FINANSIELL LICENSIERING
SWED SEC

Proficiency requirements 2014

ANNUAL KNOWLEDGE UPDATE

SW. ÅRLIG KUNSKAPSUPPDATERING (ÅKU)

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The function served by the proficiency requirements

This document defines the proficiency, in the form of an annual knowledge update, which is required of SwedSec's licence holders as a complement to the licensing examination. The proficiency requirements are divided into headings and checkpoints. A checkpoint specifies what the licence holder is expected to master within a limited field of knowledge.

The proficiency requirements are intended to function as a support when developing relevant syllabuses and also to serve as a basis when setting examination questions. They are designed to give an overview of what is expected of a licence holder. It is the task of each professional training provider to interpret the proficiency requirements and develop a relevant and instructive course based on such interpretation.

The table below describes various *cognitive levels*.

Level	Explanation
Recall (R)	The licence holder is required to recognise and remember concepts, definitions, and facts.
Comprehend (C)	The licence holder is required to understand and be able to explain various connections and contexts.
Apply (A)	The licence holder is required to be able to apply, for instance, formulae, rules, laws/acts, and methods

Subjects ÅKU 2014

What does holding a SwedSec license entail?

Being a licence holder entails both rights and obligations. The licence holder must understand and be able to explain the requirements for being granted a SwedSec licence, namely that a licensing test must be passed; that one is employed at a company which is affiliated to SwedSec; and that one is considered by the company as suitable to hold a licence. The licence holder must also understand and be able to explain the disciplinary procedure within SwedSec in terms of the process and disciplinary measures.

SwedSec's illustrated film on being a licence holder can profitably be used for this subject.
http://www.SwedSec.se/om-SwedSec/om-oss/SwedSec-licens/#film
http://www.youtube.com/watch?v=xFh0YcBQXoY

The Alternative Investment Funds (Managers) Act

In July 2013, the new Alternative Investment Funds (Managers) Act (*Sw. Lagen (2013:561) om förvaltare av alternativa investeringsfonder)* entered into force. According to the Act, Alternative Investment Funds (AIFs) may be marketed to retail investors if the fund is a non-UCITS fund or if the fund units are admitted to trading on a regulated market and a key information document about the fund is available. The licence holder must understand the conditions for marketing to investors and also what is meant by "marketing" within the meaning of the Act.

Information about the new rules is available in Government Bill 2012/13:155
http://www.regeringen.se/content/1/c6/21/66/63/74ef0f80.pdf

Suitability assessments, provision of advice and structured products

Structured products are normally complicated products within the meaning of the Act (the Securities Market Act (2007:528)). Consequently, a person who handles a customer's order or provides advice regarding such a product must obtain information regarding the customer's

knowledge and experience, in order to assess whether or not the product is suitable for the customer (referred to as a 'suitability assessment'). Structured products may be structured in many different ways and a suitability assessment must be made based on the specific product in question, not on "structured products" in general. At the end of 2012, the Swedish Financial Supervisory Authority imposed sanctions on a company for, among other things, having failed to carry out suitability assessments correctly. The licence holder must understand the requirements which, according to the Authority's decision, are imposed as regards suitability assessments when providing various structured products.

Information about the Financial Supervisory Authority's decision is available here (the various structured products which the company offered are described on pages 3-4 and the issue of suitability assessments is addressed on page 10):
http://www.fi.se/upload/45_Sanktioner/10_Finansiella_foretag/2012/devise_12-2525.pdf

Active and passive management

The debate about active or passive management is constantly relevant, not least due to the higher fees which usually apply in the case of actively managed funds. The exact delineation between active and passive management can be difficult to determine in practice.

Passive management is often equated with index tracker products with low fees. With respect to such tracker products, it is of interest to consider the index on which the product is based. Is it with or without dividends? Does it cover all or parts of the market in question, etc? The fee structure is another issue. Is the fee is reasonable for a tracker product, or should it be lower? A third question is the way in which the passive management is carried out in practice. Is the entire underlying index replicated in full, or is an attempt made to minimise deviations from an index by means of a more limited portfolio of assets? The licence holder must be familiar with the analysis problems which should be discussed when studying index tracker products.

"Active management" normally means all management other than pure index tracker management. An initial issue to determine is whether or not the product in question really offers active management. It is important to differentiate between pure passive management,

the intermediate form which is usually referred to as 'enhanced indexing', and true active management. There are several common measurements which are used in this context. Tracking error is a first measurement, which is used to gauge the degree of the management's deviation from its index. The management's turnover rate is another measurement which can conceivably reflect the degree of activity. A third measurement comprises the management's Active Share, i.e. the total of the differences between the weights of the assets and corresponding weights in their benchmark indices, divided by two. All of these measurements have both strengths and weaknesses. In order to be able to answer questions and address comments correctly, it is important that the licence holder understands and is able correctly to explain the difference between active and passive management; is familiar with exactly how the different measurements are calculated; understands and is able to explain how one can find out about the degree of active management; and is familiar with both the strengths and weaknesses of each measurement.

A related (and possibly more important) issue is whether or not the active management has provided the customer with added value. Classic evaluation measurements such as Jensen's alfa are, of course, used in such evaluations. However, in more recent times the information quotient measurement has also become more common. The licence holder must understand and be able to explain exactly how these two different measurements are calculated in practice, how they differ from each other, and must be able to explain in which contexts it might be appropriate to use the one measurement or the other.

Review of already filed tax returns (also referred to as self-correction)

Since 1 January 2012, the Tax Procedure Act (*Sw. skatteförfarandelagen, SFL*) contains provisions which allow for the possibility of self-correction. The Act states that a tax surcharge shall not be imposed when an individual, on his or her own initiative, corrects inaccurate information (Chapter 49, section 10, subsection of the Tax Procedure Act).

Normally speaking, it is possible to carry out self-correction as regards the past six years. Thus, in 2014 it is possible to correct information as from the 2008 income year.

The licence holder must be familiar with the possibilities for review. The licence holder must also be aware of the fact that Sweden will soon have agreements regarding exchanges of information with all countries (as distinct from the situation regarding automatic disclosure of information).

Retirement abroad

Many people consider moving abroad in connection with retirement. It is important that the licence holder be aware that the situation can change for the customer from a tax and social security perspective.

Even if one is no longer domiciled in Sweden, in the event of a permanent stay in Sweden or if one has a so-called significant connection, from a tax perspective one may be treated in the same way as when domiciled in Sweden. On the other hand, it is possible that one might not be covered by the social security system in Sweden.

Limited and unlimited tax liability

The licence holder must be familiar with the reasoning as to when a taxpayer is, or is not, liable to pay taxes in Sweden. The licence holder must be familiar with the following concepts: the concept of domicile, permanent stay, and significant connection. In addition, the licence holder should be familiar with the most common criteria regarding significant connection.

The licence holder must be aware of the consequences of a whether or not a person has unlimited tax liability, and must be familiar with the way in which the special income tax for residents abroad (*Sw. SINK-skatten*) functions. The licence holder must be familiar with the way in which dividends are taxed (withholding tax), the so-called 10-year rule, and the way in which the sale of any permanent residence is taxed. In addition, the licence holder must be familiar with the impact on tax of any double taxation treaty. The licence holder must be able to draw the customer's attention to this aspect.

The licence holder must be aware of the reasons why certain countries are often mentioned in connection with retirement abroad. The licence holder must be aware of the fact that if the

customer is domiciled in another country, inheritance rules and inheritance tax may be changed and social security protection in Sweden may cease to apply. The licence holder must be aware of the fact that rules are often changed and that this may result in entirely changed circumstances.

Case descriptions

Purpose and area of use of case descriptions

SwedSec has decided that each year the annual knowledge update must include at least one case description. The case descriptions depict different situations which the licence holders may encounter in their work, and contain dilemmas in respect of which there is sometimes no correct answer; instead, the situation is more complex in nature. Even if there is a correct or obvious alternative, the licence holder should understand why that is the case – i.e. the ethical or moral considerations on which a certain rule might be based.

The purpose of the case descriptions is to serve as a basis for skills development and greater in-depth knowledge. Through such knowledge, SwedSec wishes to contribute with content (but not method) as regards each affiliated company's work going forward, i.e. it is up to each employer to decide *how* these cases are to be used. For example, seminars might be held for in-depth discussions in which several perspectives may be shown to advantage and/or the content of the case descriptions might be integrated in what is referred to as e-learning, provided that the content is structured in such a way as to reflect the same complexity as in these case descriptions. The case descriptions themselves may also need to be tailored to the operations of the individual affiliated company. It may very well be the case that the issues addressed in the descriptions can be better addressed through entirely different scenarios. This is up to the individual affiliated company – the essential thing is that the issues raised in the case descriptions are addressed in the seminar/training course and that the seminar/training course is carried out in such a manner that the licence holder doesn't merely "tick the correct box" or learn a certain rule, but rather reflects over why one particular alternative is better than another.

Two case descriptions are included in the proficiency requirements for the 2014 annual proficiency update. One case addresses confidentiality, while the other addresses rules of conduct in the trading room. It is mandatory for the license holder to accomplish at least one of the two case descriptions.

Confidentiality

Anders works as a private adviser at a bank. For many years, a married, middle-aged couple (Sebastian and Linda) have been his customers. Anders has always considered them to be competent and serious, not least when it comes to personal finances. They both have several bank accounts of their own. They do not have any joint account, but in principle they have always met Anders together and have always indicated that they have shared finances. On a number of occasions over the years it has happened that one of them has requested to receive information about the other's finances. This has involved relatively mundane information, such as whether a particular bill has been paid or the balance on a particular account pending a holiday or a major purchase. In these cases, Anders has disclosed the information and felt entirely confident in doing so. No written power of attorney has been drawn up between Sebastian and Linda, but when information has been disclosed they have never subsequently raised any objection. On the contrary, they have both given the impression that it has been obvious that they have full insight into each other's accounts and finances. Sebastian and Linda have many irons in the fire and are quite "entrepreneurial" and thus their contacts with the bank have been quite close and frequent. However, during the past six months contacts have been only sporadic.

One day, Sebastian calls. He is unusually abrupt in tone and sounds somewhat stressed. He explains that he requires information about the balance on Linda's account. In addition, he wishes to know whether any large payment has recently been made from the account. Sebastian also wishes to deposit a large sum on the accounts of his and Linda's three grandchildren. Finally, he wishes to have help in depositing EUR 90,000 in cash, since two weeks ago he sold the couple's swanky car, barely a year old, to an acquaintance who lives in France. Sebastian explains that he personally drove the car down to France and received payment in cash.

Anders carries out these measures. Subsequently, through the grapevine Anders hears that Sebastian and Linda have filed for divorce and that Linda has moved out of their house – a fact which is substantiated through photos that Sebastian and Linda have put on their Facebook pages. When in town over the weekend, Anders also happens to see Sebastian driving the car which he recently stated he had sold in France. The bank subsequently also

receives an anonymous but reliable tip that Sebastian is laundering money from unlawful gambling activities.

As a result of what has happened, Anders reports to the compliance department his suspicion that the deposit of EUR 90,000 constitutes money laundering. It transpires that the compliance officer who is handling the matter, Steven, knows Sebastian and Linda since their grandchildren play in the same football team. Anders and Steven discuss conceivable reasons for Sebastian's extremely unexpected behaviour, whereupon Anders informs Steven that Sebastian and Linda are getting a divorce and that Linda is living at another address. A complaint regarding suspected money laundering is also sent to the Financial Intelligence Unit.

The same day, Steven has lunch with Nicole, who heads the bank's internal audit. Nicole lives nearby Sebastian and Linda and has a slight acquaintance with them. Steven mentions of the suspicion against Sebastian and that it appears that Sebastian and Linda are getting a divorce. Nicole regards what has happened as an appropriate occasion to ask Sebastian and Linda whether they are interested in selling their boat berth to her. She thereafter contacts Anders to have it confirmed that Linda has moved out and to enquire a little about Anders' contacts with Sebastian and Linda and about the situation in general.

When Nicole calls, Anders feels himself a bit of a "gossip". However, he makes the assessment that the information regarding the divorce is not covered by confidentiality, since it does not derive from either Sebastian or Linda personally. In addition, Anders considers that the information about the divorce can hardly damage either of them, since they have put on their Facebook pages photos which indicate that they are no longer a couple. Furthermore, if they are soon to get a divorce, it would be beneficial for them to quickly find someone who would like to take over their boat berth. Anders argues that, in any event, it must be possible to disclose the information to a colleague, who is also a senior manager and head of the internal audit, whose work is closely related to that of the compliance department.

After a time, the Financial Intelligence Unit contacts Anders and wishes to obtain information about the transactions during the past five years on all of Sebastian's and Linda's accounts,

including securities accounts and accounts belonging to Linda's own limited company. Spontaneously and in surprise, Anders asks the person handling the case why such extensive information is required. The person handling the case is unable to give any explanation which has any bearing on the actual complaint, but explains that he is new at the department and thus, to be on the safe side, he wishes to compile as much information as possible. He also says that the Financial Intelligence Unit often comes back with requests for supplementation in the matters it is handling, and therefore it is more efficient to obtain as much information as possible from the outset.

Issues to discuss

- What type of information about a customer is subject to confidentiality?
- When is it permitted to disclose, to anyone within one's own company or to any external party, information about customers which is classified as confidential?
- Are there any special rules or routines applicable regarding disclosure to a person who is closely related to the customer?
- What other matters should be considered when handling information classified as confidential?

Purpose with the case

One purpose with the case is to underscore the fact that, as a starting point, confidentiality applies to all information about the company's customers (within the company's business) which is not in the public domain. 'Public domain' means, primarily, that the information is available in publicly available documents, not that it has appeared in the mass media or social media. Confidentiality initially applies irrespective of the circumstances about the customer to which the information relates, the way in which the company has learned of the information, and irrespective of how important it may be considered for the customer that the information is not disclosed. Nor is there any time limit as to how long the information is protected.

There is a right to disclose information classified as confidential only if the recipient of the information has a legitimate interest in the information, i.e. in principle requires the information in order to perform a service on behalf of the customer or a necessary task in the activities of the company. The aforesaid applies irrespective of whether the disclosure takes

place internally at the company or to any external party. Therefore, the fact that a particular employee holds a certain formal position within the company does not mean that such person is automatically entitled to receive customer information which is classified as confidential.

In accordance with the aforesaid, in conjunction with the issue of disclosure, the party handling the matter must consider whether the recipient has such a legitimate interest. If such an interest exists, it must also outweigh the confidentiality interest. In certain cases, e.g. upon suspicion of money laundering or insider dealing, according to law the company is obliged to disclose certain specific information and, in such case, it is of course a given that there is a legitimate interest. It is often also the case that public authorities request certain information without the company being subject to any statutory obligation to disclose precisely that specific information. In these cases, too, it may be assumed that the authority has a legitimate interest, particularly if it is an authority with close connection to the company's operations, such as the Financial Intelligence Unit. Nevertheless, an authorisation assessment should be carried out also in these cases and, if it transpires that the circumstances indicate that the authority lacks a legitimate interest (with respect to all or certain information), the company should request that the authority state reasons why it requires the information. If (contrary to expectations) no satisfactory reply is provided, the company must refuse to disclose the information.

Bank secrecy, as well as confidentiality within other financial companies, applies also in relation to a spouse or other closely-related party (provided they are not formally authorised to represent the customer, e.g. through a power of attorney or in the capacity of guardian, trustee or custodian pursuant to the Code on Parents and Children). With respect to spouses, in exceptional cases a spouse may be deemed to have given implied consent to the lifting of confidentiality. It is, however, important that no routine assessment is made as to whether there is implied consent; rather, such an assessment must be made based on cogent reasons and extremely good customer due diligence. In the event of implied consent, the party handling the matter must pay attention to any changed circumstances as a result of which the implied consent can no longer be assumed to apply. Even if there is implied consent, for the peace of mind of all involved, it is advantageous if a written power of attorney is drawn up.

With respect to other closely related parties, a deviation from confidentiality may be made in a particular, commonly occurring circumstance, namely where the risk of abuse of the information is low and disclosure of the information is to the benefit of the customer. This is the case where, in connection with an impending pecuniary gift to a customer from close relative, for example the maternal or paternal grandparents of a customer who is a minor, a bank is deemed entitled to confirm whether the customer holds a particular account. However, in this situation, as a rule there is no right to disclose information as to which account a customer holds, despite the fact that a close relative with good intentions is involved.

Also in respects other than the assessment of authorisation, information which is classified as confidential must be handled professionally and with care regarding the customer. Even if the information is publicly available, and thereby no longer formally classified as confidential, the company should exercise restraint in disclosing information which may be to the customer's disadvantage. The party providing the information should endeavour to ensure that the information is protected also at the recipient. An employee who was received information classified as confidential is also prohibited from using the information in a manner which may damage the customer. Even if use of the information would not damage the customer, the employee should be extremely cautious when using the information for his or her personal gain.

For more information about the confidentiality rules, see Per-Ola Jansson, *Banksekretess och annan finansiell sekretess* [Bank secrecy and other financial confidentiality], 2010.

Rules of conduct in the trading room

Sven has worked for a long time at the Bank as a trader in fixed income instruments. Thanks to his experience and high level of skills in trading in fixed income instruments, he has built up and enjoys a large degree of confidence among both his colleagues at the bank and representatives of customer companies with whom he has had contact and got to know over the years. As a result of the day-to-day contacts with traders at customer companies, he has also come close to several of them and, in certain cases, developed personal relations. Thus, discussions about possible transactions often also include elements of a more personal nature. The procedures for traders in fixed income instruments at the Bank prescribe that transactions may only take place from the trading room. Several senior managers are entitled to engage in transactions outside the trading room, but in such cases special procedures apply. Sven is not authorised to engage in such a so-called "off-premises dealing".

Daniel, who works with liquidity management at the Internet bank of a large corporate customer with property construction as its main business, is one of Sven's customers. Daniel is extremely trading-intensive and makes a large number of transactions, and thus his trading generates significant revenues for the Bank and, indirectly, also bonuses for Sven.

One morning, Sven's mobile telephone rings just as he arrives at his workplace and is taking off his coat. It is Daniel who is on the phone and — while Sven is on his way to his desk in the trading room — discussing certain transactions in fixed income instruments which Daniel's company has carried out over the course of a few weeks. It concerns a particular corporate bond, of which Daniel's company has been a major net purchaser, and in which he thus holds a large position. The bond price performance has been positive for Daniel but – as he says – the holding "sticks out" and represents a potential problem for the next quarterly reporting. Daniel wants Sven to buy the holding at the prevailing market interest rate, but that they simultaneously enter into a futures contract whereby he is entitled to buy back the bond at the same rate of interest on a future date. However, he requests that Sven wait with booking the futures contract, on the ground that he must first make "certain internal reconciliations". He emphasises, however, that this is mainly a technicality and that it should not be of any significance since, in effect, he has "merely lent the bonds to the Bank". Sven believes that Daniel has always honoured by his word, and thus there should be no problems this time

either. Since Daniel represents a large, important customer of the Bank, Sven agrees to the transaction before he ends the call and sits down at his workstation. Since Sven has not yet managed to start up his computer, he jots down the terms for the transactions on a piece of paper, with the intention of booking the purchase in the trading system when he has time. Since Daniel has requested that he wait with booking the futures contract, he doesn't book it; instead, he merely makes a note that "Daniel will get back with a confirmation".

When the market opens, the company which issued the bond issues a press release in which it is announced that the rating has been reduced from investment grade till high yield. In the press release it is, however, emphasised that the company's financial position is unthreatened, and that it has no short-term problems in paying its debts. However, the news has a severely negative impact on the price of the company's shares and its listed bonds. As a result of this news, together with general turbulence on the market, the phones start ringing at the Bank. As a consequence of the chaos which prevails in the trading room, Sven does not have time to book the transaction with Daniel until the market has closed the same day. After Sven has booked the transaction, he turns off his computer and goes home for the day.

The price of the bond continues to fall during the following days, and thereafter stabilises at a higher interest rate level. Daniel has not yet got back to Sven about the futures transaction, and Sven has a sense of gnawing unease about the price trend of the bonds he has bought from Daniel. However, the price is still sufficiently good for Daniel to have made a profit on the original transactions. In order for Sven's holding to better reflect the market value of the bonds, Sven and Daniel thus reach an agreement that Daniel will buy back the bonds at the interest rate which Sven paid, and that Sven will thereafter immediately buy them back at the prevailing market interest rate. They also adjust the terms of the futures contract, which has one week until expiry. One week later, Sven sells the bonds back to Daniel at the futures price.

Issues to discuss

Discuss the transactions carried out by Sven and Daniel in the example above and how they relate to the rules of conduct applicable to activities in a trading room.

- Has Sven or Daniel violated any rules and, if so, which?

- How has Sven handled the transactions from an ethics perspective?
- Assume that you are a colleague of Sven and observe the transactions that have taken place. Assuming that Sven has violated some formal rules or the ethics standard applied within the Bank, how should you suitably act?

Purpose with the case

The purpose with the case is to illustrate a situation which may arise in a trading room, irrespective of whether the trading involves shares, fixed income instruments, currencies or any other type of asset. On an overall level, the intention with the case is to bring up for discussion what constitutes "generally sound behaviour" in the trading room, but also to describe in more concrete terms several situations which may arise in different guises which violate generally accepted principles and, often, also formal rules and regulations. The example illustrates the importance of discussions with customers always being conducted by means of a telephone connection which is recorded, and that conducted transactions are promptly registered in relevant systems. The example also addresses the problems of "Warehousing" and "Historic Rate Rollover". Finally, the example is aimed at showing the risk of a trader coming "too close to the customer" and the importance of differentiating between a customer (in this case the corporate customer) and the customer's representative (in this case Daniel).