

## **V. SPECIAL EVENTS**

### **14. CAPITAL ADJUSTMENTS**

When there is a change in the capital structure or composition of the issuer of the underlying securities of an option class or in any other exceptional circumstances, the Exchange may make adjustments to the terms of the option contracts which are currently traded in accordance with the *Operational Trading Procedures*. The required changes will be executed in DCASS. The Exchange and SEOCH generally refer to the processes surrounding this as “capital adjustments”.

#### **14.1 Circumstances Which May Give Rise to Capital Adjustment**

Please refer to the Operational Trading Procedures for the types of events in which the Exchange will make standard adjustments to the terms of the options contract and the standard adjustment methodology that will be adopted.

Special events like offering of shares in another company and change of domicile are not common entitlement or corporate events and standard adjustments may not be applicable. Under such circumstances, the Exchange, in consultation with SEOCH and the Commission, will decide on a case by case basis whether an adjustment is needed, and if so, the adjustment method.

**14.1.1** Repealed

**14.1.2** Repealed

**14.2** Repealed

**14.2.1** Repealed

**14.2.2** Repealed

**14.3** Repealed

#### **14.4 Capital Adjustment Process Conducted by SEOCH**

For entitlement events, the capital adjustment process will normally be conducted by SEOCH on the night of the last day the share is traded cum-entitlement, which is also two settlement days prior to CCASS entitlement processing. Pending stock positions arising from exercise / assignment of existing options contracts on or before capital adjustment day of SEOCH will normally be settled in CCASS on or before the day immediately prior to the book-close day. Hence, the relevant SEOCH Participant will receive its entitlement via CCASS pursuant to the *HKSCC Operational Procedures*.

The capital adjustment process conducted by SEOCH for mergers (with share exchange, whether or not with cash offer), stock splits and consolidations will occur on the night before the corporate action effective date announced by the issuer of the underlying securities, which is also the last trading day in the old shares. Pending stock positions arising from exercise / assignment of existing options contracts on or before the capital adjustment day of SEOCH will undergo corporate action adjustment in CCASS pursuant to the *HKSCC Operational Procedures*.

For mergers (with cash offer only) and privatisations, all existing options contracts will be cash settled based on the share offer price / cancellation price immediately after the last day of dealing on the options contracts as announced by the Exchange.

14.4.1 Repealed

14.4.2 Repealed

## **14.5 Effect of Capital Adjustment**

The following describes how existing contract terms, open options positions, pending stock positions, stock collateral are normally being treated under the capital adjustment process of SEOCH.

### **14.5.1 Adjustment of Contract Terms for Existing Options Contracts**

Using the adjustment ratio, the exercise prices and contract sizes of all existing option contracts are adjusted. As a result of rounding, the adjusted contract size result in odd lots as well as fractional shares upon exercise. Particulars of adjusted series are shown in a report generated by DCASS. SEOCH Participants can also enquire about the adjusted contract sizes via DCASS.

While the adjusted series can still be traded, new standard series may be introduced in accordance with the standard procedures for issuing new series. Therefore, in that option class, there may be some series whose contract sizes and strike prices are standard and there may be others whose contract sizes and strike prices are adjusted. While standard series will continue to be traded in HKATS and cleared in DCASS under the original class code specified in the *Operational Trading Procedures*, a new class code will be assigned for adjusted series for trading in HKATS and clearing in DCASS.

### **14.5.2 Open Options Positions**

The number of open positions in the old series will be transferred to the respective adjusted series. It should be noted that only the exercise price and contract size are being adjusted and there will not be any changes to the number of open positions whatsoever after the adjustment. Open positions in adjusted series can be enquired via DCASS. All such open contracts will be traded and if exercised, will be settled under the adjusted contract terms of adjusted exercise price and adjusted contract size per contract from effective day onwards. As the adjusted series and newly generated series are of different contract terms, there will not be any offsetting between them in respect of options positions or exercise and assignment.

14.5.2.1 Repealed

14.5.2.2 Repealed

14.5.2.3 Repealed

### **14.5.3 Pending Stock Positions**

Pursuant to HKSCC Operational Procedures, the CCASS conversion cycles will handle the necessary processing with regard to adjustments on pending stock positions resulting from exercise of options contracts on or before the capital adjustment day, SEOCH will not make adjustments to such pending stock positions.

### **14.5.4 Collateral Held By SEOCH in CCMS During Capital Adjustment**

For entitlement events, although the securities collateral of a SEOCH Participant are recorded in its CCMS Collateral Account designated for SEOCH collateral purpose, the entitlements based on the quantity of the underlying securities designated for SEOCH collateral purpose will be handled by

CCASS. Any cash entitlement amount, after deducting any necessary CCASS charges, and any stock dividends or bonus shares will be credited to the sub-account of the money ledger and stock accounts in CCASS maintained by that SEOCH Participant or the CCASS GCP, where applicable.

In case of a capital adjustment, the shares used for covering short call positions will be de-covered automatically on the evening on which the capital adjustment is processed. However, margin calculation will not be affected as it occurs before the de-covering action in the day end processing of the Business Day on which the capital adjustment process is conducted. SEOCH Participants should re-input cover call requests via DCASS to cover their short call positions again on the Business Day immediately following the capital adjustment to minimise the margin requirement. Any naked short call positions for which SEOCH Participants have not entered any cover call requests will be subject to intra-day and day end margin calls.

#### **14.5.5 Exercise of Adjusted Options Series**

Exercise of adjusted options series may result in settlement of odd lots and/or fractional shares. The fractional shares of each adjusted options contract exercised will be settled in cash while the odd lots will be settled by physical delivery. Please refer to 8.10.

**14.6** Repealed

**14.6.1** Repealed

**14.6.2** Repealed

**14.6.3** Repealed

**14.6.4** Repealed

**14.6.5** Repealed

**14.6.5.1** Repealed

**14.6.6** Repealed