes that the Portfolio Decomposition Model also reflects a number of other enhancements to the ICC Risk Management Framework. Examples of these changes include: Replacing standard deviation with mean absolute deviation as a measure of spread volatility, implementing an autoregressive process to obtain multi-horizon risk measures, expanding spread response scenarios, introducing liquidity margin requirements for CDS index products, and base concentration charges.

In addition, implementation of the Portfolio Decomposition Model will also allow ICC to provide portfolio margin treatment between index CDS contracts and offsetting single-name CDS contracts. These portfolio benefits will generally involve ICC providing margin offsets across single-name CDS contracts and index CDS contracts that are held in a clearing participant's portfolio based on correlation measurements.

To date, ICC has not offered such portfolio margin treatment strictly for operational reasons. However, ICC has informed the Commission that it will be operationally ready to offer portfolio margining with respect to its clearing participants' proprietary positions sometime in mid-December 2011. In its filing with the Commission, ICC noted that the portfolio margining treatment will only be available to ICC clearing participants' proprietary positions because ICC does not currently clear single-name CDS contracts for customer-related transactions. Accordingly, there are currently no customer-related positions in single-name CDS contracts that would qualify for portfolio margining treatment. Because the portfolio margining benefits afforded by the enhancements to the model are available to all of ICC's participants with respect to their proprietary positions, ICC believes that the proposed rule change does not unfairly

discriminate with respect to similarly-situated participants.<sup>5</sup>

According to ICC, the enhancements effected by this proposed rule change have been reviewed and/or recommended by the ICC Risk Working Group, ICC Risk Committee, ICC Board of Managers, the Federal Reserve Bank of New York and the New York State Banking Department. In addition, ICC commissioned a third-party risk-management consultant to complete a model assessment of ICC's Portfolio Decomposition Model.

### III. Comments

The Commission received three comment letters on the proposed rule change from two commenters, both of which were supportive of the changes.<sup>6</sup> Specifically, one commenter noted that by permitting portfolio margining to occur with respect to clearing participants' proprietary accounts, ICC's proposed Portfolio Decomposition Model would optimize more efficient risk management through netting, thereby promoting greater stability for central clearing.<sup>7</sup> This commenter noted that, because of the high degree of correlation between single-name CDS contracts and index CDS contracts, market participants often maintain hedged portfolios of these products, thereby increasingly the impact that these changes are likely to have throughout the market. The second commenter, which represented a group of eight large financial firms, expressed a similar view with respect to the ability of portfolio margining to bring about a more stable central clearing regime and concluded that the proposed rule change represented "an initial positive step for the industry."<sup>8</sup>

### IV. Discussion

Section 19(b)(2)(B) of the Act directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such

<sup>5</sup> ICC further indicated in its rule filing that it would expect to offer portfolio margining treatment to customer-related transactions following: (i) The commencement of clearing single-name CDS contracts for customer-related transactions and (ii) the granting of certain relief by the Commission and the Commodity Futures Trading Commission ("CFTC") in response to requests by ICC. Specifically, on November 7, 2011, ICC formally filed with the Commission a petition to provide portfolio margining treatment for customer-related positions in anticipation of ICC offering clearing of single-name CDS contracts for customer-related transactions in the future. Available at: <http://www.sec.gov/rules/petitions.shtml>. ICC filed a similar request with the CFTC on October 4, 2011, available at: <http://www.cftc.gov/PressRoom/PressReleases/pr6145-11>.

<sup>6</sup> See *supra* note 4.

<sup>7</sup> See SDMA Letter.

<sup>8</sup> See Allen & Overy Letters.

proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization.<sup>9</sup> For example, Section 17A(b)(3)(F) of the Act<sup>10</sup> requires, among other things, that the rules of a clearing agency be designed to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions and to assure the safeguarding of securities and funds in the custody or control of the clearing agency or for which it is responsible.

If approved, the proposed rule change would allow ICC to provide portfolio margining offsets to its participants to the extent that the participants maintain proprietary portfolios that hedge index CDS products against single-name CDS products. ICC believes that these changes promote greater capital efficiency and further contribute to the development of a national system for the prompt and accurate clearance and settlement of CDS contracts. The Commission carefully reviewed the proposed changes to ICC's Risk Management Framework to ensure that those changes continue to allow ICC to adequately manage the risks associated with the clearing of both index and single-name CDS contracts. In particular, the Commission notes that the Portfolio Decomposition Model will introduce new requirements to provide additional margin to address liquidity and jump-to-default risks in connection with the clearing of index CDS products. After considering these changes, including each of the representations made by ICC in the filing, the Commission believes that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act, including ICC's obligation to ensure that its rules be designed to assure the safeguarding of securities and funds in the custody or control of the clearing agency or for which it is responsible.

### V. 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>11</sup> and the rules and regulations thereunder.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>12</sup> that the

<sup>9</sup> 15 U.S.C. 78s(b)(2)(B).

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

<sup>11</sup> 15 U.S.C. 78q-1.

<sup>12</sup> 15 U.S.C. 78s(b)(2).

proposed rule change (File No. SR-ICC-2011-03) be, and hereby is, approved.<sup>13</sup>

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>14</sup>

**Kevin M. O'Neill,**  
*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-65990; File No. SR-OCC-2011-17]

### Self-Regulatory Organizations; The Options Clearing Corporation; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Novation of Trades at OCC

December 16, 2011.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934,<sup>1</sup> notice is hereby given that on December 12, 2011, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("the Commission") the proposed rule change as described in Items I and II below, which items have been prepared primarily by OCC. OCC filed the proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>2</sup> and Rule 19b-4(f)(4) thereunder<sup>3</sup> so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of Terms of Substance of the Proposed Rule Change

The proposed rule change would make clarifying amendments to provisions of OCC's By-Laws relating to the timing of OCC's acceptance or "novation" of exchange transactions in order to provide clearing members with certainty as to when their credit exposure to the original counterparty to a trade is terminated and OCC becomes obligated with respect to such trades.<sup>4</sup>

<sup>13</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>14</sup> 17 CFR 200.30-3(a)(12).

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

<sup>2</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>3</sup> 17 CFR 240.19b-4(f)(4).

<sup>4</sup> The proposed rule change neither alters the rights of members nor the timing of OCC's novation. Telephone conference between Steve Szarmack, Vice President and Associate General Counsel, OCC, and Pamela Kesner, Special Counsel, Securities and Exchange Commission Division of Trading and Markets on December 14, 2011.

#### II. Self-Regulatory Organization's Statement of Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, OCC 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. OCC has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

##### A. Self-Regulatory Organization's Statement of Purpose of, and Statutory Basis for, the Proposed Rule Change

Recently, certain OCC clearing members have expressed uncertainty as to the time when an exchange transaction is accepted for clearing and the "novation" of such transaction occurs under OCC's By-Laws and Rules. The purpose of this proposed rule change is to make clarifying amendments to provisions of OCC's By-Laws relating to the timing of OCC's acceptance or "novation" of exchange transactions in order to provide clearing members with certainty as to when their credit exposure to the original counterparty to a trade is terminated and OCC becomes obligated with respect to such trades.

##### Background

Article VI, Section 5 of OCC's By-Laws generally establishes that exchange transactions (*i.e.*, matched trades in an option, future, or other cleared contract) are deemed to be accepted by OCC for clearing at the "commencement time" for such transactions, or in the case of a future, when a matched trade has been properly reported to OCC. The definition of "commencement time" in Article I of OCC's By-Laws contains substantive provisions establishing specific times when exchange transactions are deemed accepted for clearing for the majority of exchange transactions (*i.e.*, commencement time is when daily position reports are made available to clearing members) as well as exceptions establishing different commencement times for cross-rate currency options, FX Index Options and certain non-competitively executed transactions in cleared futures. However, neither Section 5 of Article VI nor the definition of "commencement time" expressly state that OCC's "novation" of trades occurs at this time, and the term "novation" is used only once in OCC's By-Laws—in an interpretation following

Section 6 of Article IV (Issuance of Cleared Contracts).

Confusion may also arise from the fact that Article VI, Section 5 of the By-Laws states that futures contracts are accepted for clearing when they are properly reported to OCC, rather than at the commencement time of such transactions. This provision appears to give futures contracts more favorable treatment than options, although there is no such result as a practical matter. Section 8 of Article VI provides that, except with respect to trades in certain narrow categories of options, OCC generally has no right to reject any exchange options transaction due to the failure of the purchasing clearing member to pay any amount due to OCC at or before the settlement time.<sup>5</sup> Accordingly, exchange transactions in most option products will inevitably be accepted for clearing and novated under the rules at the commencement time of such transactions simply due to the passage of time. Prior to the 1987 crash, OCC reserved the right to reject trades in options due to non-payment of premiums. However, OCC subsequently gave up that right (with limited exceptions) in order to create greater certainty for clearing members.<sup>6</sup> Therefore, the right to reject an exchange transaction for non-payment is now the exception rather than the rule. When OCC began clearing futures, it was deemed appropriate to state in the By-Laws that futures contracts would be accepted when properly reported because futures do not require premium payments.<sup>7</sup>

##### Proposed By-Law Changes

OCC proposes to amend the definition of "commencement time" in Article I of the By-Laws to (i) remove the substantive provisions establishing the specific times when exchange transactions in various products are deemed accepted for clearing (as such provisions should be placed in the

<sup>5</sup> The exceptions are contained in the Articles governing specific products. For example, Section 5 of Article XX (addressing cross-rate foreign currency options and Section 7 of Article XXIII (addressing FX Index Options) condition OCC's acceptance of trades in those products for clearing on the completion of settlement payments in respect of such trades. These exceptions apply because settlements involving foreign currencies in different time zones create heightened exposure to OCC if a Clearing Member were to default.

<sup>6</sup> The staff notes that this change was adopted in filing SR-OCC-90-05. See Securities Exchange Act Release No. 29853 (October 25, 1991), 56 FR 55968 (October 30, 1991).

<sup>7</sup> Article XII, Section 7 of the By-Laws makes an exception for non-competitively executed futures trades. Because such trades may be executed away from the market price, OCC does not accept them until the initial variation payment is made.