







## **The Markets in Financial Instruments Directive - Implementation at the institutional level in the Nordic Region**



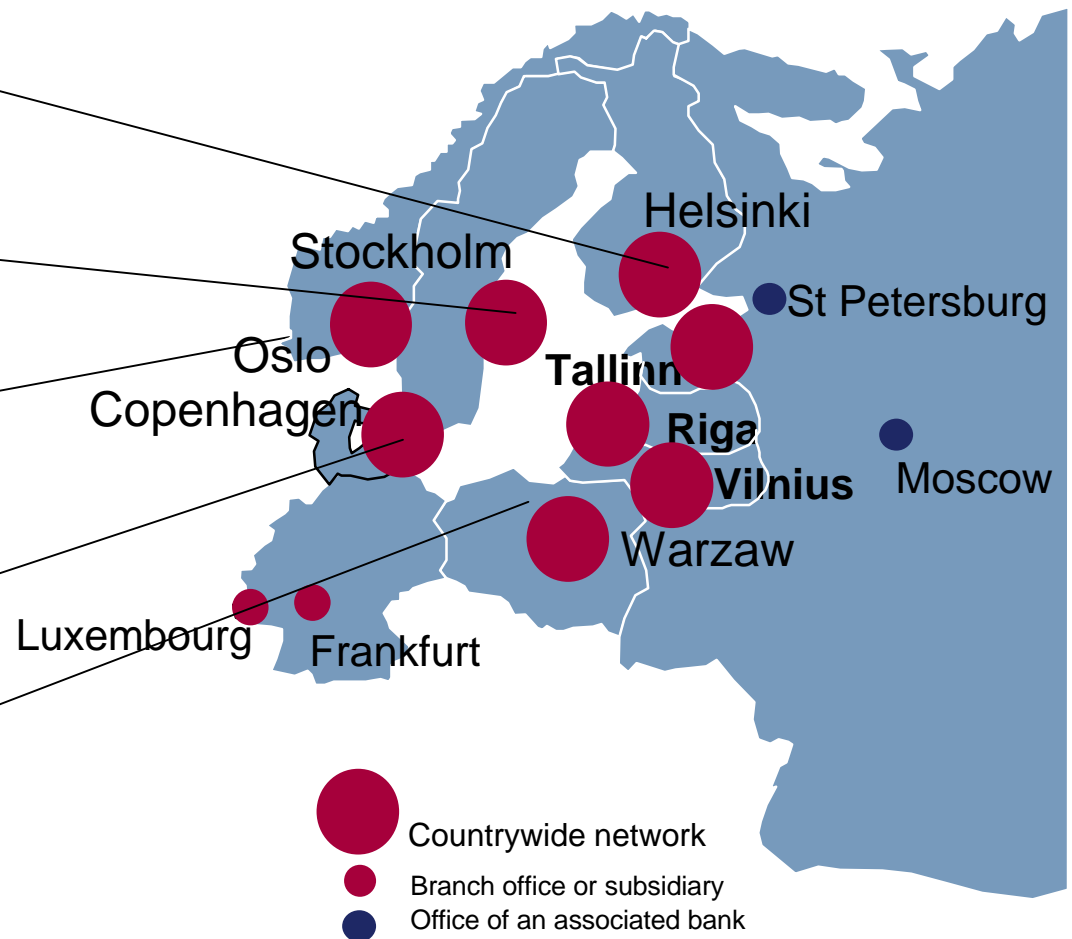
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**NCMF June 12th 2006**

- 11 millions customers whereof 4,4 millions are also e-customers
- operating through three business areas: Retail Banking, Corporate and Institutional Banking and Asset Management & Life
- 1,160 bank branches - 28,800 employees (FTEs)

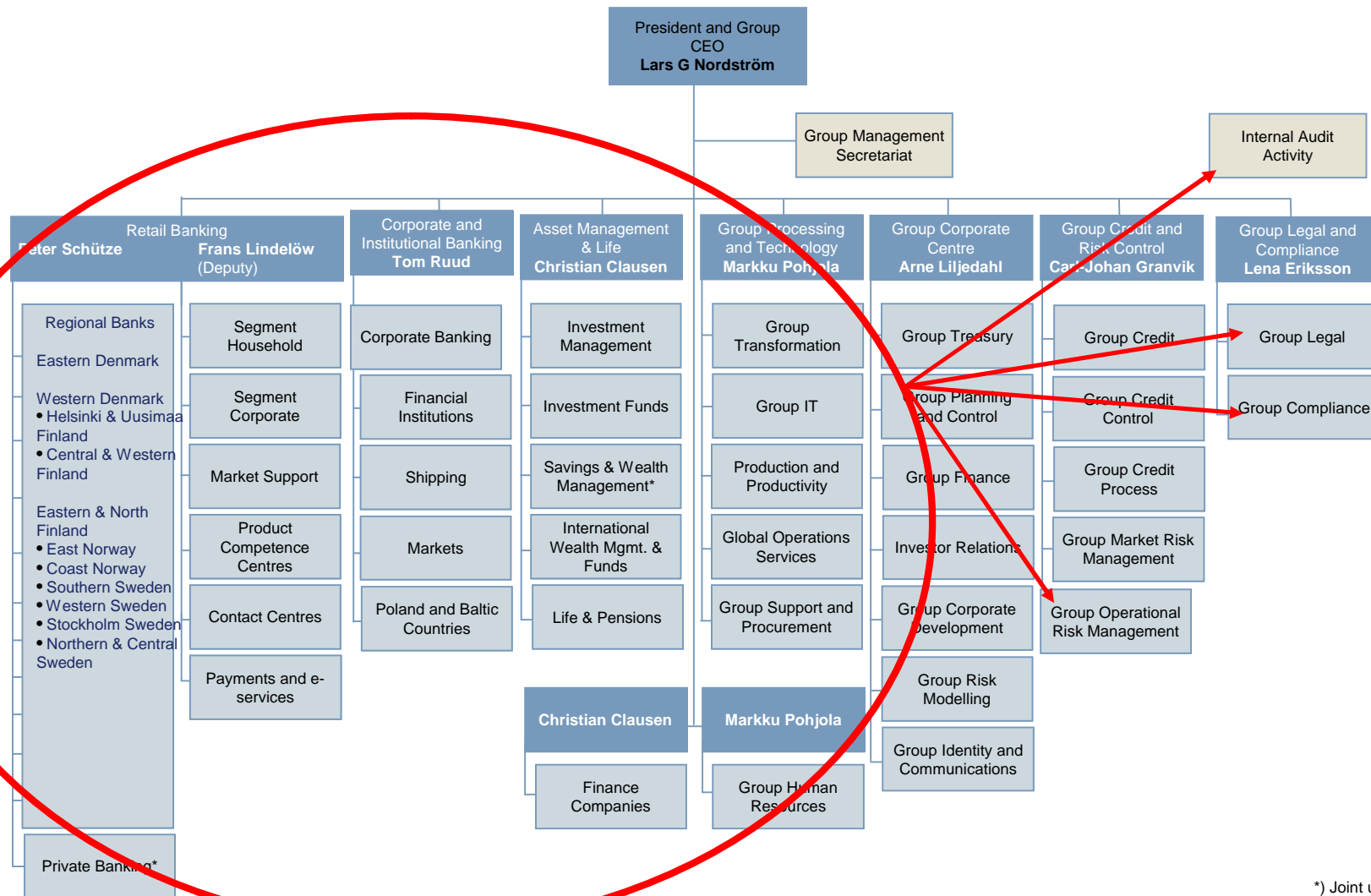
	 DK	 FI	 NO	 SE	Baltic Sea Region	Total
<i>Banking customers (1,000)</i>						
Personal customers	1,590	2,980	620	3,860	340	9,390
Corporate customers	72	333	72	437	45	960
Life insurance customers (1,000)	638	343	304	460	65	1,810
E-banking customers (1,000)	727	1,300	327	1,704	90	4,148

# The largest financial institution in the Nordic and Baltic Sea region

	Finland		
	Branch offices	376	
	Personnel	8,281	
	Sweden		
	Branch offices	249	
	Personnel	7,146	
	Norway		
	Branch offices	125	
	Personnel	3,406	
	Denmark		
	Branch offices	344	
	Personnel	8,445	
	Poland and Baltic		
	Branches/salepoints	64	
	Personnel	1,546	
	Total locations	1,158	
	Total personnel (FTEs)	28,824	



## Group structure



# Content

- 1. MiFID - Why and when**
- 2. Challenges**
- 3. Conduct of Business**
  - **Client Classification**
  - **Suitability / Appropriateness / Execution only**
  - **Best Execution**

# 1. Why and when

## Why MiFID?

- **Ensure investment companies may operate all over EU with home state license.**
- **Harmonise the organisational requirements for investment companies.**
- **Ensure high level of client protection within the whole EU – strict conduct of business rules, requirements to manage conflicts of interest, provide best execution to clients.**
- **Cover a wide range of investment services and financial instruments.**
- **Set standards for order execution platforms – regulated markets, multilateral trading facilities (MTF, alternative trading facility) and internalising.**
- **Ensure high transparency on the depth of the liquidity in securities.**
- **Strengthen the co-operation between Supervising Authorities.**

## **EU Level**

- **The Directive on Markets in Financial Instruments 2004/39/EY “MiFID”, previously known as the Investment Services Directive, was adopted 21 April 2004.**
- **Commission is authorised to give Level 2 ruling in 18 articles**
- **Commission has given proposal for one directive and one regulation – estimated to be in place in August / September 2006 / Latest ESC drafts 2.6.2006**
- **The national legislation must be in place by 31 January 2007 and the implementation finalised by 31 October 2007**
- **Vote in ECON committee 30 May / Vote in Plenary June/July?**
- **Adoption and approval by ESC and EP July?**
- **Time schedule for local authorities is open / Level 3 still open**

## Nordic implementation

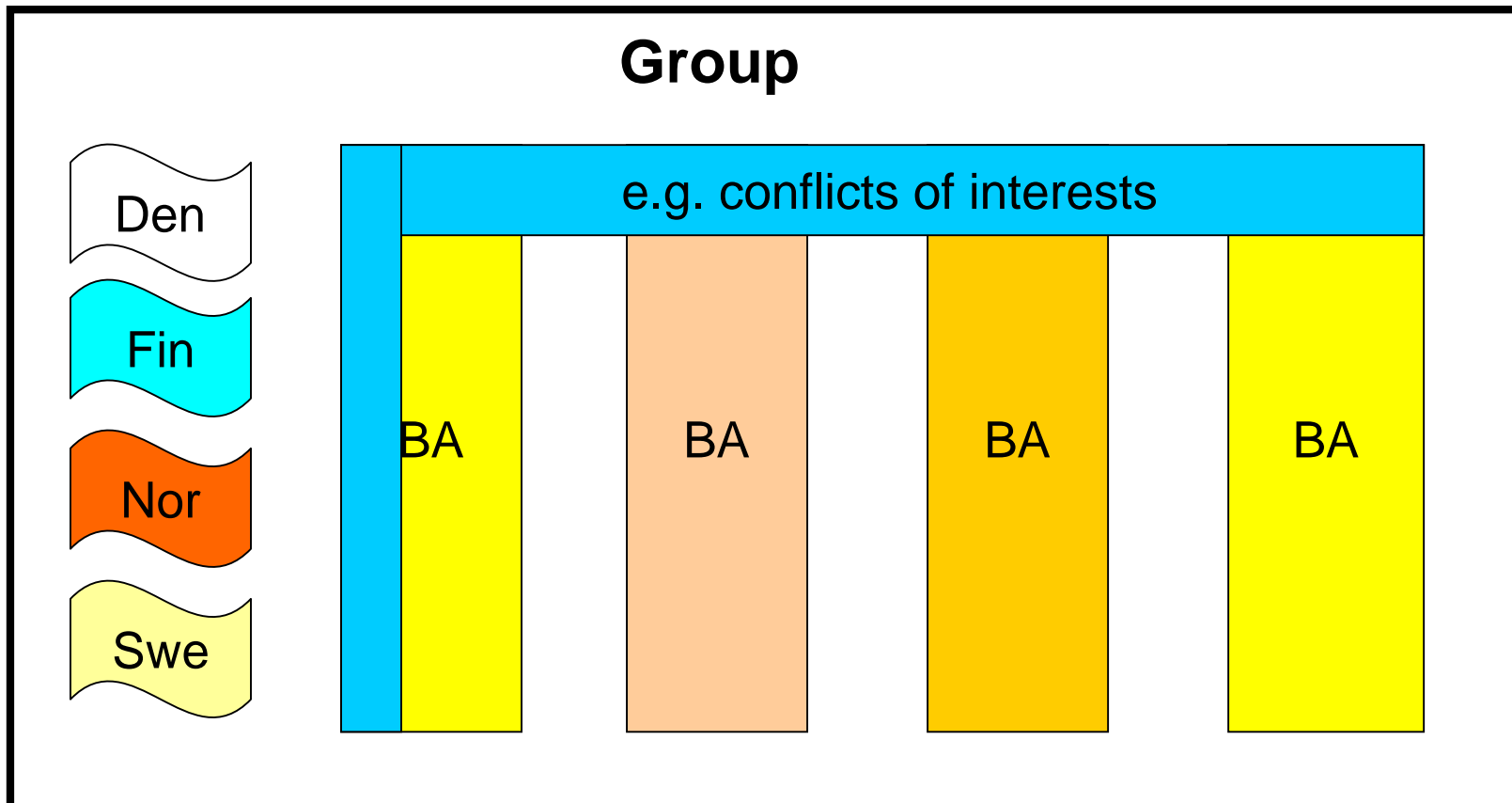
- **Denmark** - proposal for a government bill is expected before summer (unofficial version given June 2nd). Time table for legislation will be held - legislation in place 1 February and in force 1 November 2007.
- **Finland** - proposal for a government bill expected by July 2006, legislation may not be in place in February (probably July 2007). Legislation in force 1 November 2007.
- **Norway** - the Committee report on MiFID has been published in February. Proposal for a government bill expected in November and legislation in place in spring (?) 2007. Legislation in force 1 November 2007.
- **Sweden** - the Committee report on MiFID has been published in April (last part to be published in July). Proposal for a government bill expected in November and legislation in place in February (?) 2007. FSA work parallel. Legislation in force 1 November 2007.
- **Co-operation between Nordic Industry Associations**

## **Nordea expectations**

- **To be very costly**
- **To change the way stock exchanges and other markets operate**
- **Cause a migration of professional players towards Multilateral Trading Facilities**
- **To change the way information is distributed due to a change in transparency requirements and to allow transaction disclosure using proprietary arrangements or a third party.**
- **No “gold plating” in form of additional rules on organisational, transparency or reporting requirements.**
- **Give flexibility in a form of customers’ choice of protection level, best execution determination based on the need of individual customers’ or customers’ instruction or that the information given to customers must not be excessively detailed.**

## 2. Challenges

# Implementation challenges



## **Nordea will focus on**

- ✓ **Scope and definitions (Art. 1-4)**
- ✓ **Home state principal (Art. 31 and 32)**
- ✓ **Organisational requirements (Art. 13 and 18)**
- ✓ **Client Handling (Art. 19, appendix 2)**
- ✓ **Execution (Art. 21 and 22.1)**
- ✓ **Market Transparency & Internalisation (Art. 27 and 29)**
- ✓ **Trade reporting to authorities ( Art. 25 and 58)**

**and other new issues/changes in MiFID**

Compliance

Risk management

Internal audit

General requirement: double functions not compromise performance

Always

Policies methods

Independent Compliance function

Policies methods

Mechanisms for Internal control

Compliance officer

Appropriate

C O not take part in business supervised  
Remuneration not compromise

Risk management function which functions independently

Internal audit function which is separate and independent from other activities

- **Even more policies and procedures?**
- **Personal account dealing instructions - new employees restricted?**
- **Additional requirements for managing conflict of interests / Can Nordic countries require Col policies to set out only the general nature and sources of conflicts of interest detrimental to customers?**
- **Record keeping procedures - heavy burden for IT**
- **Identifying and assessment of all outsourcing arrangements**
- **Assessment of current custody arrangements**
- **Freedom to organise the activities and risk control functions in a way that fits the best for each investment firm.**

## 3. Conduct of Business

## Client classification

Non-professional clients

Professional clients

Eligible counterparties

## Client classification

Protections afforded by  
conduct of business rules  
apply however different  
extent:

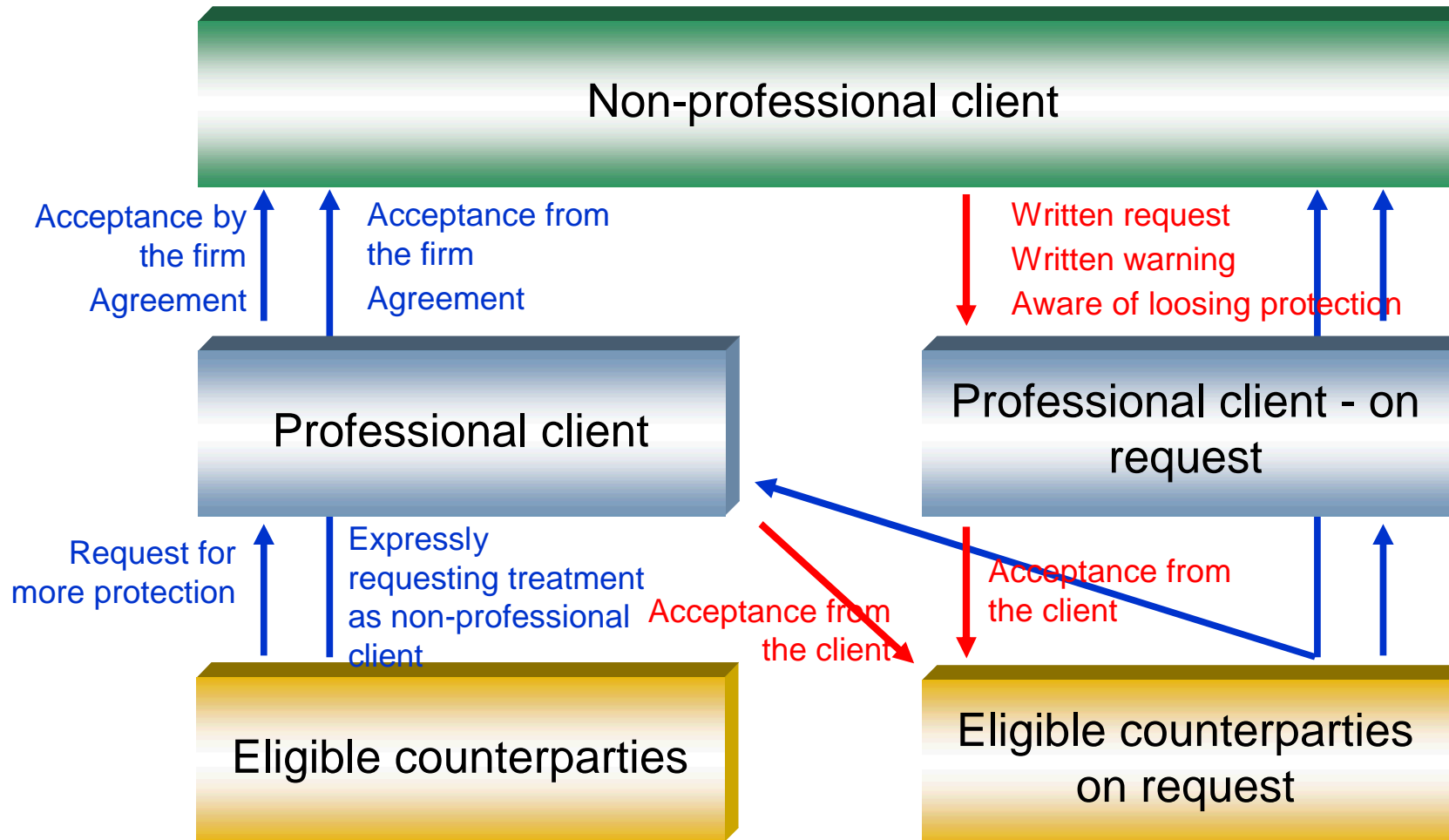
Professional client

Non-professional  
clients

Protections does not  
apply:

Eligible counterparties

# Requests for different classification



- **Client classification exists in all countries but starting point entirely different (e.g. Sweden and Finland)**
- **Does present classification of professional clients stand when MiFID's rules are applicable (one or more countries)?**
- **Current (and new) clients have to be informed about their right to require additional protection - time limit?**
- **Best practice and customer friendly approach both country wise and business area wise?**
- **Written client classification policy and procedures has to be created**
- **IT support mandatory**
- **Product adjustments**
- **Institutions need to make business decisions how to proceed !**

# Suitability / Appropriateness / Execution only

## **Investment Advice**

- “ A personal recommendation to a client in respect of one or more transactions either upon its request or at the initiative of the investment firm;**
- When a recommendation should be considered as personal:**
  - Presented as suitable for the client or based on consideration of the circumstances of the client or potential client**
  - Excluding general recommendations: advice about financial instruments given in a newspaper, journal, magazine or any other publication addressed to the general public (including by means of the internet), or in any television or radio broadcast**
- When a personal recommendation is not an investment advice:**
  - If it does not refer to particular financial instruments (=generic advice**

## **Suitability**

- **Assessment when providing investment advice and portfolio management**
  - **The investment firm must find out:**
    - 1) **Knowledge and experience (concerning specific service/product)**
    - 2) **Financial situation**
    - 3) **Investment objectives**
  - **Relieves concerning professional clients relating to some requirements mentioned above.**
  - **If client does not provide required information, no service shall be given.**
- > **Investment firm must always have procedures (instructions, training) in place in order to verify compliance with requirements**

## **Appropriateness**

- **Has to be done in connection to other services than investment advice and portfolio management.**
- **Investment firm has to assess client's knowledge and experience.**
- **Professional clients are assumed to have required knowledge and experience relating to those products/services they are classified as professional.**
- **Client has to be warned if product/service is not appropriate.**

## Execution only

- When providing execution and/or reception and transmission of client orders
- No assessment of appropriateness if:
  - 1) Non-complex financial instruments
  - 2) Initiative was of the client's
  - 3) Client is clearly informed that appropriateness test is not done and
  - 4) The firm complies with obligations under art 18 (conflict of interest).

## Non-complex product

- Shares in regulated markets, money market instruments, bonds and other securitised debt, UCITS and...

....other non-complex financial instruments:

- It does not fall within Article 4(1)(18)(c) or points (4) to (10) of Section C of Annex I to Directive 2004/39/EC
- There are frequent opportunities to realise the instrument
- Does not involve any liability exceeding the cost of acquiring the instrument
- Understandable and comprehensive information on its characteristics is publicly available

- **How to differ investment advice from rest of normal client contacts? Many services shall be re-assessed**
- **Establish appropriate procedures and filing systems to handle the different assessment requirements - IT support mandatory**
- **The definition of non-complex product may challenge those who provide investment services through electronic systems - warrants are very popular retail products in Sweden and Finland, how to handle ordinary flow of subscriptions rights ? etc.**
- **How to ensure well functioning electronic services?**

### Best execution

## **Best Execution**

- **All reasonable steps to obtain the best possible result taking into account...price, costs, speed,likelihood of execution and settlement, size, nature or any other consideration relevant to the execution**
- **Rules apply to all financial instruments under MiFID**
- **Establish a written execution policy : execution arrangements, venues used and the factors determining choice**
- **The policy shall be updated and monitored regularly**
- **The clients consent / investment firm is shall be able to prove it has followed the execution policy**

**Step 1: Selection of factors**

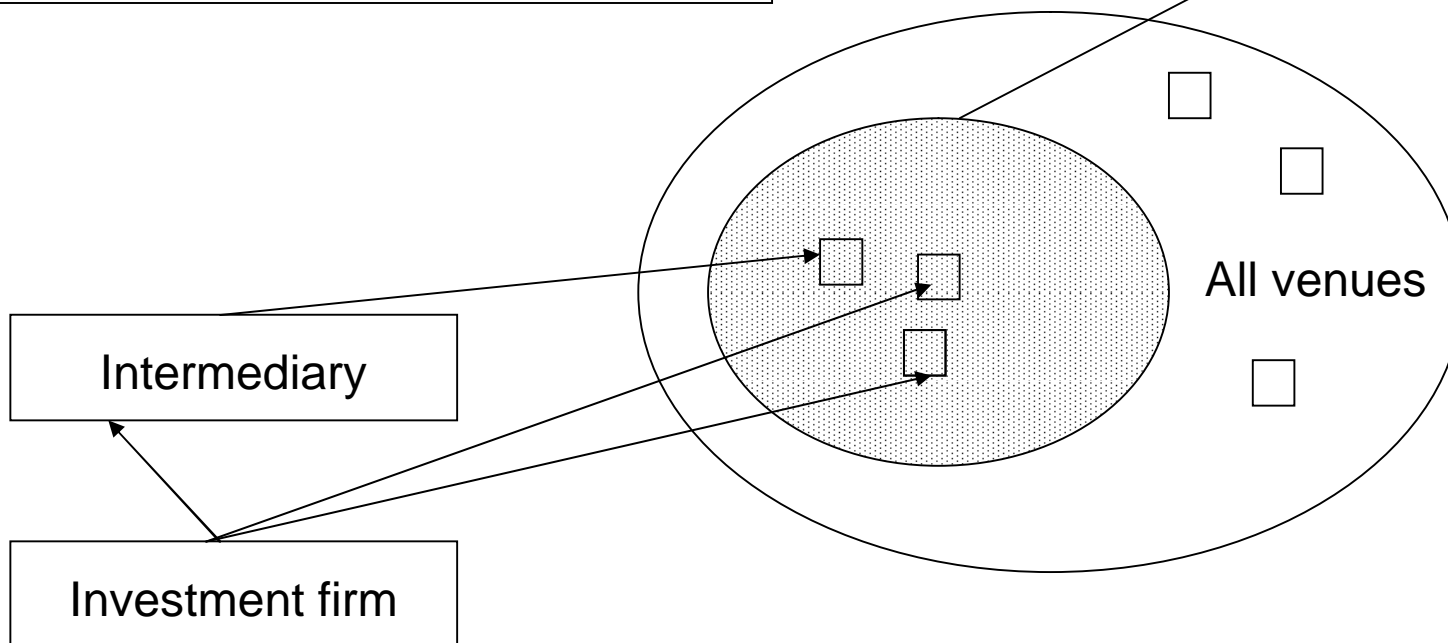
Depending on the nature of a client and its needs, a firm should decide which factors affecting execution should be given for clients generally, or for particular group of clients or, as a minimum, establish the process by which it determines the relative importance of these factors

Factor 1: speed	Factor 2: price	Factor 3: cost
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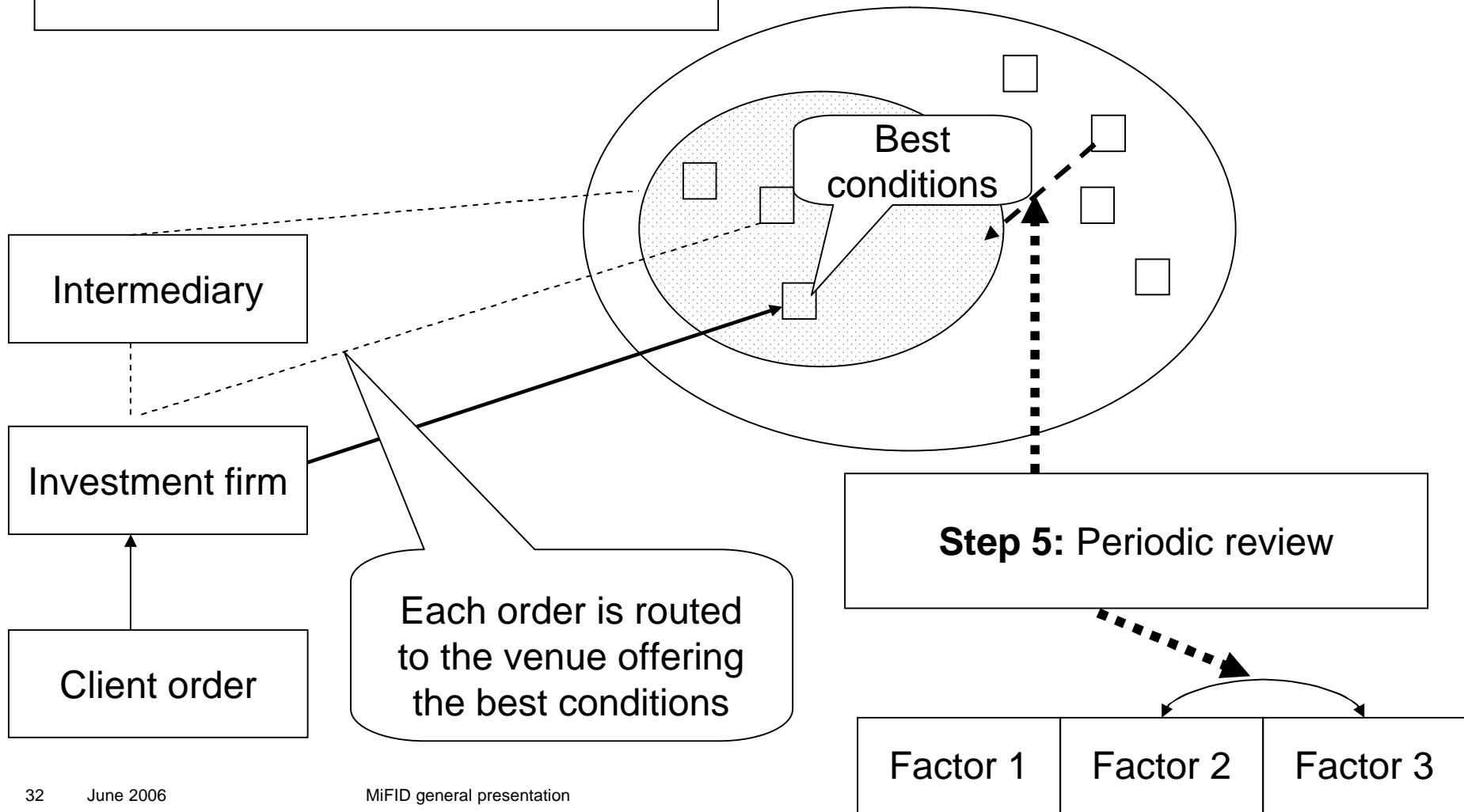
**Step 2:** Analysis and selection of Execution Venues considering the different factors

**Step 3:** Linkage to execution venues

Venues enabling investment firm to obtain the best possible result on a consistent basis in light of factors established in Step 1



**Step 4: Execution of orders**



- **All Nordic countries have best execution requirements already today; still needs to be assessed whether all MiFID requirements are fulfilled**
- **Need to adopt an appropriate execution policy - should each business unit have own policy?**
- **Need to establish procedures for getting acceptance from clients/informing changes - is internet enough to fulfil “communication”?**
- **Need to establish monitoring and filing systems to be able to prove it has followed the adopted execution policy - Administrative overkill?**
- **For some OTC products it is not clear how investment firms can measure best execution. There may be no transparent markets or there may be no other providers of a particular product.**
- **Where is the beef? Did we have problems before?**
- **Is this relevant for all retail clients? Costs vs. benefits?**