

## ***CRM2: Ready or not...***

Industry perspectives on  
Client Relationship Model  
– Phase 2



## CRM2 at a glance

Banks, dealers, insurance companies with asset management businesses and asset managers are the 'registrants' that need to meet CRM2's requirements. However, some investment vehicles—notably segregated funds—are exempt from CRM2 at this time; whether they'll eventually come under the CRM2 umbrella remains to be seen.

Canada's securities regulators designed CRM2 to address the needs of retail investors and achieve two main objectives:

### 1. *Transparency in fees and performance reporting:*

CRM2 requires registrants to provide investors with clear, complete disclosure of all charges and compensation associated with the investment products and services they receive. As well, registrants must provide meaningful reporting on how their investments are performing.

### 2. *Appropriate, quality advice:*

CRM2 also compels registrants to ensure that investors have access to sound, appropriate advice from advisors working on their behalf.

### Implementation timeline

- **July 15, 2014** – Firms were required to provide pre-trade disclosure of charges for all securities transactions and report on compensation from debt securities transactions.
- **December 31, 2015** – Firms must provide enhanced client statements that detail position cost information and market value using a prescribed method.
- **July 15, 2016** – Firms must begin delivering annual reports on charges and other compensation as well as an annual investment performance report.

## Survey background

### Purpose

The objective of the Client Relationship Model – Phase 2 (CRM2), is to increase transparency in the financial advice industry. This study sought to assess the financial services firms' journey to CRM2 readiness, as well as the challenges they face and the opportunities they've identified.

### Scope

The survey examined five key areas that will be affected due to CRM2 regulations:



### CRM2 timeline



### Interview base<sup>1</sup>

#### Asset managers

Covered over half of the Canadian asset management industry based on assets under management

#### Banks

Four out of the five major banks in Canada

#### Insurance companies

Wealth management arms of the majority of the country's largest insurers



1. Collectively our interview base represents over 50% of the market based on 'Assets Under Management' as reported by the banks' annual 2014 report.

In July 2013, Canada's securities regulators introduced a set of regulatory changes as part of an ongoing effort to provide investors with more transparency and better disclosure around fees and performance. Client Relationship Model – Phase 2 (CRM2), as these changes are collectively known, is meant to increase Canadians' confidence in the financial advice industry.



We've now reached the mid-point of CRM2's three-year adoption period. Will Canada's financial services firms be ready? To find out, we surveyed a number of banks, insurers and asset management firms and interviewed a number of industry leaders. We wanted to understand firms' progress to date as well as the challenges they face and the opportunities they've identified.

We found a diversity of attitudes towards CRM2, and these attitudes influence how firms are approaching the implementation of the new requirements. Some firms view CRM2 as yet one more compliance exercise, while others are treating it as an opportunity to improve their customer relationships and derive meaningful business value.

In general, however, Canada's financial services firms have rapidly discovered that CRM2 is proving to be more work than anticipated. In some cases dedicated project management offices have been established to oversee the complex, sprawling work of implementation as project budgets rise into the millions in many cases. While some firms were quick to grasp CRM2's impact on everything from IT to advisor networks and customers themselves, others are only now coming to realize just how big CRM2 can be.

In this report, we explore some of the themes that emerged out of our conversations with some of the industry leaders. If you wish to discuss any of the findings further, please do not hesitate to contact our CRM2 team or me at 416-869-8678.

A handwritten signature in black ink, appearing to read 'Raj Kothari', with a stylized flourish underneath.

**Raj Kothari**  
*National Asset and Wealth Management Leader*

## CRM2 implementation status

The story of CRM2 implementation to date is a positive one. Nearly all the firms we spoke to reported that they successfully met CRM2's 2014 milestones for pre-trade disclosures and advisor compensation. They also report that they're on track for meeting the 2015 requirements for enhanced client statements.

Looking ahead to 2016, a somewhat different picture emerges: While all the banks and most insurers report they're on track, only half of asset managers say the same. Nearly half of the asset management firms we contacted have yet to begin their 2016 implementation work.

Project Status	% of bank respondents	% of insurance respondents	% of asset management respondents	% of all respondents
<b>2014</b>				
Outstanding	0%	0%	9%	5%
Implemented	100%	100%	91%	95%
<b>2015</b>				
Not started	0%	0%	9%	5%
Implemented	0%	0%	27%	16%
On track	100%	100%	64%	79%
<b>2016</b>				
Not started	0%	25%	45%	32%
Implemented	0%	0%	0%	0%
On track	100%	75%	55%	68%





The difference may well lie in how the firms are approaching CRM2 overall. Banks and some insurers have established formal cross-functional project teams under the direction of steering committees. Other insurers have adopted CRM2 projects using a less structured approach. As for asset managers, a number of them have set up similar program offices; others haven't moved beyond talking about the idea; and a small number have no program in place at all.

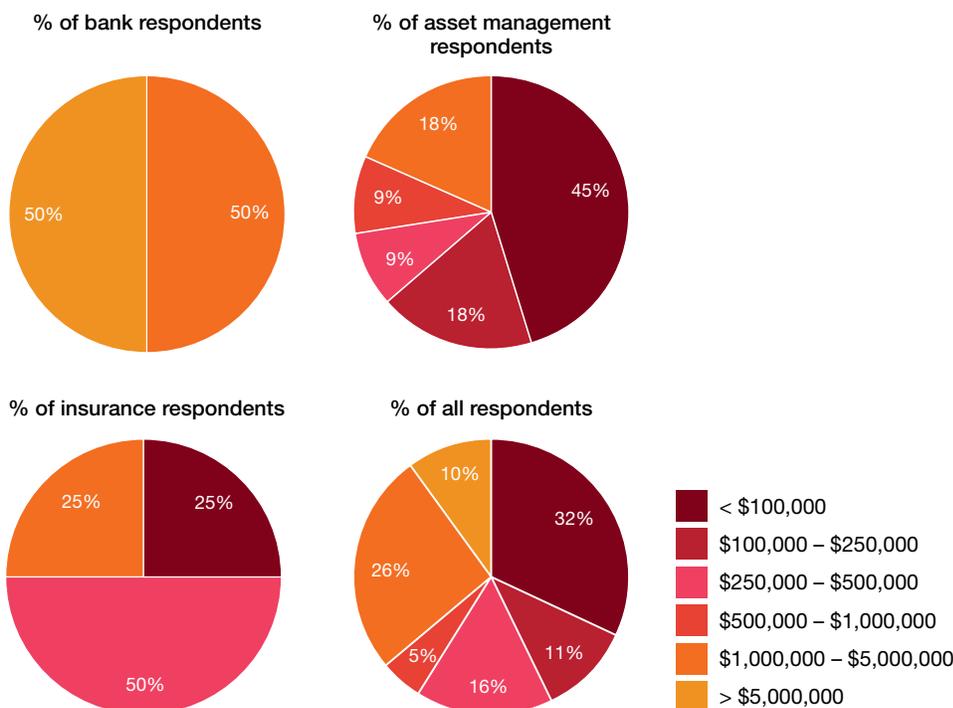
The decision of the banks and their insurer counterparts can be seen as a reflection of their organizations' complexity and their experience with large-scale change implementations. That's true—but we also see a different factor at play.

Through our conversations, it became very clear that most asset management firms and insurers view CRM2 as a compliance matter. As a result, they're taking a highly tactical approach, doing only what's needed to meet the requirements. This is in part due to the fact that asset managers depend on their third-party outsourcers to manage the communication requirements with clients. They hope that standard client statements will suffice—otherwise there are high costs associated with customizing the statements.

The banks, in contrast, see CRM2 strategically. The new requirements are a catalyst for wider change and an opportunity to accomplish other objectives—from improving data quality or integrating IT systems to building the brand or improving customer relationships.

These contrasting attitudes are reflected in the budgets that firms have set aside for CRM2. Banks expect to spend from \$1 million to \$10 million or more on their CRM2 effort. The majority of insurers plan to spend \$500,000 or less, while the majority of asset managers expect to spend \$250,000 or less.

In our view, taking a compliance-focused approach to CRM2 represents a missed opportunity for Canada's financial services firms. We encourage firms across the sector to take a more strategic approach to CRM2, including considering whether it can be used to streamline processes or build stronger relationships with customers.



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## *Participants perspective of CRM2 regulations*

We also sought firms' perspectives on the CRM2 regulations themselves, in order to better understand which rules or requirements are causing the most concern. Those we spoke with shared several key insights.

### ***Technical complexity***

The main issues cited by firms involve technical calculations and technical implementations.

An example is concern that while statements are required to provide dollar-weighted rates of return, firms have the option of including time-weighted rates of return as well. Will firms that provide only dollar-weighted returns be at a disadvantage? Will customers be confused by statements that show returns calculated in two ways? The answers to these questions aren't clear.

Some were also concerned about discrepancies between investment cost base under CRM2 and investment cost base for tax purposes. This confusion and lack of clarity is making it difficult for firms to move forward as quickly and decisively as they might like.

### ***Clarity and consistency of interpretation***

Exacerbating these issues is a perceived lack of clarity and consistency around some regulatory requirements (e.g. which type of fees should be disclosed) and the fact that some CRM2 regulations have yet to be articulated.

### ***Aggressive timelines***

While firms are comfortable with their ability to meet the 2015 CRM2 requirements—the deadline for which has been pushed back to December 2015—they expect meeting the July 2016 requirements will take significant effort. In particular, firms are concerned about the complexity of CRM2's Investment Industry Regulatory Organization of Canada (IIROC) requirements.

### ***Advisor education and training***

There's broad agreement that it's absolutely critical that advisors put effort into thoroughly understanding the CRM2 requirements surrounding fee and cost disclosures. CRM2 will profoundly change the relationship dynamic between financial advisors and their customers—and advisors have to be ready for it.

Advisors will need the skills to clearly explain to customers what various fees and charges are for, and articulate the value those costs represent. They will need to have the knowledge and ability to answer customers' questions and concerns.

### ***Information overload for investors***

While CRM2 is designed to improve transparency and disclosure around investment fees and performance, many firms are worried it will actually have the opposite effect. Will customers be able to make sense of their new statements, or be overloaded by the new information? Will they be able to understand the nuances of the costs, fees and performance information now set out before them?

What firms fear is that CRM2 changes could spark a backlash from customers as they may fail to see value provided for the fees and charges now being shared with them. This may result in investors going it alone without professional advice. Such concerns reinforce the need for firms and advisors to persuade customers that they're getting value for their money.

## Improved transparency and customer experience

The majority of firms we surveyed believe that CRM2 will, in the end, improve transparency and customers' understanding of the cost of advice, the role of the advisor, fees, and investment performance.

Do you anticipate that CRM2 can add additional value to enhance the client perception of product/firm/advisor experience?	% of bank respondents	% of insurance respondents	% of asset management respondents	% of all respondents
Enhanced:				
Client understanding of fees	100%	75%	55%	68%
Client understanding of performance	100%	50%	36%	53%
Client understanding of role of advisor	100%	75%	36%	58%
Client understanding of cost of advice	100%	75%	73%	79%
Perception of firm due to greater transparency	75%	50%	36%	47%
Perception of advisor due to greater transparency	75%	75%	36%	53%
Other	25%	25%	18%	21%

The extent to which this happens will depend in large part on how effectively firms communicate with their customers. While banks are making a concerted effort to engage their customers in a dialogue around the new reporting requirements, insurers are only just starting to have conversations—and asset managers are, for the most part, doing little, as their dealer networks will be primarily responsible for the communication. However, it is important to note that investors could overlook this important information when it's contained in all-too-familiar—and rarely read—emails and online or mailed statements and communications.

As well, few firms have given much consideration to how to tailor their CRM2 communications—not to mention the statements they'll need to provide—to best suit the needs of different customer segments. The sophistication and information needs of a baby-boomer high net worth investor are

likely to be very different from a millennial taking their first steps into investing. One may crave a highly personal approach; the other may wish for little more beyond a statement they can easily digest on their tablet or smartphone. While CRM2 may require the same information to be delivered to all investors, that doesn't mean it should be delivered in an identical fashion. As well, the value proposition of the various dealers range from highly bespoke to do-it-yourself and one would expect a differentiated delivery.

What is certain is that firms and advisors alike should be proactive in discussing what CRM2 means to their customers and starting the conversation around fees, costs and performance. This will lay down a solid foundation upon which to have more in-depth discussions in the months and years to come—and it may provide firms with the chance to manage customer expectations about their investments.

## Advisor experience

Banks, insurers and asset managers believe that 74% of advisors are concerned about the impact of CRM2, but are less anxious about the loss of clients.

They may have a point. In a survey of mutual fund investors we conducted in 2014, 96% of investors were satisfied with their current advisor, and 44% had been with the same advisor for more than 10 years. Given this level of customer loyalty—or inertia, depending on your perspective—CRM2 revelations may not be enough to provoke customers into looking elsewhere.

Some advisors are considering a pre-emptive move to change their business model entirely—however, we believe few are equipped to bring off such a fundamental change successfully on their own.

Advisors concerned about impact of CRM2 on their practice area, and their asset base and therefore income?	% of bank respondents	% of insurance respondents	% of asset management respondents	% of all respondents
Yes	75%	75%	64%	74%
No	0%	0%	0%	5%
Unsure	25%	25%	36%	31%
If Yes:				
Client concerns with amount of fees	75%	50%	45%	53%
Client discussion on value of advice	50%	50%	45%	47%
Changing their business model	50%	50%	36%	42%
Complexity of changes and communication thereof to clients	75%	50%	36%	47%
Loss of clients to (lower) fee based firms/advisors	0%	25%	27%	21%
Transitioning their business/loss of income on short-medium term	25%	25%	27%	26%
Other	50%	0%	0%	11%

Truth in transparency: Findings from PwC's mutual fund investor survey. PwC. November 2014.

## IT and systems changes

Meeting CRM2's 2015 and 2016 requirements for enhanced statements and more detailed cost and performance information will heavily depend on firms' ability to update and upgrade their relevant IT systems. Not surprisingly, firms generally see these technology matters as the most costly—and challenging—part of CRM2 implementation. Banks in particular have found the technology aspects of CRM2 to be complex and slow going, because they must develop the tools and processes needed to integrate a host of systems across multiple business units.

In contrast to the banks' mostly do-it-yourself approach (blending in-house and third party vendors on projects), insurers and asset managers are largely relying on outsourced service providers to help them meet the requirements of CRM2. While this approach may save these firms some time, cost and frustration, it's not without risk. Will these third parties be ready to provide the statements and other data in time for CRM2 deadlines? Will wildly different statement formats confuse customers? It will be vital that those firms that choose to outsource aspects of their CRM2 responsibilities stay in close contact with their providers to understand what they and their customers will receive—and that they'll receive it with 100% accuracy and on time.

Are there external 3rd party IT vendors supporting the implementation?	% of bank respondents	% of insurance respondents	% of asset management respondents	% of all respondents
No, all in house	0%	0%	18%	11%
Some support (25%)	0%	0%	18%	11%
50%	75%	0%	9%	21%
Mostly outsourced (75%)	25%	75%	18%	32%
All outsourced	0%	0%	36%	21%

One of the more encouraging findings of our survey is that firms are determined to automate as much of CRM2's requirements as possible. It seems very likely that few firms will find themselves resorting to cumbersome and potentially inaccurate manual workarounds in order to provide customers with the information they need.

That said, we suspect that many firms may not fully comprehend the complexity of the effort needed to meet CRM2's 2016 milestone. The 2016 requirements may seem straightforward, but the work needed to meet those requirements can be significant. Firms that expect to tackle these issues after they deal with 2015's requirements may be in for a shock—which is why we urge firms to take time *now* to better understand what's needed to meet the final requirements of CRM2.

To what extent are the solutions a manual workaround (e.g. using spreadsheets) versus automation?	% of bank respondents	% of insurance respondents	% of asset management respondents	% of all respondents
0% (all automatic)	50%	0%	45%	37%
25%	50%	50%	27%	37%
50%	0%	0%	0%	0%
75%	0%	0%	0%	0%
100% (all manual)	0%	0%	9%	5%
Unsure	0%	50%	19%	21%

## Managing change—challenges and opportunities

Change is hard—and as every organization knows, it can prove to be much more complex and time-consuming than expected. And after more than a year and a half of implementing CRM2, the firms we spoke with were quick to identify the many challenges they’ve encountered in their journey.

### Firms frustrated by technology issues

Firms cite resource constraints and technology issues as significant challenges to their CRM2 efforts. The technology implications of CRM2 are proving to be the most expensive aspect of the project, not to mention one of the most complicated. Addressing the new rules has required technology and systems integration projects. As a result, firms look to bring together IT systems originally developed to meet the unique needs of separate business units. Compounding the challenge for larger firms is the fact that many of these IT challenges are a result of decades-old legacy systems never designed with today’s needs in mind.

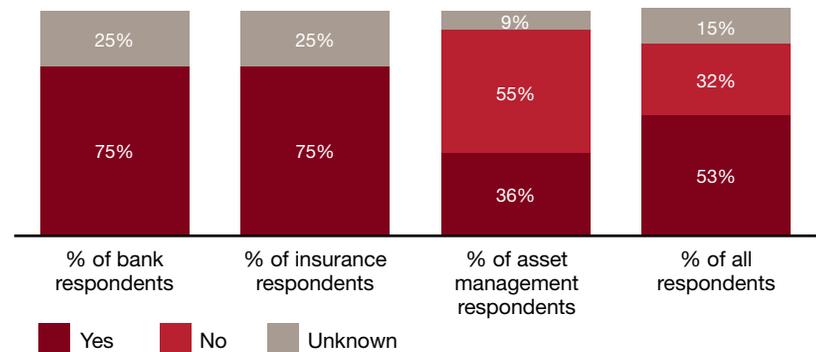
### Regulatory arbitrage a concern

Some of those we spoke with raised the spectre of potential “regulatory arbitrage” as segregated funds sold by insurers lie outside CRM2’s scope. The sales process and disclosure requirements are less and dually licensed advisors may choose a simpler path and avoid regulations that apply to mutual funds and other securities. These funds may provide a cost advantage to the asset manager as the cost of supporting compliant disclosure are not insignificant.

### Are advisors up to the communication task?

We heard numerous concerns voiced about the challenges advisors face in clearly communicating with clients about the changes required by CRM2—and the new information being shared. Firms will need training programs to ensure advisors are ready to face this challenge.

### Change management plan to assist advisors



### Despite the challenges, firms see CRM2’s benefits as well

We weren’t entirely surprised that firms were so quick to outline the challenges they face in implementing CRM2. As our conversations progressed, however, many of those we spoke with acknowledged that there were some important benefits to the effort.

Larger organizations were most likely to see the strategic value in CRM2 on a number of fronts. In operational terms, these firms felt CRM2 provided a useful opportunity to review their processes and data, align and centralize key functions and identify new efficiencies. Some felt that CRM2 opens up new ways to differentiate in a crowded market, even as transparency itself becomes table stakes—from providing clearer explanations to highlighting waived fees.

From an advisor’s perspective, CRM2 can be seen as a springboard for promoting more open communication between advisors and their customers. Leading advisors are already having this sort of open dialogue, but CRM2 offers an opportunity for others to catch up.

Investors, of course, stand to realize the greatest benefits from CRM2. They’ll gain a clearer, consistent view into what goes on “behind the scenes” of their investment portfolios—enabling them to better compare what different investment firms offer in terms of service and value. This richer information, coupled with greater attention from advisors, may well help customers feel more in control of their investments and deepen their loyalty to their advisors.

## The time is now

Implementing regulatory change is rarely straightforward, and CRM2 is proving to be no exception. We're encouraged by the optimism shown by Canadian banks, insurers and asset managers, who are relatively confident that they'll meet CRM2's timeframe. We urge these firms to not underestimate the time and effort required by the 2015 and 2016 milestones: CRM2 is more complex than it first appears.

We believe that companies should start with the following actions:

### 1. Create a differentiation strategy:

Identify the unique value propositions for both investors and advisors, then build the tools and applications that distinguish you from the competition.

### 2. Invest in internal change management and communications:

Internally bring all stakeholders together to provide training on new reporting, calculations and how to discuss the changes. Externally, it's never too early to begin the investor education process on how reporting will change.

### 3. Set project milestones and metrics for success post-implementation:

Create a checklist of implementation measures of success, and track benefits and misses starting now.

### 4. Plan for outsourcing support for delivery success:

Begin to customize the communications over the course of CRM2 implementations.

We also encourage firms to regard CRM2 as much more than another compliance exercise, because to do so is to overlook potentially significant opportunities to improve their business, enhance customer relationships and secure competitive advantage. Regulatory change can, and has, provided the spark for innovative thinking and fresh approaches—there's no reason CRM2 can't do the same for Canadian financial services firms.

### For a deeper discussion of our findings, please contact:



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