



# Client Relationship Model, Phase 2

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# Presentation Outline

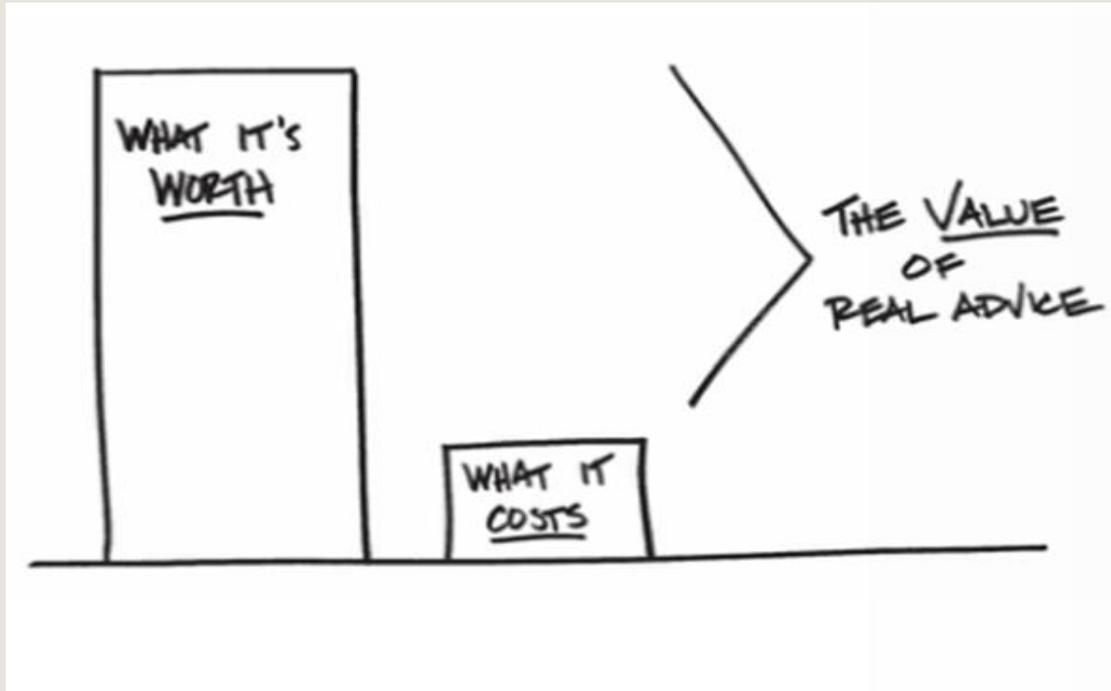
- CRM2 in a nutshell
- Transition news
- Review of requirements and commentary
  - relationship disclosure information
  - trading cost disclosure
  - client statements
  - market valuation methodology
  - annual report on charges & other incentives
  - Annual performance report
  - impact on particular registration categories
- Questions



# CRM2 in a nutshell

# The Value of Advice

(from Carl Richards' "The Behavior Gap")



# Overview

- The Client Relationship Model - Phase 2 (CRM2) amendments to NI 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103) and Companion Policy
- Came into effect on July 15, 2013, to be phased-in over a three-year period
- Introduces new requirements for reporting to clients about the costs and performance of their investments, and the content of their accounts

# Common Standards for Registrants

- Focus on retail investors, with carve-outs for “permitted clients” that are not individuals
- Applicable to all dealers and advisers – the requirements are almost all the same regardless of registration category (SRO Member rules are highly harmonized)
- Flexible delivery requirements
  - new disclosures can be combined or separate
  - no prescribed forms for reports
  - prescribed notifications in “substantially” the form in the rule

# Already Implemented Provisions

- Minor clarifications to NI 31-103, such as enhancements to relationship disclosure information, were implemented as of July 15, 2013
- Beginning July 15, 2014, dealers and advisers were required to
  - provide certain information about how benchmarks can be used (but there is no requirement to provide benchmark information on an ongoing basis)
  - provide pre-trade disclosure of charges (except for managed accounts)
  - report on compensation from debt securities transactions in trade confirmations (applies to dealers only, not advisers)

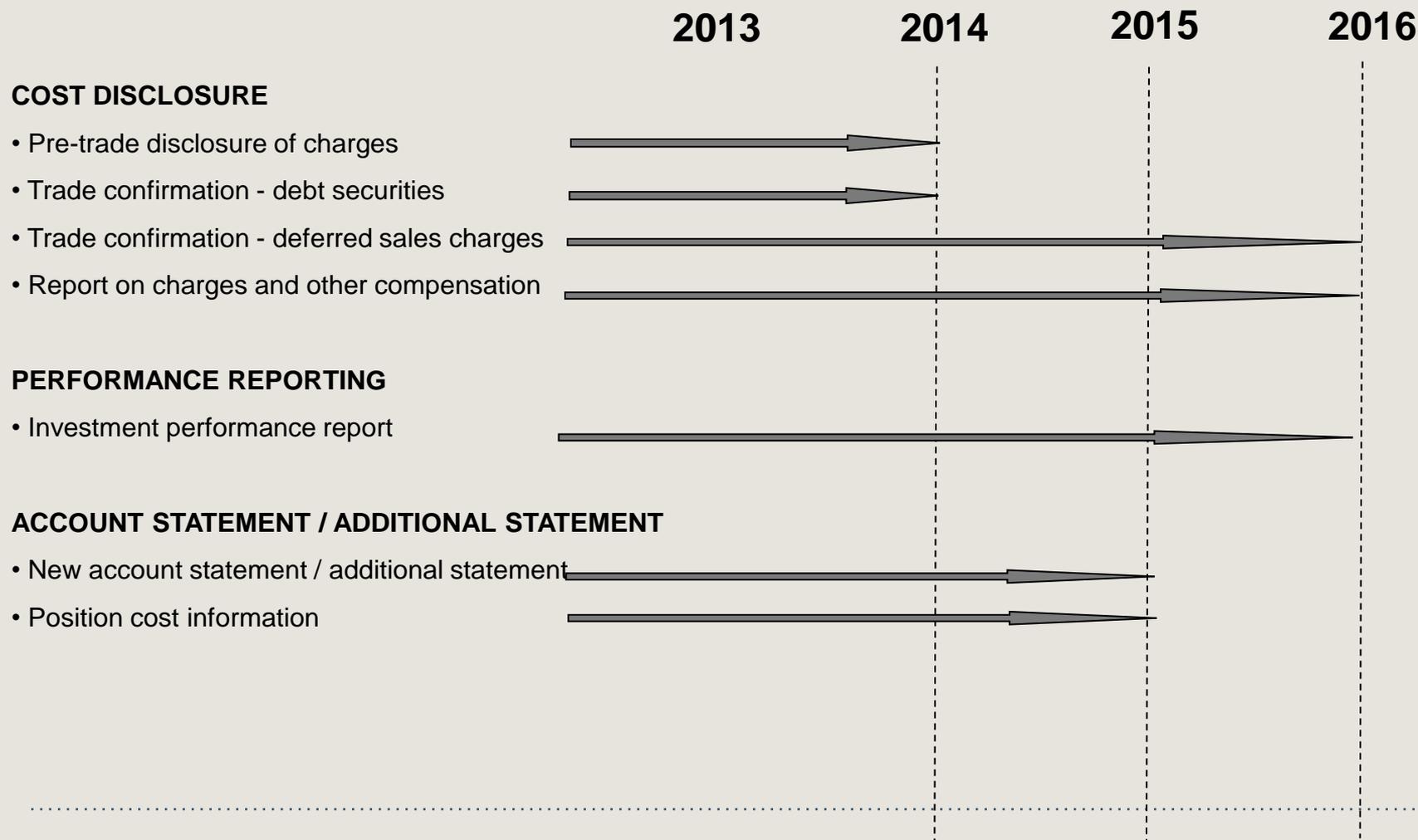
# 2015 Implementation

- Expanded account statement requirements to cover all of a client's securities
  - whenever they are held by the dealer/adviser (nominee name or certificate), and
  - in most circumstances where they are controlled or held in client name by a third party
- Included for all securities in a statement
  - position cost (using either book cost or original cost)
  - whether may be subject to a deferred sales charge if sold
- Using a prescribed method for determining market value
  - hierarchy of valuation methods based on availability of relevant information
  - if dealer/adviser reasonably believes cannot determine MV, client statement to say so

# 2016 Implementation

- Two new annual reports delivered together to clients:
  - Report on charges and other compensation that shows, in dollars
    - what the dealer or adviser was paid for the products and services it provided
    - specified other incentives payments, e.g. trailing commissions
  - Investment performance report that shows investors
    - how much they invested and what it is worth today
    - deposits and withdrawals for past year and since inception of account
    - their actual percentage returns for specified periods

# Phased Transition





# Transition News

# Transition News

- To be set out in CSA orders and SRO harmonizing amendments expected to be published mid-May 2015:
  - implementation of CSA Chairs' response to request for more time
  - relief addressing certain operational issues
  - for non-SRO members, suspension of investor protection fund coverage
  - for SRO members, comply with CRM2 as set out in member rules

# 2015: More Time to Roll-out New Client Statement Information

- New requirements relating to
  - market value
  - position cost
  - account statements
  - additional statements

may be met in statements covering the period that ends December 31, 2015 (instead of beginning with the period that includes July 15, 2015)

# 2016: Reduced Burden for Calendar Year Reporting

- Firms that will use calendar year for their annual performance reports starting with 2016 will not have to include comparative data from 2015 or any earlier date. Instead,
  - for market value, information as at and since January 1, 2016 or the firm's choice of one or more dates earlier than January 1, 2016, so long as it's the same for all "similar clients"
  - for annualized total percentage returns, information for 2016 (unless the firm chooses an earlier date, this also becomes the deemed inception date)

# “Similar Clients”

- “Similar clients” for these purposes means:
  - clients whose accounts or security positions were transferred together,
  - clients on the same reporting system if a registered firm has more than one reporting system, or
  - other clients whose accounts or security position would appear to a reasonable person to be similar in a way that relates to the recording or calculation of market value or position cost

# Position Cost: Operational Issues Using Market Value

- For all firms, if providing market value in place of actual position cost
  - for transfers, may now state that market value, not the cost of the security position, is being disclosed – without having to specify that it is the market value as of the transfer date
  - for existing accounts, may use December 31, 2015 or the firm's choice of one or more dates earlier than December 31, 2015, so long as it's the same for all "similar clients" (vs *all* clients of the firm holding the security)

# Performance Reports – If Not Based on Calendar Year

- For firms that choose not to report on a calendar year basis (e.g., first reports cover July 15, 2016 to July 14, 2017),
  - comparative market value information can be as at and since July 15, 2015 or the firm's choice of one or more dates earlier than July 15, 2015, so long as it's the same for all similar clients (vs July 15, 2015 in all cases)
  - annualized total percentage return information can be
    - since inception, or
    - for the period since July 15, 2015 or the firm's choice of one or more dates earlier than July 15, 2015, so long as it's the same for all "similar clients" (the firm is no longer required to conclude that it believes information since inception is not available)

# Investor Protection Fund Disclosure

- For non-SRO members:
  - requirement to identify securities that may be covered under an investor protection fund in their additional statements is suspended
  - CSA will propose new text for public comment
- IIROC's existing investor protection fund disclosure requirements remain in effect
- MFDA's new requirements will come into effect December 31, 2015

# SRO Member Rules

- Materially harmonized IIROC and MFDA rules for CRM2 have been approved
- IIROC and MFDA members may comply with their SRO rules for CRM2 requirements without also looking to the CRM2 requirements in NI 31-103
- IIROC and MFDA members seeking discretionary relief from CRM2 provisions (other than those relating to IFM or SPD activities) apply only to their SRO



# Review of requirements and commentary

# Relationship Disclosure Information

- In effect – Relationship Disclosure Information (RDI)
  - core principle requiring disclosure about relationship with registrant
  - specified relationship disclosure requirements
- Beginning July 15, 2014, dealers and advisers were required to
  - provide certain information about how benchmarks can be used (but there is no requirement to provide benchmark information on an ongoing basis)
  - provide pre-trade disclosure of charges (except for managed accounts)
  - report on compensation from debt securities transactions in trade confirmations (applies to dealers only, not advisers)

# Cost Disclosure

- Relevant information at the relevant times ...
- At account opening, enhanced general cost (“charges”) and advisor incentive information
  - operation of the account
  - making, holding and selling of investments
  - other compensation received by dealer or adviser
- When transacting, disclosure of actual charges
- Annually, new summary of:
  - all charges actually incurred by a client
  - dollar amount of trailing commissions or similar compensation tied to a client’s investments

# Pre-Trade Disclosure

- Prior to the registrant accepting the client's order, specific disclosure of the charges a client will have to pay or a reasonable estimate
- Verbal disclosure sufficient
- Carve-outs
  - permitted client that is not an individual
  - dealer executing trades as directed by adviser
  - managed accounts

# Trade Confirmation

- Trade confirmations must now include for fixed income securities
  - the annualized yield (purchase only)
  - compensation taken, either:
    - total \$ amount of compensation, or
    - total \$ amount of any commission paid to the firm + general notification (mark-up/mark-down, service charge)

# Client Statements

- Expanded client statement requirements to ensure common standards
  - account statement – at least quarterly, covering
    - transactions carried out during the period
    - securities held by the dealer or adviser
  - additional statement – at least quarterly, covering some securities held in client name
- Include for all securities in the statement
  - position cost (using either book cost or original cost)
  - whether may be subject to a deferred sales charge if sold
  - whether covered by an investor protection fund
- Use a prescribed method for determining market value
- Account-based (limited option for consolidation)

# Account Statement

- Account statement – every 3 months, or monthly (if requested or transaction was effected)
- Additions to account portion of statement
  - notification re: estimated market value, if applicable
  - investor protection fund – whether covered and name
  - which securities subject to deferred sales charge if sold

# “Additional” Statement

- “Additional” statement covers securities not held in account if
  - the dealer/adviser has trading authority
  - the dealer/adviser receives continuing payments tied to the securities (e.g., trailing commissions)
  - the security is issued by a scholarship plan, a mutual fund or LSIF and the dealer/adviser is the dealer/adviser of record
- Content corresponds with account portion of account statement, plus name of the party that holds or controls each security and description of the way it is held
- Flexible delivery, every 3 months (for advisers, client may request monthly)
  - combined with account statement
  - accompany account statement
  - within 10 days of account statement
- Carve-out for permitted client that is not an individual

# Market Value Methodology

- Prescribed methodology
  - security issued by an investment fund which is not listed on an exchange – determined by reference to NAV
  - any other security – the amount the firm reasonably believes to be its market value using policy and hierarchy of valuation methods based on availability of relevant information
  - if reasonably believe that cannot determine market value, must say so and exclude from calculations in client statements and investment performance report

# Position Cost

- Position cost information for security positions in client statements provides a comparator for market value of those securities
- Can use either book cost or original cost for its clients
- Can use market value for existing client positions when first implementing this new requirement, and for transferred positions (some conditions apply)
- Deliver position cost information for securities reported in account statement and additional statement every 3 months
  - combined with an account/additional statement
  - as a separate document accompanying statement
  - as a separate document within 10 days of statement (must include market value information)
- Carve-out for permitted client that is not an individual

# Other Client Statements

- Security holder statements
  - If there is no dealer or adviser of record for a security holder on the records of an IFM
  - Annually
    - transactional information in account statement
    - information in additional statement
    - position cost information
- Scholarship plan dealer statements
  - If not registered in another dealer or adviser category, deliver annually
    - transactional information in account statement
    - information in additional statement

# Annual Report on Charges & Other Compensation

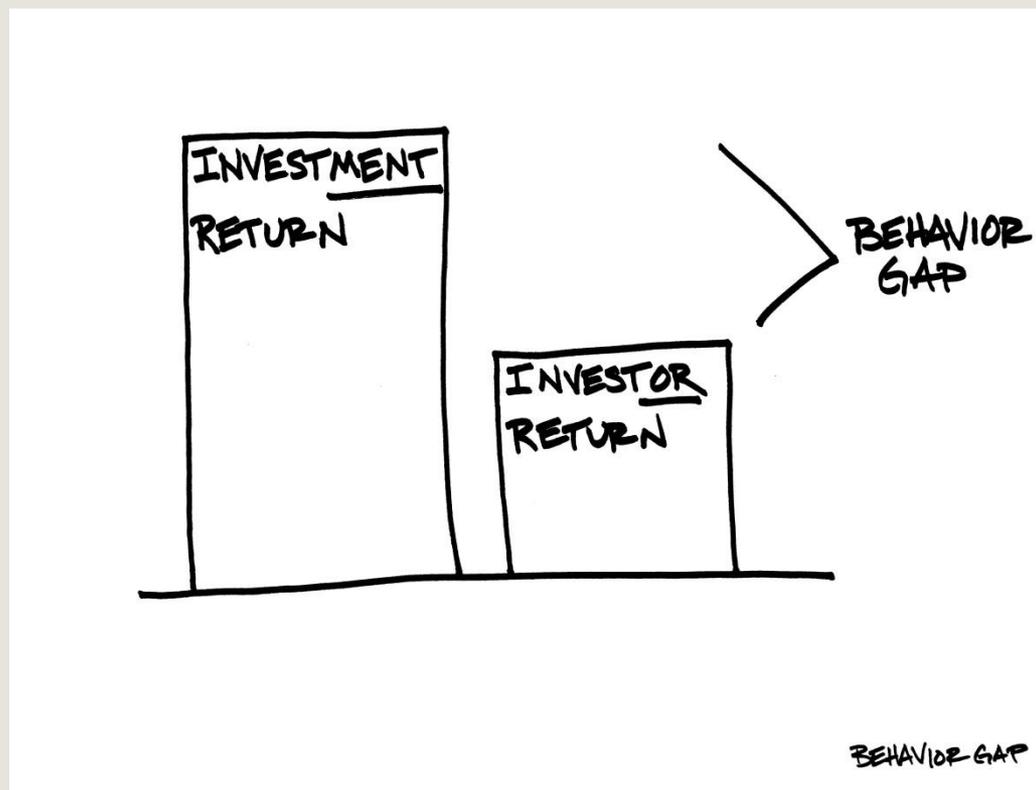
- For each 12-month period, what the dealer or adviser was paid, in dollars, for the products and services it provided, plus other financial incentives received in re the client's investments:
  - operating charges and transaction charges
  - payments from issuers of securities or other registrants in relation to registerable services to client
  - trailing commissions (actual dollar amount received in re the clients' investments)
- Delivery together with investment performance report and one of combined with/accompanying/within 10 days of client statements
- Carve-out for permitted client that is not an individual
- Sample report in Companion Policy

# Investment Performance Report

- For each 12-month period, a report that covers
  - market value as at beginning and end of period
  - deposits into, and withdrawals from, the account
  - change in value of the account
  - percentage returns for 1, 3, 5 and 10 years and since inception using using a money weighted rate of return
- Delivery as per annual report on charges and other compensation; must be for same 12-month period
- Carve-outs
  - permitted client that is not an individual
  - dealer executing trades as directed by adviser
  - a client's account less than 12-months old
- Sample report in Companion Policy

# Where an Advisor Can Make the Difference

(from Carl Richards' "The Behaviour Gap")



# Limited Application to IFMs

- IFMs are carved out of most CRM2 requirements (except to extent may also be dealers or advisers)
- Annual security holder statements for orphaned accounts
- Duty to provide dealers and advisers with information they need to comply with new client reporting requirements
  - deferred sales charges and any other charges deducted from the net asset value of securities
  - trailing commissions on an account basis

# Scholarship Plan Dealers

- Scholarship plans are unique products, so SPDs have special provisions in CRM2
- Disclosures include
  - total amount client has invested
  - total amount returned to the client if the client ceased to make prescribed payments
  - reasonable projection of future payments to designated beneficiary
  - a summary of any terms of the plan that, if not met by the client or the client's designated beneficiary, might cause loss



# Web Links

# CRM2 Web Links

- CRM2 Guidance on OSC Website's "Registrant Outreach" page
    - Educational Seminar, Nov. 21, 2013: Client Relationship Model Phase 2 [[http://www.osc.gov.on.ca/documents/en/Dealers/ro\\_20131121\\_crm2-cost-performance.pdf](http://www.osc.gov.on.ca/documents/en/Dealers/ro_20131121_crm2-cost-performance.pdf)]
    - Staff Notice 31-337 *Cost Disclosure, Performance Reporting and Client Statements - Frequently Asked Questions and Additional Guidance as of February 27, 2014* [[http://www.osc.gov.on.ca/en/SecuritiesLaw\\_csa\\_20140227\\_31-337\\_faqs-guidance-31-103\\_2.htm](http://www.osc.gov.on.ca/en/SecuritiesLaw_csa_20140227_31-337_faqs-guidance-31-103_2.htm)]
    - CRM2 Planning Tips: Email sent to CCOs of all registered dealers and advisers as of March 7, 2014 [[http://www.osc.gov.on.ca/documents/en/Dealers/eb\\_20140307\\_crm2-faq-published.pdf](http://www.osc.gov.on.ca/documents/en/Dealers/eb_20140307_crm2-faq-published.pdf)]
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# Additional Web Links

- Consolidation of NI 31-103 and Companion Policy incorporating the CRM2 amendments for ease of reference

[\[http://www.osc.gov.on.ca/documents/en/Securities-Category3/ni\\_20140501\\_31-103\\_unofficial-consolidated.pdf\]](http://www.osc.gov.on.ca/documents/en/Securities-Category3/ni_20140501_31-103_unofficial-consolidated.pdf)

- National Policy 11-201 *Electronic Delivery of Documents*

[\[http://www.osc.gov.on.ca/en/SecuritiesLaw\\_pol\\_20111118\\_11-201\\_amd-electronic.htm\]](http://www.osc.gov.on.ca/en/SecuritiesLaw_pol_20111118_11-201_amd-electronic.htm)

# Questions?

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