

P.R.I.M.E. Finance

Panel of Recognized International Market Experts in Finance

2002 ISDA Close-Out Amount



P.R.I.M.E. FINANCE
Panel of Recognized International Market Experts in Finance



Presentation by Jonathan Ross
2017 P.R.I.M.E. Finance Annual Conference
23 & 24 January, Peace Palace, The Hague

Close-out netting – What is the goal?

- Close-out netting is ISDA's third pillar
- The Goal (assuming Two-Way Payments) is:
 - If the Non-defaulting Party is harmed by the default, to *compensate* the Non-defaulting Party for the cost (actual or theoretical) of replacing its trade with the Defaulting Party
 - If the Non-defaulting Party benefits from the default, to *charge* the Non-defaulting Party for the benefit (actual or theoretical) of replacing its trade with the Defaulting Party



Close-out netting – valuation of derivative transactions upon termination

- A key issue is how derivative transactions are valued under the ISDA Master Agreement when the ISDA Master Agreement is terminated



2002 ISDA Master Agreement – Close-out Amount

- Close-out Amount is a single valuation measure
- Close-out Amount replaces choice between Market Quotation and Loss
- Close-out Amount is designed to:
 - Overcome the perceived difficulties associated with Market Quotation
 - Provide more guidance and transparency than Loss
 - Take account of the development in transaction types



2002 ISDA Master Agreement – Close-out Amount (2)

- Close-out Amount involves a calculation by a Determining Party of how much it would cost it (or how much it would be paid) to replace, or provide the economic equivalent of:
 - (a) the material terms of the Terminated Transaction(s), including the payments and deliveries by the parties under Section 2(a)(i) that would, but for the occurrence of the Early Termination Date, have been required after that date (assuming satisfaction of the conditions precedent in Section 2(a)(iii)) and
 - (b) the option rights of the parties in respect of the Terminated Transaction(s)



2002 ISDA Master Agreement – Close-out Amount (3)

- The Determining Party must:
 - act in good faith
 - use commercially reasonable procedures
 - [and do so] in order to obtain a commercially reasonable result
- Close-out Amount may be determined for an individual Terminated Transaction or a group of Terminated Transactions (so long as, in aggregate, a Close-out Amount or Close-out Amounts is/are determined for all Terminated Transactions)
- Close-out Amount is determined as of the Early Termination Date or, if that would not be commercially reasonable, as of such later date or dates as would be commercially reasonable



P.R.I.M.E. Finance

Panel of Recognized International Market Experts in Finance



P.R.I.M.E. FINANCE
Panel of Recognised International Market Experts in Finance



2017 P.R.I.M.E. Finance Annual Conference
23 & 24 January, Peace Palace, The Hague