



## INVESTIGATION REPORT

**Date** June 26, 2020  
**Consumer** Ms. X  
**Participating Firm** WealthTerra Capital Management (WealthTerra)

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### Overview

In 2011, Ms. X was 44 years old and self-employed, offering services such as house cleaning and pet sitting. She had an annual income of \$20,000. Ms. X was recently divorced and had two young children living with her full time. Ms. X had a Locked-In Retirement Account (LIRA) worth approximately \$46,000 that held pension money she received in the early 2000s from a former employer. Her only other asset was \$12,000 in emergency savings, making her total net worth \$58,000.

Ms. X was not looking for an investment advisor but decided to meet with a WealthTerra representative, based on the recommendation from a mother at her children's school. In October 2011, Ms. X opened a LIRA with WealthTerra and transferred in cash totaling \$46,372. The firm representative recommended she invest her retirement fund in high-risk exempt market securities.

### Key findings

Ms. X's account was unsuitably invested in high-risk exempt market securities.

As a result of being unsuitably invested, Ms. X incurred financial harm of \$50,810.

WealthTerra is responsible for the financial harm Ms. X incurred.

### Recommendation

We recommend WealthTerra compensate Ms. X \$50,810 and, to ensure no possibility of double recovery, that Ms. X transfer all rights and interests in her exempt market securities to WealthTerra.

We considered and investigated all the concerns Ms. X raised and the counterarguments from WealthTerra. This report outlines our decision which is based on three key findings. We note that WealthTerra disagrees with our findings on these issues. The appendices contain our financial harm calculations.

### **Primary consumer issues**

Ms. X is asking WealthTerra to compensate her for her financial harm because:

- her investments were unsuitable for her
- she incurred financial harm as a result of her unsuitable investments

### **WealthTerra's primary objections**

WealthTerra refused to compensate Ms. X as OBSI recommends because:

- it says Ms. X accepted the risk of her investments and that they were suitable for her
- Ms. X did not question the suitability of her investments for nine years

### **Our recommendation**

We recommend that WealthTerra compensate Ms. X \$50,810. To ensure no possibility of double recovery, we also recommend that Ms. X transfer all rights and interests in her exempt market securities to WealthTerra. We make this recommendation because:

- Ms. X's account was unsuitably invested in higher-risk exempt market securities
- as a result of being unsuitably invested, Ms. X incurred financial harm
- WealthTerra is responsible for the financial harm Ms. X incurred

## Finding one – Ms. X’s account was unsuitably invested in higher-risk exempt market securities

We find that:

- Ms. X had a low to medium risk tolerance
- the investments in Ms. X’s account exceeded her risk tolerance

### Ms. X had a low to medium risk tolerance

In 2011, Ms. X was recently divorced and living full-time with her two young children. She was self-employed and offered services such as house cleaning and pet sitting for clients. She earned an annual income of approximately \$20,000 and was living with her mother as she could not afford to live on her own.

A mother at the school Ms. X’s children attended was an insurance agent. She offered to introduce Ms. X to her boss and the WealthTerra representative to discuss insurance and investment options. Ms. X met with all three parties approximately six times. During these meetings, the WealthTerra representative recommended Ms. X transfer her LIRA to WealthTerra and invest in exempt market securities.

The account opening documents Ms. X signed indicated she had:

- an annual income of \$20,000
- a net worth of \$58,000, comprised entirely of liquid assets
- good investment knowledge
- a five to seven-year time horizon
- a long-term growth investment objective
- a “high risk / high return” risk tolerance

### *Annual income and net worth*

All parties agree that, in 2011, Ms. X was self employed with an annual income of \$20,000 and a total net worth of \$58,000. Ms. X’s net worth was comprised of her LIRA (\$46,000) and emergency savings (\$12,000).

### *Investment knowledge*

During our interview, Ms. X told us she had minimal investment knowledge. Prior to opening an account at WealthTerra, she had invested \$100 a month in mutual funds which she withdrew in 1997 to buy a condo. Her only other investment experience was opening a LIRA in the early 2000s, when she received a pension payout from her former employer. Ms. X does not remember what investments she may have held in her LIRA but said that it was held at a bank and she did not have an advisor.

The representative who worked with Ms. X is no longer employed at WealthTerra and we were unable to interview him. WealthTerra said that Ms. X attested to having good investment knowledge and understanding the concept of risk and return when she signed the account opening forms. Ms. X said she just signed the account opening forms where the firm representative told her to. There are no file notes or other evidence to indicate how the firm representative or WealthTerra concluded Ms. X had good investment knowledge in 2011.

We found Ms. X had limited investment knowledge at the time she opened her accounts at WealthTerra because:

- she had limited investment experience
- she had no prior experience investing in exempt market securities

#### *Time Horizon*

All parties agree that Ms. X had a long-term time horizon. Given Ms. X's age (44 years) and that she was relying on her investments to help fund her retirement, we found a long-term time horizon reasonable and accepted it as accurate.

#### *Investment objectives and risk tolerance*

Ms. X told us her LIRA was very important to her because it represented nearly all of her financial assets. Ms. X said that she was hoping for some growth in her investments but mainly wanted capital protection. She said she did not want high-risk as she could not afford to lose any money.

WealthTerra said Ms. X was aware she was investing in high-risk securities. As evidence, WealthTerra points to the account opening forms and risk acknowledgement forms that Ms. X signed and/or initialed indicating that she had a high-risk tolerance and understood she was investing in high-risk securities. WealthTerra also said it found a high-risk tolerance suitable for Ms. X despite her limited income and net worth because she:

- wanted higher returns
- was invested in a long-term LIRA, where she was unable to access the funds until she was 55 years old
- had a \$12,000 cash emergency fund
- could replace investment losses as she was relatively young, in her prime earning years and had the ability to significantly grow her business
- had no debt and was living rent free with her mother
- could continue to feed and house her children if she lost her entire investment

Ms. X said the firm representative completed the account opening forms at one of their meetings and told her where to sign. She said they had very little discussion about her risk tolerance, but she remembers telling him that she did not want high-risk or to lose her money. Ms. X acknowledged that they "briefly skimmed over the documents" before she signed and initialed. She says that when she asked about the high-risk disclosure on the various forms, the firm representative told her the disclosure was a formality and that the investments he was recommending were not high-risk.

The WealthTerra representative made a note on the account opening forms indicating that Ms. X wanted higher returns but that she was also unhappy with the losses her LIRA had experienced. We found no other notes or documentation in the file indicating the firm representative explored Ms. X's tolerance for losses in any detail or took any other steps to determine her risk tolerance.

While there is conflicting evidence regarding the risk tolerance discussions that took place between the firm representative and Ms. X, we find it unlikely that Ms. X would have expressed a tolerance for high levels of financial risk had she understood the nature of such risks. We find it more likely that Ms. X would have expressed a low to medium risk tolerance because:

- she was newly divorced and trying to recover financially after paying off marital debts
- she had a low income that she was using to support two young dependents
- the firm representative's note on the account opening form indicates she had an aversion to investment losses
- the WealthTerra account represented approximately 80% of her total net worth and she was relying on it to help fund her retirement
- given her precarious financial situation, she may have needed to withdraw from the account prior to retirement, pursuant to the financial hardship rules
- she could not afford to invest almost all her net worth in illiquid, high-risk investments as she did not have sufficient income to replenish significant losses
- she did not have the investment knowledge or experience to understand the risks associated with exempt market securities

Ms. X says she had a low to medium risk tolerance, which we find reasonable given her personal and financial circumstances at the time. We note that a medium risk tolerance would also have been within range of reasonableness for Ms. X, as she was relatively young and had a long-term time horizon. Based on her personal and financial circumstances, however, we find that high-risk exceeded Ms. X's risk tolerance and ability to withstand loss.

Given Ms. X's circumstances, we find it reasonable that her investment objectives would include both growth and capital preservation. Therefore, in the circumstances, we find that either a 60% medium risk and 40% low risk portfolio of investments or a 100% medium risk portfolio of investments would have been suitable for Ms. X. We have used these parameters in determining the suitability of Ms. X's investments at WealthTerra and her investment losses.

### **The investments in Ms. X's account were unsuitable because they exceeded her risk tolerance**

When Ms. X opened her LIRA at WealthTerra in 2011, the firm representative recommended she purchase the following high-risk exempt market securities:

- Walton GA Crossroads Investment Corp. Class B common shares (\$23,000)
- Sincerus (Clairmont) Investments Ltd. Bonds (\$20,700)
- Sincerus (Clairmont) Investments Ltd. Class B shares (\$2,300)

From December 2011, when Ms. X purchased these securities, until May 2020, which is the most recent valuation date, her entire account was invested in these securities.

These three securities are all high-risk, illiquid exempt market securities which exceed Ms. X's risk tolerance and were therefore unsuitable for her.

### **Finding two – As a result of being unsuitably invested, Ms. X incurred financial harm**

The accurate calculation of financial harm requires an ending or current value for all securities in the portfolio. We use market value as our ending value whenever it is available or can be calculated. Given the illiquid nature of exempt market securities, however, it is not always possible to determine their current

market value. Therefore, in cases involving securities that have been sold unsuitably and that are not possible to accurately value, we:

- calculate financial harm by assigning such securities an ending value of \$0; and
- include in our recommendation that in exchange for the payment of our recommendation amount, the securities be transferred to the firm responsible for the unsuitable sale

This ensures both accurate calculations of financial harm and that there is no double-recovery of any residual value of the securities.

### Our calculations

To calculate if a consumer has incurred financial harm, we first calculate the performance of the consumer's actual unsuitable investments. Using a comparative benchmark, we then calculate the investment performance the consumer would have experienced had they been suitably invested. The difference is the consumer's financial harm. See Appendix A for our financial harm calculations.

Our analysis demonstrates that:

- Ms. X's account decreased by \$39,564 during the period she was unsuitably invested
- had Ms. X's account been invested in 60% medium and 40% low risk securities, it would have increased by \$11,246
- had Ms. X's account been invested in 100% medium risk securities, it would have increased by \$11,841
- Ms. X's financial harm is therefore between \$50,810 (\$39,564 + \$11,246) and \$51,405 (\$39,564 + \$11,841). Given the narrowness of this range, we find it reasonable to recommend that WealthTerra compensate Ms. X \$50,810.

We used the period of December 2011, when Ms. X first purchased the exempt market securities, to May 2020, which is the most recent valuation date, for our calculations. To determine what Ms. X's investment performance would have been had the account been suitably invested, we completed the following analysis:

- we assigned an ending value of \$8,190 for the Walton investment, which was the market value reported on Ms. X's May 2020 account statement
- we assigned a \$0 ending value for the Sincerus investments as we could not accurately value these exempt market securities
- we constructed a notional balanced portfolio, comprised of 60% medium-risk and 40% low-risk investments
- we constructed a notional growth portfolio, comprised of 100% medium-risk investments
- we used the iShares Canadian Universe Bond Index ETF for our low-risk benchmark
- we used the S&P/TSX Composite Total Return index for our medium-risk benchmark
- we reduced the performance of the benchmarks by the actual and embedded fees charged

## **Finding three – WealthTerra is responsible for the financial harm Ms. X incurred**

### **WealthTerra is responsible for the actions of its advisors**

The firm representative recommended the unsuitable investments to Ms. X as WealthTerra's agent and/or employee. WealthTerra is therefore responsible for the financial harm Ms. X incurred as a result of its representative's advice.

### **Ms. X does not share responsibility for the financial harm she incurred**

WealthTerra said that Ms. X's complaint should be denied because she had nine years to raise her concerns about the suitability of her investments and did not do so. We disagree with this position because we observed that during this time, Ms. X's account statements did not reflect any investment losses or other red flags that would reasonably have caused her to be concerned about her investments. Furthermore, Ms. X did not have the investment knowledge or experience to assess the risks associated with exempt market securities. In 2017, Walton International Group entered into creditor protection and, in 2018, Ms. X's Walton investment was switched into a "roll-up corporation." She subsequently asked an advisor at another firm to review her investments and complained to WealthTerra when she learned they were unsuitable for her.

WealthTerra also argued that Ms. X is responsible for her investment losses because she signed several documents that disclosed the risks associated with exempt market securities and she therefore should reasonably have known they were high-risk investments. We found that the firm representative gave Ms. X risk disclosure documents to sign at the time of purchase and that she saw and signed them. However, as discussed above, Ms. X said that when she asked the firm representative about the high-risk disclosure, he told her it was a formality and that the investments he was recommending were not high-risk. We did not find any notes or other documentary evidence to indicate what Ms. X and the firm representative discussed regarding the risks associated with exempt market securities, other than a note in the file indicating that Ms. X had told the firm representative that she was unhappy about earlier losses in her LIRA.

Given Ms. X's limited investment knowledge and experience, we conclude that she acted reasonably in trusting that the representative and WealthTerra would recommend investments that were suitable for her. The WealthTerra representative and WealthTerra had a regulatory obligation to ensure that the investment recommendations they made were suitable and it was reasonable for Ms. X to believe that both would comply with this responsibility.

We therefore have no basis on which to find Ms. X shares responsibility for the financial harm she incurred as a result of the WealthTerra representative's unsuitable investment recommendations.

**Appendix A: Financial harm calculation for Ms. X**

*Actual vs. suitable performance of Ms. X's LIRA from December 2011 to May 2020 using a 60% medium and 40% low risk tolerance*

	<b>Actual Performance</b>	<b>Suitable Performance</b>
Value of portfolio at end of period	\$ 8,292	\$ 59,102
Less: net capital invested	\$ 46,000	\$ 46,000
Less: purchase fees and tax	\$ 1,856	\$ 1,856
Return on investment	(\$39,564)	\$ 11,246
<b>The actual portfolio underperformed the suitable portfolio by</b>		<b>\$ 50,810</b>

*Actual vs. suitable performance of Ms. X's LIRA from December 2011 to May 2020 using a 100% medium risk tolerance*

	<b>Actual Performance</b>	<b>Suitable Performance</b>
Value of portfolio at end of period	\$ 8,292	\$ 59,697
Less: net capital invested	\$ 46,000	\$ 46,000
Less: purchase fees and tax	\$ 1,856	\$ 1,856
Return on investment	(\$39,564)	\$ 11,841
<b>The actual portfolio underperformed the suitable portfolio by</b>		<b>\$ 51,405</b>