Narrowly Tailored Credit Events

• On April 2018, the ISDA Board of Directors published a statement critical of recent reports of credit default swap (CDS) market participants entering into arrangements with corporations that are narrowly tailored to trigger a credit event for CDS contracts while minimizing the impact on the corporation.

• With the support of regulators, ISDA worked on an industry solution to mitigate the concerns regarding narrowly tailored credit events (NTCEs).

• On July 15, 2019, ISDA published the 2019 Narrowly Tailored Credit Event Supplement to the 2014 ISDA Credit Derivatives Definitions (the “Supplement”).
The definition of "Failure to Pay" has been amended to require that the failure to pay results from, or results in, a deterioration in the creditworthiness or financial condition of the Reference Entity (the Credit Deterioration Requirement).

- Guidance Note on interpretation of the definition of "Failure to Pay" and the Credit Deterioration Requirement
- Non-exhaustive list of factors that may indicate that the Credit Deterioration Requirement is either met or not met.
NTCE Supplement

- Outstanding Principal Balance:
  - Part of the definition of “Outstanding Principal Balance” provides that the Outstanding Principal Balance is determined in accordance with applicable laws (insofar as such laws reduce or discount the size of the claim to reflect the original issue price or accrued value of the obligation). The NTCE Supplement clarifies that “applicable laws” includes bankruptcy and insolvency law.
  - Introduction of Fallback Discounting for circumstances where (i) “applicable law” will not result in discounting; (ii) the obligation is either a Bond or Loan and the issue price or amount advanced is less than ninety-five per cent of the repayment amount; and (iii) the Bond or Loan does not include customary accretion provisions.
NTCE Protocol

• The Protocol only applies to legacy, over-the-counter transactions that incorporate the 2014 Credit Derivative Definitions and in which the Reference Entity is not a Sovereign (as defined in the Definitions).

• The Protocol incorporates the Supplement into transactions entered into prior to the Implementation Date and makes “Fallback Discounting” and “Credit Deterioration Requirement” applicable for such transactions.

• For firms that solely have cleared trades, adherence to the Protocol is not required. Clearing houses will make their rule changes pursuant to their individual rule change approval process to apply the terms of the Supplement to legacy cleared trades.
NTCE Protocol

- The Protocol closes at 5pm New York time on October 14, 2019.
- The amendments made by the Protocol take effect on the Implementation Date, which is currently anticipated to be January 13, 2020.
- The Implementation Date may be extended to ensure that the rule changes implemented by the CCPs take effect on the same date as the changes for OTC credit derivatives.
- New trading incorporating the Supplement will also take place on the Implementation Date to ensure new trades are aligned with legacy transactions.