



Executive Summary
SIFMA Model Provision – Investment-Grade Bond Optional Redemption
Standardizing the make-whole redemption language and calculation.

Market participants have expressed the need for standardized language in investment-grade bond optional redemption provisions. SIFMA assembled a working group of investment banks operating in the U.S. and global capital markets to agree on general principles and model language.

The final version of the model provision was published by SIFMA on November 29, 2021.

Background

Investment-grade bond optional redemption provisions, and the calculation of the make-whole redemption price, can vary by issuer and by the methodology used by the investment bank assisting with such calculation. This variation in language and calculation results in a lack of standardization in the manner of calculating the redemption price. As a result, market participants have expressed the desire for standardized language in investment-grade bond optional redemption provisions.

In many make-whole calculations, a reference United States treasury security is selected by the issuer with the assistance of an investment bank. In others, a United States treasury constant maturity as published by the Board of Governors of the Federal Reserve System (a “Treasury constant maturity”) is used. In both cases, a ‘make-whole’ spread that was established at the time of initial pricing of the issue is added to the yield of the selected treasury security or Treasury constant maturity, and the resulting yield is used to discount the sum of the present values of the applicable remaining scheduled payments of principal and interest to the redemption date. The yield of the reference United States treasury security or Treasury constant maturity is most commonly referred to as the “Treasury Rate.”

In existing optional redemption provisions, there are variations in the method for selection of the United States treasury security or the Treasury constant maturity and the related yield. Many current provisions use a “comparable treasury issue” selected by an independent investment bank in accordance with “customary financial practice in pricing new issues” of corporate debt for determining the Treasury Rate. Ambiguity over which treasury is “comparable” and what is “customary” may result in different investment banks selecting different reference treasuries and yields.

To promote consistency and clarity for the benefit of both issuers of corporate debt as well as the holders of such debt, the SIFMA working group focused on the Treasury Rate definition, and considered, among other things, the optimal source and method of selecting and calculating the Treasury Rate, including the role of the independent investment bank. The SIFMA working group also considered additional changes to existing provisions.

The resulting model provision provides issuers, investment banks, investors, and other market participants with certainty and specificity in the calculation of the redemption price of bonds being redeemed.

Summary of Model Provision

Below is a summary of key aspects of the model provision:

- The general principles of the make-whole calculation are unchanged. Payments of principal and interest are discounted to the redemption date using a Treasury Rate determined at the time of the redemption plus the make-whole spread that was determined at pricing of the issue.
- The calculation of the Treasury Rate and redemption price are done by the issuer. It is no longer necessary for an independent investment bank to select a United States treasury security or perform the make-whole calculation.
- The primary method of calculating the Treasury Rate will be done using the most recent statistical release published by the Board of Governors of the Federal Reserve System designated as “Selected Interest Rates (Daily) - H.15” or any successor designation or publication (“H.15”) as of 4:15 p.m. New York time on the third business day preceding the redemption date and choosing the relevant Treasury constant maturity or Treasury constant maturities.
 - This is published by the Federal Reserve on a daily basis, currently at <https://www.federalreserve.gov/releases/h15/>
- Applicable calculations use the period from the redemption date to the maturity date (or, if the notes have a ‘par call’ date, the par call date), with such period being referred to as the “Remaining Life.”
- In the majority of redemptions, two yields are selected—one yield corresponding to the Treasury constant maturity on H.15 immediately shorter than the Remaining Life, and one yield corresponding to the Treasury constant maturity on H.15 immediately longer than the Remaining Life.
- The two yields are interpolated to the maturity date, or par call date, as applicable, on a straight-line basis using the actual number of days. To calculate the actual number of days, the applicable Treasury constant maturity on H.15 is deemed to have a maturity date equal to the relevant number of months or years, as applicable, of such Treasury constant maturity from the redemption date. Other than for maturities of less than one year, this means that a Treasury constant maturity will be deemed to have a maturity date with a month and day the same as the redemption date, and the applicable year matching the selected Treasury constant maturity.
- *For example, if the redemption date is November 15, 2021 and the par call date is April 15, 2027, and the period from the redemption date to the par call date is 5 years and 5 months, the issuer will select the yield corresponding to the 5-year Treasury constant maturity and the yield corresponding to the 7-year Treasury constant maturity on H.15 (there is no 6-year Treasury constant maturity). The yields will be interpolated on a straight-line basis using the actual number of days. For this interpolation calculation the 5-year Treasury constant maturity will be deemed to have a maturity date of November 15, 2026 and the 7-year Treasury constant maturity will be deemed to have a maturity date of November 15, 2028.*
- In more limited circumstances, only one treasury and yield will be used. This happens when (i) the Remaining Life matches exactly a Treasury constant maturity (for example, if the period from the redemption date to the par call date is exactly 5 years, the yield for the 5-year Treasury constant maturity on H.15 will be the Treasury Rate) or (ii) if there is no Treasury constant

maturity on H.15 immediately shorter or immediately longer than the Remaining Life, as applicable (for example, if the period from the redemption date to the maturity date, or par call date, as applicable, is less than one month or greater than 30 years).

- If H.15 or any successor designation or publication is no longer published, the model provision provides a backup which calculates the Treasury Rate using the yield of the United States Treasury security maturing on, or with a maturity that is closest to, the maturity date, or par call date, as applicable.
- Subjective determinations such as the “comparable treasury,” or what is consistent with “customary financial practice in pricing new issues” have been eliminated.
- Notice of redemption must be mailed or electronically delivered at least 10 days but not more than 60 days before the redemption date. While this period is shorter than the historical 30-day notice period, 10 days has become customary in current debt issues and should provide investors with sufficient notice of the redemption.
- After all calculations are completed, the Treasury Rate is rounded to three decimal places.

Any questions may be directed to Shearman & Sterling LLP.

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Illustrative Example

\$100,000,000 of 2.00% Senior Notes due July 1, 2027

Redemption Date: October 1, 2021	Calculation Date: September 28, 2021	Par Call Date: April 1, 2027
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1. Go to H.15 - *Selected Interest Rates (Daily) - H.15 -- Treasury constant maturities -- Nominal*
2. On the Calculation Date, find the most recent data available after 4:15 p.m., New York City time, which is data for September 27, 2021
3. Select the yield corresponding to the Treasury constant maturity on H.15 immediately shorter than the Remaining Life = 5-Year Treasury constant maturity = **0.98%**
 - a. The 5-Year Treasury constant maturity has a deemed maturity date of October 1, 2026, which is the date equal to five years from the redemption date of October 1, 2021.
4. Select the yield corresponding to the Treasury constant maturity on H.15 immediately longer than the Remaining Life = 7-Year Treasury constant maturity = **1.30%**
 - a. The 7-Year Treasury constant maturity has a deemed maturity date of October 1, 2028, which is the date equal to seven years from the redemption date of October 1, 2021.

We refer to the deemed maturity dates of the two Treasury constant maturities as the "H.15 maturity dates."

5. Day Count Calculations

Using the Microsoft Excel function =DAYS is an accurate way to find actual number of days for use in these calculations.

(X) Actual days from October 1, 2021 (Redemption Date) to, but excluding, April 1, 2027 (Par Call Date) = **2,008**

(Y) Actual days from October 1, 2021 (Redemption Date) to, but excluding, October 1, 2026 (5-Year Treasury constant maturity date) = **1,826**

(Z) Actual days from October 1, 2021 (Redemption Date) to, but excluding, October 1, 2028 (7-Year Treasury constant maturity date) = **2,557**

Then:

- a. Compute the difference in days between **(X)** and **(Y)** = $2,008 - 1,826 = 182$
 - b. Compute the difference in days between **(Z)** and **(Y)** = $2,557 - 1,826 = 731$
6. Calculate when the Par Call Date occurs in the period between the two H.15 maturity dates, as a percentage of the difference between = $182/731 = 24.8974\%$
The Par Call Date occurs 24.8974% of the way between the two H.15 maturity dates.
 7. Calculate the difference in yields between the two H.15 maturity dates ($1.30\% - 0.98\% = 0.32\%$) and multiply the result by the distance fraction ($0.32\% * 0.248974 = 0.07967\%$)
 8. Add the result (0.07967%) to the yield for the Treasury constant maturity shorter than the Remaining Life (0.98%) = $0.98\% + 0.07967\% = 1.05967\%$ and round to three decimal places = **1.060%**

The Treasury Rate is 1.060%.
