

CME IBOR Conversion Plan for Cleared Swaps

As the industry advances risk-free rate (RFR) indexed swaps, CME Group continues our collaborative approach to identify, understand, and create innovative solutions for hurdles faced by market participants.

Background:

IBOR Fallbacks are in the process of being implemented across the industry:

- ISDA IBOR Fallbacks Supplement 70 to the 2006 ISDA definitions covering new exposures and the corresponding Protocol for updating legacy contracts went into effect on January 25, 2021
- In tandem, the CME Rulebook has incorporated ISDA IBOR Fallbacks for both “new” and “legacy” cleared OTC IRS for certain currencies (as is the case with other CCPs), see Clearing Advisory [21-039](#) for more information
- Under the bilateral and cleared fallback arrangements, at the relevant Index Cessation Effective Date, OTC IRS contracts will transition from the floating index of existing IBOR exposure to an all-in fallback rate based on the RFR and the ISDA credit spread, shifting the rate fixing to ‘in arrears’
- On March 5th, 2021, the FCA made an [announcement](#) regarding the future cessation or loss of representativeness of all LIBOR benchmarks. As a result, the following Index Cessation Effective Dates have been determined by ISDA for the following LIBORs:
 - CHF, GBP, JPY, EUR LIBOR (all tenors), the first London Banking Day after publication on December 31, 2021
 - USD ICE LIBOR (all tenors), the first London Banking Day after publication on June 30, 2023

Challenges of reliance on ISDA Fallbacks:

Market participants have identified certain challenges associated with implementing ISDA Fallbacks (for both cleared and uncleared contracts), including:

- **Operationally** – After an Index Cessation Effective Date, while the IBOR-referencing swaps will “fall back” to RFRs, these resulting legacy swaps will not be on the same terms as standardized swaps referencing RFRs. As a result, participants wishing to unwind these “fallback legacy” contracts will need to execute and book additional non-standard swaps
- **Risk management** – Uncertainty will remain regarding what the liquidity profile for “fallback legacy” swaps will look like in the years post an Index Cessation Effective Date

Conversion as a solution:

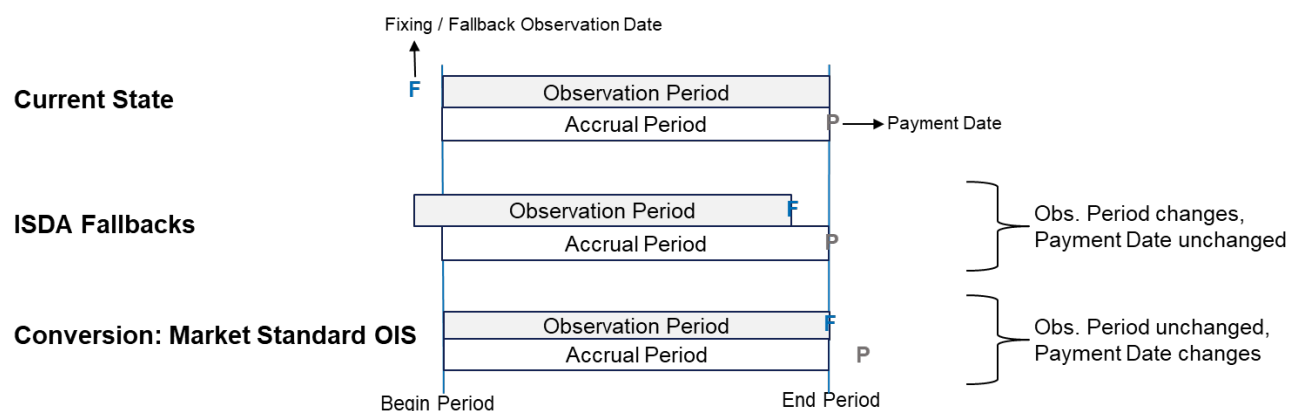
To help address these challenges, market participants have requested CCPs to consider transitioning existing IBOR swap exposures to RFR OIS trades just prior to an Index Cessation Effective Date.

CME Group recognizes the issues and has been consulting with market participants to consider the merits of a mandatory CCP-led conversion. Before addressing potential operational mechanics, we wish to emphasize that:

- Our goal is to explore an industry solution featuring, where practicable:
 - a. Coordination of approach and timing across CCPs
 - b. Currency agnostic approach that can be applied to all impacted trades
- The core principle of any conversion solution should be to minimize disruptions, considering:
 - a. Changes to duration and discounting risk
 - b. Tax and Hedge Accounting concerns

Following a series of bilateral conversations, and engagement at the CFTC MRAC, we believe the market is supportive of converting IBOR cleared swaps to market standard OIS trades referencing the relevant RFR shortly prior to the corresponding Index Cessation Effective Date by (i) adjusting the floating leg by the ISDA spread to maintain duration, discounting risk as well as accruals and (ii) processing a cash adjustment to account for any changes in valuation corresponding to the conversion

Comparison of ICE LIBOR, ISDA Fallbacks & Conversion Approach (USD shown)



	ISDA Fallbacks	Market Standard OIS
Floating Rate Index	USD-LIBOR-BBA	USD-SOFR-COMPOUND
Payment Date Offset	n/a	2D
Calculation Method	Daily Compounding	Daily Compounding
Resets	In Arrears	In Arrears
Observation Period Shift	2D	n/a
Current Accrual Periods	IBOR Fixing	IBOR Fixing
Rate Adjustment	"all in" Fallback Rate	Spread Adj. on float leg
Cash Compensation	n/a	Yes

Additional Considerations

1. **Conversion timing for trades referencing ICE LIBORs:**
 - a. CHF and JPY at close of business on December 3, 2021
 - b. GBP at close of business on December 17, 2021
 - c. USD just prior to June 30, 2023 (specific date to be determined)
2. **LIBOR fixings that occur prior to the conversion process and are yet to settle** - ICE LIBOR fixings that occur prior to the conversion process will be maintained and carried over to the market standard OIS.
3. **LIBOR fixings that occur after the conversion process and prior to the Index Cessation Effective Date** – In order to maintain the economics and cash flows associated with these trades, CME will convert these swaps after the fixing has occurred.
4. **Processing** – CME intends to characterize the conversion process as an amendment, which will be processed via a cancel and rebook for operational efficiencies.
5. **Post conversion support of LIBOR swaps (Swaption expiries)** – CME intends to support the clearing of LIBOR indexed swaps post a CCP-led mandatory conversion. Specifically, if a LIBOR trade is submitted for clearing post the conversion process, it would be accepted for clearing and then as part of the end-of-day process, converted into a market standard RFR position by (i) adding the ISDA spread to the floating leg and (ii) processing a cash adjustment to account for any changes in value corresponding to the conversion based upon the CME 3pm EST SOFR settlement curve.
6. **Basis Swaps** – will be converted into pairs of fixed/float swaps with offsetting fixed payments prior to a conversion process.
7. **FRAs** – will be converted into LIBOR indexed single period swaps with a corresponding cash adjustment to account for any changes in value prior to a conversion process.
8. **Zero Coupon and Compounding Swaps** – treatment can be found in the detailed presentation referenced below.

CME Group Next Steps and Timing Goals

CME Group will:

- Continue conversations with market participants and industry working groups with the goal of finalizing the above additional considerations
- Publish a detailed [presentation](#) outlining the approach to the additional considerations during the month of June

The above items are for discussion purposes only. This proposal is subject to change based on the feedback received, subject to implementation of final rules by CME and regulatory approval. If you would like to discuss this topic further or provide feedback, please contact your CME Group sales representative or email InterestRate@cmegroup.com.