



# ASX Short Term Interest Rate Futures

**Consultation paper on fallback  
rate provisions for 90 Day Bank Bill  
Futures**

8<sup>th</sup> June 2022

## Invitation to comment

ASX is seeking submissions on the issues canvassed in this paper by 6<sup>th</sup> July 2022. Submissions should be sent to: [E Futures@asx.com.au](mailto:E_Futures@asx.com.au)

If you would like your submission, or any part of it, to be treated as confidential, please indicate this clearly. All submissions will be provided to regulators on request. They may also be published on the ASX website, unless they are clearly marked as confidential or ASX considers that there are reasons not to do so.

ASX is available to meet with interested parties for bilateral discussions on these matters.

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# ASX Short Term Interest Rate Futures

## Consultation on fallback rate provisions for Australian and New Zealand 90 Day Bank Bill Futures

### Introduction

ASX's Australian and New Zealand 90 Day Bank Bill Futures products are key benchmark indicators for short term interest rates in their respective markets. Bank Bill Futures are characterised by strong liquidity and turnover, providing an efficient way for participants to gain exposure to Australian and New Zealand interest rate markets.

Both the Australian and New Zealand Bank Bill Futures are cash settled on a quarterly basis against an index calculated using price information from the physical Bank Bill market that underpins each contract. In Australia, this is the 3 month Bank Bill Swap rate (BBSW) while in New Zealand, this is the 3 month Bank Bill Benchmark rate (BKBM).

### Global developments in fallback rate provision

Significant investment has been made in both the Australian and New Zealand Bank Bill market to reform the BBSW and BKBM benchmarks ultimately making them more robust, reliable and where possible, transaction based. While there are no plans to discontinue the 3 month BBSW or BKBM benchmark rates, the inclusion of fallback provisions in contractual documentation is considered prudent risk management and provides contractual certainty when using any benchmark.

Interest rate benchmarks are widely relied upon in global financial markets and are referenced in contracts for derivatives, loans and securities. Financial benchmarks are also used for valuation purposes, including benchmarking portfolio performance. In recent years, the global regulatory community has been focused on strengthening the robustness of financial benchmarks. Where the robustness of a financial benchmark could not be improved (i.e. submission based benchmarks) suitable alternatives have been sought with the support of the financial community and regulators. In addition to this, regulators have strongly encouraged the use of fallback rates in all contractual documentation referencing benchmarks. This ensures that in the event of permanent benchmark cessation, there is contractual certainty in terms of the rate to be applied to settle outstanding terms.

### The consultation paper

ASX is consulting on the fallback language to be applied to the Australian and New Zealand 90 Day Bank Bill Futures in the event of permanent benchmark cessation. This is in line with global benchmark reform and best practice guidance issued by regulators worldwide to include fallback language in all contractual arrangements.

For clarity, permanent benchmark cessation involves a public statement by the benchmark administrator or regulator of the benchmark administrator, announcing that it has ceased or will cease to provide the benchmark permanently or indefinitely. This is different to the temporary unavailability or delay in publication of a financial benchmark or the use of the waterfall BBSW methodology. The process for temporary unavailability or delay in publication of BBSW is set out in the [BBSW Conventions and Methodology](#).

The agreed permanent benchmark cessation fallback provisions will be included in section 2 of the ASX 24 Operating Rules and Procedures in order to provide clarity and certainty to the market on the process to be followed in the event of benchmark cessation.

This paper is presented in two parts. **Part 1** of the consultation focuses on proposed fallback language to be included in the ASX 24 Operating Rules and Procedures. ASX is seeking feedback on the suitability of the proposed language and the approach to be taken in the event of permanent benchmark cessation. **Part 2** of the consultation focuses on the

alternative fallback rates currently available and the level of detail Participants require regarding the fallback rate and calculation ahead of any permanent cessation event.

For the avoidance of any doubt, the following consultation paper seeks feedback on fallback language and available rates for BBSW and BKBM to be applied in the event of a permanent cessation of the benchmark. This consultation paper should not be interpreted as any indication of a planned benchmark cessation by the Administrator.

Responses to this consultation paper should be submitted to ASX by 6<sup>th</sup> July 2022.

## Consultation part 1

### Proposed changes to ASX 24 Operating Rules and Procedures

BBSW and BKBM continue to remain robust following investment in these benchmarks. The addition of fallback language to the ASX 24 Operating Rules and Procedures for the 90 Day Bank Bill Futures is an important initiative to provide market participants with transparency and clarity on how ASX (Clear) Futures would respond in the event that 3 month BBSW and/or BKBM were permanently ceased.

This consultation proposes the inclusion of a framework in the ASX 24 Operating Rules to cater for the use of a fallback rate in the event of permanent benchmark cessation. By providing a framework today, increased transparency and certainty can be delivered with flexibility for future enhancements. We note that in offshore markets where a Cessation Event has occurred for Interbank Offered Rates (IBORs), exchanges have tended to transition IBOR based futures contracts (such as Short Sterling Futures and Eurodollar Futures) to alternative Risk Free Rate (RFR) based futures contracts (such as SONIA Futures and SOFR Futures). In Australia and New Zealand, there is currently no appropriate forward looking alternative Risk Free Rate or RFR based futures contract<sup>1</sup> due to the robust nature of BBSW and BKBM benchmarks. If however such a contract were to exist in the future, ASX believes it would make sense to adopt international precedent and transition remaining Open Interest in the 90 Day Bank Bill Futures into the alternative futures contract following a Cessation Event. For the purpose of this consultation, a Cessation Event is defined as a public statement or publication of information by the Benchmark Administrator or regulator of the Benchmark Administrator, announcing that the Administrator will cease to publish 3 month BBSW [BKBM] permanently or indefinitely, and there is no successor Administrator to provide the 3 month BBSW [BKBM] rate.

The proposed framework supports two potential future scenarios where 1) a fallback rate is used to settle the Bank Bill Futures following permanent cessation of the 3 month BBSW or BKBM benchmark or 2) conversion of Open Interest to a corresponding position in an alternative futures contract, where an appropriate alternative futures contract exists. ASX would further consult with the market on the process to be followed (including any one off price adjustments that may be required) and timing around conversion following a Cessation Event.

#### Question 1

**Do you support ASX's proposed approach to transition Open Interest in the Bank Bill Futures to an appropriate alternative futures contract (should one be available) following a Cessation Event?**

#### Question 2

**Is it helpful for ASX to include language in the ASX 24 Operating Rules and Procedures that provides for the potential transition of remaining Open Interest in the 90 Day Bank Bill Futures to an appropriate alternative futures contract (at a point in time as agreed by ASX and Participants), should one be available at the time of cessation?**

As stated above, this approach would be in line with international precedent and would involve the transition of Open Interest in the 90 Day Bank Bill Futures (following a Cessation Event and market consultation) into an appropriate

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<sup>1</sup> The 30 Day Interbank Cash Rate Futures (IB) is the closest alternative Risk Free Rate futures contract currently available. The 30 day nature of the contract does not make it suitable as a replacement for the AUD 90 Day Bank Bill Futures.

alternative futures contract, including any one-off price adjustments that may be required to ensure the contracts remain economically equivalent. The proposed language is provided below.

***DRAFT ASX 24 Operating Rules and Procedures with fallback provision to be included at Schedule 1 Procedure 2.25.1 for 90 Day Bank Accepted Bill Futures Contract (Cash Settled) and Procedure 2.26.1 for New Zealand 90 Day Bank Bill Futures Contract***

**Permanent cessation fallback**

Following a Cessation Event, all contracts with Open Interest as at the close of business on the day prior to the Cessation Date shall thereafter:

- I. Be settled at expiry using the applicable fallback rate for the BBSW [BKBM] benchmark as determined by ASX in consultation with Participants; or
- II. In the event that a suitable alternative futures contract is listed on the Market Operator's Exchange, all contracts with Open Interest as at the close of business on the day prior to the Cessation Date shall be converted to a corresponding position in the alternative futures contract (including any one-off price adjustment that may be required to ensure the contracts remain economically equivalent), provided the Market Operator has given at least 3 months' notice of its intention to do so.

Where:

*Benchmark Administrator*- means the licenced entity responsible for the calculation and publication of the BBSW [BKBM] Benchmark.

*Cessation Event*- means a public statement or publication of information by the Benchmark Administrator or regulator of the Benchmark Administrator, announcing that the Administrator will cease to publish 3 month BBSW [BKBM] permanently or indefinitely, and there is no successor Administrator to provide the 3 month BBSW [BKBM] rate.

*Cessation Date*- means the earlier of:

- I. The date on which the publication of the BBSW [BKBM] Benchmark will permanently cease, announced as part of the Cessation Event; or
- II. An alternative date announced by the Market Operator, following a Cessation Event, with no less than 3 months' notice given.

**Question 3**

**Do you support incorporation of the above proposed language (or some variation of) into the ASX 24 Operating Rules and Procedures? If no, please provide reason(s) why.**

*Suggested wording, mark up's or comments on the proposed language is welcome.*

**Question 4**

**Is 3 months an appropriate notification period to announce the transition of Open Interest into an alternative futures contract? If no, please provide reason(s) why.**

Note that the 3 month notification period would follow a Cessation Event and formal market consultation on the appropriate alternative futures contract.

## Consultation part 2

### Alternative fallback rates

There are two options available when referring to the ‘fallback rate’ in the ASX 24 Operating Rules and Procedures.

**Option 1** uses generic terms such as ‘fallback rate’ without specifying what that rate is and how it is calculated. The draft Procedure wording on page 5 of this consultation uses this generic wording. The benefit of option 1 is that the fallback rate can be specified at a future point in time when a more suitable alternative rate(s) may be available. ASX considers this a sensible approach to take right now as there is no existing robust forward-looking fallback rate available to enable the effective cash settlement of the AU and NZ 90 Day Bank Bill Futures. To date, fallback rates for BBSW and BKBM for certain contractual arrangements, such as OTC swap transactions, have been defined. However, it is worth noting that the fallback rates for BBSW and BKBM, as defined in the 2021 International Swaps and Derivatives Association (ISDA) Definitions for the OTC market<sup>2</sup>, are calculated on a backward looking basis with the relevant overnight Risk Free Rate compounded in arrears and a fixed credit spread applied to reach the final fallback rate. Using the ISDA calculation would mean that there would be a term structure mismatch between the backward looking fallback rate and the Bank Bill Futures which are forward looking. For this reason it may not be a viable option when considering fallback rates for futures contracts.

Under option 1, the actual fallback rate would be defined in the ASX 24 Procedures following a Cessation Event and market consultation on the appropriate fallback rate to be applied. The drawback of option 1 is that the exchange and participants will need time to incorporate the fallback rate into relevant systems and processes. If there was a Cessation Event, the time to incorporate these changes may be limited to a period determined by the regulator and benchmark administrator<sup>3</sup>. It is expected that the benchmark administrator and regulator would factor into their cessation timing decision the notice period required by the market to prepare for cessation.

**Option 2** specifies the fallback rate up front. Currently there is only one potential fallback rate, being AONIA (Interbank Overnight Cash Rate) or the Official Cash Rate (OCR) compounded 90 days in arrears plus a credit spread. This option would provide certainty by defining what the fallback rate would be well ahead of a Cessation Event, giving participants and the exchange sufficient time to incorporate the fallback rate into the relevant systems and processes. The significant drawback of option 2 is that the fallback rate would be backward looking, in contrast with both BBSW and BKBM benchmarks which are forward looking, resulting in an economic difference between the two due to the term structure mismatch.

#### Question 1

**Based on the above, ASX proposes to proceed with Option 1. Do you agree with this approach or would you prefer the fallback rate to be specified up front?**

#### Question 2

**If you agree with ASX’s proposed approach (to specify the fallback rate at a future point in time should a Cessation Event occur), what is your organisation’s required change notification period?**

#### Question 3

**At this point in time there is no robust forward looking fallback rate available to enable the effective cash settlement of the AU and NZ 90 Day Bank Bill Futures. Are there any alternative approaches to the fallback rate calculation that you would support? Please specify the underlying rate and structure.**

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<sup>2</sup> <https://www.isda.org/2021/10/04/2021-isda-interest-rate-derivatives-definitions/>

<sup>3</sup> Note ASX Benchmarks Pty Ltd is the benchmark administrator for BBSW. This is a separate legal entity from ASX Operations Pty Ltd which is responsible for the AU 90 Day Bank Bill Futures contract.



### Next Steps

ASX seeks stakeholders' views on the above questions and changes to the ASX 24 Operating Rules and Procedures. Submissions should be made by 6<sup>th</sup> July 2022 to [Futures@asx.com.au](mailto:Futures@asx.com.au).

ASX welcomes the opportunity to discuss the draft amendments with interested parties (refer to the contact details on page 2).