

Market standards for corporate actions processing - Buyer protection

This document provides customers of Clearstream Banking with an overview of the current market standards for corporate actions, in particular on buyer protection.

In the Giovannini Reports, corporate actions processing is dealt with as Barrier 3, where, referring to the existing national differences, the operational problems are characterised by “the variety of rules, information requirements and deadlines for corporate actions. These differences may require specialised local knowledge or the lodgement of physical documents locally, and so inhibit the centralisation of securities settlement.”

Corporate actions processing is deemed one of the most complex areas of post trading. Standardising these processes across all European markets, and possibly beyond, aims at achieving a significant reduction of respective costs and operational risks. To dismantle Giovannini Barrier 3, investments may be required in order to become compliant with the standards on corporate actions processing. However, upon implementation of the standards, the European securities market and its users will benefit from cost savings resulting from harmonising the processes cross border.

Individual work of associations contributing to the dismantling of Giovannini Barrier 3 was replaced in summer 2007 by the setup of the Corporate Actions Joint Working Group (CAJWG) that encompasses the main relevant constituencies, that is issuers, market infrastructures and intermediaries. The CAJWG’s objective has been to develop a comprehensive set of market standards for the operational processing of all categories of corporate actions¹ including transaction management.

This document contains the standards developed by the CAJWG, reviewed in the first quarter 2009 in consideration of the responses to the market consultation of the fourth quarter 2008 and endorsed by the involved associations: European Issuers, European Central Securities Depositories Association (ECSDA), European Association of Clearing Houses (EACH), Federation of European Securities Exchanges (FESE), European Banking Federation (EBF), European Association of Cooperative Banks (EACB), European Savings Banks Group (ESBG), European Securities Services Forum (ESSF/SIFMA).

The CAJWG has agreed on basic principles whereby the standards should be based on work already performed and should reflect future best market practices (rather than solutions currently applied in most markets) that, once implemented, should dismantle the operational part of Barrier 3 as concerns the categories of corporate actions addressed.

The market standards cover the following categories of corporate actions (rather than individual event types) as well as transaction management:

- Distributions:
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 - Cash distributions (for example cash dividend, interest payment);
 - Securities distributions (for example stock dividend, bonus issue);
 - Distributions with options (for example optional dividend).
- Reorganisations:

¹ Except for general meetings that is the subject of the Joint Working Group on General Meetings

- Mandatory reorganisations with options (for example conversion);
- Mandatory reorganisations (for example stock split, redemption);
- Voluntary reorganisations (for example tender offer).
- Transaction management:
 - Market claims (distributions);
 - Transformations (reorganisations);
 - Buyer protection (elective corporate actions);

The scope of application of the market standards includes:

- All types of the above categories of corporate actions (distributions and reorganisations);
- All securities used for direct investments (equities, fixed income instruments) deposited and settled in book-entry form with an (I)CSD in Europe; investment funds listed and traded on a regulated trading venue should be processed, where possible, in accordance with the applicable standards hereof;
- All parties involved, that is issuers, market infrastructures (trading, clearing and settlement), intermediaries and end investors, except for standards for transaction management which are directed at market infrastructures and Intermediaries only.

The **subject matter** of the standards concerns:

- The information flow throughout the chain of relevant parties;
- Key dates and their sequence;
- The operational processing of corporate actions.

Important note: Within the standards, entitlements are determined from the actual settled positions in the issuer (I)CSD's books on Record Date, whereas intermediaries may calculate on a contractual settlement basis on Ex Date.

The CAJWG acknowledges that there are other means of warranting buyer protection than an institutionalised and automated service provided by market infrastructure organisations, for example a bi-lateral agreement between the respective trading parties by means of a manual process.

The German market has decided not to introduce an automated buyer protection infrastructure. Instead the buyer protection will be handled bilaterally in Germany: As a result, only the market participants need to comply with T2S corporate action standards on manual buyer protection (BP). The CSD does not need to make any system changes in relation to **BP** since the exchange of BP instructions takes place bilaterally between the counterparties, that is outside the CSD environment.

Manual buyer protection

Extract from the CAJWG Market Standards for Corporate Actions Processing

Creation

13. A Buyer Protection instruction should be created by the buyer if the requested option is not the default option, referencing the Corporate Action, the chosen option(s), the quantity of securities and the Underlying Transaction in line with the template attached hereto.
14. The Buyer Protection instruction should be communicated from the buyer to the seller electronically using the template attached hereto or an ISO message once available.

Processing

15. The Buyer Protection Deadline should follow the Guaranteed Participation Date by a Settlement Cycle. The creation of a Buyer Protection instruction is possible until close of settlement of the date of the Buyer Protection Deadline. Buyer Protection instructions allocated by a CCP against a seller are allowed until close of settlement of the date of the Buyer Protection Deadline plus one hour.
Each market should issue Buyer Protection Guidelines that include the settlement schedule of the respective (I)CSD and related Buyer Protection Deadlines and Market Deadlines.
16. The Buyer Protection Deadline should be at least one Business Day before the Market Deadline.
17. Any Buyer Protection instruction by the buyer prior to the Buyer Protection Deadline and related to a Transaction for which the trade date is on or before the Guaranteed Participation Date, with intended settlement date no later than the Buyer Protection Deadline, should be accepted.
18. Standard 17 above should apply also in case of Buyer Protection instructions against CCPs.
19. Buyer Protection Deadlines for the same event should be identical across (I)CSDs in Europe.
20. In regard of any Buyer Protection instruction by the buyer prior to the Buyer Protection Deadline, settlement of the Underlying Transaction should be allowed until the Buyer Protection Deadline.
21. A Buyer Protection instruction issued on a Pending Transaction that finally settles on or before the Buyer Protection Deadline (end of settlement process) should be void.
22. Transactions attached with a valid Buyer Protection that are still pending on the Buyer Protection Deadline should be cancelled by both the buyer and the seller and reinstructed according to the choice of the buyer to prevent settlement after the Buyer Protection Deadline or their Transformation into the default option.
23. The Transformation of the Underlying Transaction should be carried out, in accordance with the Buyer Protection instruction, on the Market Deadline/Record Date of the concerned Elective Corporate Action.
24. For Mandatory Reorganisations with Options, non-elected Transactions should transform into the default option set by the Issuer (I)CSD.

Buyer protection in the context of TARGET2-Securities (T2S)

The T2S Corporate Actions Standards (CASG Standards) have been endorsed by the T2S Advisory Group (AG) and are addressed to all CSDs and National Central Banks (NCBs) in T2S and to their users, including central counterparties (CCPs).

The T2S Corporate Actions Standards - Buyer Protection are available on the [ECB website](#).

All CSDs and their users, including the CCPs, should abide by these standards for all activity on T2S and from the first day of such activity on T2S. CSDs and their users including CCPs should have already implemented these standards prior to the start of T2S user testing, in accordance with the relevant synchronisation point in the T2S Programme Plan.

The goal of the European community is that all European CSDs will, where applicable, abide by these standards for non-T2S settlement, so that a single harmonised European process be achieved.

T2S Corporate Actions Standards – Buyer protection

The AG mandated the T2S Corporate Actions Subgroup (CASG) to support and monitor implementation of the standards.

Comments of the CASG

The standards of the CAJWG and the CASG are based on a functional approach to buyer protection processing. The standards have been drawn up as best T2S market practices with the aim of introducing harmonisation in cross-CSD settlement in T2S.

The CASG gap analysis aims at identifying any potential barriers (legal, regulatory, operational or fiscal) for their timely implementation (prior to T2S testing) by T2S markets.

The T2S CA standards are based on the Standards of the CESAME2 mandated Corporate Actions Joint Working Group (CAJWG) that is, the market standards for corporate actions. These market standards have been endorsed by all relevant industry associations (July 2009). These same associations are using a revised version of the market standards (2012).

The standards are built on the principle that it is possible to distinguish functionally between the processing related to a corporate action on stocks or holdings (for example, the distribution of a cash dividend to record date holders) and the processing related to a corporate action on flows (for example, the generation and processing of a market claim).

The CA standards are valid for all transactions on T2S (that is both for transactions between two participants of the same CSD as well as for cross-CSD settlement).

In line with the market standards, cash payments which are the result of corporate action events should be paid via the same “payment mechanism” as any standard DVP activity. In the T2S context this means that the T2S currency cash entitlements which are the result of corporate actions should be paid via the T2S Dedicated Cash Accounts (DCAs) and not outside of the CSD/T2S environment.

The standards take as working assumptions the T2S functionalities as reflected in the [T2S User Requirements Document \(URD\) v5.02](#).

Definitions

In line with market standards for corporate actions, buyer protection (BP) is a process whereby a buyer who has yet to receive the underlying securities of an elective corporate action, instructs the seller in order to receive the outturn of his choice.

Automated buyer protection mechanism: an institutionalised and automated service provided by market infrastructure organisations (that is, where the election instruction is routed through the CSD/CCP, and where the CSD/CCP uses the BP instruction to process the transformation)

Manual buyer protection mechanism: a bi-lateral agreement between the respective trading parties by means of a manual process (no intervention from the market infrastructure regarding the exchange of BP instructions)

BP invocation

The BP deadline is invoked on “the last date and time at which a ‘buying counterparty’ that has the legal right to choose a particular event option but does not yet hold the securities (that is a party in an unsettled transaction) may instruct its counterparty to deliver the specified proceed/s”. The standards presented below provide more clarification of how the reference to “the last date and time” is defined.

Scope of BP standards

These BP standards should be applied only on matched and pending transactions.

They are applicable to automated BP services provided by CSDs as well as to the manual buyer protection regimes.

If the Issuer CSD offers automated BP services, then all Investor CSDs involved in the underlying transaction should offer BP services for pending transactions on securities issued in the Issuer CSD. The investor CSD(s) do not necessarily need to implement an automated BP service, but can also offer a manual BP service, as long as this complies with the T2S standards and issuer CSD’s timelines.

If both Investor CSDs offer automated BP services, all securities transactions between their participants can be subject to BP, including transactions in securities for which the issuer CSD does not provide BP.

Location of BP processing

BP instructions and requirements thereof are detected, generated and communicated between the buyer and the seller, outside T2S' operational framework. In case of automated BP, the BP instructions are communicated between buyer and seller through and up to the chain of intermediaries, including the CSDs. Only the potential resulting settlement (securities or cash) of the BP agreement, also referred to in this document as protected entitlements, is processed in T2S.

BP cross-CSD

In line with the CA market standards (CAJWG), the T2S CA standards do not impose that all T2S markets should implement an automated BP functionality. The AG has left the choice of implementing an automated BP functionality to each Issuer CSD. In addition, the AG fully supports the market CA standards on BP, including the requirement that when automated BP is in place, it should be done according to the agreed market standards.

This situation, this is potentially not all CSDs offering an automated BP functionality, leads to the following scenarios:

- If the Instruction Owner CSD (IOC) offers a BP service, it will handle the execution of the BP, that is take the actions on the underlying transaction (hold/ cancellation/transformation): These actions will be generated automatically by the IOC on behalf of its buyer/seller involved in the BP.
- If the IOC does not offer a BP service, the cancellation, transformation are carried out by the buyer/seller of the IOC. The objectives being that bilateral cancellation is successfully processed followed by the matching and settlement of the new transformed instructions.

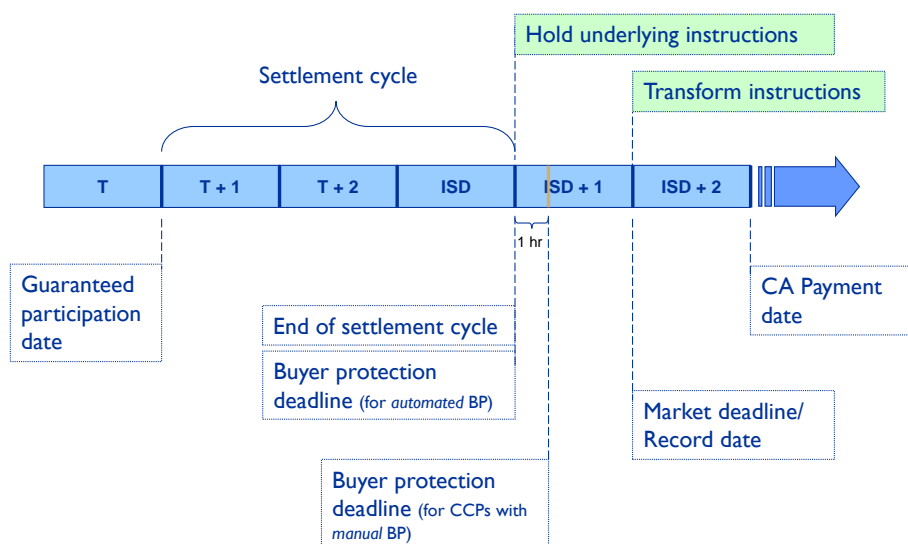


Diagram 1 – Buyer Protection Time-frame – CASG

To comply with the CAJWG standards 13 and 14 German market participants must use the buyer protection invocation (BPI) template which is available together with this document on the Clearstream website www.clearstream.com under Products and Services / Asset services / Corporate actions Corporate actions CSD Frankfurt.

The German market is planning to use the data provider Wertpapier-Mitteilungen as central source to provide and publish buyer protection key data.