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ARRC Updates Best Practices to Encourage Adherence to ISDA Protocol During Escrow Period

ISDA Protocol will Implement New Fallbacks for Legacy Derivatives Products

The Alternative Reference Rates Committee (ARRC) today updated its [recommended Best Practices](#) in anticipation of the International Swaps and Derivatives Association's (ISDA) upcoming [IBOR Fallback Protocol](#) that will be available soon. While the ARRC's Best Practices have always recommended adoption of the Protocol, this update recommends that a subset of derivatives market participants adhere to the Protocol as promptly as possible.

The IBOR Fallback Protocol is critical to ensuring that existing derivatives contracts feature durable fallbacks given that LIBOR cannot be relied on to be published after the end of 2021. Firms that choose to adhere to the Protocol will agree that existing derivatives transactions that they have entered into with other adherents will incorporate ISDA's new fallback language. As outlined in a recent [ISDA letter](#), regulated entities and other key market participants will be able to sign up to adhere to the Protocol "in escrow," meaning that they would be included among a list of early adherents announced at the time of the Protocol's official launch.

In its initial release of its recommended Best Practices earlier this year, the ARRC included Protocol adherence as among its priority recommendations related to derivatives. The Best Practices document has been updated today to specifically note that, "Dealers and other firms with significant derivatives exposures are encouraged to adhere to the protocol during the escrow period in order to promote adoption on as timely a basis as possible." The ARRC has also updated its Best Practices to reflect its current understanding of the timing of the ISDA protocol process, recommending that other market participants "should adhere to the International Swaps and Derivatives Association's Fallback Protocol for Interbank Offered Rates within the 3- to 4-month period after it is published and before the amendments to embed the fallbacks in legacy transactions take effect."

"The IBOR Fallback Protocol is crucial to ensuring that the derivatives market continues to function and that LIBOR derivatives contracts continue to perform through the transition away from LIBOR," said Tom Wipf, ARRC Chairman and Vice Chairman of Institutional Securities at Morgan Stanley. "Market participants therefore need to do everything they can to prepare for the release of the Protocol. The ARRC recommends that updates to the Best Practices be carefully reviewed and followed by market participants."

In a [letter](#) to ARRC members earlier this month, Wipf also underscored the need for institutions to take the necessary steps now in order to be ready for the Protocol's official launch. The updates to the Best Practices reflect the ARRC's continued support for the Protocol since broad adoption of it is necessary to address both individual firm risks and system risks associated with the transition.

About the ARRC

ALTERNATIVE REFERENCE RATES COMMITTEE

The ARRC is a group of private-market participants convened by the Federal Reserve Board and Federal Reserve Bank of New York in cooperation with the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Office of Financial Research, the Office of the Comptroller of the Currency, the Commodity Futures Trading Commission, the Securities and Exchange Commission and the U.S. Treasury Department. It was initially convened in 2014 to identify risk-free alternative reference rates for U.S. dollar (USD) LIBOR, identify best practices for contract robustness, and create an implementation plan with metrics of success and a timeline to support an orderly adoption. The ARRC accomplished its first set of objectives and identified SOFR as the rate that represents best practice for use in certain new USD derivatives and other financial contracts. It also published its [Paced Transition Plan](#), with specific steps and timelines designed to encourage adoption of SOFR. The ARRC was reconstituted in 2018 with an expanded membership to help to ensure the successful implementation of the Paced Transition Plan, address the increased risk that LIBOR may not exist beyond 2021, and serve as a forum to coordinate and track planning across cash and derivatives products and market participants currently using USD LIBOR.

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