

Customer Experience Solutions

MiFID II: What Does It Mean for Your Organization?



Background

As we begin 2018, security, privacy and accountability are more critical than ever to the business processes of the modern enterprise. New technology for e-commerce and communications has brought with it new ways for those intent on criminal behavior to breach systems. As has been seen in countless examples in the past few years, these breaches can wreak havoc on consumers, businesses, and their financial well-being.

The seriousness of the potential impacts is demonstrated in the continuous fine-tuning of regulations designed to protect the privacy of transactions that are enabled with communications and digital technology. These factors have taken on a new level of urgency as cybercriminal activity becomes an ever-greater threat to financial operations.

As a result, organizations in the US and around the world have come to know and understand acronyms such as PCI DSS (Payment Card Industry Data Security Standard) and HIPAA (Health Insurance Portability and Accountability Act). In addition to these types of federal-level regulations, there are also often local government standards.

On January 3, 2018, a new regulatory acronym will be added to the list of compliance responsibilities for financial institutions. The Markets in Financial Instruments Directive (MiFID) II will primarily impact companies in the European Union (EU), where the regulation was developed. It will, however, have implications for companies that are headquartered outside of the EU but do business there.

The original MiFID came into effect prior to the 2008 global financial crisis. Ad hoc changes were made by individual countries to address issues that resulted from the crisis.

The purposes and mandates of MiFID II are quite broad, and most do not pertain solely to the operation of the contact center. The elements that do affect the contact center naturally relate to the recording of financial transactions. The questions answered in this paper will center on understanding the scope of the new regulation, what companies are affected and the transaction recording and reporting requirements.

What is MiFID II?

The Markets in Financial Instruments Directive is the EU legislation that regulates firms that provide services to clients linked to 'financial instruments' (shares, bonds, units in collective investment plans and derivatives), and the venues where those instruments are traded. The directive's main objectives are to increase competition and consumer protection in investment services. MiFID was enacted in 2004 and became effective in 2007.

Note that the 2004 MiFID ends in D, which indicates that it is a directive. Directives are laws of the EU whose direct effect is on the various national governments rather than on individuals or businesses. They require the countries to adopt certain laws which they are free to do in their own way if the resulting effect is the same.

MiFID II is the second MiFID. MiFID II is accompanied by Regulation (EU) No. 600 / 2014 (MiFIR) which will have direct effect in all EU members from its implementation date. MiFIR ends in R for regulation. An EU Regulation has the force of law directly.

MiFID, without accompanying regulation, was disruptive but unsuccessful at establishing common practices across jurisdictions. MiFIR is designed to correct that. Together, the MiFID II Directive and MiFIR are collectively known as MiFID II.

MiFID II requires the capture of all communications and orders intended to lead to an execution of a trade, even if the transaction is not actually finalized during the interaction.

Why was MiFID II enacted?

The original MiFID came into effect prior to the 2008 global financial crisis. Ad hoc changes were made by individual countries to address issues that resulted from the crisis. These issues are being addressed through MiFID II, which will harmonize the rules for all firms with EU clients, across all countries.

The main goals of the MiFID II changes are:

- **Customer protection:** Enhanced requirements in terms of suitability testing and appropriateness of products, product information, product performance reporting, and pricing transparency.
- **Products:** Increased financial product governance.
- **Unbundling of advice:** Inducements, commissions and rebates for independent advisors are banned.



Why was MiFID II enacted?

- Customer protection
- Products
- Unbundling of advice
- Market infrastructure
- Best execution
- Data reporting

- **Market infrastructure:** Broader scope of supervision to include equity and non—equity trading. Increased transparency requirements for all trading facilities.
- **Best execution:** Firms must take “all sufficient steps” to ensure that transactions are executed in the best interest of customers.
- **Data reporting:** The requirements for transaction data reporting increase considerably.

Note that the original date for implementation of MiFID II rules was January 2017. Because of the enormity of the work that needed to be done to bring firms into compliance with the new rules, that deadline was extended to January 3, 2018. What has become clear as we come to the end of 2017 is that European regulators are not likely to extend this deadline again.

In what geographies will companies be most impacted by MiFID II?

The European Union (EU) is a political and economic union of specific countries in Europe. Since July 2013, there have been 28 countries in the European Union, shown in the table below. The fundamental laws of the EU are set out in the various treaties agreed and ratified by the member countries.

Under what circumstances will companies in non—EU countries be impacted by MiFID II?

Under MiFID, there was no formal approach for firms with headquarters outside of the European Union. As a result, often different countries had differing rules that applied to the same multi—national company. One of the goals of MiFID II is to harmonize the approach to so—called “third country firms” (TCFs) among the member states of the EU.

European Union Member Countries

- Austria
- Estonia
- Ireland
- Portugal
- Belgium
- Finland
- Latvia
- Romania
- Bulgaria
- France
- Lithuania
- Spain
- Croatia
- Germany
- Luxembourg
- Slovakia
- Cyprus
- Greece
- Malta
- Slovenia
- Czech Republic
- Hungary
- The Netherlands
- Sweden
- Denmark
- Italy
- Poland
- United Kingdom

MiFID II applies to third country firms providing investment services or performing investment activities through the establishment of a branch in the EU or by way of direct access to clients in EU Member States.

Are only companies in the financial sector, e.g., banks and investment firms, affected by MiFID II?

MiFID II widens the scope of MiFID I. It applies to investment firms already subject to MiFID and it also applies to a significant number of investment firms that did not previously fall under MiFID. MiFID II applies to the following types of firms:

- Investment firms
- Credit institutions providing investment services or performing investment activities
- Branches of third country firms
- Trading venues

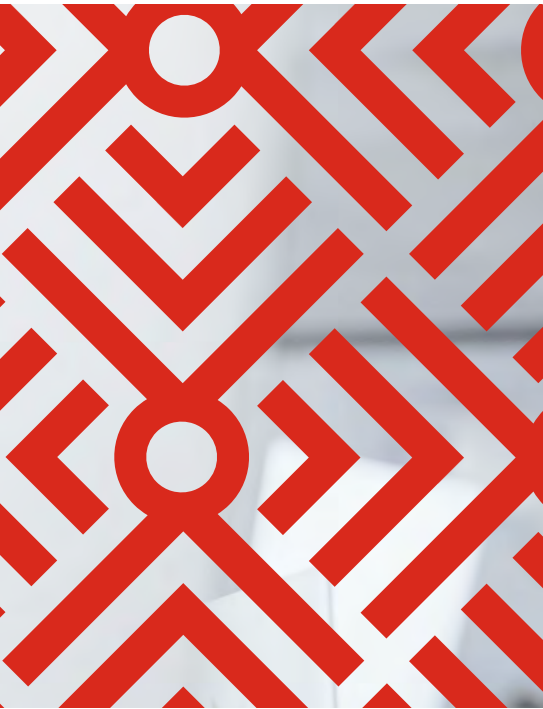
Overall, MiFID II aims to create markets that are fairer, safer and more efficient. This will have the effect of bringing some firms under the umbrella of MiFID II even if their primary business isn't financial. MiFID II will achieve this by using tests to determine if a non-financial firm's investment activities—in particular, speculative activity—are so great that it should be subject to the regulations.

If businesses are involved in investments in some way, even if it is not the main focus, they will need to investigate to understand whether this new legislation is going to affect them and what they need to do to comply.

What are the potential penalties for not complying with MiFID II?

When MiFID was originally enacted in 2007, many companies did not take the new regulations seriously. The first fine for non-compliance was given out to Barclays for inaccurate transaction reporting. Barclays' fines totaled £2.45 million for their inaccuracies between 2006 and 2008. Since then, published reports say that banks have paid over \$204 billion in compliance-related fines and infractions.

Penalties are set by the regulatory agencies in each country. The UK agency, Financial Conduct Authority, has charged a £1.50 fine per line of incorrect or non-reported data. If one considers that every day, millions of transactions are reported by hundreds of trading venues, for thousands of different financial instruments, the potential for individual company fines of tens of millions of dollars is very real. Also consider that more transactions will be subject to regulation under MiFID II than in the past under MiFID, and potential fines are even larger than in the past.



How are the transaction recording rules under MiFID II different from the rules in effect today?

Under the 2004 MiFID directive, there was no mandatory requirement to record telephone conversations or electronic communications involving client orders. Each member country has a National Competent Authority and its supervisory and investigatory powers included the right to require, in conformity with national law, existing telephone and data traffic records. EU member countries had complete and express discretion to impose obligations relating to the recording of telephone conversations or electronic communications.

After the 2008 financial crisis, as part of MiFID review process, it was recommended that individual country discretion be replaced by a more encompassing recording obligation for records of telephone conversations and electronic communications. To increase certainty, investor protection and deterrence of market abuse, MiFID II requires firms to record telephone conversations or electronic communications for the following investment services:

- Reception and transmission of orders
- Execution of orders on behalf of clients
- Dealing on own account (takes place when a firm puts its own trading books at risk)

The specific conversations and communications that are required to be recorded in relation to investment services are:

- Receipt of an order from a client
- Transmission of an order (both where the investment firm transmits the order, and where it will execute the order)

“Durable medium” means that records must be able to be replayed or copied. They also must be retained in a format that does not allow the original record to be altered or deleted. Firms are required to ensure the quality, accuracy and completeness of the records of all telephone recordings and electronic communications.

- Conclusion of a transaction when executing orders on behalf of clients
- Conclusion of a transaction when dealing on own account regardless of whether a client is involved in the transaction

It is important to note that the new MiFID II requirement covers all telephone conversations and electronic communications relating to activities intended to result in the conclusion of a transaction or the provision of client order services, even if they do not result in a financial transaction.

Do the MiFID II recording regulations apply to transactions other than contact center voice calls?

Communication of orders placed through channels other than voice must be stored in a durable medium. This includes:

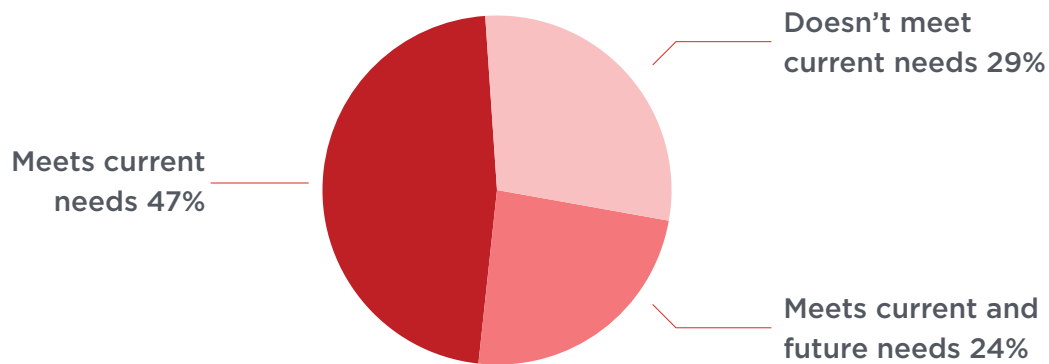
- Postal mail
- Faxes
- E-mails
- SMS or text messages
- Documentation of client orders made at meetings (e.g. face-to-face conversations recorded using written minutes)

“Durable medium” means that records must be able to be replayed or copied. They also must be retained in a format that does not allow the original record to be altered or deleted. Firms are required to ensure the quality, accuracy and completeness of the records of all telephone recordings and electronic communications. The records are to be kept for five years and, where requested by the National Competent Authority in a specific country, for up to seven years. Clients must be notified in advance of recording.

Records must cover communications made with, sent from or received by equipment provided or permitted by the investment firm. Steps need to be taken to prevent employees / contractors using privately-owned equipment where the investment firm is unable to record or copy records as required.

Will the systems organizations have in place be sufficient to be compliant with MiFID II?

The good news is that companies that have deployed a complete suite of workforce optimization (WFO) solutions in their contact centers have the tools in place not only to be compliant with MiFID II but to ensure that supervisors and managers are able to train and manage agents in the new procedures. (Important note—Businesses should perform a thorough review of their back office processes and consider extending WFO tools to back office and other customer-facing employees to ensure their interactions also comply with the new regulations.)



Does technology meet current and future needs? Interaction optimization systems (WFM, recording systems, etc.)

—2017 Dimension Data Global Contact Centre Benchmarking Report.

The question becomes, what proportion of companies that have deployed WFO solutions believe they can meet not just today's needs but those in the future?

The question becomes, what proportion of companies that have deployed WFO solutions believe they can meet not just today's needs but those in the future? Dimension Data's 2017 Global Customer Experience Benchmarking Survey asked this question of approximately 700 enterprise and medium-sized businesses. The results are shown in the accompanying graphic.

Given the number of competing demands on technology budgets, and the relatively recent adoption of omnichannel communications, it is perhaps not surprising to find that only 24 percent of the survey's respondents believe they have systems in place to meet both their current and future WFO needs. When the data is filtered for respondents from the financial services industries (e.g., 119 respondents in banking and investment), the proportion of companies that report that their WFO systems don't meet current needs increases to 32 percent. This likely reflects the ever-changing financial services regulatory environment, including the impending MiFID II effective date.

Where are the WFO solution short-falls? While not asked directly in the survey, it is likely that it is in the recording of digital communications interactions that companies may be behind regulatory considerations. The increased requirement to record and have accessible for a minimum of five years chat and SMS interactions is forcing companies to re-evaluate systems that may have been in place for many years.

For smaller firms offering financial advice, there have been concerns that the cost of installing call recording technology to be MiFID II compliant could be crippling and end up being passed on to customers. The regulatory body, however, was convinced that technology now exists

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to allow advisers to record and store calls effectively at low cost. One such alternative is a cloud-based subscription recording service. While installing and maintaining a premises-based system might be prohibitive for a small firm, per-seat licensing of a cloud solution would allow even very small businesses to remain compliant at a relatively low monthly cost.

The Time is Now

If, like so many companies, you are not sure if your current recording procedures will be sufficient to meet the requirements of MiFID II, the time is now to prioritize a review. Businesses need a comprehensive review of their compliance across all channels—phone, email, and SMS—to meet the new regulations.

In addition, they need to demonstrate that policies, procedures and management oversight of the MiFID II recording and monitoring rules are in place.

Use the following checklist to finalize your review:

- Amend policies and procedures with the help of the company compliance officer to ensure the recording of all required interactions, both voice and digital.
- Assess the need for any new permissions for recording of transactions.
- Put in place reviews of the roles of relevant staff so that they can adapt to the new rules.
- Maintain proper training so that managers, supervisors and employees act in accordance with the new rules.

How Avaya Can Help

As discussed, if you have the right workforce optimization tools in place, such as the ones within the Avaya Workforce Optimization product portfolio, you have the tools to be ready when MiFID II launches. In addition to making sure your organization meets the increased recording demands of the regulation, the Avaya WFO toolset can be part of the initial and ongoing training of personnel.

- **Recording** continuously for all or some inbound and outbound voice and other electronic communications based on business rules. The WFO tool will capture, search and retrieve calls, offer encryption for secure storage and offer pause and resume capabilities.
- **Desktop screen capture** is an undetectable back-end process that records desktop screen activity during customer interactions. Used both in the contact center and the back office, it helps organizations increase customer satisfaction, reduce costs, uncover system breakdowns, shorten cycle times and expose unauthorized personal activity of employees. Supervisors and managers can view customer interactions from beginning to end while watching and listening via synchronized screen and call recordings.

In addition to making sure your organization meets the increased recording demands of the regulation, the Avaya WFO toolset can be part of the initial and ongoing training of personnel.

- **Live call monitoring** capabilities help supervisors and managers remain compliant. Authorized users can listen to calls, look at the employee desktop in real time, record calls on demand if needed, add comments and flag calls for further evaluation.
- **Quality management** monitoring to identify and capture areas of non—compliance while measuring how well employees are delivering services that align with customer experience expectations.
- **eLearning and coaching** tools can bring employees fully up to speed on regulatory changes and any new requirements, as well as correct any non—compliance behaviors.
- **Voice analytics** can help identify areas of non—compliance. With voice analytics you can mine intelligence from large volumes of recorded calls to proactively identify, measure and isolate areas of non—compliance.
- **Customer feedback**—Collect and analyze voice of the customer interaction feedback to ascertain potential areas of non—compliance.
- **Workforce management**—leverage this tool to schedule employee compliance training while ensuring you have enough support personnel with the right skills to serve customers.

For a thorough review of your current MiFID II processes, connect with Avaya at info@avaya.com. They are there to help and want to ensure that you don't experience even the most minor of hiccups once MiFID II comes into play.

About the Author

Sheila McGee—Smith, the founder and principal analyst at McGee—Smith Analytics, is a leading communications industry analyst and strategic consultant with a proven track record in new product development, competitive assessment, market research, and sales strategies for customer care solutions and services. Her insight helps enterprises and solution providers develop strategies to meet the escalating demands of today's consumer and business customers. She is the contact center track chair for Connect. Her views on the market can be found regularly on NoJitter.com and through her Twitter feed @mcgeesmith

