

ISDA Adopts Standard Definitions for Digital Asset Derivatives

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At a time when the digital asset market is badly in need of good news, the International Swaps and Derivatives Association (ISDA) has delivered the long-awaited [ISDA Digital Asset Derivatives Definitions](#) (the “Definitions”).

Until now, there has been no standardized approach to documenting OTC derivatives referencing digital assets. Market practices for the trading of digital asset derivatives have varied from using ISDA-based (but highly adapted) documentation and in often cases entirely bespoke documentation. The resulting inefficiencies and lack of transparency with this approach has placed unnecessary burdens on parties in this space. ISDA – being uniquely placed to bring together members of the digital asset community, market participants, and other stakeholders – has laid the groundwork for the development of a robust, liquid market in digital asset derivatives. The creation of the Definitions is central to that mission.

Promoting contractual standards for more than 35 years, ISDA has considerable experience bridging the gaps between mainstream financial markets and digital asset markets, taking a close look at how novel technologies such as distributed ledger technologies (DLT) and smart contract code can be integrated within ISDA’s contractual framework. Recent efforts include launching a working group (the ISDA Digital Assets Legal & Documentation Group) to identify and consider the unique issues that bear on digital asset derivatives. Their work culminated in the publication of ISDA’s Contractual Standards for Digital Asset Derivatives last year, in which they suggested that the use of digital assets together with smart contract code could revolutionize financial markets by improving efficiency and accuracy through automation. The publication also identified other issues regarding disruption events, valuation issues, and consideration of how digital assets could fit within the ISDA documentation framework. ISDA followed that work with an analysis on digital asset risks and the use of futures and ETFs for hedging digital asset exposure. In many ways those publications set the table for the arrival of the Definitions, which could not have come at a better time as the industry recovers from a recent wave of destabilizing events.

The Definitions initially cover non-deliverable forwards and options on Bitcoin and Ether but have been drafted with an eye to expansion in the future to cover additional product types, including tokenized securities and digital assets executed using DLT. Significantly, the Definitions set out the rights and obligations of the parties to a digital asset derivatives transaction following a market disruption.

ISDA has also published a [whitepaper](#) that addresses some of the legal issues raised by numerous and highly publicized bankruptcies in the digital asset market, including ownership and intermediation of customer assets in the digital assets space and the importance of close-out netting and collateral arrangements for digital asset derivatives. They have also signaled the forthcoming release of a second whitepaper addressing custody matters.

According to ISDA “the ISDA Digital Asset Derivatives Definitions are intended to bring greater clarity to this nascent asset class by creating an unambiguous contractual framework for digital asset derivatives under the umbrella of the ISDA Master Agreement, reducing credit and market risk by setting clear provisions for execution and settlement.” Uniquely, the Definitions have been designed on electronic format, which eases the process of updating and supplementing as the market and technology evolves.

In the months ahead, much will unfold as legislative efforts to fill the broader policy and statutory voids have stalled with the recent change in government. However, these publications may serve as a calming reminder of the transformational influence that digital assets will have on financial markets. Chapman lawyers are focused on these topics and look forward to sharing our views as the market continues to evolve.

For More Information

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