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2014 ISDA Credit Derivatives Definitions Protocol and Implementation for Emerging Market Regions – FAQs on Changes

Background

Previous communications from ISDA regarding implementation of the 2014 ISDA Credit Derivatives Definitions (the “2014 Definitions”) have indicated that the 2014 Definitions would not apply via a Protocol to existing transactions on sovereign and financial Reference Entities, and so those transactions would remain on the 2003 ISDA Credit Derivatives Definitions (the “2003 Definitions”). Based on member feedback during the consultation phase on the draft Protocol, an alternative approach has been requested for certain emerging market regions. This change has implications for existing transactions as at September 22, 2014 (“Legacy Transactions”) and new trades from that date forward (“New Transactions”).

What has changed?

Latin America and Emerging EMEA: Both sovereign and financial entities will be included in the Protocol so Legacy Transactions can move to the 2014 Definitions, but without asset package delivery (“APD”) and financial entities will not adopt the Governmental Intervention Credit Event (“GI”). New Transactions would be expected to use the 2014 Definitions, but without APD and (for financials) without GI.

Asia-ex Japan (including Singapore, but excluding Australia/New Zealand): Asia sovereigns (not financials) will be included in the Protocol so both Legacy Transactions and New Transactions can be on the 2014 Definitions, but without APD.

The overall position for the Latin America, Emerging EMEA and Asia regions are summarized in the table on the next page. Please note that, for New Transactions, parties are responsible for deciding the terms on which they wish to trade. The table below assumes for New Transactions that the terms of the ISDA Credit Derivatives Physical Settlement Matrix would be applied, and in the case of financial entities, the relevant Transaction Type identified below would be specified for the transaction.

	Latin America	Emerging EMEA	Asia		
			Asia Ex-Japan	Japan	Australia/New Zealand
Sovereigns	Legacy Transactions: included in Protocol, but without APD. New Transactions on 2014 Definitions: APD will not apply.	Legacy Transactions: included in Protocol, but without APD. New Transactions on 2014 Definitions: APD will not apply.	Legacy Transactions: included in Protocol, but without APD. New Transactions on 2014 Definitions: APD will not apply.	Legacy Transactions: excluded from Protocol. New Transactions on the 2014 Definitions: APD will apply.	Legacy Transactions: excluded from Protocol. New Transactions on the 2014 Definitions: APD will apply.
Financials	Legacy Transactions: included in Protocol, but without GI or APD. New Transactions on 2014 Definitions: on “corporate” Transaction Type so without GI or APD.	Legacy Transactions: included in Protocol, but without GI or APD. New Transactions on 2014 Definitions: on “corporate” Transaction Type so without GI or APD.	Legacy Transactions: excluded from Protocol. New Transactions on 2014 Definitions: on “financial” Transaction Type so GI and APD will apply.	Legacy Transactions: excluded from Protocol. New Transactions on 2014 Definitions: on “financial” Transaction Type so GI and APD will apply.	Legacy Transactions: excluded from Protocol. New Transactions on 2014 Definitions: on “financial” Transaction Type so GI and APD will apply.

Why has the approach changed?

The reason sovereign and financial entities were originally proposed to be excluded from the Protocol was that asset package delivery in the 2014 Definitions could not apply to Legacy Transactions, because the change would have a material economic impact on those transactions. This view has not changed. However, market feedback has indicated that there would be a liquidity cost to having two pools of transactions (Legacy Transactions under the 2003 Definitions and New Transactions under the 2014 Definitions), and in some cases the benefits of asset package delivery may not outweigh those costs. Although asset package delivery is an important component of the 2014 Definitions, the 2014 Definitions contain several other upgrades

compared to the 2003 Definitions. As a result, it was proposed for some entity types to take most of the benefits of the 2014 Definitions, but without needing to split liquidity into two pools.

How will this change be implemented?

Financial entities (Latin America and emerging EMEA regions): No financial entities from these regions will be included on the Protocol's "Excluded Reference Entity List", so Legacy Transactions on those entities can be covered by the Protocol and move to the 2014 Definitions on their existing "corporate" trading terms. To maintain fungibility with Legacy Transactions, New Transactions on those entities would continue to use "corporate" trading terms with the 2014 Definitions, which means that APD and GI will not apply.

For sovereign entities (Latin America, emerging EMEA and Asia regions): No sovereign entities from these regions will be included on the Protocol's "Excluded Reference Entity List", so Legacy Transactions on those entities can be covered by the Protocol and move to the 2014 Definitions. In addition, a new global amendment will be included in the Protocol to provide that APD will not apply to any sovereign Reference Entity covered by the Protocol. For New Transactions, a new supplement to the 2014 Definitions will be published to remove the possibility of APD for sovereign Reference Entities. This supplement will be included via ISDA's Credit Derivatives Physical Settlement Matrix for the relevant sovereign Transaction Types, i.e. Standard Latin America Sovereign; Standard Emerging European & Middle Eastern Sovereign; Standard Singapore Sovereign; Standard Asia Sovereign; and Standard Sukuk Sovereign.

Does this prevent these markets from adopting asset package delivery in future?

No. If market participants in affected regions want to start trading financial or sovereign Reference Entities with APD and (for financials) GI applicable, new trading standards could be created at that time to allow for adoption of APD and (for financials) GI for new trades going forward.