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Interest Rates Watch: Canadian Alternative Reference Rates Working Group Announces Development of a Term CORRA Benchmark

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Welcome back to our *Interest Rates Watch* series, developed to provide timely updates and practical advice on developments related to interest rates and benchmarks on a regular basis. As always, we are here to help.

On January 11, 2023, the Canadian Alternative Reference Rates working group (CARR) confirmed that efforts are underway to develop a forward-looking Canadian Overnight Repo Rate Average (CORRA) term rate (Term CORRA) as an alternative benchmark to the Canadian Dollar Offered Rate (CDOR), the publication of which will cease following a final publication on June 28, 2024. CARR aims to have 1- and 3-month Term CORRA benchmarks available for use by the end of Q3 2023.

CARR has developed recommended methodology for calculating Term CORRA, which will be derived from transactions and executable bids and offers from CORRA interest rate futures traded on the Montréal Exchange. The CARR methodology is consistent with the approach for the recommended replacement rate for USD LIBOR (Term SOFR).

Term CORRA has been designed in compliance with the International Organization of Securities Commissions (IOSCO)'s Principles for Financial Benchmarks and Canadian benchmark regulation. One of the key IOSCO principles is that the design of a benchmark should take into account the relative size of the underlying market from which the benchmark is created in relation to the exposure that references the benchmark. Accordingly, in an effort to ensure that the size of the market referencing Term CORRA is appropriate to the size of the market used to determine Term CORRA, the use of Term CORRA will be restricted through its licensing agreement to specific uses, including loans and derivatives associated with loans, but excluding floating rate notes, securitizations and certain derivatives uses, among other uses.

Notwithstanding that CARR has endeavoured to create a robust and sustainable benchmark replacement, the long-term sustainability of Term CORRA is not guaranteed. If the depth of liquidity in the underlying CORRA futures contracts used to derive Term CORRA is not sufficiently robust, the Term CORRA administrator will be required to amend the methodology, and if changes to the methodology do not result in a sufficiently robust benchmark, the benchmark administrator will be required to either (i) take steps to ensure that the benchmark accurately and reliably represents that part of the market or the economy that it is intended to represent or (ii) cease the publication of the benchmark with appropriate notice. As a result, contracts that use Term CORRA as a reference rate must include robust fallback language, and users of Term CORRA should ensure that they have the operational capacity to transact in these fallback rates should Term CORRA cease to be published in the future. Please see our previous article for more information on recommended Term CORRA fallback language.

Subject to necessary regulatory approvals, Term CORRA will be produced and managed by CanDeal Innovations Inc., as the benchmark administrator, and with TMX Datalinx, TMX Group's information services division, providing the licensing and distribution capabilities.

CARR has also announced that it will host, in partnership with TMX, a series of webcasts to provide those affected by CDOR's upcoming cessation with advice and guidance. Parties interested in accessing these webcasts can register on the TMX website.

We will be monitoring developments and issuing further articles relating to interest rates. Find other articles in our Interest Rates Watch Series here.
