

ISDA Benchmarks Supplement – FAQs

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1. What is the ISDA Benchmarks Supplement?

The ISDA Benchmarks Supplement (the ‘**Benchmarks Supplement**’) enables parties to include certain triggers and generic fallbacks in transactions which reference benchmarks and incorporate one or more of the following definitional booklets (the ‘**relevant definitional booklets**’):

- 2006 ISDA Definitions
- 2002 ISDA Equity Derivatives Definitions
- 1998 FX and Currency Option Definitions
- 2005 ISDA Commodity Definitions

It has been produced primarily in order to address certain requirements under the EU Benchmarks Regulation.¹ However, parties may also choose to incorporate the Benchmarks Supplement in light of IOSCO’s *Statement on Matters to Consider in the Use of Financial Benchmarks*² or if they otherwise consider that doing so will enhance the contractual robustness of relevant transactions.

2. What does the EU Benchmarks Regulation require in this context?

(a) Contracts need to reflect plans for material change to, and cessation of, a benchmark

Article 28(2) of the EU Benchmarks Regulation requires EU supervised entities that use a benchmark to produce and maintain robust written plans setting out the actions that they would take in the event that a benchmark materially changes or ceases to be provided. Where feasible and appropriate, those plans are required to nominate one or several alternative benchmarks that could be referenced to substitute the benchmark no longer provided, indicating why such benchmarks would be suitable alternatives. The plans must be reflected in the contractual relationship with clients.

The definition of ‘supervised entities’ includes credit institutions, investment firms, insurance undertakings, reinsurance undertakings, UCITS, alternative investment fund managers, institutions for occupational retirement provision, creditors and non-credit institutions for the purposes of credit agreements, market operators, CCPs and trade repositories.

(b) Prohibition on use of a benchmark

Article 29(1) of the EU Benchmarks Regulation prohibits supervised entities from using a benchmark (or a combination of benchmarks) in the EU unless the benchmark is:

- provided by an administrator located in the EU and included in the register of administrators and benchmarks maintained by the European Securities and Markets Authority (‘**ESMA**’); or
- provided by an administrator located outside the EU and is a benchmark which is included in ESMA’s register of administrators and benchmarks.

If an administrator fails to make a successful application to have itself or its benchmark included in ESMA’s register before expiry of the EU Benchmarks Regulation’s transitional period on 1 January 2020, or if its inclusion in the register is subsequently withdrawn (or, in certain circumstances, suspended) by regulators, use of the benchmark by EU supervised entities will not be permitted.

¹ Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014

² <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD589.pdf>. See Question 3 of this FAQ for further information.

3. What does the IOSCO's Statement on Matters to Consider in the Use of Financial Benchmarks³ require?

In January 2018, IOSCO issued guidance which recommends that users of benchmarks in financial contracts and financial instruments should have robust written plans in place to deal with the material change to, or cessation of, a benchmark. This guidance is similar to the requirements under the EU Benchmarks Regulation but is aimed at users of benchmarks globally. Like the IOSCO 'Principles for Financial Benchmarks'⁴, which the IOSCO Statement complements, the guidance does not, on its own, have legislative or regulatory force.

4. How does the Benchmarks Supplement address the issues raised by the EU Benchmarks Regulation and IOSCO's Statement on Matters to Consider in the Use of Financial Benchmarks?

When used in combination with the relevant definitional booklets, the Benchmarks Supplement incorporates:

- fallback arrangements which apply if a benchmark ceases to be provided;
- fallback arrangements which apply if a benchmark or its administrator is not authorised (or similarly approved) or included in an official register (including where such authorisation or inclusion is suspended or withdrawn) in accordance with applicable law; and
- acknowledgements regarding the consequences following a change to a benchmark.

Given that some of the relevant definitional booklets already contain fallbacks which apply upon the occurrence of some of these events, the amendments which would be made by incorporating the Benchmarks Supplement into the terms of a transaction vary from booklet to booklet.

5. Does the Benchmarks Supplement include fallback arrangements following material change to a benchmark?

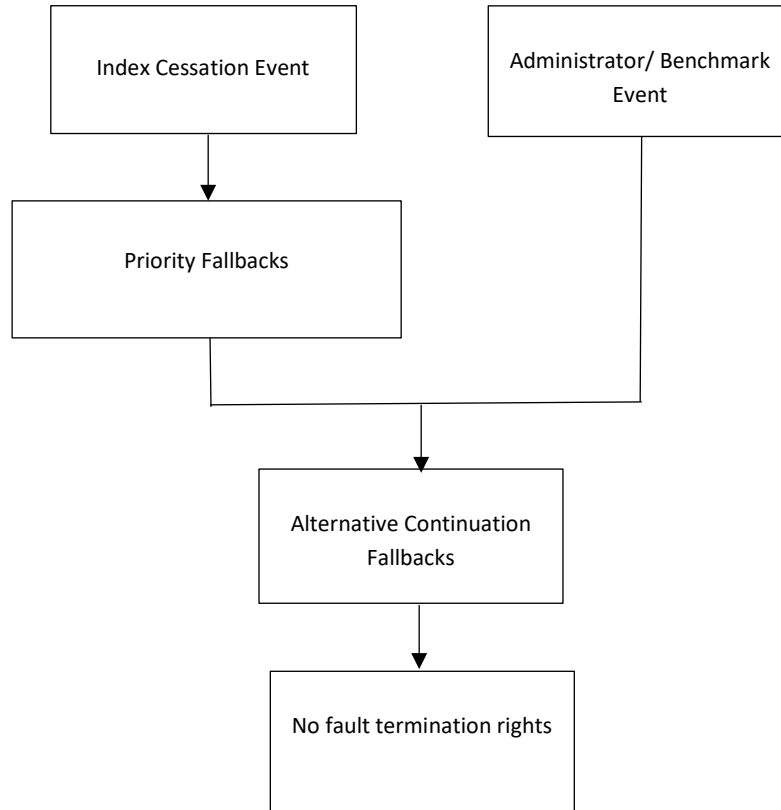
The Benchmarks Supplement does not introduce new fallback arrangements for material change to a benchmark (although some of the relevant definitional booklets already have provisions which may apply upon such an event). Instead, with respect to the 2006 ISDA Definitions and the 1998 FX and Currency Option Definitions, an acknowledgement that the transaction will continue to reference the benchmark as changed is included.

³ <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD589.pdf>

⁴ <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD415.pdf>

6. How does the Benchmarks Supplement amend the 2006 ISDA Definitions?

The 2006 ISDA Definitions Benchmarks Annex ('**2006 Annex**'), which forms part of the Benchmarks Supplement, sets out fallbacks to be applied in the event that either an Index Cessation Event or an Administrator/Benchmark Event⁵ occurs.



(a) Priority Fallbacks

If the definition of a benchmark (for example, contained in the 2006 ISDA Definitions) includes a reference to an ‘index cessation event’, then the fallbacks specified within that definition (called ‘**Priority Fallbacks**’) will apply upon the occurrence of an index cessation event in priority to the fallback arrangements which would otherwise apply under the Benchmarks Supplement. Only if the Priority Fallbacks fail to provide a means of determining an index level in this scenario would the fallback arrangements in the Benchmarks Supplement apply.

By way of example, the definition of USD-SOFR-COMPOUND⁶ in the 2006 ISDA Definitions includes fallbacks which are stated to apply upon the occurrence of a ‘SOFR Index Cessation Event’. These fallbacks will constitute Priority Fallbacks and will apply in priority to the fallbacks set out in the Benchmarks Supplement if a ‘SOFR Index Cessation Event’ occurs.

The fallbacks to specific rates (see Question 7 below) that ISDA is developing for the London Interbank Offered Rate (‘LIBOR’), the Tokyo Interbank Offered Rate (‘TIBOR’), the Euro Interbank Offered Rate (‘EURIBOR’), the Australian dollar Bank Bill Swap Rate (‘BBSW’), the Hong Kong Interbank Offered

⁵ An Administrator/Benchmark Event encompasses circumstances in which a benchmark or its administrator is not authorised (or similarly approved) or included in an official register (including where such authorisation or inclusion is suspended or withdrawn) in accordance with applicable law.

⁶ <https://www.isda.org/a/kKHEE/Supplement-57-USD-SOFR-COMPOUND.pdf>

Rate ('HIBOR') and potential other 'interbank offered rates' (referred to as 'IBORs') will result in the definitions of those IBORs being amended in the 2006 ISDA Definitions to include the concept of an 'index cessation event' and related fallbacks to specific rates that would apply upon the occurrence of such an event. Under the terms of the Benchmarks Supplement, once the IBOR Fallbacks are incorporated into the terms of a transaction (whether by entering into new transactions incorporating the amended 2006 ISDA Definitions or by incorporating the amended definitions into existing transactions by protocol or otherwise), those fallbacks will automatically constitute Priority Fallbacks for the purposes of an index cessation event.

It is important to note, however, that the Priority Fallbacks only apply if there is a permanent cessation of the relevant benchmark which constitutes an 'index cessation event'. Under the terms of the Benchmarks Supplement, therefore, the Priority Fallbacks will not apply upon the occurrence of an Administrator/Benchmark Event⁵ (unless there is also an 'index cessation event') and instead the fallbacks set out in the Benchmarks Supplement will apply.

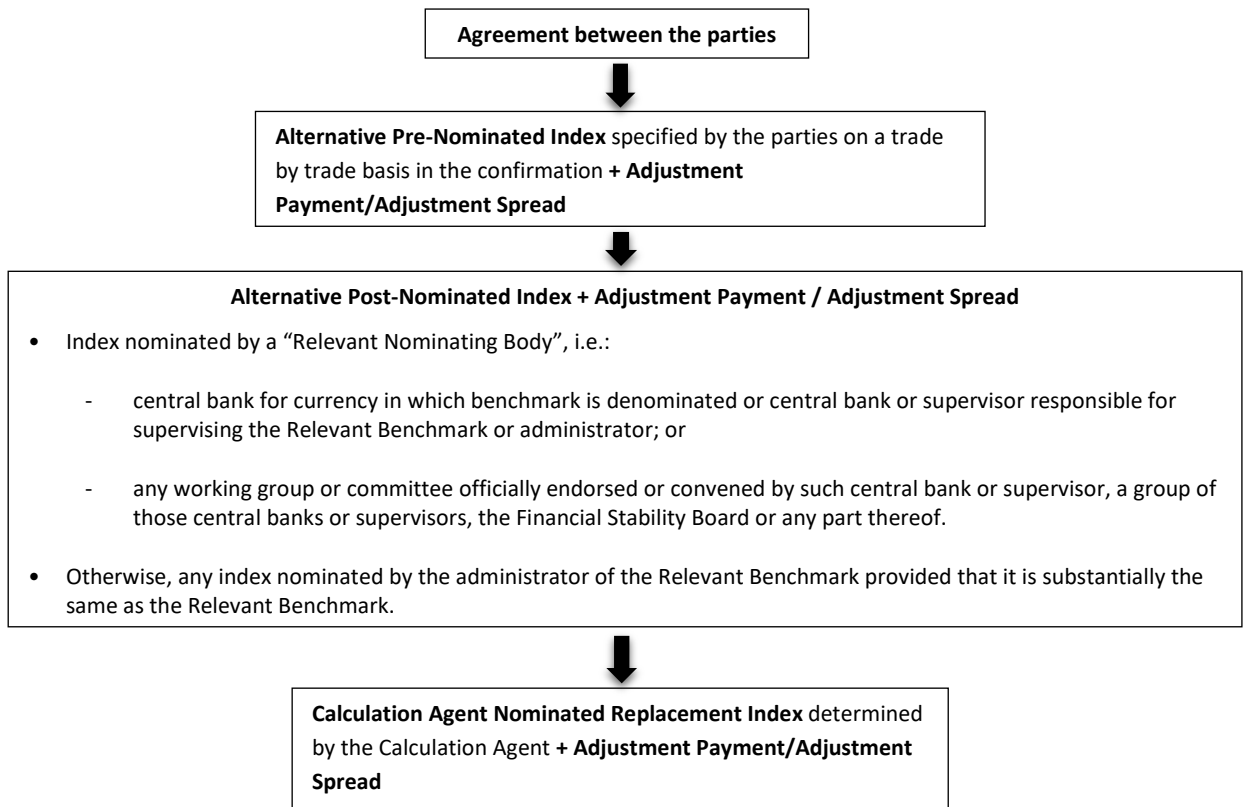
(b) Alternative Continuation Fallbacks within the Benchmarks Supplement

If:

- an Index Cessation Event occurs and either there are no Priority Fallbacks or they fail to produce a level for the index; or
- an 'Administrator/Benchmark Event'⁵ occurs without an Index Cessation Event also occurring,

the Benchmarks Supplement sets out a waterfall of 'Alternative Continuation Fallbacks' each of which the parties agree to seek to apply during a period of 15 business days (subject to extension in some circumstances) in order to allow the transaction to continue. If, at the end of this period of time, more than one Alternative Continuation Fallback can be used, the first in the hierarchy below will prevail.

Alternative Continuation Fallbacks to be pursued in parallel



(c) Adjustments to the transaction

The alternative index applied under an Alternative Continuation Fallback may have different characteristics from the index it replaces. Provision is therefore made for an ‘Adjustment Payment’ or an ‘Adjustment Spread’. The Calculation Agent may make other adjustments to account for the effect of using the new index in the transaction.

(d) Dispute rights

The 2006 Annex gives parties the right to dispute Calculation Agent determinations in relation to the Adjustment Spread, its nomination of the Calculation Agent Nominated Replacement Index, and any other adjustment it makes to the terms of a transaction. The dispute needs to be reasonable and supported by data. If a dispute cannot be resolved by agreement, the relevant Alternative Continuation Fallback is disregarded.

(e) No fault termination rights

If none of the Alternative Continuation Fallbacks can be successfully applied within the allotted period of time, each party acquires the right to terminate the relevant transaction using a no fault termination methodology. This termination right expires after 10 Business Days if it has arisen (but not been exercised) after any of the Alternative Continuation Fallbacks were disregarded following a dispute. Thereafter, the relevant Alternative Continuation Fallback will be applied using the determination made by the Calculation Agent under the relevant Alternative Continuation Fallback either before, or as part of, the dispute process.

(f) Temporary fallbacks and discontinuation of tenors

If the level of an index is required after the original benchmark has ceased to exist, or after its use has been prohibited following an Administrator/Benchmark Event, but before the relevant Alternative Continuation Fallback has been applied, the 2006 Annex provides a series of temporary fallbacks that can be used. It also specifies that if a tenor of a benchmark is discontinued, the provisions of the ISDA 2013 Discontinued Rates Maturities Protocol⁷ will apply, even if the parties are not adherents to that protocol.

(g) Non-compliant fallbacks

In the event that:

- it would be unlawful under any applicable law or regulation to determine the benchmark in accordance with a fallback,
- a fallback would contravene any applicable licensing requirements, or
- the Adjustment Spread constitutes a benchmark whose production would subject the Calculation Agent to additional regulatory obligations which it is unwilling to undertake,

the fallback is deemed not to apply.

⁷ <https://www.isda.org/protocol/isda-2013-discontinued-rates-maturities-protocol/>

7. How does the Benchmarks Supplement interact with the work that ISDA is doing on fallbacks to specific rates for IBORs?

The Benchmarks Supplement covers a broader range of benchmarks than ISDA’s work to implement robust fallbacks to specific rates for certain IBORs at the request of the Financial Stability Board’s Official Sector Steering Group.

If the terms of both the IBOR fallbacks (once available) and the Benchmarks Supplement are incorporated into a transaction, the IBOR fallbacks will constitute ‘Priority Fallbacks’ for an index cessation event and will apply in priority to the fallbacks set out in the Benchmarks Supplement. Refer to the answer to Question 6(a) above for further information on Priority Fallbacks. In particular, please note that Priority Fallbacks only apply following an index cessation event and will not apply upon the occurrence of an Administrator/Benchmark Event in the absence of an index cessation event.

8. How does the Benchmarks Supplement amend the 2002 ISDA Equity Derivatives Definitions (the ‘Equity Definitions’)?

(a) Alternative Pre-nominated Index

The Benchmarks Supplement introduces the ability for parties to specify an ‘Alternative Pre-nominated Index’ that can be used in substitution for an index which has been subject to an Index Cancellation (as defined in the Equity Definitions) or an Administrator/Benchmark Event (described further below). This is aimed at addressing the requirements of Article 28(2) of the EU Benchmarks Regulation (see Question 2(a) above). The specification of an Alternative Pre-nominated Index is not mandatory and its application is contingent upon the parties agreeing an ‘Adjustment Payment’, to the extent that either party considers that one should be payable.

(b) Administrator/Benchmark Event

The 2002 ISDA Equity Derivatives Definitions Benchmarks Annex (which forms part of the Benchmarks Supplement) also introduces a new trigger, the Administrator/Benchmark Event⁸. Unless the parties specify otherwise, the fallbacks applicable upon an Administrator/Benchmark Event will be the Alternative Pre-nominated Index (plus Adjustment Payment), if specified, and otherwise those which apply following an Index Cancellation.

(c) Non-compliant fallbacks

In the event that it would be unlawful under any applicable law or regulation to determine an index in accordance with a fallback or a fallback would contravene applicable licensing requirements, the fallback is deemed not to apply.

9. How does the Benchmarks Supplement amend the 1998 FX and Currency Option Definitions (‘FX Definitions’)?

(a) In-scope Transactions

The 1998 FX and Currency Option Definitions Benchmarks Annex (which forms part of the Benchmarks Supplement) applies to transactions to which the FX Definitions apply to the extent that an amount payable under such transactions is determined by reference to an index (or a combination of indices) under applicable law/regulation.

⁸ An Administrator/Benchmark Event encompasses circumstances in which a benchmark or its administrator is not authorised (or similarly approved) or included in an official register (including where such authorisation or inclusion is suspended or withdrawn) in accordance with applicable law.

(b) Deliverable Transactions

For the most part, Deliverable Transactions do not use a benchmark to determine amounts payable. However, there are limited circumstances in which this is not the case (for example, where Non-Deliverable Substitute (as defined in the FX Definitions) applies or where the ‘In-the-Money Amount’ is relevant for the purposes of Automatic Exercise of a Currency Option Transaction (each as defined in the FX Definitions)). It also specifies that Price Source Disruption will be applicable in relation to in-scope Deliverable Transactions unless otherwise specified.

(c) Administrator/Benchmark Event

The 1998 FX and Currency Option Definitions Benchmarks Annex also introduces a new trigger, the Administrator/Benchmark Event⁹. Unless the parties specify otherwise, the fallbacks applicable upon an Administrator/Benchmark Event will be those which apply following a Price Source Disruption or otherwise in Section 5.2(e)(i)(E) and Section 5.2(f) of the FX Definitions.

(d) Non-compliant fallback

In the event that it would be unlawful under any applicable law or regulation to determine an index using a fallback or a fallback would contravene applicable licensing requirements, the fallback is deemed not to apply.

10. How does the Benchmarks Supplement amend the 2005 ISDA Commodity Definitions (the ‘Commodity Definitions’)?**(a) Administrator/Benchmark Event**

The 2005 ISDA Commodity Definitions Benchmarks Annex (which forms part of the Benchmarks Supplement) introduces a new trigger, the Administrator/Benchmark Event⁹. Unless the parties specify otherwise, the fallbacks applicable upon an Administrator/Benchmark Event will be those specified to apply following Disappearance of Commodity Reference Price (as defined in the Commodity Definitions) or otherwise in Sections 7.5(d)(i) and (ii) of the Commodity Definitions.

(b) Additional Relevant Benchmarks

The 2005 ISDA Commodity Definitions Benchmarks Annex provides the parties with the ability to extend the application of certain Market Disruption Events (as defined in the Commodity Definitions) to benchmarks which are not Commodity Reference Prices (as defined in the Commodity Definitions) and provides that the fallbacks will mirror those agreed between the parties, or otherwise deemed to apply, with respect to such events in relation to Commodity Reference Prices.

(c) Non-compliant fallbacks

In the event that it would be unlawful under any applicable law or regulation to determine the index pursuant to a fallback or doing so would contravene applicable licensing requirements, the fallback is deemed not to apply.

11. How can the Benchmark Supplement be implemented?

The Benchmarks Supplement can be incorporated into transactions by parties agreeing to its application, either bilaterally (on a confirmation-by-confirmation basis or at a relationship level), or by adhering to any protocol that

⁹ An Administrator/Benchmark Event encompasses circumstances in which a benchmark or its administrator is not authorised (or similarly approved) or included in an official register (including where such authorisation or inclusion is suspended or withdrawn) in accordance with applicable law.



ISDA publishes for such purpose in the future. Firms will need to determine whether incorporation of the Benchmarks Supplement is appropriate for each transaction.