**ISDA Operations Committee - Interest Rates Products Working Group**

**Best Practice Statement**

**Interest Rates Novation “Pair-offs”**
(also known as “Step-outs” or “Collapsed trades”)

**Background:**

The ISDA Operations Interest Rates Products Working Group (IRPWG) noted that contrary to the credit market, in the rates products market there is no common way of determining who should be considered the Remaining Party after a client steps out of two offsetting positions leaving two dealers facing each other.

**Scenario:**

An end-user has equal and offsetting trades (same tenor and fixed rate as well as identical Payment and Termination Dates) with two dealers so that he pays a fixed rate to one dealer and receives the same fixed rate from another dealer. The end-user wishes to step-out of the two transactions which leaves the two dealers facing each other. Both dealers would then consider themselves to be the Remaining Party. However, since there were initially two transactions in place, one dealer must agree to ‘unwind’ his trade and to step-in, while the other dealer should book the Novation Agreement as Remaining Party.

**Best practice guideline:**

In April 2008 the following best practice was formally agreed to determine who should be the Remaining Party, and who should therefore draft the Novation Agreement for Interest Rate Products:

1. The remaining fixed rate payer (buyer) of the transaction should be considered the Remaining Party.

2. In the absence of a fixed rate payer, the dealer with the earliest Trade Date for the trade with the stepping-out party should be considered the Remaining Party.

April 2008

Capitalised terms have the meaning given to them in the relevant ISDA definitional booklet

The precise documentation of each Transaction remains the responsibility of the parties concerned. ISDA assumes no responsibility for any use to which this Best Practice Statement may be put.

Each party following the recommendations contained in this Best Practice Statement should satisfy itself that those recommendations are appropriate to reflect the commercial intentions of the parties.

Copyright © 2008 by International Swaps and Derivatives Association, Inc.
**Additional Clarification:**

In case of a Swaption, the buyer of the option will be considered the Remaining Party, regardless of whether they are the Fixed or Floating Rate Payer of the underlying swap.

July 2008