JUNE 28, 2024 - CDOR WILL BE NO MORE

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On May 16, 2022, Refinitiv Benchmark Services (UK) Limited ("**RBSL**"), the administrator of the Canadian Dollar Offered Rate ("**CDOR**"), announced[1] that it would permanently cease the calculation and publication of CDOR after June 28, 2024. Simultaneously, the Ontario Securities Commission and the Autorité des marchés financiers, each of which regulate CDOR as a designated critical benchmark, authorized the discontinuation of CDOR in accordance with RBSL's proposed timeline. [2]

Market participants with cash or derivatives products referencing CDOR have a relatively short window to take all necessary steps to effect an orderly transition to an alternative benchmark rate.

This transition will be a significant task. CDOR was introduced over 40 years ago and is currently the most widely used interest rate benchmark in Canada.[3] Market participants will need to transition billions of dollars' worth of existing financial products from CDOR to alternative rates. Market participants will also need to develop pricing and documentation so that new products also reference alternative rates.

The RBSL's announcement comes as the result of feedback received during its public consultation[4] (the "**RBSL Consultation**") held between January and February 2022. The RBSL Consultation followed the Canadian Alternative Reference Rate Working Group's ("**CARR**") review of CDOR which was published in a white paper[5] (the "**CARR White Paper**") on December 16, 2021. The CARR White Paper recommended that RBSL cease publication of CDOR and that the Canadian market adopt a new benchmark reference rate.

CARR was established in 2018 in response to the international Financial Stability Board's recommendations, which emphasized the need to strengthen existing interbank offered rate benchmarks and develop risk-free reference rates.[6] CARR is comprised of financial sector firms, large financial instrument end users and public sector institutions. Its mandate is to guide benchmark reform in Canada.[7]

The CARR White Paper

The CARR White Paper found that CDOR was not determined in a manner consistent with global best practices, which promote reference rates based on high volumes of actual arm's length transactions rather than expert judgement. Although CDOR is based on actual transactions, it is determined based on submissions from market participants rather than transaction data. Specifically, CDOR is based on the bankers' acceptances (“**BA**”) market, which has been diminishing with the introduction of new capital rules that require banks to match the terms of funding and lending. Without a robust BA market, CDOR would become even less reflective of actual transactions and even more dependent on expert judgement. While CARR considered reforming CDOR, it concluded that such a reform was not feasible. CARR ultimately recommended that the Canadian Overnight Repo Rate Average (“**CORRA**”) be adopted as the Canadian dollar benchmark reference rate upon CDOR’s discontinuation.

The CARR White Paper recommended a two-stage approach to ensure a seamless transition, which was supported by all respondents to the RBSL Consultation:

1. By June 30, 2023: All new Canadian dollar interest rate derivative contracts and cash securities referencing CDOR, with limited exceptions, will have transitioned to CORRA; and
2. By June 28, 2024: All bilateral and syndicated loans referencing CDOR will have transitioned to alternative rates such as CORRA, or any other available alternative rate.[8]

Potential for creation of Term CORRA

The CARR White Paper acknowledged that it may be difficult to transition loans from a forward-looking rate (i.e., CDOR) to an overnight rate (i.e., CORRA), [9] and suggested that there may be a need for a term CORRA rate in the Canadian market. This view was confirmed during the RBSL Consultation. Many respondents commented that a term rate was required for corporate lending and trade finance, and that such a rate should be made available prior to CDOR’s discontinuation.

On that basis, CARR consulted on the need for “Term CORRA.” This consultation[10] has been extended to June 30, 2022 and it is expected that a summary of responses will be posted publicly shortly after this deadline. [11] It is widely anticipated that CARR will recommend the creation of one month and three month tenors of Term CORRA and limit its use to corporate loans and trade finance.

Expectations of market participants

In an Industry Letter[12] released on the same date as RBSL’s cessation announcement, the Office of the Superintendent of Financial Institutions (“**OSFI**”) communicated that the transition is entering a critical phase and that it expects federally regulated financial institutions (“**FRFIs**”) and federally regulated private pension plans (“**FRPPs**”) to follow CARR’s two-stage transition approach. OSFI also stated that for FRFIs “with material exposure to CDOR… OSFI will take supervisory actions, as appropriate, based on its evaluation of transition preparedness.” FRFIs are also expected to ensure adequate contingency plans are in place. [13]

In addition to the consultation on Term CORRA, CARR is working on a number of initiatives to ease the transition for Canadian loan market participants from CDOR. The two main initiatives are:

- the development of market standard loan fallback language, including standard terms for Term CORRA referencing loans; and
- setting a date for ceasing the issuance of new CDOR referencing loans, which will likely be well before the cessation date for CDOR[14].

Although, CARR is not a regulator and has no authority to enforce a date on which new loans may no longer reference CDOR, it is almost certain that OSFI and provincial financial market regulators will adopt the timeline that CARR proposes.

Respondents to the RBSL Consultation also asked that CARR and relevant regulators begin educating market participants about the transition process and provide guidance on what actions need to be taken by lenders and borrowers in order to prepare for the transition away from CDOR.

Conclusion

There was a strong sentiment among respondents to the RBSL Consultation that the timelines proposed by CARR (and adopted by OSFI) were "tight but achievable." The prevailing view was that market participants would face challenges in being ready but without rapidly approaching deadlines there would be insufficient motivation to take the necessary transition steps.

In our next bulletin, we will discuss the steps that market participants should already be taking to prepare for the end of CDOR, even without certainty about Term CORRA and transition timelines.

[1][ps2id id='1' target=''/] See RBSL, "Refinitiv Benchmark Services (UK) Limited Issues Canadian Dollar Offered Rate Cessation Notice" (May 16, 2022); see RBSL, "Announcement of Cessation of CDOR in June 2024" (May 16, 2024).
[2][ps2id id='2' target=''/] See Ontario Securities Commission (OSC), "Notice" (May 16, 2022); see Autorité des marchés financiers (AMF), "Decision n° 2022-PDG-0032" (May 16, 2022).
[3][ps2id id='3' target=''/] See CARR, "Consultation on a potential new term interest rate to replace CDOR in certain financial instruments" at 1.
[4][ps2id id='4' target=''/] See RBSL, "Consultation on Potential Cessation of CDOR" (January 31, 2022).
[5][ps2id id='5' target=''/] See CARR, "CARR's Review of CDOR: Analysis and Recommendations" (December 16, 2021).
[6][ps2id id='6' target=''/] See Canadian Alternative Reference Rate Working Group, "Canadian Alternative Reference Rate Working Group – Terms of Reference" (21 September 2020).
[7][ps2id id='7' target=''/] See CARR, "CARR's Review of CDOR: Analysis and Recommendations" (December 16, 2021) at 5.
[8][ps2id id='8' target=''/] See CARR, "CARR's Review of CDOR: Analysis and Recommendations" (December 16,

2021) at 28; See CARR "CDOR transition roadmap and milestones" (May 16, 2022) at slide 2, 5; see CARR, "Consultation on a potential new term interest rate to replace CDOR in certain financial instruments" (May 16, 2022) at 1; see OSFI, "OSFI's expectations for CDOR Transition" (May 16, 2022).

[9][ps2id id='9' target=''/] CORRA would have to be compounded in arrears such that the interest rate and cash flows would not be predictable; interest payments would be determined immediately prior to the payment date based on the overnight rate prevailing on each date from the previous payment to the current payment. A forward-looking term rate based on CORRA would allow participants to determine interest payments in advance and maintain the mechanics used for CDOR referencing loans.

[10][ps2id id='10' target=''/] See CARR, "Consultation on a potential new term interest rate to replace CDOR in certain financial instruments" (May 16, 2022).

[11][ps2id id='11' target=''/] See CARR, "Consultation on a potential new term interest rate to replace CDOR in certain financial instruments" (May 16, 2022) at 2.

[12][ps2id id='12' target=''/] See OSFI, "OSFI's expectations for CDOR Transition" (May 16, 2022).

[13][ps2id id='13' target=''/] See OSFI, "OSFI's expectations for CDOR Transition" (May 16, 2022).

[14][ps2id id='14' target=''/] One of the concerns expressed by respondents to the RBSL Consultation was that as the transition dates drew closer and the BA market further diminished in volume, there would have to be steps taken to ensure that CDOR remained reflective of market conditions and lending costs until the cessation date.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.