

## **6. EXERCISE CRITERIA, EXERCISE AND ASSIGNMENT**

The Exercise function allows a SEOCH Participant to exercise its or its client's right as an option holder to buy or sell the underlying shares, according to the terms of the OCH Contract.

Exercise requests for OCH Contracts can be input via DCASS at any time prior to the System Input Cutoff Time on any Business Day, including the last trading day on which the option trades. It is also possible to purchase an option and exercise it on the same day. Exercise requests can be input during the day but the actual assignment process will only be performed after the System Input Cutoff Time.

SEOCH Participants can prescribe their own in-the-money exercise criteria, i.e. the difference between the strike and fixing price as a percentage of the strike or a fixed amount, via DCASS at any time prior to the close of trading on any Business Day. Acceptance of such exercise criteria by SEOCH will be at the discretion of SEOCH and subject to such conditions and limits as SEOCH may from time to time specify. SEOCH Participants shall prescribe their exercise criteria by account and instrument type. Once setup in DCASS, such exercise criteria will override SEOCH's prescribed exercise criteria and take effect immediately. SEOCH Participants should review their prescribed exercise criteria and make necessary adjustments from time to time.

### **6.1 No Automatic Exercise Except on Expiry**

A SEOCH Participant shall input its exercise requests through DCASS in respect of each and every OCH Contract it wishes to exercise. DCASS will not automatically generate exercise requests in respect of in-the-money expiring contracts on behalf of SEOCH Participants except on an expiry day.

On an expiry day, DCASS will automatically generate exercise requests in respect of each and every open long position in expiring contracts which meets the exercise criterion, prescribed (i) by the relevant SEOCH Participant; or (ii) if no such exercise criterion is prescribed by the SEOCH Participant, by SEOCH. A report showing only those expiring contracts which are expired and to be exercised automatically based on SEOCH's prescribed criteria will be available shortly after the close of the underlying market on each Business Day. SEOCH Participants shall enquire via DCASS for a complete list of automatically generated exercise requests, including those generated based on the exercise criteria prescribed by themselves. SEOCH Participants may elect to deny any automatically generated exercise requests for positions in any particular series at any time prior to the System Input Cutoff Time on the expiry day (see 6.1.3). For the purposes of the Clearing Rules and these Procedures, exercise requests automatically generated by DCASS, if not so denied, are deemed as exercise requests input by SEOCH Participants and shall be binding and irrevocable.

Exercise requests will not be automatically generated by DCASS for those expiring contracts which do not meet the exercise criterion prescribed (i) by the relevant SEOCH Participant; or (ii) by SEOCH as aforesaid. SEOCH Participants shall exercise such contracts by input of exercise requests themselves via DCASS (see 6.1.1).

SEOCH will determine the in-the-money percentage criteria for automatic generation of exercise requests for expiring contracts in its absolute discretion from time to time and inform SEOCH Participants of such in-the-money percentage.

The in-the-money criterion is the difference between the strike and fixing price as a percentage of the strike or a fixed amount. For this purpose, the fixing price of the underlying stock will be determined by SEOCH at its absolute discretion and, under normal circumstances, it will be the closing price quoted on the Exchange of the underlying stock on the expiry day.

The automatic exercise feature of expiring contracts described above will be applicable on any expiry day which is a Business Day.

#### **6.1.1 Input of Exercise Requests**

Open long positions can be exercised regardless of whether they are in-the-money, at-the-money or out-of-the-money.

SEOCH Participants can input exercise requests for their open long positions via DCASS. Once input in DCASS, the exercise requests will be at pending state until the actual assignment process is performed after the System Input Cutoff Time on the same day. SEOCH Participants can view and reject their pending exercise requests via DCASS before the System Input Cutoff Time on the same day.

### **6.1.2 Amendment of Exercise Requests**

Amendment of exercise requests is only possible on the same day that the request was entered, up to the System Input Cutoff Time. After the System Input Cutoff Time, all exercise requests entered for the day will become final and irrevocable. DCASS will exercise all available long open positions in a particular series if the number of open long positions is equal to or smaller than the requested quantity.

To make an adjustment, a SEOCH Participant will have to reject the original exercise request and input a new exercise request for the correct account, series and quantity. Please refer to the *DCASS User Guide* for details.

### **6.1.3 Denying Exercise Requests Automatically Generated by DCASS**

SEOCH Participants may deny exercise requests automatically generated by DCASS for any expiring contracts by specifying the quantity of contracts which should not participate in the automatic exercise via DCASS at any time prior to the System Input Cutoff Time on the expiry day. SEOCH Participants can enquire about the result of their denial of automatically generated exercise requests and obtain the report for all positions exercised or assigned which is generated by DCASS.

### **6.1.4 On Behalf Exercise/Exercise Adjustment/Denying Automatic Exercise Requests by SEOCH**

Normally, SEOCH Participants should input their exercise requests, reject pending exercise requests or deny automatically generated exercise requests via DCASS. However, under certain circumstances such as power or equipment failure, a SEOCH Participant may request SEOCH to input such instructions on their behalf. For details, please refer to 17.2.

## **6.2 Assignment**

Each day after the System Input Cutoff Time, all exercise requests recorded during the day will be allocated across open contracts by a random process in DCASS.

### **6.2.1 Assignment Mechanism**

The random assignment process works by first locating all short positions in the series and arranging them in a list. The exercise routine selects the short positions by selecting a short contract randomly from the applicable list of short positions as a starting position and allocating a fixed number of exercised contracts down the list from that position until the allocation of that fixed number of exercise contracts has been completed. If exercise contracts remain to be allocated after going down the list, this process (draw short contract and allocate) is repeated until the allocation of all exercise requests has been completed.

It is possible that a SEOCH Participant will be assigned against series that it has exercised itself or on behalf of its clients. These are termed internally assigned contracts. Internal assignment can be mapped across various Position Accounts of the SEOCH Participant.

Stock transactions resulting from internal assignment will be reported and settled in the same manner as those assigned to other SEOCH Participants.

After assignment by DCASS, SEOCH Participants must perform a random assignment of their clients' positions, through their back office systems.

### **6.2.2 Assignment Notice**

Once assigned, the relevant SEOCH Participant is required to deliver or buy the underlying securities depending on whether the assigned position is a call or a put. On the evening of the day of exercise, following completion of the assignment process, SEOCH will notify SEOCH Participants of the results of exercise and assignment by means of a DCASS report. SEOCH Participants can also enquire about the results of exercise and assignment via DCASS after completion of the day end processing.

