INVESTIGATION SUMMARY FOR PUBLICATION PURPOSES

BACKGROUND

In 2004, Mr. O, an investment advisor with Armstrong & Quaile Associates Inc., recommended that Mr. and Mrs. H borrow a total of $200,000 to invest ($100,000 each). At the time, Mr. and Mrs. H were both retired and in their mid-sixties. They lived on a fixed income comprised of Old Age Security and Canada Pension Plan payments. In addition to their modest home valued at $149,000, they owned a residence in Florida valued at $89,000, but they still had an outstanding mortgage of $110,000. Their investments at Armstrong & Quaile totaled about $217,740, making their total net worth approximately $345,740.

Mr. O's recommendation to borrow $200,000 to invest was part of a "RRIF meltdown strategy". Mr. O recommended that Mr. and Mrs. H each borrow $100,000 and invest half in mutual funds and half in segregated funds. He recommended that they withdraw money from their RRIF accounts to make interest payments on their loans. Mr. and Mrs. H say Mr. O told them this was a safe investment strategy that would make them some money.

At first the strategy did fairly well and the Hs even took some "profits" early on to pay for some expenses as Mr. O said they could. However, over time the investments they purchased with the borrowed money began to decline in value. Mr. and Mrs. H say that when they raised concerns with Mr. O he told them not to worry and to continue with the strategy. They say that as their long-time advisor, they trusted him and followed his advice.

By the end of 2012, the Hs were so concerned they could not afford the interest payments on the loans that they sold the investments to pay down the loans as much as possible. The Hs still have outstanding loans and we calculate they have sustained in excess of $34,000 in losses to date on the part of the strategy involving mutual funds.

COMPLAINT

Mr. and Mrs. H complained to Armstrong & Quaile that:

- They understood that the investments they purchased using borrowed money were guaranteed and Mr. O assured them there would be no financial risk as long as they held the funds for ten years;
- They only found out in 2010, after reviewing their investments with their new advisors, that only half of their funds were guaranteed at maturity;
- As of July 2010, their mutual funds had declined by $30,000; and,
- Based on their financial circumstances and minimal government pensions, Mr. O should not have recommended they borrow to purchase investments that were not guaranteed.

Mr. and Mrs. H requested Armstrong & Quaile compensate them for their losses.

ARMSTRONG & QUAILE'S RESPONSE

Armstrong & Quaile responded to Mr. and Mrs. H saying:

- Based on their documented Know-Your-Client information, a leverage strategy was appropriate for them;
- It has no record of any instructions to purchase only segregated funds with the borrowed money;
- It cannot determine what Mr. O told them;
- It has no knowledge of the status of their current investments since they transferred to another firm; and,
- Their current advisor should be able to recommend an investment strategy to recoup most, if not all, of their losses.

Armstrong & Quaile did not offer Mr. and Mrs. H any compensation.

OBSI FINDINGS

OBSI does not investigate complaints regarding segregated funds (an insurance product), therefore we limited the scope of our investigation to the suitability of Mr. O's recommendation to borrow $100,000 to purchase mutual funds. That being said, we did consider as part of our affordability analysis that the Hs had borrowed an additional $100,000 to purchase segregated funds.

The investigation and analysis of the part of the complaint involving segregated funds was referred to the Ombudservice for Life and Health Insurance (OLHI), the ombudsman for life and health insurers, manufacturers of segregated funds.

Borrowing to invest (often referred to as leveraging or leveraged investing) is generally considered a risky strategy. Leveraging may be considered suitable for investors who have sufficient knowledge to understand the risks, who are willing and able to tolerate the potentially significant risks, who can afford to make loan interest payments without relying on distributions from the leveraged investments, and who have sufficient assets to repay the loan if the leveraged investments decline in value and/or the strategy fails.

Prior to Mr. O's recommendation, the Hs had never borrowed money to invest. During our interviews, we found that the Hs did not understand the risks associated with the leverage strategy. While there was some risk disclosure on the loan applications the Hs signed, we find Mr. O did not provide them with a balanced presentation of the risks involved. All of the illustrations Mr. O provided them emphasized only positive results. None of the illustrations explained the potential downside and risks associated with borrowing to invest. Armstrong & Quaile's only internal policy regarding leverage at the time was that advisors were required to have clients sign an Armstrong & Quaile Leverage Disclosure Document. However, neither Mr. O nor Armstrong & Quaile were able to provide us with a copy signed by the Hs.

The Hs were not willing or able to take significant risk with their investments. If the strategy failed they would be forced to withdraw money from their limited retirement savings jeopardizing their financial situation. They also could not afford to make the interest payments on the loan from their limited income.

Mr. O acknowledged during our investigation that he did not assess the affordability of the leverage strategy. He said that was the responsibility of the loan provider. We do not agree. It is the responsibility of advisors to ensure their recommendations are suitable for their clients.

We recommended that Armstrong & Quaile compensate the Hs for their losses but Armstrong & Quaile has refused to compensate them any amount.