

Market Standards for Corporate Actions Processing

Question & Answer Document

Prepared by the Corporate Actions Joint Working Group

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Processing of securities distribution with fractions

The questions on the processing of Securities Distribution with fractions arise from the interpretation of the **standard 16b and 16c of the securities distribution** chapter.

Standards:

16b) The Payments should be processed by rounding down to the nearest whole number (top-down method).

c) When Fractions occur and the Issuer compensates them in cash at the level of the Issuer (I)CSD, the Issuer (I)CSD participants and all the Intermediaries down the chain should on their turn, each at its respective level, also compensate any Fractions in cash.

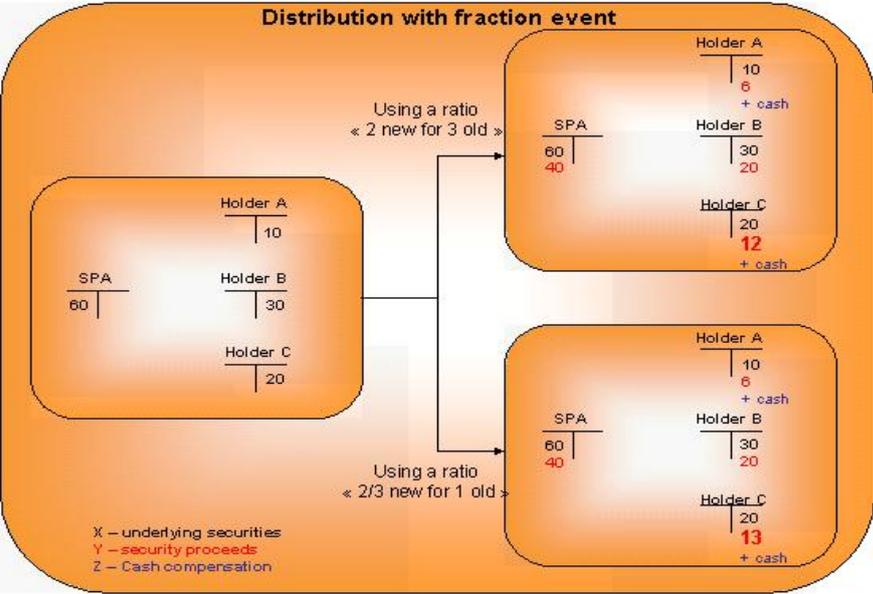
Interpretation of the standard:

Our current understanding of these standards are that the security proceeds have to be calculated taking into account the ratio communicated by the issuer, rounding down the result, and that fractional part has to be compensated in cash if decided by the issuer.

However several calculation methods can be used for the processing of the corporate event. Additionally our understanding is that the distribution has to occur directly in proceeds, not through the usage of an interim security.

Example 1:

Ratio of the corporate event is: 2 new B shares distributed for 3 old ISIN A shares. The picture below describes the target solution without use of an interim security.



Question 1: Is the usage of an interim security to process the distribution against the standards?

Answer: Yes, the usage of an interim is not an efficient solution as it will imply a second process (i.e. the reorganisation of the interim against new securities). In addition it will conflict with the Top Down method.

Question 2: Should we always apply the process maximizing the result of the corporate event (i.e. using a “n/m new for 1 old” ratio type), even if the ratio communicated by the issuer or the agent is “n new for m old”, as there is no economic rationale to create additional fractions. Or does the CSD have to process the corporate event taking into account the initial quantum as provided by the issuer or its agent? Should an additional indicator be used to define if the initial quantum has to be taken into account, whatever the expression of the ratio is?

Answer: *Yes, this is correct. It is recommended that the CSD and all intermediaries through the chain apply the same calculation method for the distribution of new securities, i.e. to multiply the existing position by the ratio n/m and leaving the decimals (or, compensate them in cash). The integer part of the result will be credited on the relevant securities account.*

It is recommended to apply one unique algorithm regardless of the way it is announced and take into account the full balance even if not explicitly mentioned in the announcement as it leads to a more optimal result maximising the new shares and minimising the fractions.

Examples of possible announcements:

*0,1 new A share for 1 old A share
1/10 new A share for 1 old A share
1 new A share for 10 old A shares*

The calculation method for an existing position of 123 old shares is:

123 multiplied by 1/10 = 12,3 rounded down to 12 new shares

Question 3: When should the reference price be announced by the issuer?

Answer: *If the Issuer decides to announce a reference price, he has to communicate it no later than one business day before the record date of the distribution event.*

This will enable the Issuer CSD to process on Record Date positions both the credit of new shares and the payment of the cash compensation. The Issuer CSD’s participants will be paid (compensated) at that reference price irrespective of the actual market price that the Issuer will receive through the sale of the fractions.

Question 4: When should the compensation in cash be paid to the issuer CSD participants?

Answer: *There are two possible scenarios:*

In the first one, the reference price has been announced before the Record Date and the Issuer CSD is therefore able to calculate and pay the cash compensation on the Payment Date of the distribution of the new securities based on Record Date positions.

In the second scenario, the reference price has not been announced and it is up to the Issuer (or the Issuer Agent) to process the cash compensation for the Issuer CSD participants with the cash stemming from the sale of fractions. In this scenario the Issuer CSD participants should be paid preferably no later than one settlement cycle after the Payment Date of the distribution of the new securities.

Question 5: When should the compensation in cash be paid by intermediaries down the chain?

Answer: *The reasoning is exactly the same for the intermediaries who should be able to determine the number of fractions of their respective clients on Record Date (via the top down method) and sell*

them as soon as possible once the credit of the new securities has been processed. Therefore, the intermediaries should also compensate their clients ideally no later than one settlement cycle after the Payment Date of the distribution of the new securities (via the top down method without any intervention on the part of clients).

Question 6: For cash compensation by the Issuer CSD, should the reference price as announced by the issuer be used?

Answer: *Yes, once the reference price has been announced by the Issuer, that price will be used by the Issuer CSD to process on Record Date the calculation of cash compensation of the fractions for the Issuer CSD's participants.*

Let's take the previous example:

0,1 new A share for 1 old A share and a reference price of EUR 5,68 per new A share;

an existing position of 123 old shares giving 12 new shares and 0,3 new share to be converted into cash: 0,3 multiplied by EUR 5,68 = EUR 1,70.

Question 7: For cash compensation by the intermediaries down the chain, can another price (i.e. the real selling price on the market) be used instead of the reference price announced by the issuer?

Answer: *Yes, the price applied by the intermediaries can be different and there is no obligation to apply the reference price.*

Processing of securities distribution with fractions in an investor CSD environment

The question on the processing of Securities Distribution with fractions arises from the interpretation of the standard 16c of the securities distribution chapter.

Standards:

16c) When Fractions occur and the Issuer compensates them in cash at the level of the Issuer (I)CSD, the Issuer (I)CSD participants and all the Intermediaries down the chain should on their turn, each at its respective level, also compensate any Fractions in cash.

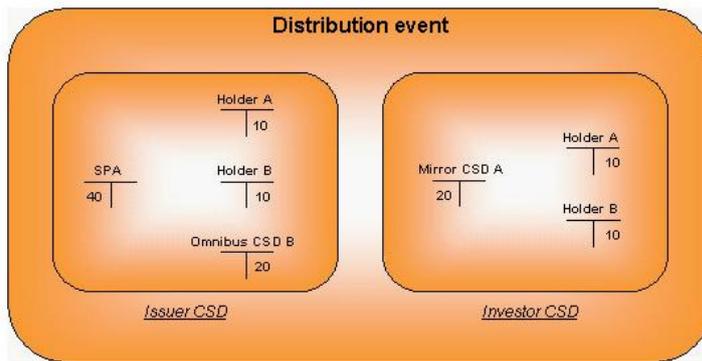
Interpretation of the standard:

Our current understanding of this standard is that in case of a securities distribution including fraction compensation from the issuer, when processed in an issuer CSD / investor CSD environment, would imply that the investor CSD has to compensate in cash part of the distribution that has been received under security proceed format.

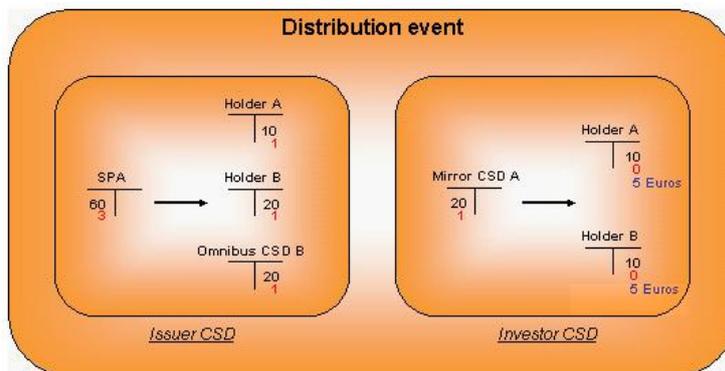
Example 2:

Example of a security distribution, where the ratio is 1 new ISIN B for 20 old ISIN A, with cash compensation of the fraction, with a reference price of 10 Euros for an ISIN B.

Initial situation (end of day balances in ISIN A):



After corporate action processing:



Question 8: Does that mean that the investor CSD can be paid in securities and cash, and would have to process to a cash compensation of the fractions towards its own account holders?

In that case the investor CSD would have to sell on the market the fractional part of the distribution.

Answer: Yes. There is no specific rule for the Investor CSD and the Investor CSD participants. The Investor CSD and the Investor CSD participants should apply the standards like all Intermediaries. The Investor CSD is an Issuer CSD participant. As per the standards, the Investor CSD should thus compensate any fractions in cash, in its turn, for the Investor CSD participants.

Question 9: In that case, when should the compensation in cash should be paid to the investor CSDs participants?

Answer: As mentioned under Question 5, Intermediaries should be able to determine the number of fractions of their underlying clients on Record Date (top down method) and sell them as soon as possible once the credit of the new securities has been processed and no later than one Settlement Cycle after the Payment Date of the distribution.

Question 10: For cash compensation by an Investor CSD, should the reference price as announced by the issuer be used?

Answer: The Investor CSD can apply a different price (i.e. the real selling price) like Intermediaries do in an Issuer CSD scenario (see also answer to Question 7).

Question 11: Should this process (selling of fractional part on the market, cash compensation...) be achieved via the services of a local agent?

Answer: The Investor CSD can use the service of a local agent.

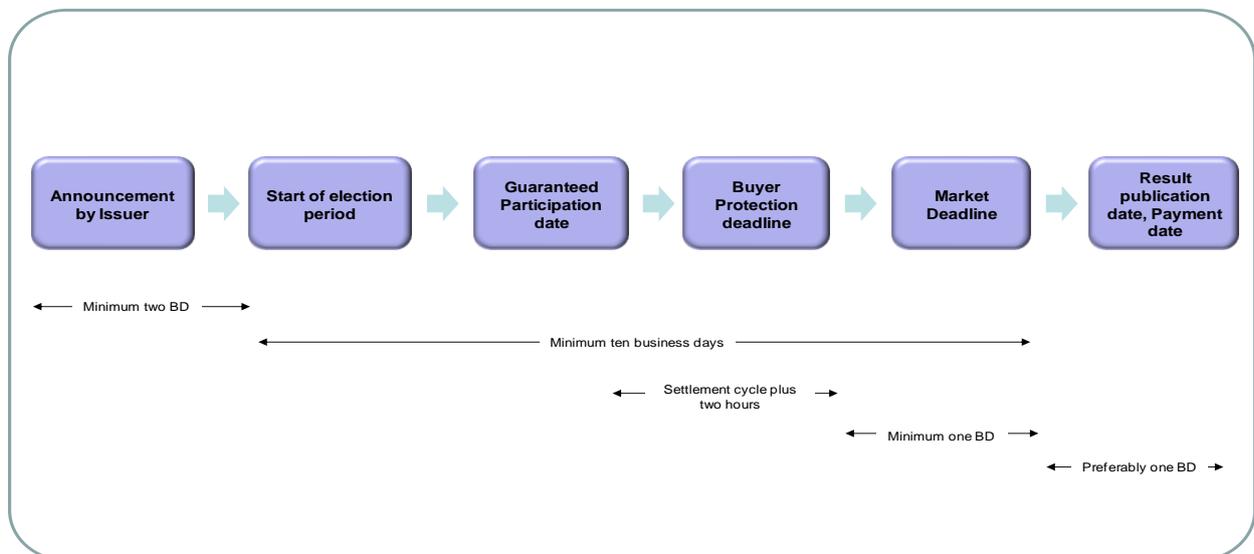
Key dates and processing of voluntary reorganisations (Offers)

The questions regarding reorganisations with options key dates and processing arise from the guaranteed participation date definition as mentioned in the Glossary and the sequence of dates of the reorganisations with options.

Standards:

Guaranteed Participation Date definition: Last date to buy the Underlying Securities with the right attached to participate in an elective corporate action.

Sequence of dates:



Question 12: Do we have to consider that the aim of the Guaranteed Participation Date is to 'guarantee' to the buyer that he will be able to participate to the corporate action if he has traded before such date?

This will be the case either because the transaction has settled prior to the Market Deadline or if it has not settled prior to the Market Deadline because the buyer has sent a buyer protection instruction to the seller prior to the Buyer Instruction Deadline.

For trades made after the Guaranteed Participation Date, such guarantee would not exist anymore, but the buyer could still be able to participate to the corporate action either because the trade has settled before the Market Deadline or the seller accepts a buyer protection instruction from the buyer even if he is not obliged to do so.

In that case, a transaction traded after GPD and settled prior market deadline would be eligible to the voluntary event.

In that case, we would suggest that the definition of the Guaranteed Participation Date is updated as follows: “Last date to buy the Underlying Securities with the absolute guarantee to participate in an elective event, via the usage of the Buyer Protection mechanism”

Answer: *To answer the initial question, the Guaranteed Participation Date, as defined by the glossary, is the “last date to buy the Underlying Security with the right attached to participate in an Elective Corporate Action”, therefore the assumption is right that anything traded on or before this date is guaranteed, whether it be via settlement or a buyer protection.*

Please note, however, this methodology is based on the standard settlement cycle, meaning that the intended settlement date must be on or before the Buyer Protection Deadline and not the Market Deadline. This means that the buyer is fully entitled to the event and that the seller cannot dispute this. The buyer must however adhere to the Buyer Protection Standards to ensure full participation. For example, if a buy trade is executed with a trade date on the Guaranteed Participation Date, the settlement date cannot be after the Buyer Protection date in order to guarantee the buyer’s entitlement.

Question 13: Should the market practice be that all suggested dates are positioned close to the end of the operational day?

Answer: *The following dates need not be positioned close to the end of the operational day: Announcement by the Issuer, Start of the Election Period, Results publication date, Payment Date. Guaranteed Participation Date, Buyer Protection Deadline and Market Deadline are positioned close to the end of the operational day (see also glossary), whereby Market Deadline should be after final settlement.*

COAF and option numbering in an investor CSD environment

The questions on the COAF allocation and on the option numbering arise from the standards labelled under ‘Information from Issuer (I)CSD to its participants’ and ‘Information flow from (I)CSD participants to End Investors’.

COAF (Official Corporate Action Event Reference) definition:

The definition of COAF is “Official and unique reference assigned by the official central body entity within each market at the beginning of a corporate action event”.

Interpretation of the standard:

Our current understanding of these standards is that an issuer CSD should be in charge to allocate the COAF, while each investor CSD should communicate the COAF allocated by the issuer CSD. For option identification, option numbering should remain the same all along the chain of investors.

Question 14: Should the investor CSD communicate the COAF allocated at the issuer CSD level? In that case, should the CORP remain allocated by the investor CSD?

Answer: *The CAJWG defers to the global market practice as created by the Securities Market Practice Group (SMPG). The SMPG states that ‘The COAF should be assigned by the official source as soon as*

the event has been publicly announced by the issuer (or its agent). The public announcement and assignment of COAF should take place according to the applicable market rules, but by latest before the event has reached the entitlement and/or instructions stage. When the COAF has been assigned, it must be relayed through the processing chain to all market participants who should include it in their communications regarding the event.'

The CAJWG defers to the global market practice and ISO standards for the CORP reference. This reference is assigned by a sender of a notification concerning a particular corporate actions event, and the unique reference will be included by the sender in all messages sent for the event. Each account servicer may have its own CORP reference, which is to be included in all messages sent to that account servicer for the particular event, but there is no need to replicate a CSD's reference throughout the chain.

Question 15: Should the option numbering at investor CSD level be similar to the option numbering allocated at the issuer CSD level?

Answer: *Standard 18 in Mandatory Reorganisations with Options and standard 19 in Voluntary Reorganisations both state that 'Each option should have a unique identifier provided by the Issuer, that will be maintained by the Issuer (I)CSD and all Intermediaries'. Since the only way to uniquely identify an option in an ISO 15022/20022 message is to use the combination of Corporate Action Option Code (CAOP) and Number (CAON), and the Market Standards for Corporate Actions Processing specifically refer to industry standards such as ISO, it follows that the CAON and CAOP combinations sent in the notification from the Issuer to the Issuer (I)CSD for onwards communication must be maintained throughout the chain of Intermediaries.*

Interim securities in Distributions with Options (Standard 1)

Question 16: In Denmark we have a domestic system for investors' selection between stock dividend or cash dividends on investment funds. This is registered on the CSD account (direct holding account system) without a need for a "selection ISIN". The investor receives immediately after the GM the cash and/or additional securities according to previous registration on the securities account. It is a simple STP-reinvestment of the dividend (after tax) and should be possible. Operating with a "selection ISIN" in regards to the example above is disadvantageous to investors since it will impose a 2 week delay on receipt of cash dividend. This can also pose a problem in regards to deadlines for reporting to and payment of withheld dividend to the tax-authorities according to existing deadlines. It was the impression at the E-MIG workshop in Munich (2011) that CAJWG would dig into this item again and hopefully state that both variants - a) above version registered on the securities account and b) the version according to the standards operating a "selection ISIN" - are possible. Hence, DK-MIG seeks clarification of whether the Danish market can operate with a STP-reinvestment regarding investment funds. The investment funds decides whether investors shall have the possibility to choose between cash or additional securities. If possible it will be processed in accordance with the existing model registered on the securities account. And it will not be possible - at the same time - to comply with a request for a "selection ISIN" from an investor.

Answer: *Please note the scope of application of the Market Standards for Corporate Actions Processing, where investment funds are only included when listed and traded on a regulated trading venue. Provided that the investment funds mentioned are covered by the standards, the requirement for distribution of an interim ISIN and election on this ISIN applies. There is no barrier for accepting and processing standing instructions for a particular account and event type, and the process mentioned could be kept as a standing instruction on the interim ISIN. This will mean a delay compared to the current process, but a greater harmonisation with optional dividends on shares, and may also make it easier for investors to have a more flexible approach to their standing instructions.*

Reversal of payments

Question 17: If the payment is completed it cannot be reversed by the CSD due to legal matters. It was the impression at the E-MIG workshop in Brussels (2011) that CAJWG would dig into this item again. Perhaps by drafting a more soft paragraph where the issuer CSD can ask it's members to execute a reversal if possible - and where the members are obliged to do their utmost. The problem was also discussed at the E-MIG workshop in Milan (2012).

Answer: *The existence of a legal barrier to implementation of a standard is not necessarily a reason for amending a standard, even if the barrier is shared by other markets. In this instance, the barrier is likely to be significant to overcome for direct-holding markets, but is nonetheless more related to technical difficulties and insufficient authority vested in the CSD than a true legal impediment. The technical difficulties can be overcome (though the market may be unwilling to bear the cost), and it should be possible to amend the CSD rules / account agreements to specifically allow the CSD to perform debits in relation to reversal of payments.*

Time of payments

Question 18: Should the time of cash payments be moved in a T2S environment?

Answer: *The market standards for corporate actions processing currently state that cash payments should be made as early as possible and no later than 12 noon. The main focus of this standard is to ensure payments to CSD participants are made as early as possible, in order for them to be able to use the cash for payment of settlement transactions. With T2S and other market/CSD changes, it is the intent of the CAJWG to gradually move the last payment time. By the time of T2S going live, the standard should be amended to 'The Issuer should make Payments as early as possible after opening of the Payment system and no later than 9 am Issuer (I)CSD local time.'*

Unique identifiers

Question 19: How should the unique identifier (Each option should have a unique identifier provided by the Issuer, that will be maintained by the Issuer (I)CSD and all Intermediaries.) be created?

Answer: *The unique identifier of an option in an event needs to be separated from the unique identifier for an event.*

The former is the Corporate Action Option Number (CAON), supported by the Corporate Action Option Code (CAOP). This is required by the market standards for corporate actions processing. The number, as well as the code, for each specific option provided by the issuer is assigned by the issuer (or the issuer CSD on behalf of the issuer). The option number and option code for each issuer-provided option is unique per event and must be communicated without changes for the issuer CSD throughout the chain of intermediaries.

The latter is the Official Corporate Action Event Reference (COAF), which is a unique reference assigned to a corporate action event by the market's official body for this purpose. This official body is commonly a CSD, but may also be a stock exchange or a data reference utility. The COAF is not

required by the market standards for corporate actions processing, but the CAJWG recommends and strongly supports the use of it.

Buyer Protection

Question 20: Which fields are Mandatory on the Buyer Protection Template?

Answer: All fields on the template should be considered mandatory and populated with the requisite information. The template has been designed to keep the information transmitted between counterparties to the essential detail allowing identification of the Corporate Event, the transaction and the option selected.

Question 21: What is the guidance of the Corporate Actions Joint Working Group with regards to receiving or providing confirmation on Buyer Protection?

Answer: It is important to note that both the buyer and seller have a responsibility under good market practise to ensure the confirmation is obtained. A Buyer Protection can involve significant market exposure for both parties and therefore good market practise is to ensure the safe passage of the instruction from buyer to seller by ensuring a confirmation is in place prior to the market deadline.

The **buyer** should;

- Endeavour to send the buyer protection at the earliest opportunity prior to the Buyer Protection deadline.
- Ensure the relevant contact details for confirmation are on the Buyer Protection.
- Expect a confirmation of acceptance email from the seller within 2 business hours of issuing the Buyer Protection.
- If the buyer does not have an existing Asset Servicing relationship with the seller they should contact the seller by telephone to establish appropriate contact details. An internet search can usually establish the company's main office line and key words such as 'Operations Department', 'Asset Servicing Department', 'Corporate Actions Department' can usually ensure connection with the appropriate person(s).
- If a confirmation email has not been received from the seller after 2 business hours, re-contact the seller by telephone to confirm receipt.

The **seller** should;

- Send a confirmation of acceptance email to the Buyer within 2 business hours.
- If the outturn is cash confirm when it would expect to release payment.
- If the outturn is securities, confirm the particulars of the new booking and when it will be effected.

Question 22: Is there a centralised repository for storing contact details that can be used for Buyer Protection?

Answer: There are no plans for the Corporate Joint Working Group to provide a centralised repository of contact information. However, we encourage local market implementation groups to assess the demand locally and, where required, collate and provide this information on the CSD website.

Question 23: If we have multiple transactions with the same counterparty, should we issue 1 Buyer Protection containing all transactions or one per transaction?

Answer: This is really up to the discretion of the buyer and there is no formal guidance on this matter from the Corporate Actions Joint working group. There are instances where either scenario may be preferable and items to consider prior to issuing one or many could be;

- Whether one transaction has a significantly higher value than the others.
- Whether a partial is anticipated on one or more transaction.
- Whether there are split and non-split elections at a transactional level.

Irrespective of which option is chosen good market practise will be to ensure confirmation of each Buyer Protection issued.