Best practice for booking/confirming single-name Credit Default Swap Transactions spun off from Index Transactions following a Restructuring Credit Event

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Below is a summary of the discussions that took on recent Credit Market Infrastructure Group ("CIG") calls regarding the booking and confirmation of "spin-off" single name CDS from index Credit Derivatives Transaction ("Index Transactions") following a Restructuring Credit Event.

This summary provides best practice guidance and is not meant to be binding in any way. As with all market information and guidance that ISDA disseminates, parties are free to choose alternate means of addressing such events.

Any capitalized term not otherwise defined herein shall have the meaning assigned to such term in the 2014 ISDA Credit Derivatives Definitions.

Background

When parties enter into an Index Transaction they effectively enter into a separate and independent single name CDS in respect of each Reference Entity specified in the relevant index (each a "Component Transaction"). If a Restructuring Credit Event occurs with respect to a Reference Entity of a Component Transaction (the "Restructured Entity"), that Restructured Entity is deemed to have been removed from the index and the Component Transaction is spun-off from the Index Transaction into a separate single name CDS contract with the Restructured Entity as the Reference Entity (the "Spin-off Trade"). The parties then confirm the Spin-off Trade such that the economic terms preserve, as closely as possible, the economic equivalent of the Component Transaction.

Norske Skogindustrier ASA Restructuring Credit Event

On the 2nd June 2016, the Credit Steering Committee ("CSC") noted that it was concerned about "certain operational issues and constraints" that the industry faced during the processing of the Spin-off Trades in respect of the Norske Skogindustrier ASA Restructuring Credit Event. The concern was that the economic equivalent of the Component Transactions had not been preserved because the Spin-off Trades had been booked/confirmed in DS Match/DTCC TIW with a new Trade Date/Effective Date. The CIG determined that the reason firms had booked/confirmed the Spin-off Trades with a new Trade Date/Effective Date was to prevent historical cash-flows being regenerated by DTCC TIW.

Best Practice

The CIG developed an efficient best practice to book/confirm Spin-off Trades with the original Trade Date/Effective Date of the Index Transaction and requested DTCC to advise on a procedure that would allow firms to follow this best practice without regenerating historic cash-flows in the DTCC TIW.

DTCC revised procedure for booking/confirming Spin-off Trades.

DTCC advised that in order to follow this best practice without regenerating historic cash flows, a Spin-off Trade must be booked in DSMatch: (i) as a “non-standard” Transaction Type (e.g. European Corporate, North America Corporate, etc.), and (ii) with the “First Payment Period Accrual Start Date” specified as the date of the Fixed Rate Payer Payment Date immediately prior to the relevant DC Credit Event Announcement.

Cleared trades

The CIG noted that cleared Spin-off Trades are booked/confirmed as new cleared single name positions with a Trade Date equal to the cleared date of the restructuring matched pairs (“RMP”) processing , an Effective Date equal to Trade Date + 1, and are netted with existing single name positions consistent with clearinghouse rules. As a result, the concerns noted above do not apply to cleared trades, therefore this best practice only applies to non-cleared trades.