IFIC THE INVESTMENT FUNDS INSTITUTE OF CANADA | L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA

PREPARING CRM2 REPORTS FOR YOUR CLIENTS

A GUIDE FOR MUTUAL FUND DEALERS

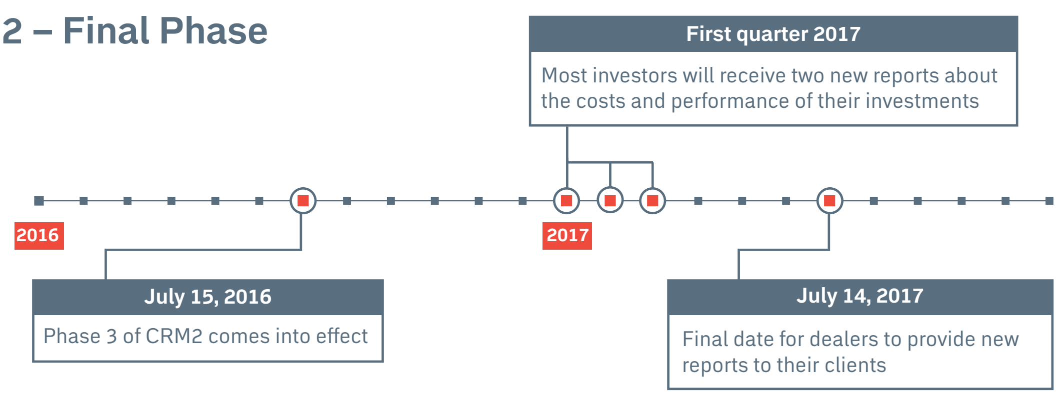
The third and final phase of CRM2 is underway. Sometime between **July 15, 2016 and July 14, 2017**, dealers must issue an account-level report on the performance of each client's investments over several time periods, along with a report on charges and compensation.

Most dealers are planning to issue the first set of these annual reports to their clients early in 2017, reporting information for the 2016 calendar year.

This guide provides details of key requirements for both reports, along with practical tips on how to ensure your reports achieve regulatory goals while strengthening the investor-advisor relationship. It includes references to the *Model Report on Charges and Compensation* and the *Model Report on Investment Performance*. These model reports were developed by IFIC members and staff in April 2015 to help the industry develop effective disclosure materials.

Please note that the regulators may issue clarifying FAQs or other documents on implementation matters. It is recommended that dealers check these documents before finalizing their reports to investors.

CRM2 – Final Phase



Measuring Success

As you design your reports, keep in mind that the purpose of CRM2 is to ensure that all investors receive timely, easy-to-understand information about the cost and performance of their investments so that they can have better discussions with their advisors and make more informed decisions.

CRM2 offers the industry a significant opportunity to realize these regulatory goals while strengthening the investor-advisor relationship. Ways to achieve this include:

- Using a common approach where possible, such as in the methodology used to calculate money-weighted rates of return, and consistent plain language to describe important terms (e.g., market value, benchmark, money-weighted rate of return, front-end commission, deferred sales charge and trailing commission). Plain language descriptions of these terms have been developed through significant industry collaboration and are available at the back of this publication and on IFIC's website.
- Providing enough information to make the reports meaningful to clients without overwhelming them with too much detail. IFIC's model reports reflect the level of information put forward in the CSA's skeleton reports, enhanced with clear descriptions and colourful graphics to facilitate understanding.
- Ensuring advisors are prepared to:
    - Use *Fund Facts* to discuss the potential benefits, costs and risks of new investments before the client purchases them.
    - Clearly describe to their clients what dealers are paid, along with the services the client receives from the dealer and the advisor.
    - Explain how the client's individual investments have performed, taking into account the timing of the client's purchases and withdrawals (i.e., using a money-weighted rate of return), and how this differs from a fund's performance and the performance of the fund's benchmarks, if any (i.e., time-weighted rate of return).

Delivery of a consistent experience to investors – one that reflects the spirit of CRM2 with plain language, simple designs and clear explanations – will be key to achieving good outcomes for investors.

Performance information must be presented using text, tables and charts in a manner that is as understandable as possible to investors.

Dealers are reminded to consider the visual needs of seniors in the design of their reports.

Time Periods Covered in the Reports

Both reports will cover the same 12-month period and must be delivered together. They can be combined with the most recent quarterly account statement, included with the account statement, or sent within 10 days after the account statement has been sent.

Dealers who are unable to provide data since the account was opened should make best efforts to go as far back as possible to meet the requirement to provide 1-year, 3-year, 5-year and 10-year performance information. In these cases, a dealer should have a reasonable basis for selecting that date (i.e., it is linked to a system conversion). Dealers are not permitted to select an inception date solely on the basis that use of that date would present better returns.

Since inception dates could differ from firm to firm, or for categories of business within a firm, it would be helpful to inform clients about the choice of date, using language along the following lines:

We may not have complete historical data about your account for the full period that you have been with us. The "inception date" that we have listed on your account is the earliest date for which we have full historical data. Over time, you will receive 1-year, 3-year, 5-year and 10-year data on an ongoing basis based on the inception date in this report.

Industry Collaboration

The mutual funds industry is collaborating to develop materials that will help dealers achieve the goals of CRM2 – to help investors make more informed decisions by improving their understanding of the cost and performance of their investment products and advisory services.

Our materials illustrate what can be achieved when stakeholders work collaboratively in the interest of the investor. Dozens of people from IFIC member companies are participating in various IFIC committees to share information and reach consensus on implementation issues related to CRM2 and other regulatory topics.

Widespread use of these materials – which feature plain language, simple designs, and clear explanations – will deliver a consistent experience to investors and demonstrate the industry's commitment to achieve positive outcomes for investors.

IFIC encourages the industry to take a uniform approach to CRM2 reporting in the interest of investors by adopting the approach reflected in these materials.

Report on Charges and Compensation

Dealers are required to include all charges and compensation for all registrable securities that they distribute to the client.

The Mutual Fund Dealers Association of Canada (MFDA) strongly encourages dealers to disclose charges and compensation for all investments that the client has purchased through the member, including segregated fund contracts, annuities and GICs. The MFDA has stated that this disclosure will further assist investor decision-making and is consistent with the obligation of MFDA members to deal fairly, honestly and in good faith with their clients. If it is impractical to report on these investments, the report must identify them and indicate that compensation was received for these investments but that it is not included in the report.

The chart on page 2 of IFIC's model report lists the types of costs that would generally be charged to clients' accounts. If there are costs charged to your clients' accounts that are not captured by this list, include them by adding a line to your charges and compensation reports.

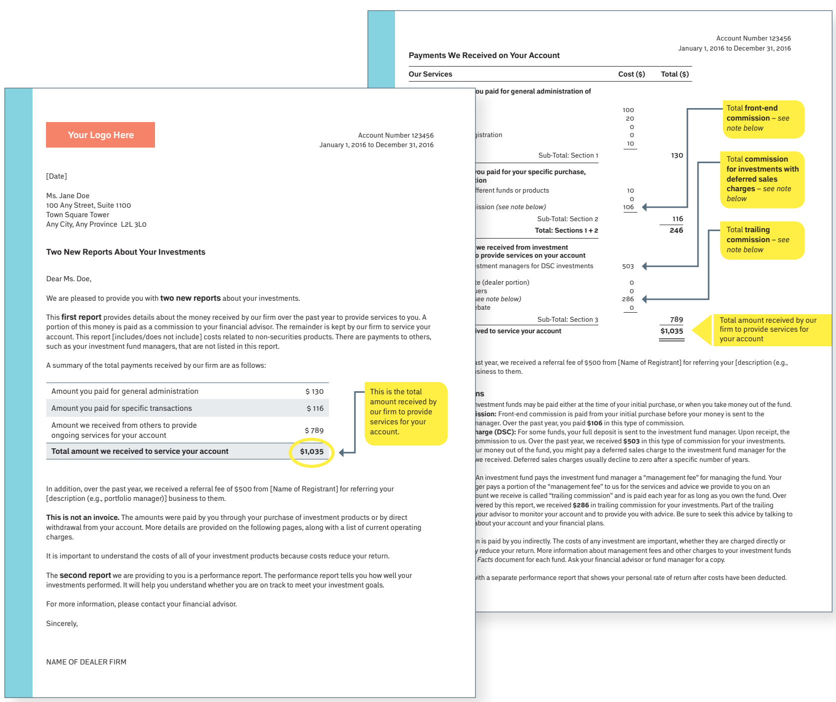
Operating Charges

The schedule that lists operating charges (page 3 of IFIC's model report) should contain only those charges that are generally applicable to the client's account.

Referral Fees

Referral fees received for securities-related activities in support of a client who has been referred to another registrant are to be reported at the client level (rather than the account level). The information can be provided either within the charges and compensation report or in a separate document. In IFIC's model report, referral fees are listed in the covering letter and repeated on the next page because some dealers might not use a covering letter in future years.

Referral fees received from an entity for non-securities services provided to a client, such as referral fees paid by a mortgage broker, are not required to be reported.



Your Logo Here

Account Number 123456
January 1, 2016 to December 31, 2016

[Date]

Ms. Jane Doe
100 Any Street, Suite 1100
Town Square Tower
Any City, Any Province L2L 3L0

Two New Reports About Your Investments

Dear Ms. Doe,

We are pleased to provide you with **two new reports** about your investments.

This **first report** provides details about the money received by our firm over the past year to provide services to you. A portion of this money is paid as a commission to your financial advisor. The remainder is kept by our firm to service your account. This report [includes/does not include] costs related to non-securities products. There are payments to others, such as your investment fund managers, that are not listed in this report.

A summary of the total payments received by our firm are as follows:

Amount you paid for general administration	$ 130
Amount you paid for specific transactions	$ 116
Amount we received from others to provide ongoing services for your account	$ 789
Total amount we received to service your account	**$1,035**

This is the total amount received by our firm to provide services for your account.

In addition, over the past year, we received a referral fee of $500 from [Name of Registrant] for referring your [description (e.g., portfolio manager)] business to them.

This is not an invoice. The amounts were paid by you through your purchase of investment products or by direct withdrawal from your account. More details are provided on the following pages, along with a list of current operating charges.

It is important to understand the costs of all of your investment products because costs reduce your return.

The **second report** we are providing to you is a performance report. The performance report tells you how well your investments performed. It will help you understand whether you are on track to meet your investment goals.

For more information, please contact your financial advisor.

Sincerely,

NAME OF DEALER FIRM

Report on Investment Performance

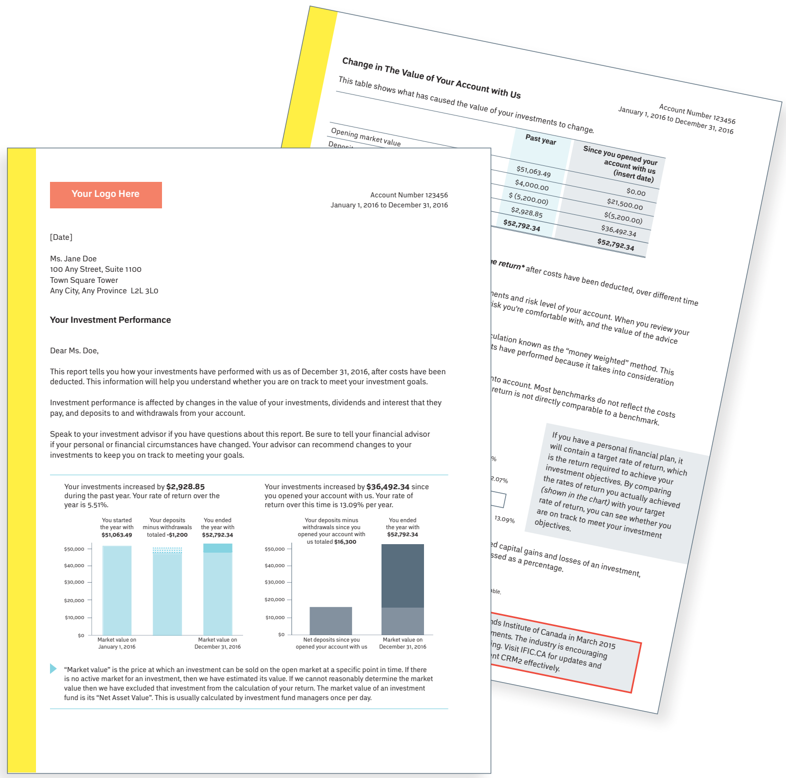
The performance report must include all assets in the client's account, including all investments required to be reported on the account statement, as well as cash.

The CSA encourages dealers to use charts and graphs to make the information easier for investors to absorb. IFIC's model report provides charts showing performance over one year and since inception.

In order for these charts to be as clear as possible, it is recommended that dealers use a light colour or light hatching for net withdrawals or losses, and a dark colour to depict net deposits and gains. The base amount should be depicted by a middle tone.

Where the client's personal total percentage return is provided, reference is made to the investor's target rate of return. Some dealers might wish to insert the client's target rate into this section.

If you wish to incorporate a description of benchmarks into this material, please refer to the plain language definition in the last section of this guide.



Money-Weighted Rate of Return (IRR Formula)

Dealers are required to use a generally accepted money-weighted formula to provide clients with their personal rates of return.

Discussions on various IFIC committees has led industry members to conclude that a common approach will better assist clients' understanding of their performance reports and facilitate client conversations.

Members of IFIC support the use of the Internal Rate of Return (IRR) formula shown on the right to calculate money-weighted rate of return.

$$NPV = \sum_{n=0}^{N} \frac{C_n}{(1+r)^n} = 0$$

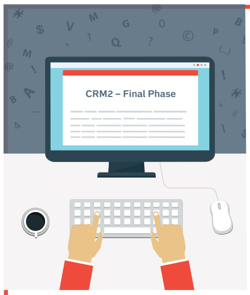
Where:

NPV = net present value
N = number of periods
n = period
C = external cash flow
r = internal rate of return

Advisor Basics

Encourage your advisors to share the following information with their clients over the next several months, prior to the release of the new reports:

- Next year, you will begin to receive two new reports about your investments from each dealer and portfolio manager with whom you have an account. These new reports will provide information about all of the securities that you own, including mutual funds. They are being provided in addition to the quarterly account statements that you already receive. The two new reports will be sent to you **once per year** – either with your current quarterly account statement or separately.
- The report on charges and compensation provides you with details about the money received by the **dealer firm** over the previous year to provide services to you. **It does not indicate** how much is paid to the advisor from your account. Each dealer firm determines this amount differently, based on its business model and split in responsibilities between the firm and the advisor.
- The report on charges and compensation will **not** tell you the **total** cost of your investments. It will tell you the amount paid directly or indirectly through your account to the dealer firm. For mutual funds, it does not include the amount paid to the investment fund manager. For an understanding of the total cost of a mutual fund, you can review the fund's management expense ratio (MER), which can be found in the *Fund Facts* document for the individual mutual funds, as well as the fund's financial statements.
- The report on investment performance will provide your personal rate of return. Your personal rate of return is based on your specific deposits into and withdrawals out of your account, dividends and interest earned from your investments and credited to your account, and changes in the value of the securities held in your account. Since each investor has a different combination of deposits and withdrawals, and a different mix of investments, each investor will have a different personal rate of return.
- Benchmarks may help us understand how a fund has performed over a period of time, but they are not relevant comparisons to your personal rate of return. This is because the benchmark does not take into account the timing of your individual day-to-day deposits or withdrawals. You should compare your personal rate of return to your target rate of return to evaluate whether you are on track to meet your investment goals.



Advisor Training

IFIC's education arm, IFSE Institute, has launched a continuing education module designed to teach financial advisors about disclosure requirements and advisor obligations under CRM2.

The module includes a sample account statement, explanations of key elements of the account statement, and sample cost and performance reports.

The course presents advisor-client conversations on key concepts, such as individual versus fund performance measurement, book cost, suitability and cost disclosure.

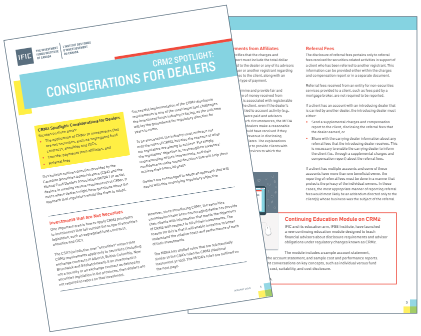
Plain Language Descriptions of Key Terms

Benchmark	A benchmark is information that helps you compare performance. Students compare their marks to the class average to understand how well they did. In the same way, an "investment benchmark" helps you understand how well your investments performed. Investment benchmarks are usually a group of securities known as a "market index". One common example is the S&P/TSX Composite Index. There are many different benchmarks and it is important to use the right one. Most benchmarks do not reflect the costs of managing and operating a fund, so your personal rate of return is not directly comparable to a benchmark.
Deferred sales charge (DSC)	When you buy a fund with a deferred sales charge (DSC), 100% of your money is invested in the mutual fund, and the fund manager pays a commission to your dealer. This type of fund encourages long-term savings because the longer you own it, the less you'll be charged when you sell it. The DSC declines every year according to a fixed schedule and if you own it long enough (typically five to seven years), the DSC will reach zero.
Front-end commission	Front-end commission is paid to your dealer from your initial purchase before your money is invested in the fund(s) that you have chosen.
Market value	The price at which an investment can be sold at a specific point in time. The market value of your investment funds changes daily. Therefore, the market value of your funds will always be linked to a specific date, such as the beginning of a statement period or the date of purchase.
Money-weighted rate of return	The "money-weighted rate of return" measures how well your account has performed. It takes into consideration the timing of your personal deposits and withdrawals, as well as most of the costs that are charged to your account.
Target rate of return	A "target rate of return" is the return that your investments need to earn in order to achieve your investment objectives. By comparing the rates of return you actually achieved with your target rate of return, you can see whether you are on track to meet your goals.
Trailing commission	An investment fund pays the investment fund manager a "management fee" for managing the fund. The investment fund manager pays a portion of the management fee to your dealer firm for the services and advice that the dealer provides to you on an ongoing basis. The portion of the management fee that the dealer receives is called "trailing commission" and is paid regularly for as long as you own the fund.

Resources

IFIC has prepared a series of materials to help the industry and investors prepare for CRM2 changes. IFIC's model reports and other useful tools are available for the use of all dealers (whether or not they are members of IFIC) at IFIC.CA > Member Centre > Member Resources.

More tools will be added over the next several months, so please visit often to obtain the latest information.



CRM2 Spotlight: Considerations for Dealers

This bulletin outlines direction provided by the Canadian Securities Administrators and the MFDA to assist dealers in meeting various requirements of CRM2. It focuses on three areas: the application of CRM2 to investments that are not securities, such as segregated fund contracts, annuities and GICs; transfer payments from affiliates; and referral fees.

Advisor Insights – CRM2 Myths and Facts

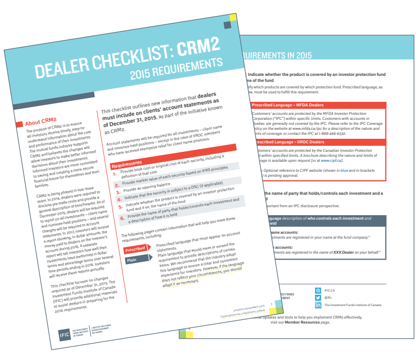
This fact sheet focuses on frequent factual errors observed in media coverage about the timing and content of CRM2 reporting requirements. It has been prepared to provide advisors with accurate information about key aspects of CRM2. The same information has been provided to journalists in an effort to improve the accuracy of media coverage.

Advisor Insights – Benchmark Disclosure

This bulletin helps companies meet the 2014 requirement to provide investors with a description of benchmarks.

Advisor Insights – Pre-Trade Disclosure

This bulletin helps companies meet the 2014 pre-trade disclosure requirement.



Dealer Checklist: CRM2 – 2015 Requirements (updated November 2015)

This checklist outlines new information that dealers must include on clients' account statements as of December 31, 2015, and provides insights and practical information to help dealers meet these requirements.