

Introduction to the 2021 ISDA Interest Rate Derivatives Definitions

The 2021 ISDA Interest Rate Derivatives Definitions will replace the 2006 ISDA Definitions as the standard definitional book for cleared and non-cleared interest rate derivatives. ISDA finalized the new definitions on May 18, 2021, ahead of publication on a new web-based user platform (expected on June 4, 2021). An implementation date has been set for the weekend of October 2/3, 2021.

1. Why is ISDA publishing a new interest rate definitional booklet?

Since the 2006 ISDA Definitions were published 15 years ago, there have been numerous changes in market structure, regulations, technology and market practice. Important lessons have also been learned from various unscheduled market closures. While ISDA has published over 70 supplements to keep the 2006 ISDA Definitions current, this has led to the definitional booklet becoming unwieldy and difficult to use. The 2021 Definitions will consolidate these supplements into the main book, as well as making other necessary updates.

2. Why should I adopt the 2021 Definitions?

The 2021 Definitions will be updated to reflect various changes in market practices. Importantly, ISDA will stop updating the 2006 Definitions after the implementation weekend in October 2021. Market participants are therefore encouraged to use the 2021 Definitions to benefit from future evolutions of ISDA's interest rate definitions. Major infrastructure providers, including clearing houses and trading venues, will also adapt their rule books to reflect the 2021 Definitions.

3. What is expected to change from the 2006 ISDA Definitions?

The most significant areas of change include:

- Cash settlement methodologies
- Floating rate options
- Some payment and calculation provisions
- Calculation agent provisions
- Introduction of generic fallbacks
- Means of publication and amendment of the definitions

4. What is not expected to change from the 2006 ISDA Definitions?

The 2021 Definitions will retain as much as possible of what worked well under the 2006 ISDA Definitions. Examples of areas that will be substantively retained include:

- Fallbacks for interbank offered rates (IBORs) following index cessation events
- Risk-free rate (RFR) floating rate options
- Compounding methods, including new RFR compounding conventions being added to the 2006 Definitions
- The fundamental mechanics for determining a fixed amount and a floating amount
- The material terms of most floating rate options (excluding fallbacks)
- Mark-to-market swaps and currency provisions
- The fundamental mechanics for exercising swaptions and optional early terminations
- Physical settlement, cleared physical settlement and certain cash settlement methods (collateralized cash price, par yield curve – unadjusted)
- Rounding and discounting provisions
- A large proportion of other provisions currently in the 2006 Definitions

5. Why are the cash settlement provisions changing?

Certain methodologies for determining a cash settlement amount following early termination or swaption exercise will be replaced with more robust methods that reflect changes in market conventions over the past 15 years – such as the increased use of collateral, the use of XVAs in valuations and the shift to overnight index swap discounting. Dealer polls, where relevant, will be made more standardized and robust, with both parties having the right to seek quotations in some instances to increase their likelihood of success. Where dealer polls fail, a fallback to a calculation agent determination will require the same prescribed methodology to be followed.

6. Why are the floating rate options changing?

Floating rate options will be transposed from a narrative format into a grid or matrix structure. This will make them more standardized and easier to read, process and update. The matrix format will divide different types of floating rate options into standardized categories with a common naming convention to enhance predictability and allow integration with trading systems. Publication sources will be removed as a defining characteristic of floating rate options in favor of the administrator of the benchmark – a move that will facilitate fungibility for clearing and streamline the definitions. Outdated references will also be corrected.

7. Which payment and calculation provisions are changing?

Terms relating to the payment of floating amounts will be updated in the 2021 Definitions, with the addition of new business day calendars and conventions. For example, the concept of ‘unscheduled holiday’ will enable certain dates (such as payment dates) to shift to the next good business day when there is insufficient notice of a market closure/holiday. Wherever possible, inputs required to make calculations under the 2021 Definitions (such as day-count fractions and interpolation) will be set out as formulae rather than narrative. The ability to derive a floating rate through use of interpolation if publication of the selected maturity is withdrawn will be introduced.

8. How are the calculation agent provisions changing?

The 2021 Definitions will specify that whenever the calculation agent is required to act or make a determination, it shall do so in good faith using commercially reasonable procedures to produce a commercially reasonable result. This is the same standard used for the close-out provisions of the 2002 ISDA Master Agreement. There will also be new provisions enabling parties to request further information from the calculation agent, as well as a framework for disputing determinations made under the cash settlement and generic fallback provisions.

9. What are the generic fallbacks that are being introduced?

Although floating rate options with specific fallbacks for index cessation events¹ will continue to fall back under those provisions, many floating rate options do not have such specific arrangements. The 2021 Definitions will set out a generic framework that will allow parties to work towards identifying a fallback rate and any adjustment². It will also introduce a trigger in case law or regulation prevents one of the parties from being permitted to use the relevant floating rate option, called an administrator/benchmark event.

10. How will the 2021 Definitions be published and maintained?

The 2021 Definitions will be published in a purely electronic format through a new interactive web-based user interface. Instead of issuing supplements, any changes will be made by publishing a new version of the 2021 Definitions in full. These innovations will enable users to navigate directly to the consolidated version of the definitions that applied at the relevant trade date, making them much easier to use and reducing the scope for operational mistakes.

This new interactive format will include comparison tools that allow different versions of the definitions to be viewed in blackline. Versions will be differentiated by version numbers and dates of publication. There will also be hyperlinking between defined terms, links to other relevant documents and multimedia content, bookmarking and advanced search facilities. The 2021 Definitions will be accessible on mobile devices as well as desktop computers.

11. Will there be a protocol?

ISDA is liaising with working group members on whether it would be helpful to publish a protocol to allow firms to convert their legacy 2006 Definitions trades to the 2021 Definitions, although no decision has yet been reached. Market participants will need to consider any value, tax, accounting, margining, clearing and other impacts of conversion.

¹ For example, those for the IBORs covered in Supplement 70 to the 2006 Definitions or recently published RFRs

² These provisions have been largely based on the 2018 ISDA Benchmarks Supplement

12. What are the key dates?

ISDA finalized the 2021 Definitions on May 18, 2021, ahead of publication on the user interface (expected on June 4, 2021). An implementation process for adopting the new definitions by clearing houses, trading venues and other market infrastructures is being targeted for the weekend of October 2/3, 2021. So the 2021 Definitions can be used as the market-standard booklet from Monday October 4, FpML will be updated to facilitate trading under the 2021 Definitions. The last-call working drafts of FpML 5.12 and 4.2 were released on May 19, 2021, with testing targeted for July/August and publication before the implementation date. Further information on FpML's implementation plans can be found on www.fpml.org.

13. What will happen to the 2006 Definitions?

While the 2006 Definitions will continue to exist, ISDA will stop maintaining or updating them after the implementation weekend in October 2021. They will therefore quickly become stale as new updates to the 2021 Definitions are published. Consequently, market participants are encouraged to adopt the 2021 Definitions from October 2021 to benefit from future evolutions of the ISDA interest rate definitions. Most major clearing houses have stated they will continue to accept trades for clearing under the 2006 Definitions but such trades will effectively be cleared subject to the 2021 Definitions. Some venues have indicated they will only permit on-venue trades under the 2021 Definitions.

Further information can be found at www.isda.org/2021Definitions

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Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 925 member institutions from 75 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional

banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on [Twitter](#), [LinkedIn](#), [Facebook](#) and [YouTube](#).