

VIA CFTC Portal

9 September 2020

Mr Christopher Kirkpatrick  
Commodity Futures Trading Commission  
115 21<sup>st</sup> Street NW  
Three Lafayette Centre  
Washington DC 20581

Dear Mr Kirkpatrick

### **ILS Swaps**

Pursuant to CFTC regulation §39.5(b), LCH Limited (“LCH”), a derivatives clearing organization (“DCO”) registered with the Commodity Futures Trading Commission (the “CFTC”), is submitting Israeli New Shekel (ILS) based swaps for determination of whether mandatory clearing should apply.

### Background

Israel has a relatively small but active OTC market for interest rate derivatives, with participation from both international and local participants. LCH proposes to add ILS to the eligible product set for clearing, with the eligible products representing only the most liquid of the market structures. The products will use ILS as a deliverable currency, with Variation Margin passed through in ILS, and cashflows settled in ILS. The set of eligible margin products and currencies will remain unchanged, and ILS will not be permitted for posting of Initial Margin.

The proposed IRS product for clearing is one with a fixed leg against a TELBOR 3M floating leg. In addition to the vanilla swap, the proposed scope includes Variable Notional, Zero Coupon and Compounding variants. Maximum Swap eligibility is set at 11Y (formally as 4,050 days).

For FRAs, only contracts versus the TELBOR 3M rate will be eligible for clearing. Maximum FRA eligibility is set at 3.25Y (formally as 1,225 days).

### Factors for determination

#### ***The existence of significant outstanding notional exposures, trading liquidity, and adequate pricing data***

Based on the statistics of the latest Triennial Survey of the Bank for International Settlements<sup>1</sup>, the daily average turnover in ILS represents less than 1% of that in USD denominated OTC interest rate swaps in the overall market. All market data is from existing sources i.e. Bloomberg and Reuters using the most liquid (industry standard) instruments at each tenor point.

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<sup>1</sup> <https://www.bis.org/statistics/rpfx19.htm?m=6%7C381%7C677>

***The availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded***

LCH has a well-developed rule framework and support infrastructure for clearing interest rates swaps. LCH intends to leverage this existing operational capability when extending its offering to ILS swaps and FRAs.

In order to prepare for the launch of these products, LCH will perform testing to ensure that it is able to clear them in a manner which is consistent with the terms on which they are traded.

Further to this, LCH will notify its Clearing Members of a number of minor changes to the procedure documents, which will be made in order to support the clearing of the products. The changes will be certified with the CFTC and be made available on the LCH website.

***The effect on mitigation of systemic risk, taking into account the size of the market for such contract and the resources of the DCO available to clear the contract***

ILS based products do not introduce any novel risks to LCH, as the operational capability to manage the product are already in place.

LCH expects current SwapClear Clearing Members to start clearing ILS Swaps and FRAs, once the service is live.

Based on the statistics of the latest Triennial Survey of the Bank for International Settlements<sup>2</sup>, the introduction of ND IRS eligibility is unlikely to have a significant impact on the risk profile or total resources held by the SwapClear service. As such, the systemic risk profile of LCH remains unchanged as a result of the new product offering.

***The effect on competition, including appropriate fees and charges applied to clearing***

LCH's fees and charges for the above product will be in line with those charged for existing SwapClear contracts. No material impact.

***The existence of reasonable legal certainty in the event of the insolvency of the relevant DCO or one or more of its clearing members with regard to the treatment of customer and swap counterparty positions, funds and property***

The level of legal certainty around the clearing of ILS contracts is in all material respects the same as that of the products already cleared in the SwapClear service at LCH.

Insofar as legal certainty in the event of the insolvency of the DCO is concerned, LCH would be wound up under English law.

***Further information §39.5(b)(iii-viii)***

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<sup>2</sup> <https://www.bis.org/statistics/rpfx19.htm?m=6%7C381%7C677>

Product terms for ILS Swaps and FRAs are market standard and follow **2006 ISDA Definitions** and are also part of the Financial products Markup Language (FpML) standard (specifically <http://www.fpml.org/coding-scheme/floating-rate-index> published on 21<sup>st</sup> December 2017), which is a protocol for sharing information on derivatives and other products.

The participant eligibility standards for ILS are the same as those for existing SwapClear Clearing Members.

No material revisions to the existing risk models/parameters and/or liquidity management framework are required for LCH to offer the clearing of these products.

No changes are needed to the default rules; however, the procedures and product terms and eligibility manuals will be updated in order to show ILS based trades as eligible. The amendments will be submitted to the CFTC pursuant to §40.6(a), following notification to LCH's Clearing Members.

LCH engages its Clearing Members in the design and testing of new products at an early stage, through regular meetings and working groups. Clearing Members have been formally notified of the changes which LCH is required to make to its Rulebook.

Notice of this submission under CFTC regulation §39.5(b) was given to SwapClear Clearing Members on 24 August 2020 and a copy of this notice is provided at Appendix A. Furthermore, this submission is publicly available at: <http://www.lch.com/rules-regulations/regulatory-responses>

LCH intends to launch these products with its Clearing Members and clients no earlier than 14 September 2020.

Should you have questions please contact me.

Yours sincerely



Julian Oliver  
Chief Compliance Officer  
LCH Limited

**Appendix A**

**Notice of this submission provided to SwapClear Clearing Members**

# Memo

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To	SwapClear Clearing Members
From	David Horner, Head of In-Business Risk Rates
Date	24 August 2020
Subject	<b>Israeli New Shekel submission for determination of clearing requirements</b>

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Pursuant to CFTC regulation §39.5(b), LCH Limited (LCH), a derivatives clearing organization (DCO) registered with the Commodity Futures Trading Commission (the CFTC), is submitting Israeli New Shekel (ILS) based swaps and FRAs for determination of whether mandatory clearing should apply.

As per CFTC regulation §39.5(b)(viii), LCH is required to notify members of its submission. This note does not constitute a notification that the products are live for clearing. A notice announcing the live date and arrangements for the formal product launch will be published separately.

Israel has a relatively small but active OTC market for interest rate derivatives, with participation from both international and local participants. LCH proposes to add ILS to the eligible product set for clearing, with the eligible products representing only the most liquid of the market structures. The products will use ILS as a deliverable currency, with Variation Margin passed through in ILS, and cashflows settled in ILS. The set of eligible margin products and currencies will remain unchanged, and ILS will not be permitted for posting of Initial Margin.

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For FRAs, only contracts versus the TELBOR 3M rate will be eligible for clearing. Maximum FRA eligibility is set at 3.25Y (formally as 1,225 days).

## Factors for determination

### ***The existence of significant outstanding notional exposures, trading liquidity, and adequate pricing data***

Based on the statistics of the latest Triennial Survey of the Bank for International Settlements<sup>3</sup>, the daily average turnover in ILS represents less than 1% of that in USD denominated OTC interest rate swaps in the overall market. All market data is from existing sources i.e. Bloomberg and Reuters using the most liquid (industry standard) instruments at each tenor point.

### ***The availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded***

LCH has a well-developed rule framework and support infrastructure for clearing interest rates swaps. LCH intends to leverage this existing operational capability when extending its offering to ILS swaps and FRAs.

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<sup>3</sup> <https://www.bis.org/statistics/rpfx19.htm?m=6%7C381%7C677>

In order to prepare for the launch of these products, LCH will perform testing to ensure that it is able to clear them in a manner which is consistent with the terms on which they are traded.

Further to this, LCH will notify its Clearing Members of a number of minor changes to the procedure documents, which will be made in order to support the clearing of the products. The changes will be certified with the CFTC and be made available on the LCH website.

***The effect on mitigation of systemic risk, taking into account the size of the market for such contract and the resources of the DCO available to clear the contract***

ILS based products do not introduce any novel risks to LCH, as the operational capability to manage the product are already in place.

LCH expects current SwapClear Clearing Members to start clearing ILS Swaps and FRAs, once the service is live. Based on the statistics of the latest Triennial Survey of the Bank for International Settlements<sup>4</sup>, the introduction of ND IRS eligibility is unlikely to have a significant impact on the risk profile or total resources held by the SwapClear service. As such, the systemic risk profile of LCH remains unchanged as a result of the new product offering.

***The effect on competition, including appropriate fees and charges applied to clearing***

LCH's fees and charges for the above product will be in line with those charged for existing SwapClear contracts. No material impact.

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The level of legal certainty around the clearing of ILS contracts is in all material respects the same as that of the products already cleared in the SwapClear service at LCH.

Insofar as legal certainty in the event of the insolvency of the DCO is concerned, LCH would be wound up under English law.

***Further information §39.5(b)(iii-viii)***

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The participant eligibility standards for ILS are the same as those for existing SwapClear Clearing Members. No material revisions to the existing risk models/parameters and/or liquidity management framework are required for LCH to offer the clearing of these products.

No changes are needed to the default rules; however, the procedures and product terms and eligibility manuals will be updated in order to show ILS based trades as eligible. The amendments will be submitted to the CFTC pursuant to §40.6(a), following notification to LCH's Clearing Members.

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LCH engages its Clearing Members in the design and testing of new products at an early stage, through regular meetings and working groups. Clearing Members have been formally notified of the changes which LCH is required to make to its Rulebook.

Further information will form part of the full §39.5 filing which will be publicly available on the LCH website. LCH looks forward to working with Clearing Members and the CFTC in the determination of clearing requirements. Please do not hesitate to contact me regarding any questions raised by this information.