
Suggested Operational Practices: OTC Derivatives Interest Compensation Claims

Purpose

The purpose of these Suggested Operational Practices (“SOP”) is to outline the guidelines for the submission and processing of interest compensation claims arising from payments relating to OTC Derivatives transactions confirmed under the terms of the 2002 ISDA Master Agreement (or the 1992 ISDA Master Agreement).

This document describes the industry suggested guidelines for compensation and claims arising out of failed settlement of coupon and fee payments on OTC derivative transactions. For claims arising out of parties’ failure to meet their obligations with respect to the movement of collateral (cash or securities), please refer to the 2021 Suggested Operational Practices for the OTC Derivatives Collateral Process ([link](#)).

The SOP address the procedure firms may follow to initiate, submit and process compensation claims. This document also provides an overview of certain factors that a party may wish to consider when determining the amount of a claim. However, this document does not (nor does it intend to) prescribe or provide guidance on how the compensation rate or the value of any claim may be determined.

This document is an update to the guidelines that were published by ISDA on October 26th, 2010 ([link](#)). Given the amount of time that lapsed since the publication of the original document, ISDA members felt that a comprehensive review was required.

Please Note: The SOP do not constitute legal, accounting, regulatory, financial or any other professional advice. The SOP provide an overview of the views expressed by market participants in an ISDA Working Group forum 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 alternative means of addressing the event. Parties are responsible for considering their own documentation and the specific terms of any transactions and should satisfy themselves that the recommendation is appropriate and is properly applied in the context of those transactions to reflect the commercial intention of the parties. The SOP are not intended to impact parties’ contractual rights or amend the terms of any existing contract.

Current State

- There have been numerous iterations of market practice guidelines addressing the submission and processing of interest compensation claims produced by market wide organizations that are product or currency specific.
- Guidelines specifically addressing interest compensation claims in relation to OTC Derivatives transactions have been in place since 2010. These industry guidelines have been reviewed to

identify any updates required in order to bring them in line with current market practices.

- Individual ISDA Master Agreements generally contain reference to the contractual right of a disadvantaged party to claim compensation for payments not received on the agreed date. For example, Section 9(h)(i)(1) of the 2002 ISDA Master Agreement provides that if a party defaults on the performance of any payment obligation, it will (to the extent permitted by applicable law) be required to pay interest on the overdue amount to the other party on demand at the Default Rate.¹ The SOP are not intended to affect, amend or override these contractual rights.

Commentary

- The ISDA Derivative Operations Group has discussed current practices for interest compensation claims arising from payments relating to OTC Derivative transactions confirmed under the terms of the 2002 ISDA Master Agreement (or the 1992 ISDA Master Agreement) and members of that working group have discussed the following guidelines in order to assist the efficient and orderly management of the settlements function.
- In general, the SOP will relate to amounts not received on the due date for payment made in the ordinary course of business as a result of administrative errors. Administrative errors may include (but are not limited to) counterparty calculation errors, missing funding deadlines, insufficient funding, agent bank handling errors, incorrect or missing SSI data, late confirmation of transactions, payments credited to the wrong account.
- The process outlined is to recover losses incurred by the disadvantaged party resulting from the late payment, and it is understood by all that the claim process is not looking to unnecessarily enrich the disadvantaged party.
- It is hoped that these voluntary guidelines will be widely accepted as standard market practice although they are in no way intended to supersede the terms of individual ISDA Master Agreements. Where possible the SOP are designed to be consistent with other published compensation guidelines.
- It is understood that the SOP may not be relevant in certain situations and in these cases it is anticipated that the current practice of bilateral discussion would continue.

Suggested Operational Practices

Claim threshold (*de minimis*)

Claims submitted are expected to be no less than USD **500** or equivalent, which is regarded as *de minimis* amount. This minimum threshold applies on a per claim basis; multiple claims cannot be aggregated to reach this amount, unless otherwise agreed bilaterally.

¹ Defined in the ISDA Master Agreement as a rate per annum equal to the cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount plus 1% per annum.

Note: minimum threshold will be subject to review semi-annually. If there is sufficient industry consensus that minimum needs to be changed, the SOP will be updated accordingly.

Timing of claims processing

- Submission of claims is expected to occur in the period from and including the actual settlement date to and including the 60th calendar day from the actual settlement date (as opposed to the contractual settlement date).
- Continue the interdealer practice of issuing outgoing claims within 30 calendar days.
- Current practice does not issue claims on credit payments settling TIW(CLS). This amnesty should continue on TIW(CLS) payments, until there is sufficient industry consensus that the amnesty process needs to be reviewed, and at such time, the SOP document will be updated accordingly. However, all non-TIW(CLS) payments will be subject to claim, if minimum claim requirements are met.
- Communication method is in writing via email or authenticated Swift.
- Submission of claims and communication regarding a claim should be between the parties to the trade (i.e. the investment manager, not the custodian).
- If there is a payment chain, each link in the chain should be considered separately.

The receiving bank should provide an email acknowledgment of receipt of claim within 7 calendar days of the claim's receipt.

Acceptance or rejection of claim should be advised within 15 calendar days of receipt via email/Swift.

- The claimant will have a window of 15 calendar days to refute any rejected claims (refutals received after this period may be subject to rejection).
- The receiving bank should be able to reject a claim if (a) the claimant has not provided the minimum information required or if (b) based on the information received by the claimant, they dispute the claim amount based on the claimant's calculation.
- If the receiving bank rejects the claim due to (a) above, the claimant needs to resubmit the information required within 7 calendar days of the rejection by the receiving bank.
- If the receiving bank rejects the claim due to (b) above, they should provide details of their claim's compensation calculation at the time of the rejection.
- 7 calendar day cycle will continue until claim is mutually agreed or rejected.
- The parties will endeavor to resolve claims disputes within 60 calendar days from the date on which the claim was submitted by the claimant to the receiving bank.
- If parties bilaterally agree to do so, they may settle the agreed portion of the claim if they are unable to agree the claim within 40 calendar days since the initial claim submission. The remaining portion of the claim that is still disputed by the parties will continue to be investigated in accordance with the timelines above.
- Once the liability of a claim has been agreed by the parties, payment should occur within 15 calendar days. Unless otherwise agreed between the claimant and the receiving entity, payment should not be withheld pending receipt of a counterclaim by another party.
- Back valuation is an accepted method of settlement of claim, but settlement method needs be

agreed at time of claim agreement.

- Netting of claims permissible upon bilateral agreement and may settle at pre-determined intervals outside of 15 calendar day suggested practice.

Claim Content

All claims should contain the minimum information below in order to facilitate the claims process.

- Legal Name of Claimant (including branch)
- Legal Name of Recipient (including branch)
- Claim ID
- Claimant's trade references
- Recipient trade references (if known by claimant)
- Trade Details (see below for further detail)
- Derivative Product class (FX/Interest Rate/Equity/Credit/Commodities)
- Principal Amount and Currency
- Expected Contractual Settlement Date
- Actual Settlement Date
- Claim Amount
- Claim Calculation (see below for further detail)
- Settlement Method (if settlement method is wire, should include settlement instructions)
- Brief description of fail / reason for claim
- Claimant contact details (email and telephone)

Trade Details:

- Trade Date
- Termination Date/Expiration Date/Maturity Date
- Buy/Sell
- Notional Amount
- Underlier/Security description (e.g. Floating Rate Option/Settlement Rate Option/Share/Index/Basket/Note/Bond/Commodity Reference Price)
- Underlier/Security identifier (e.g. ISIN, SEDOL, etc.)
- UTI

Standard reference rates

- FX rates used for conversion in the calculation of the *de minimis* amount should be based on the value date of the original contractual settlement date.
- WMRSPOT (the spot rate for the relevant currency pair reported by Refinitiv Benchmark Services UK Limited) or WMRSPOT (the closing spot rate for the relevant currency pair reported by Refinitiv Benchmark Services UK Limited) should be used as standard source for FX rates.
- In case such rate sources are not available or in case a currency pair is not referenced in the above

sources then parties should bilaterally agree a rate source in accordance with standard market practice.

Claim Calculation and Compensation rates

- As agent banks impose different overdraft rates depending on relationship, these guidelines are not looking to set compensation rates but to set out how a party should communicate the basis of the claim.
- The rate used to calculate the claim amount should be intended to compensate the disadvantaged party for the costs incurred.
- Costs may include the overdraft rate charged by the disadvantaged party's correspondent bank, the cost of funding the account incurred by the disadvantaged party, or the cost incurred by the disadvantaged party due to the inability to utilise the funds that would have been received (e.g. the loss of interest associated to those funds). The claim should not include any additional spread or administration fees.
- The outgoing claim should be clear to distinguish the compensation rate used;
 - Overdraft / account funding charges
 - Use of funds (loss of interest) charges
- Back valuation of the original payment may also be used where the effect will equally compensate the disadvantaged party. Back valuation as settlement method needs to be part of claim agreement.

Back Valuation

- If agreed between the parties during the claim agreement process, back valuation will be applied as the claim settlement method. In this case, the receiving bank will back value the original payment to the date original contractual settlement date.
- The following formula may be used for calculating the back valuation compensation amount, unless otherwise agreed between the parties:

(Principal Amount) x (Compensation Rate) x Day Count Fraction

Where:

- Principal Amount: an amount in the relevant currency as specified in the claim request;
- Compensation Rate: the compensation rate, expressed as a percentage, as determined by the claimant in a commercially reasonable manner;
- Day Count Fraction: the quotient of: i) the actual number of calendar days in the

period from and including the original contractual settlement date to but excluding the claim payment date and, b) the denominator in accordance with the standard market practice for the Principal Amount currency.

Compensation Process Grid

Compensation Process	Process Details
Claim Calculation	The rate applied should be intended to compensate the disadvantaged party for the costs incurred
Minimum Claim Threshold	USD 500 or equivalent
Claim Communication Method	In writing via email or authenticated Swift
Initial Claim Submission	Within 60 calendar days from and including the <u>actual</u> settlement date
Initial Claim Acknowledgement	Within 7 calendar days from and including the claim receipt
Claim Agreement / Rejection	Within 15 calendar days from and including the claim receipt
Claim Rebuttal (if rejected)	Within 15 calendar days from and including the claim rejection receipt. Rejection and Rebuttal may continue following a 7 calendar day cycle for a period up to 60 calendar days from and including the claim receipt. Parties may agree to settle the agreed portion of the claim if the claim is not agreed by 40 calendar days .
Claim Settlement	Within 15 calendar days from and including the claim agreement
Settlement Methods	Via wire or Back Valuation when agreed by the parties
Netting of Interest Claims	Permissible upon bilateral agreement