**Problem Statement:** SWIFT recommended that EXRI events are to be processed as CHOS

**Introduction**:

When there is a Rights Exercise (interchangeably termed as Rights Issue) event, normally the event processing will carry 2 types of distributions:

* The first distribution is the Nil-Paid Rights (based on investors’ shareholdings on Record Date or date equivalent to Record date) which is processed as CAEV//RHDI (Distribution of the Intermediate Securities). In most cases, RHDI is processed under Mandatory category (CAMV//MAND) as investors will receive the rights based on their parent holdings in the company on ‘mandatory’ basis.
* The second distribution comes later when investors wish to participate in the event and exercise their rights. This event ideally is processed as CAEV//EXRI and investors are not obliged to exercise their rights.

**Content** :

Theoretically RHDI (Refer to 1, Distribution of the Intermediate Securities) is processed as Mandatory (Refer to 2, CAMV//MAND) based on the parent holdings in the issuing company (refer to 3, ISIN of shares in the issuing company). So the Mandatory handling of this event is already addressed under RHDI and Custodians are widely adopting this SWIFT recommendation.

:23G:NEWM

:22F::CAEV//RHDI …………….**1**

:22F::CAMV//MAND…………**.2**

:98A::PREP//20180315

:25D::PROC//COMP

:16S:GENL

:16R:USECU

:35B:ISIN SG1EC70XXXXX…..**3**

FJ BENJAMIN

:16R:ACCTINFO

Example of MT564 NEWM : For a new Rights Distribution event based on ordinary shares of issuing company

To notify investors on the details of the rights exercise event, a whole new set of advices (from MT564 to MT566) will be sent to eligible investors carrying CAEV//EXRI (Refer to 1) based on ISIN of the Rights (Refer to 3).

:23G:NEWM

:22F::CAEV//EXRI……………….**1**

:22F::CAMV//VOLU…………….**2**

:98A::PREP//20180315

:25D::PROC//COMP

:16S:GENL

:16R:USECU

:35B:ISIN SG1EC70XXXXX……**3**

FJ BENJAMIN R

:16R:ACCTINFO

Example of MT564 NEWM : For a new Rights Exercise event based on Rights of issuing company

Point 2 in the example above is in question, although it is recommended for SWIFT users to use CAMV//CHOS however the usage of CHOS does not fully fit the definition of exercise of rights in some markets. Going back to the fundamental of theory of Rights Exercise, investors are normally given the flexibility to opt for the following:

a.      If holders are keen to participate in the event, clients will send their instructions and pay to relevant subscription cost.

b.     Otherwise, company may apply default which will result in rights being lapsed:

i. In most markets, when rights are marked as ‘Lapse’, the holders will not benefit / gain anything from the lapse exercise except removal of the expired rights from holders’ securities accounts.

ii. On the other hand, in few other markets, ‘Lapse’ may mean issuers will convert the lapsed rights into monetary value and the proceeds will be credited into investors’ cash account.

Below demonstrates some market practices in the Asian countries on lapse handling:

|  |  |
| --- | --- |
| **Market** | **Handling of Lapse Rights** |
| Australia | Default option is lapse. The handling varies :   1. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors 2. Some issuing companies do distribute proceeds to investors on lapsed rights |
| China | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| Indonesia | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| Malaysia | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| Philippines | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| Singapore | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| Thailand | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| Vietnam | Default option is lapse. Upon expiry, lapsed rights will be removed from investors’ accounts and will not result in any benefits / proceeds distribution to the investors |
| UK | The default option for UK Rights Issues is to Lapse except in the case of entitlements to be claimed from the market from stock loans or open market trades where the counterparty default will be to Exercise.  Most UK Rights Issues are underwritten and for rights that have not been taken up at the deadline, the underwriters will either attempt to find subscribers or take them up themselves (at the Issue Price). If the underwriter finds subscribers then the sale proceeds (after deduction of the issue price and sale expenses) will be distributed to the relevant shareholders as lapsed proceeds |

**Argument:**

1. This article questions the usage of recommended code of CHOS for EXRI events.
2. The sample from few markets above illustrate that handling of rights purely by voluntary basis i.e. investors need to send in their instructions to confirm their participation in the EXRI event and pay corresponding Subscription Fees. If Default Option applies, which in most cases would be Lapse, then the lapse rights will be removed from investors’ account and investors will not enjoy any monetary benefits.

CHOS on the other hand best fit events where holders have the obligation to receive the benefits (on mandatory basis) by their preferred distribution option (if clients send in their instructions) or by default option (if nil client instruction). A simple example would be Dividend with Options event where clients can opt for HKD or USD, and the payment of this event will result in payment of HKD (by client preference) or USD (by client preference or default) at the end of the event lifecycle.

Another example where holders have the obligation to receive the benefits would be handling of lapsed rights which will result in monetary benefit paid to investors as illustrated by Australia market practice.

1. Even more so, EXRI events are normally announced based on the Rights ISIN / Security Code which carry a whole series of MT564 – MT566, compared to RHDI events which are announced based on the ordinary shares of the issuing company. Hence the two events (RHDI and EXRI) are to be handled separately due to the event nature and do not have to be treated as ‘the whole package’ (Referring to verbal phone conversation dated 6th Aug 2018)
2. If CHOS is applicable to EXRI events where there is presence of Lapse handling, what about

Handling of other ‘Voluntary’ events which also carry Lapse handling such as CAEV//EXWA?

**Recommendation:**

With clear differences in the nature of the event handling between the two different handling of lapsed rights, SWIFT standard should give flexibility on the code for Exercise of Rights to VOLU and CHOS depending on the market practices.