

# Legal Masterclass on SORA Transition

02 December 2020, 10:30am to 12:30pm



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This presentation is strictly private and confidential. It is designed for update and information purposes. It is also incomplete without the accompanying oral briefing. The presentation is not designed to provide any specialist advice and shall not be used for such purposes.

# Programme

**10:30 AM**      **Opening Remarks**  
Ong-Ang Ai Boon  
*Director*  
*The Association of Banks in Singapore*

**10:35 AM**      **Briefing on Compendium**  
Kok Chee Wai  
*Partner*  
*Allen & Gledhill*

Francis Mok  
*Partner*  
*Allen & Gledhill*

Glenn Foo  
*Partner*  
*Allen & Gledhill*

**11:30 AM**      **Break**

**11:35 AM**      **Panel Q&A**

**Moderated by:** Lam Chee Kin,  
*Chair of Steering Committee for SOR Transition*  
*to SORA Sub-Group on Legal and*  
*Managing Director, Head, Group Legal,*  
*Compliance & Secretariat, DBS Bank*

**Panellists:**      *Members of the Steering Committee for SOR*  
*Transition to SORA Sub-Group on Legal and*  
*Allen & Gledhill LLP*

**12:25PM**      **Closing Remarks**  
Ong-Ang Ai Boon  
*Director*  
*The Association of Banks in Singapore*

# Briefing on Compendium

## **Kok Chee Wai**

Partner

Allen & Gledhill LLP

## **Francis Mok**

Partner

Allen & Gledhill LLP

## **Glenn Foo**

Partner

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# Introduction

- A market guide on application of SORA across product classes
- Facilitate awareness / drive adoption of Singapore Overnight Rate Average in financial products
- Explain (1) reasons for transition from SOR to SORA and (2) the nature, methodology and features of SORA

# Derivatives

- At present, SGD interest rate derivatives typically refer to SOR
- Going forward, they will reference SORA instead of SOR
- For legacy SOR derivatives transactions, Fallback Rate (SOR) has been selected as the fallback.

# Documentation for SORA Derivatives

- ISDA has published definition of “SGD-SORA-COMPOUND” as a supplement to the 2006 ISDA Definitions
  - average of SORA over each business day over the calculation period
  - compounded so that the interest rate applies to both the principal as well as the accumulated unpaid interest
- Market participants can incorporate the 2006 ISDA Definitions as part of an ISDA Master Agreement, or in the confirmation for a SORA derivatives transaction

# SC-STs Template Confirmations

## 1. Self-compounding Overnight Interest Rate Swap (OIS)

- Fixed-to-floating swap, references SGD-SORA-COMPOUND

## 2. Cross Currency Rate Swap

- References SGD-SORA-COMPOUND and USD-SOFR-COMPOUND
- Notional amounts remain fixed

## 3. Interdealer Mark-to-Market Currency Swap

- References SGD-SORA-COMPOUND and USD-SOFR-COMPOUND
- USD notional amount changes, based on USD-SGD FX spot rate at the beginning of each calculation period

## 4. Rate Swap Transaction

- References SGD-SORA-COMPOUND and SGD-SOR-VWAP
- However users are more likely to enter into a SORA OIS together with a SOR IRS



# SOR and SORA Swaps – Comparison of Market Conventions

	SOR swaps	SORA swaps
<b>Interest rate determination</b>	In advance	In arrears
<b>Reset Rate</b>	1st day of Calculation Period	Last day of Calculation Period
<b>Payment Date</b>	Last day of Calculation Period	“Delayed Payment” of 2 Business Days, i.e. Payment Date is 2 Business Days after last day of Calculation Period



# SOR Derivatives: Contractual Fallbacks

- Issue: What happens to a SOR derivative when publication of SOR ceases?
- Existing IBOR fallbacks were designed to address temporary unavailability of rates, not permanent cessation
- For SGD-SOR-VWAP, the fallback is “SGD-SOR-VWAP-Reference Banks”
  - Relies on USD LIBOR
  - If USD LIBOR is unavailable, relies on polling banks in the London interbank market

# Fallback Rate (SOR): The new contractual fallback for SOR

- Published by ABS Benchmarks Administration Co, commencing 30 September 2020
- Similar in construct to SOR: An FX-implied rate, based on actual transactions in USD/SGD FX swap market
- Will reduce the risk of value transfer compared to a SORA-based fallback

# ISDA IBOR Fallbacks Supplement and Fallbacks Protocol

- IBOR Fallbacks Supplement published by ISDA on 23 Oct 2020: Amends the definitions of certain IBORs to incorporate fallbacks based on risk-free rates
  - Effective date is 25 Jan 2021: SOR transactions entered into on or after that date will incorporate Fallback Rate (SOR) as the fallback
- For existing transactions, ISDA has published the IBOR Fallbacks Protocol
  - Effective date is also 25 Jan 2021
- The Supplement and Protocol provide that upon an “Index Cessation Event”, Fallback Rate (SOR) will apply instead of SOR

# The Fallbacks Protocol

- Multilateral contractual amendment mechanism: Will amend agreements entered into with other market participants who have signed up to the protocol
- Protocol covers several types of agreements other than ISDAs, for example:
  - Global Master Repurchase Agreement (GMRA)
  - Global Master Securities Lending Agreement (GMSLA)
  - Overseas Securities Lender's Agreement (OSLA)
  - Master Securities Loan Agreement (MSLA)
  - Master Repurchase Agreement (MRA)
- Does not amend documentation covering cleared transactions
- ISDA has also published bilateral forms of amendment agreements

# Timing for transition to SORA derivatives

- Fallback Rate (SOR) is intended only as an interim rate
  - Should not be used for new transactions
  - Publication will cease after about 3 years after the fallback trigger date
- Market participants should actively transition to SORA, reduce exposure to SOR by end 2021
- LCH Limited has offered clearing of SORA derivatives since May 2020
- ABS aims to reduce banks' gross exposures to SOR derivatives to 50% of May 2020 level by Q2 2021, and 20% by Q3 2021

# Capital Markets – Legacy Products

- What is affected?
  - Securities that have already been issued that reference SOR as a base rate on an ongoing basis
  - Rates that require fixing beyond 2021

# Capital Markets – Legacy Products

- What is going to happen post 2021?
  - Existing SOR fallback mechanics
    - a. Replacement Bloomberg / Reuters screen page
    - b. Rate published by recognised industry body
    - c. Quotations from reference banks
    - d. Using SOR from the preceding interest period

These fallback procedures tend to be appropriate for a temporary unavailability

- What should you do now?
  - Need to revisit your existing documents
  - Talk to your professional advisors

# Capital Markets – Transition Period

- Recommended SOR fallback replacement language from SC-STS
  - Benchmark Event Triggers
    - Permanent cessation of USD LIBOR
    - Determination by the FCA that USD LIBOR is no longer representative of its underlying market

This is designed to be aligned with triggers for SOR and USD LIBOR derivatives contracts



# Capital Markets – Transition Period

So a Benchmark Event has happened....

- Appoint an Independent Advisor
  - Independent financial institution of good repute with experience in the local or international debt capital markets
  - Failing which, Issuer to determine the replacement rate

# Capital Markets – Transition Period

What will the Replacement Rate be?

- Benchmark Replacement
  - Interpolated benchmark
  - Term SORA
  - Compounded SORA
  - Successor rate nominated by the central bank
  - ISDA Fallback Rate
  - Alternative rate
  
- Possibility of an Adjustment Spread

# Capital Markets – The Future

- SORA! SORA! SORA!
  - Compounded Daily SORA – in line with market convention and the derivatives market
  - Weighting of SORA
  - Observation periods

# Capital Markets – The Future

- Possible Observation Periods
  - Lockout - daily SORA is observed up to a certain number of days prior to the end of an interest period. SORA of the day prior to the start of the Lockout Period is applied for the remaining days of the interest period.
  - Lookback - the SORA rate for each day in an interest period is based on the SORA rate of a certain number of business days prior to that day. Essentially, the Observation Period starts prior to the first day of the relevant interest period and ends prior to the end of the interest period.

# Capital Markets – The Future

- Possible Observation Periods
  - Backward shifted - similar to the Lookback Observation Period except that the weightings in the compounding formula is based on the number of business days and non-business in the relevant Observation Period (instead of the relevant interest period).
  - Payment delay - interest payments are delayed by a certain number of business days

# Corporate Loans – Background

- Swap Offer Rate (SOR) and SIBOR are common reference rates in Singapore corporate loans markets
- Effect of discontinuation of USD LIBOR on SOR
  - SOR will similarly cease as US dollar LIBOR is a component of SOR
  - Conventional market disruption clauses in loan agreements may apply but the long-term default to Cost of Funds is neither contemplated nor desirable
  - SIBOR will also be discontinued by 2024

## Corporate Loans – Transition Period

- For existing loan agreements, it is preferable for legacy SOR corporate loans to include additional contractual fallbacks
- Recommendations of the Fallback Rate (SOR) to apply for legacy SOR loans
- Fallback Rate (SOR) is temporary – eventual transition to SORA

# Corporate Loans – Transition Period

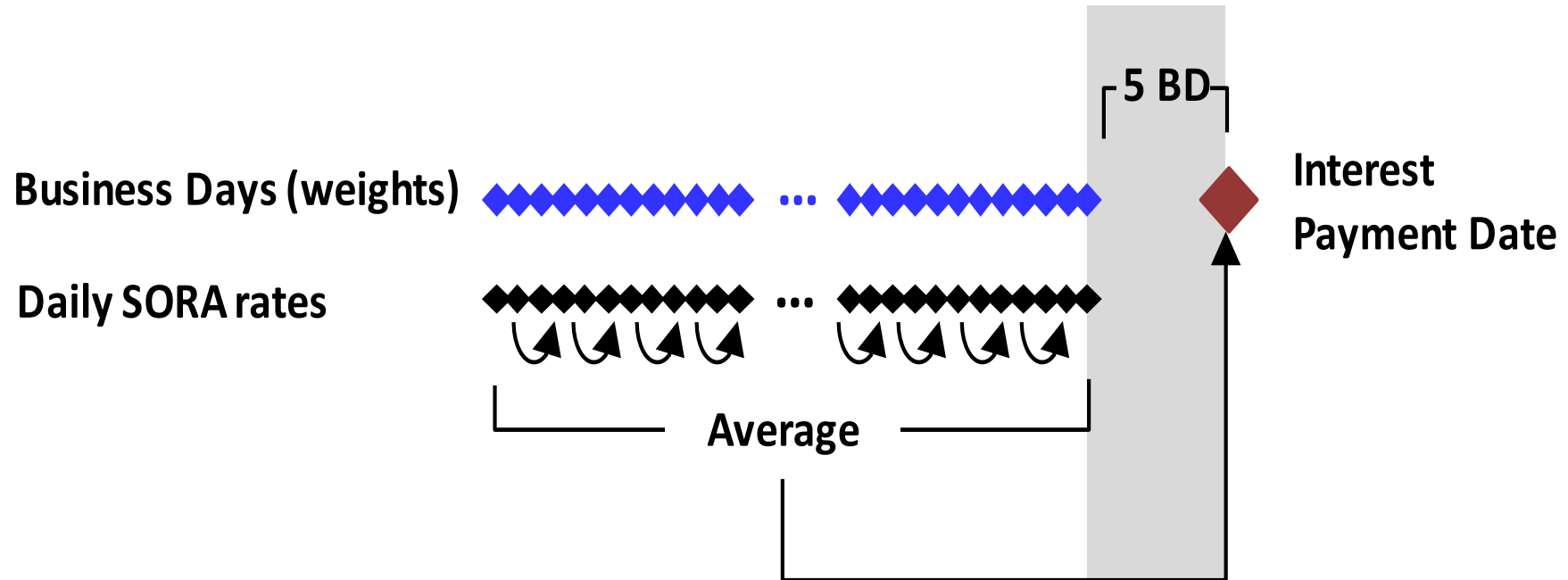
- Need to amend loan documents to include Fallback Rate (SOR)
- Recent loan agreements based on the APLMA template may include a Replacement of Screen Rate clause which sets out a regime for parties to agree on alternative rates
- The operative clause will still need to be agreed by the parties



# Corporate Loans – New Products

- SC-STS has released recommendations on SORA loan market conventions and fallbacks for new bilateral and syndicated loans.
- Considerations
  - Urgent need for lenders and borrowers to transition away from the use of SOR
  - Need for consistency across currencies, products and markets
  - Alignment between loan and derivatives market conventions
  - Advance notice of payment – both “Lookback with Observation Shift” and “Lookback without Observation Shift” are suitable options for the SORA loan market
  - Summary table of indicative terms

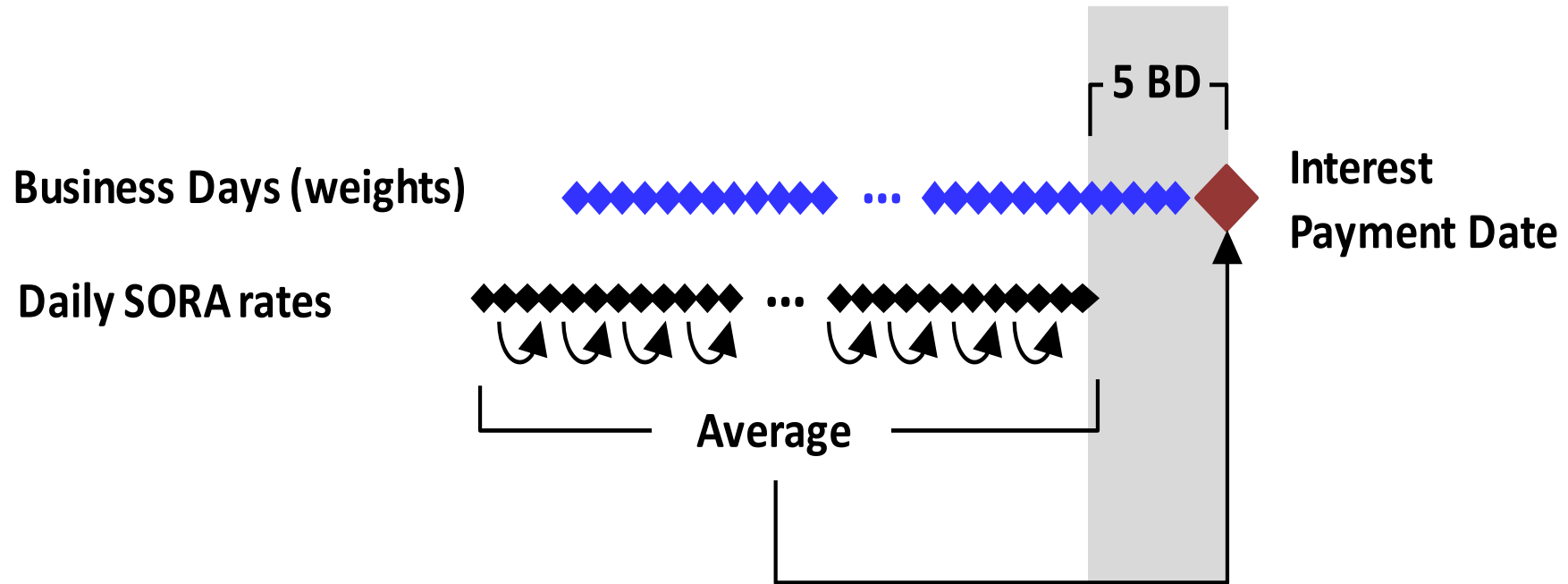
# Corporate Loans – Lookback with Observation Shift



# Corporate Loans – Lookback with Observation Shift

- Pros
  - Compatibility with central bank-published rates
  - Alignment with derivatives hedges
- Cons
  - Harder to operationalise prepayments or loan trading
- Situations where Lookback with Observation Shift would be appropriate
  - Parties wish to use the SORA Index
  - Parties want loan interest payments to be better matched to derivative hedges
  - Parties do not expect loan to be prepaid or traded

# Corporate Loans - Lookback without Observation Shift



# Corporate Loans - Lookback without Observation Shift

- Pros
  - Alignment with global default recommendations
  - Easier to operationalise prepayments or loan trading
- Cons
  - Less transparent due to requirement for internal computation of interest rate
- Situations where Lookback without Observation Shift would be appropriate
  - Parties wish to align with recommended conventions for global currencies such as USD and GBP
  - Parties expect loan prepayment or trading

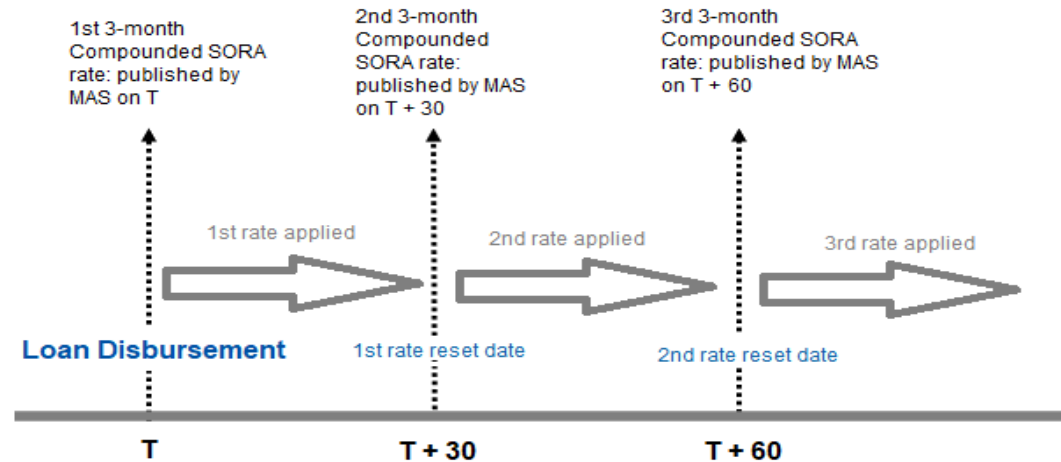
# Retail Loans – Background

- Wider variety of interest rate options e.g. fixed rates, prime lending rates, floating rates
- Most financial institutions had already ceased offering SOR retail loans since about 2011

# Application of SORA in new retail loans

- SORA-centred approach with cessation of SOR and discontinuation of SIBOR
- Compounded SORA in advance gives customers certainty of the rate which will apply for a period at the beginning of that period

## Example: 3-month Compounded SORA rate with 30-day rate reset



# Proposed industry approach to deal with legacy SOR loans

- Explain industry-wide approach to deal with legacy loans in line with MAS Guidelines on Fair Dealing
- Communication and provide options and information (including disapplication of MAS Notice 645/632A etc.)
- Consumer choice



# Panel Q&A

## Moderated by:

**Lam Chee Kin**

*Managing Director, Head, Group Legal, Compliance & Secretariat  
DBS Bank*

## Panellists:

### *Members of SC-STs Sub-Group on Legal*

**Joyce Lai**

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and Compliance, Treasury & Markets  
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**Koh Hwee Keow**

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# Thank You!

- Today's session can be accessed on demand at:

<https://abs.org.sg/benchmark-rates/events>



- Feedback survey form on today's session can be found on:

<https://pigeonhole.at/>

Passcode: SORA1202

- For further queries relating to this subject matter, please write to:

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