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# CARR's approved use cases for Term CORRA

Globally, many major jurisdictions are transitioning their financial system from a forward-looking interbank bank offered rate (IBOR) to an overnight risk-free rate (RFR). In Canada, our IBOR rate is the Canadian Dollar Offered Rate (CDOR) and our overnight RFR is the Canadian Overnight Repo Rate Average (CORRA). CARR expects that the vast majority of the financial products (or exposure) currently referencing CDOR will transition to overnight CORRA calculated in-arrears. This is consistent with the practice in other jurisdictions. The importance of adopting overnight risk-free rates, where possible, has been underscored by the Financial Stability Board[1] as well as by the Bank of Canada and other central banks and regulators.

It has also been recognized that in certain use cases a forward-looking "term RFR" is appropriate in the successful transition from IBORs to RFRs. To determine if a forward-looking term rate is appropriate for particular products, these jurisdictions have created working groups comprised of relevant stakeholders. Similarly, the Canadian Alternative Reference Rate working group (CARR) formed such a group to determine the permitted use cases for Term CORRA. The resulting use cases have been approved by CARR and Canadian Fixed-Income Forum (CFIF)[2] members. The use of Term CORRA will be restricted through applicable licensing agreement to these specific use cases.

The goal of limiting Term CORRA's use to only those products that truly need it is to help ensure that the size of the market referencing Term CORRA is appropriate to the size of the market used to determine Term CORRA (i.e., managing the "inverse pyramid" issue). To this end, the use of Term CORRA will be only allowed as a reference rate for loans and derivatives associated with loans, similar to Term SOFR (see table below).[3] This use aligns with the majority of responses CARR received in its consultation on Term CORRA.

[1] For example, see: FSB Statement Welcoming Smooth Transition Away from LIBOR, FSB 2022 Progress report on LIBOR and Other Benchmarks Transition Issues, Global Transition Roadmap for LIBOR, FSB statement on the impact of COVID-19 on global benchmark reform.

[2] CFIF is a senior level industry committee established by the Bank of Canada to discuss developments in fixed-income market structure and functioning, market practices and related policy issues.

[3] Term CORRA will not be allowed to be used as fallback reference rate to CDOR in cash securities.

<table>
<tr><th>Approved uses for Term CORRA</th><th>Not approved uses for Term CORRA</th></tr>
<tr><td><ul><li>Loan products</li><li>Trade finance (i.e. the discounting of receivables)</li><li>Single currency derivatives for end-users hedging Term CORRA based loans, where the end user is the lender, borrower or guarantor under such loans[4]</li></ul></td><td>All other uses of Term CORRA, including but not limited to:<ul><li>Floating rate notes</li><li>Securitizations</li><li>Capital securities</li><li>Structured notes</li><li>Derivative uses not explicitly identified as eligible, including cross-currency basis swaps[5]</li></ul></td></tr>
<tr><td colspan="2">The decision of whether to add inter-dealer single currency derivative transactions into the Term CORRA approved use cases will be made by CARR prior to the official launch of Term CORRA in Q3-2023.</td></tr>
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Notwithstanding the above use cases, CARR encourages those borrowers that have the operational and technical capacity to use overnight CORRA to do so in preference to using Term CORRA, particularly those that hedge their loans with derivatives.[6] It is expected that the overnight CORRA derivative market will be much deeper and more liquid than the Term CORRA derivative market. Furthermore, all CDOR derivatives subject to the International Swaps and Derivatives Association (ISDA) 2020 fallbacks protocol or supplement, or ISDA 2021 Interest Rate Derivative Definitions will be converted to a rate based on overnight CORRA following the cessation of CDOR on June 28, 2024.

Borrowers that wish to hedge Term CORRA loans with Term CORRA derivatives could see higher hedging costs than if they were using overnight CORRA for both their loan and their derivative hedge. This is due to the one-sided nature of the hedging demand from bank loan end-user clients. The higher hedging costs would be in the form of a positive 'basis' (additional spread relative to overnight CORRA derivatives), similar to that seen in the Term SOFR derivative market. In an effort to encourage a more balanced market for Term CORRA derivatives, CARR will include lenders' Term CORRA hedging transactions in the approved Term CORRA derivatives use cases.

These approved use cases will be defined with greater specificity in the applicable licensing agreements.

## Robust Fallbacks for Term CORRA

CARR has worked with subject matter experts across the various stakeholders in the financial industry to create an International Organization of Securities Commissions (IOSCO) compliant, forward looking, Term CORRA benchmark. While CARR has endeavoured to create a robust and sustainable benchmark, there are certain dependencies underpinning Term CORRA that mean its long-term sustainability is not guaranteed. In particular, the ongoing viability of Term CORRA will depend on the liquidity of the

[4] Lenders can hedge their Term CORRA derivative exposure internally with their own dealer or with external dealers.

[5] CARR will consider adding cross-currency basis swaps if other jurisdictions adopt the use of their term RFR in these instruments.

[6] Note that Prime based borrowing also references an overnight rate.

underlying CORRA futures contracts that are used to derive Term CORRA. If the depth of liquidity in these contracts is not sufficiently robust, the benchmark administrator will be required to amend its methodology.[7] If changes to the methodology do not result in a sufficiently robust benchmark, the benchmark administrator will be required to either (i) take steps necessary 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) to cease the publication of the benchmark with appropriate notice. **CARR therefore expects any users of Term CORRA to have robust fallback language in place, in most cases referencing overnight CORRA calculated in-arrears. Users also need to build the operational capacity to transact in these fallback rates should Term CORRA cease to be published in the future.**

[7] Changing the methodology could result in Term CORRA becoming a T+1 instead of a T+0 rate.