

APAC CA WG Meeting Minutes – 10th December 2013

Time: 2 – 3pm SGT

Attendees:

Ken Lim	Bank of America – Merrill Lynch
Cheryl Ma	Citi
Cherine Yeo	Deutsche Bank
Girish Pandit	Deutsche Bank
Prashant	Information Mosaic
Ankush Zutshi	Information Mosaic
Vikas Sahni	Information Mosaic
Mai Le	JP Morgan
Ryo Takahashi	Morgan Stanley
Andreas Rudorfer	Smartstream
Chueh Jyi-chen	Standard Chartered
John Soo	Standard Chartered
Harry Rana	Sungard
Janardhan Yalapalli	Thomson Reuters
Nithin Krishnamurthy	Thomson Reuters
Magdalene Goh	SWIFT
Mireia Guisado-Parra	SWIFT
Alexandre Kech	SWIFT

1. RHTS/RHDI/EXRI Versus PRIO in TW market (Follow up)

Background information:

Rights in TW are non-renounceable (not tradable) but transferrable (transferrable to other investors without any proceed exchange). In addition, there is no interim securities code/name assigned by Taiwan Stock Exchange (TSE) because TSE will only assign securities code to tradable securities. The existing issue for Taiwan is that there has been no market standard qualifier for rights issue. Currently, three qualifiers (RHTS, RHDI/EXRI and PRIO) are commonly used by custodian banks in TW but neither one can clearly present rights event in TW.

RHTS and RHDI/EXRI:

If the custodian bank intends to use “Rights Issue (RHTS)” as the Qualifier for MT564, Sequence C “An Intermediary Security” is required. Some custodian banks may use a dummy ISIN in order to meet the requirement. Issues of using dummy ISIN:

1. Different dummy ISINs assigned by custodian banks that will cause clients’ confusions.
2. Dummy ISIN may lead to wrong holding reconciliation i.e. there is no holding nor pending trade of such dummy ISIN but statement shows a line of the holding under this dummy ISIN.

PRIO:

Some custodian banks use “Priority Offer (PRIO)” as the Qualifier. However, since a rights issue in Taiwan is not a public or open offer, using PRIO is not as appropriate as using RHTS.

From the CA SMPG Johannesburg meeting:

UK has similar situation with allotment letters that are issued with an ISIN. The UK market practice is to announce RHDI with the ISIN from the allotment letter with a PRIO. Two other markets in the Americas (Brazil and Mexico) also have similar situations. From the discussion at the SMPG meeting, PRIO was recommended since in TW’s case, there are no actual rights distributed and the offer is opened to selected investors if the company was not able to raise enough capital from the pool of existing shareholders.

A number of solutions have been put up so far – 1) submitting a change request to remove the network validated rule (NVR) on the intermediate securities instrument when using RHTS, 2) creating a new CA event to suit TW’s situation, 3) using the PRIO event instead (with a modification to the definition of PRIO) or 4) using the parent share ISIN in the intermediate securities field. However, there has been no consensus on a consistent market practice.

From the APAC CA working group meeting:

Jyi-chen, who was present at the CA SMPG Johannesburg meeting, gave an update on the issue and further explained why PRIO was recommended by the SMPG. The reason why PRIO was proposed at the SMPG is because in TW, there are no actual rights distributed. If there wasn’t an intermediate security credited on the accounts in the CSD, then RHTS or RHDI/EXRI should not be used as there is no ISIN published. Cheryl, who was representing Citi TW in the call, indicated that this issue has been discussed and consulted among various parties with SWIFT in TW and PRIO was said to be wrong, hence no consensus was reached at the last TW NMPG meeting. However, Cheryl agreed that if this was the recommendation from the SMPG and if there is a valid reason for using PRIO, then this information should be provided to the TW NMPG for them to make their decision. Jyi-chen further shared that from the discussions with Karla McKenna, the representative of Citi at the Johannesburg meeting, it was

understood that the practice of using RHTS was a recommendation given to Citi in the past. However, because of the absence of rights security, even though there is a concept of rights in TW, it is actually creating more issues to the downstream investors if using the dummy ISIN. In addition, out of the 5 major custodians in TW, 3 are using PRIO today.

Mai queried if this recommendation will apply to all markets. Jyi-chen answered that this may not necessarily apply to all markets as this was discussed specifically in the case of TW. One of the reasons PRIO was suggested was that most custodians in TW are already using PRIO and also because in TW's case, there is a preference given to existing shareholders. The issuer will only turn to external investors to raise additional capital if they are not able to raise enough capital from existing shareholders. If there are similar scenarios in the other markets, then this could be a case to interpret as PRIO. What was also clear at the SMPG meeting in Johannesburg was that there was also a change request added in SR 2014 which clearly refines the definition of the RHTS event. With this new change request, there is a need to have an intermediate security in order to use RHTS. Therefore, the practice to use a DSS in the RHTS to remove the ISIN may no longer fit.

Alex enquired if there are any other examples of countries of similar scenarios. Mai responded that her concern was that we might start seeing markets deviate in how they announce non-renounceable rights when an intermediate security is not distributed as even with the change requested added in for SR 2014, institutions can still use RHD1 to distribute an intermediate security using a dummy. Mai also mentioned that what the SMPG is recommending for TW is also practiced in some other markets in the APAC region. For example, in Australia where there is an accelerated rights issue that is offered to institutional investors by a company, if the company is unable to raise all the capital needed through the institutional investors, then it will be open to the retail investors as well. This gets announced as a PRIO because there is no intermediate security distributed. However, there is still a concern that the practice of non-renounceable rights will start to vary globally.

Alex agreed and suggested that it will be interesting for the group to collectively gather market information on subjects where there is no NMPG and make an inventory of the types of distribution in APAC. Jyi-chen and Mai both agreed that it would make sense to go to NMPGs to see what the common practice is in other markets and if there are no clear common usage – particularly on non-renounceable rights issue where no intermediate security is distributed. Lastly, Jyi-chen raised up the point that the suggestion by the TW NMPG to use the parent share ISIN in the intermediate securities field wasn't an acceptable solution as this could instead create more problems to the downstream systems where there will be an incorrect crediting of parent shares as a result of the distribution of the rights.

Action:

To reach out to existing NMPGs and to regional/global custodians to get more information on the current practice and usage of non-renounceable rights issue where no intermediate security is distributed in APAC; to see if we can make it more harmonized in APAC.

Cheryl – to relay the message back to TW NMPG on the discussions made in the SMPG and APAC CA WG meetings for their further discussions.

2. Oversubscription for rights exercise MP (Follow up)

From the CA SMPG Johannesburg meeting:

Discussions at the SMPG meeting has led to the proposal to ask for a standards change by removing the term 'underlying' from the long definition for QINS in the MT565 and use QINS at all times for OVER. See QINS definition proposed change below:

QINS	Quantity of Securities Instructed	Quantity of underlying securities to which this instruction applies.
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Actions:

1. NMPGs are requested to investigate use of QREC (securities, investment funds, etc.) as sender or receiver and if it can be removed from the standard.
2. NMPGs to approve/reject the above proposal.

From the APAC CA working group meeting:

Jyi-chen commented that this solution to modify the QINS definition is a pragmatic approach as QINS is the most used in the industry and changing the definition of QINS will take the least effort in terms of adapting to the standards.

Decision:

No objection was raised in this meeting. The APAC CA WG approves the proposal to modify the QINS definition.

3. Malaysia's Stock Dividend Event where Odd Lot Entitlement is paid in cash instead of stock as initiated by the issuer company (Follow up)

From the discussion at the last meeting, consensus was to treat the odd lot sale as cash-in-lieu using CINL qualifier within the parent event.

Feedback received from Yek Ling: CINL is being used to denote fractional at the present time. The case in Malaysia is that the cash payment will/can be made for odd lot and fractional unit within a CE payment so how/where we can part this information.

From the APAC CA working group meeting:

Jyi-chen and Mai both agreed that this should be treated as cash-in-lieu. If the event is not paying odd lot entitlement but cash instead, then that should be considered as cash-in-lieu as even though it is not a fractional share, but it is a fraction of an odd lot. The odd lot sale in the Japanese market for example, there is no crediting of any odd lot, but cash instead and hence, by definition, it is cash-in-lieu.

Action:

Magdalene to liaise with Yek Ling again – to inform her of the discussion made in this meeting.

4. Treatment for Taiwan return of capital (ROC) with tax (Ken Lim, BAML)

In the past, Taiwan ROC is always tax free or without any tax. However, after 17 Aug 2012, there is some of such ROC with tax. Our vendor DTCC feeds this type of event as special dividend as opposed to return of capital. That is because most of the participant banks' systems are not able to process ROC event type with tax element. However, a custodian bank is using event type as CAPD (capital distribution) instead of DVCA (cash dividend) on their swift MT564/MT566 which creates an issue.

What is the APAC CA WG opinion and how would other custodian banks treat this? What is the general consensus for this type of event?

Example: -

Capital distribution with tax for Taiwan Mobile

ISIN:- TW0003045001

Ex-date: 08Jul2013

Record date: 09Jul2013

Distribution ratio: TWD 0.1 Per share

Payday: 26Jul2013

From the APAC CA working group meeting:

JP Morgan announces it as a CAPD as even though the vendor announces a special dividend, it is not classified as a ROC if the proceeds they are getting back are capital and not profit. Similarly for Standard Chartered, CAPD is also used. The reason is because there could be different tax treatments. In different markets, the withholding tax applicable in CAPD might be of a different rate to DVCA. The fact that the company clearly announces that this is being paid from the capital reserve rather than profit making makes using event type CAPD right. Standard Chartered also checked with their colleagues in TW and was told that this was the consensus adopted in TW. Jyi-chen added that the limitation on the vendor side coupled with the fact that most of the CAPD are not taxable hence systems were not built to take on the tax element does not justify that a capital return should be treated as a DVCA. Ryo Takahashi representing Morgan Stanley also agreed that CAPD should be used, for the same reasons mentioned by Mai and Jyi-chen that this is a capital rather than profit.

Decision:

Consensus was to treat this as a CAPD rather than DVCA.

5. Oversubscription for rights issuance event (Ken Lim, BAML)

APAC exchanges and authorities do not state or require registrars or companies to park the over subscription funds for rights issuance event to an escrow account.

Concern: if the Companies or their agents or registrars are insolvent, we would have high risk that our monies paid to them for over subscription of rights would not be claimed back since they do not ring fence it in a separate escrow account. What is the general practice and what can be done for this?

From the APAC CA working group meeting:

This is a valid concern raised and indeed it is a challenge to find a solution since the depository and paying agent primary focus is to receive the subscription money from the investors. The concept to park the funds in an escrow account needs to be discussed in various other industry forums (e.g. AGC and ASIFMA) as it is more of a lack of regulatory or business practice framework rather than a standards issue and it goes beyond the scope of the APAC CA WG.

Action:

SWIFT – to raise this concern to ASIFMA and/or AGC, to check if it is part of their scope.

6. In case of fully franked dividend, some custodians in the region repeat the dividend rate under FLFR code on top of providing a GRSS rate (Prashant, Information Mosaic)

From the APAC CA working group meeting:

In case of fully franked dividend, some custodians in the region repeat the dividend rate under FLFR code on top of providing a GRSS rate in field 92F. What is the use of FLFR as a qualifier?

Action:

This topic was raised up by Prashant in the call and Alex requested Prashant to send in an email with more information for SWIFT to investigate and to be discussed in our next APAC CA WG meeting.

Prashant - to also circulate the email to Jyi-chen for discussion with the Tax SMPG WG.

7. APAC CA WG Sub-groups

Magdalene informed the group that the response and uptake for the various sub-groups has been weak. Since the current bi-monthly conference calls with the APAC CA WG are working well, suggestion is to continue with the bi-monthly calls and the sub-groups can be set up in the future when there is a demand for it.