IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

Case Number: FAIS 08999/12-13/ GP 1

In the matter between:

TERESA KARWOWSKI **Complainant**

and

L LOXTON NEL AND ASSOCIATES CC **First Respondent**

LLEWELLYN CLAUDIUS LOXTON **Second Respondent**

DETERMINATION IN TERMS OF SECTION 28(1) OF THE FINANCIAL ADVISORY AND INTERMEDIARY SERVICES ACT 37 OF 2002 ('FAIS Act')

A. INTRODUCTION

[1] This is a complaint arising from a failed investment made by Complainant in the now defunct Relative Value Arbitrage Fund (RVAF), a fund that was managed and operated as a hedge fund - by one Herman Pretorius, (now deceased) - with no license of its own. Complainant's claim against Respondents are based on the latter's failure to appropriately disclose the risks involved in investing in the scheme, which Complainant was led to believe was a legitimate investment.

[2] Following the death of Herman Pretorius and the collapse of RVAF, Complainant claims Respondents, as authorised financial service providers

(FSP), failed in their duty to appropriately advise Complainant and as a result, seeks recourse against Respondents for repayment of her invested capital.

[3] In particular, and as a result of Respondents' advice, Complainant invested in RVAF. This has now been exposed as a Ponzi scheme, the result being Complainant's funds have been lost.

[4] The quintessence of Respondents' response is that they understood that they were dealing with a registered financial services provider. Further, that clients by their own choice, and whilst being aware of the risks, elected to invest in Abante Capital. Respondents further submitted that they did not provide Complainant with "financial advice or services" as defined in the Act.

B. THE PARTIES

[5] Complainant is Teresa Karwowski, an adult female, whose full contact details are on file with the Office.

[6] First respondent is L Loxton Nel and Associates CC t/a Plan Right Investments, a close corporation duly registered in accordance with the laws of South Africa with its registered business address being 10 Tiptol Avenue, Randpark Ridge, Randburg, 2194. First respondent was at all relevant times a licensed Financial Services Provider (FSP10020).

[7] Second respondent is Llewellyn Claudius Loxton, an adult male member, and key individual of the First Respondent who resides at 10 Tiptol Avenue, Randpark Ridge, Randburg, 2194.

[8] At all material times hereto, second respondent rendered advice to complainant

whilst acting on behalf of the first respondent. Respondent or Respondents must be read to mean the same person in this determination.

C. THE COMPLAINT

[9] The complaint is as follows:

9.1. That as a result of a failure on the part of Respondent to render appropriate advice Complainant has lost money.

9.2. Respondent had been Complainant's adviser since 2004. In 2010 and with Complainant and her husband wishing to invest some savings for capital growth, they met with Respondent.

9.3. The outcome was a recommended monthly investment in Allan Gray along with a R120 000, lump sum in RVAF. Complainant was introduced to RVAF by Respondent, having had no prior knowledge thereof.

9.4. Complainant was assured that although the investment carried a moderately aggressive risk, it was safe. Respondent informed complainant that he had both recommended it to some of his best clients and that he had also invested quite a large sum of money.

9.5. Complainant argues that this failed to alert her to the extent of the risks. In particular that she could lose the investment. On the contrary she was advised to make further investments in the fund.

9.6. As late as June of 2012 and in a conversation with complainant's husband, respondent again offered assurances that everything was in

order with the RVAF fund, and the high returns were attributable to good performance. Significantly, complainant's husband had inquired about the investment's sustainability, as the returns were too high.

9.7. Yet, only a few weeks later, complainant's husband was contacted by Respondent; then advising that withdrawal forms should be submitted as there were negative reports in the media. This however, was too late. The death of the Herman Pretorius and the collapse of the fund followed almost immediately thereafter.

9.8. Complainant points out that about a month before the collapse of RVAF, Respondent withdrew all his money that was invested whilst encouraging Complainant to stay in the investment.

9.9. The amount of R120 000 had been paid into the RVAF Trust on the 21st July 2010 and confirmed in a letter from respondent dated the 6th August 2010. The letter dated 21st July 2010 enclosed correspondence from Eduard Brand who was said to be acting 'for and on behalf of RVAF EN COMMANDITE PARTNERSHIP.'

9.10. Quarterly statements were emailed by respondent to complainant. In the e-mails, respondent advised that, '*additional investments can be added to this investment.'*

9.11. In her complaint, complainant mentions a risk assessment form as well as what she terms a 'letter of introduction with Abante Capital (Pty) Ltd'. Complainant states that a copy thereof was only provided by respondent in March of 2013 pursuant to the lodging of the complaint.

9.12. The risk assessment reflects complainant as a 'Moderately Aggressive' risk profile.

9.13. The introductory letter is headed 'INVESTMENT WITH ABANTE CAPITAL (PTY) LTD' and contains the following salient points:

9.13.1.'*Abante Capital is an approved investment manager with the Financial Services Board (FSB). It is a member of key hedge fund industry organizations and the management of the company has significant experience in the financial services arena. Please note that hedge funds are not regulated by the FSB in South Africa.'*

9.13.2.*'Abante Capital's arbitrage techniques are based on a combination of statistical and fundamental models that monitor the relevant markets to seek out situations where similar pockets of economic exposure are priced differently. Upon identifying such situations the company employs its funds and the funds under its control to take advantage of mis-pricing.'*

9.13.3.*'The advisor receives a once off commission of 7.5% (including VAT), in other words R7,500 (inc.VAT) per R100,000.00 invested.'*

[10] I note that this introductory letter is not written in plain language. Instead it contains complex jargon no lay person could possibly understand. On the probabilities, even if complainant read it, she would not have understood it.

[11] Having come to the conclusion that she had lost her investment and having achieved no success in resolving the matter with Respondent Complainant turned to this office. In her complaint, complainant seeks the return of the

amount invested.

D. RESPONDENTS' REPLY

[12] Before detailing respondent's reply, it should be noted that this Office has received a number of complaints regarding RVAF involving both respondent and other FSP's. For the most part the key issues are similar if not identical. Accordingly and where applicable, this Office forwarded similar notices in terms of section 27(4) of the FAIS Act in respect of the complaints and invited respondent to respond to the complaints by furnishing all documents and any other material that may support respondent's case.

[13] Respondents provided comprehensive written submissions, including a reply to complainant's comments.

[14] The crux of respondents reply follows:

14.1. Complainant and respondents spouse[1] were friends. In May of 2010 respondent was informed by his spouse that complainant wished to discuss a possible investment in 'Abante Capital's Relative Value Arbitrage Fund.'

14.2. Likely, complainant had heard about RVAF from his spouse. Complainant then met with respondent on the 7th July 2010. Complainant informed him that she wished to invest a monthly amount of R2000 alongside the capital amount.

1 At that stage also a member of the respondent.

14.3. Respondent explained the RVAF investment philosophy in detail, whilst stressing the risks involved in investing in a hedge fund. The option of investing in a portfolio of unit trusts was also offered. Then and with the documentation provided, Complainant left to discuss the matter with her husband.

14.4. Complainant, alongside her husband returned on the 16th July 2010. Both RVAF and Unit Trust funds were discussed, along with their respective risks, fees and conditions. After discussing both options with her husband Complainant elected to place the lump sum with the '*high risk one*'[2] meaning RVAF and the recurring premium in the Allan Gray Balanced Fund. Complainant was thus both aware of and accepted the risks involved. Risks, which respondent contends the complainant is able to take.

14.5. As part of his later submissions, respondent submitted that, given the circumstances under which the business was concluded the information did not constitute advice. Respondent, having merely provided information *'without any express or implied recommendation, guidance or proposal*' is of the view that no advice was rendered to complainant.

14.6. All documentation including the standard three page RVAF application form common to other matters were signed on the 16th July 2010.

14.7. As to the advice record pertaining to RVAF, respondent attached the introductory letter as referred to in paragraph 9.12 I point out that

2 Complainant's words according to respondent

nowhere does the so called advice record deal either with the real risks, or why a hedge fund had any place in complainant's portfolio.

14.8. With respect to Abante Capital, respondent had the following to say:

14.8.1. '*Abante Capital was crowned as the top hedge fund in its category in 2008.'*

14.8.2. A presentation detailing, '*all relevant information about the management of the fund, safety measures implemented by management, the different hedging strategies…..costs'* was done by Pretorius himself at a meeting in Pretoria in 2008. '*The content of this presentation was conveyed to the client verbally with graphic explanations when I explained the investment to them.'*

14.8.3. 'The risks were explained to the client verbally and visually. The type of hedge namely "pairs trading" was illustrated to the client in the same way as it was communicated to me by Mr. Pretorius namely apart from the fact that mathematical models were used to identify a possible trade, the entire portfolio was divided between five managers each dealing with different "pairs"…….What would be the chance that all 5 managers would encounter the same problems at the same time. Margins were low, but several trades would occur in a month resulting in above average returns…'

14.8.4. Abante Capital was FSB registered with license number 874.

Later enquiries revealed that Abante was no longer registered; whereafter Pretorius informed the respondent that the license was held by a subsidiary, Polus Capital, manager of RVAF funds.

14.8.5. Pretorius further assured respondent that Abante Capital was registered with the South African Hedge Fund Association hence it did not require registration with the FSB.

14.8.6. Respondent refers to a conversation he had with one Lynton at the FSB wherein he was informed that his license did authorise him to sell hedge fund investments. To this end he provided a copy of an e-mail to the FSB on 10th May 2007 confirming the said conversation.

14.8.7. Contained in the e-mail is a request for written confirmation that respondent be allowed to offer its clients the opportunity to invest in the RVAF hedge fund. However other than a read receipt, no such confirmation was produced.

14.8.8. Respondent also includes copies of third party communication between one Wilhelm Erwee and Tefo Moatshe of the FSB dated the 11th May 2009. This reads:

'*Hedge funds are currently not regulated in South Africa we only regulate a person who manages a hedge fund portfolio. This means that a person who renders financial services to a client to invest in hedge fund is not a financial services provider and not required to be licensed. This situation*

may change as discussions are underway to have hedge funds regulated. The FSB is generally not in favour of the marketing of hedge funds whether is by the hedge fund manager or by third parties.' (Emphasis added)

I must point out that this attitude of the FSB towards hedge funds was not conveyed to Complainant. Nor did Respondent follow up to ask the FSB why it adopted this stance.

14.9. Respondent argues that the duty rests on the FSB to assess the fitness of the product provider. That there is little purpose in expecting a financial adviser to take responsibility for the due diligence of a very complex product. Respondent further points out that the FSB investigated Pretorius and gave a clean bill of health. In a nut shell, respondent blames the FSB.

E. DETERMINATION

Respondents' Role as Adviser

[15] Prior to dealing with the issues common to most RVAF matters, it is necessary that I first deal with the advice aspect. In particular whether any recommendation, guidance or proposal was made or financial advice was rendered as contemplated in the Act. This in light of respondents' contention that complainant chose the RVAF option over the recommended Allan Gray unit trusts and that respondent had offered factual information and not advice.

[16] This requires that I highlight a number of factors. First and foremost being that at the time of this investment, respondent was complainant's investment

adviser.

[17] Complainant it would seem, heard about RVAF from respondent. In particular second respondents' wife, who at the time was a member of first respondent.

[18] No prior knowledge or understanding of RVAF is imputed to complainant. All additional interaction pertaining thereto; before, during and after the investment took place directly between complainant and respondent. Amongst which is the content of Pretorius's presentation on RVAF, which was, '*conveyed to the client verbally with graphic explanations.'*

[19] The letter of introduction provided to complainant on the 7th July 2010 states that respondent '*is accredited to sell the products of the following product suppliers.*' Abante Capital is amongst those listed.

[20] The forms were completed and submitted through the office of respondent. This entitled respondent to commission of 7.5% of the R120 000. In other words R9000 which was not disclosed as required in terms of section 3 (1) (a) (vii) of the Code[3].

[21] The normal commission as indicated in the letter of introduction being 3% plus an annual management fee of 0.5%.

[22] Respondent, in earning its fee as complainant's financial adviser, had, in terms of section 2 of the Code, a duty of care to '*render financial services honestly, fairly, with due skill, care and diligence, and in the interests of clients and the integrity of the financial services industry'.*

[23] In particular as will become clear, respondent owed a duty to apprise

3 must, as regards all amounts, sums, values, charges, fees, remuneration or monetary obligations mentioned or referred to therein and payable to the product supplier or the provider, be reflected in specific monetary terms:..

complainant of the real risks of investing in RVAF; a product which complainant had no prior knowledge of. Not a single written word evidences that complainant was in any way dissuaded from investing in this high risk product. One must bear in mind that complainant specifically pointed out that her investment goal was capital growth. Specifically there is no indication anywhere in respondent's papers that complainant was in pursuit of extra – ordinary returns to grow her capital. In a word there is no case made for this choice of investment, which at all times exposed complainant to the risk of losing her capital.

[24] On the contrary, respondents reply to this office, impugns the real risk inherent in RVAF, a hedge fund. See para 12.9 in this regard. There can be no question that this same failed understanding was conveyed to complainant.

[25] Respondent argues that, '*they instructed me to invest their funds in the RVAF irrespective of the fact that I suggested an investment in a unit trust portfolio with Allan Gray'.* The question is why is respondent's version not supported by section 8 (4) (b) of the code which requires that where a client:

> *'elects to conclude a transaction that differs from that recommended by the provider, or otherwise elects not to follow the advice furnished, ……..., the provider must alert the client as soon as reasonably possible of the clear existence of any risk to the client, and must advise the client to take particular care to consider whether any product selected is appropriate to the client's needs, objectives and circumstances.'*

[26] Nowhere is this version supported by a record of advice as required by section 9 of the code. In fact nowhere is there a proper record of advice as required by

section 9 of the Code.

> '*A provider must…maintain a record of advice furnished to a client as contemplated in section 8, which record must reflect the basis on which the advice was given..'*

[27] As to any suggestion that there was no advice, this is unsustainable. Respondent introduced, presented and guided complainant on her understanding of RVAF, thus leading to an investment in RVAF. Hence at a minimum a '*recommendation*' or '*guidance*'[4] occurred as defined in the FAIS Act. This much is apparent from respondents' own version.

Commonality with other RVAF matters

[28] It is noted that the main concerns regarding investments in RVAF were comprehensively dealt with in the determination of Inch vs Calitz[5], (Inch) where this Office dealt with the key issues. Principally these issues pertain to the Respondent's failure to understand the entity (RVAF), and the risks to which Respondent was exposing his client whilst advising her to invest in RVAF.

Thus, the findings in the Inch determination apply to this case *mutatis mutandis*.

[29] As with Inch, an identical set of key questions were put to respondent by means of a notice in terms of section 27(4) of the FAIS Act.

[30] Key to being able to answer these questions is an understanding of the legal requirements governing the rendering of advice in particular in respect of a

4 Section 1 of the FAIS Act, definition of advice.
5 Graig Stewart Inch v Impact Financial Consultants cc and Michal Johannes Calitz, FAIS 0497/12-13/MP1

hedge fund. Accordingly it is appropriate that I commence with those.

[31] The Registrar of Financial Service Providers, in Board notice 89 of 2007 defined a hedge fund FSP as follows:

‘‘**Hedge fund FSP**’ means a financial services provider-

(a) that renders intermediary services of a discretionary nature in relation to a particular hedge fund or fund of hedge funds in connection with a particular financial product (own emphasis) referred to in the definition of ‘administrative FSP’ in subsection 2.1 of section 2 of Chapter 1 of this Schedule; and

(b) acting for that purpose specifically in accordance with the provisions of the respective codes set out in this Chapter III of this Schedule read with the Act, the General Code of Conduct for Authorised Financial Services Providers, /2002 (where applicable), and any other applicable law;’

[32] RVAF was promoted and sold as a hedge fund. The fund itself not only exercised complete control over client’s monies, but additionally carried out all administrative/intermediary services. In this regard I note that the fund statements were on the letterhead of ‘RVAF Trust IT 932/2004.’ There was no separate licensed administrator. Accordingly the RVAF fund, as it purported to operate, fell squarely within the above definition. As will now be demonstrated there are legal requirements that flow from this conduct.

Authorisation to conduct business as a financial services provider

[33] I commence with section 7(1) of the FAIS Act which requires that: ‘With effect from a date determined by the Minister by notice in the Gazette, a person may

not act or offer to act as a financial services provider unless such person has been issued with a license under section 8.'

[34] In terms of section 7(3), an authorised financial services provider may only conduct financial services related business with a person rendering financial services if that person has, where lawfully required, been issued with a license for the rendering of such financial services.

[35] Neither Pretorius nor the RVAF itself was licensed in any way. There was thus a clear contravention of section 7(1), which led to Respondents' contravention of section 7(3) in conducting financial services related business with a person not so authorised.

[36] Further section 8 (8) (b) of the FAIS Act requires that a licensee must ensure that a reference to the fact that such a license is held is contained in all business documentation, advertisements and other promotional material. Neither that of Polus Capital, nor Abante, nor any other license was displayed in any documentation provided to this office. This despite Respondents' version as already mentioned being that; '*Abante Capital was* registered with the *FSB…I recently checked Abante Capital's status on the FSB website again and realised that they were no longer registered with the FSB. I then contacted Mr Pretorius and he informed me that the FSB license was held by Polus Capital, a subsidiary company, and that RVAF investment funds were managed by them.'*

[37] Given the definition of a 'Hedge fund FSP'; for this version to have any credibility one would expect to see the requisite FSP numbers and applicable supporting documentation.

[38] That this did not tie up should have immediately alerted Respondent to the fact

that they should make further enquiries. There is no evidence that this occurred and accordingly such conduct is indicative of Respondent's ignorance of the basic legislative requirements.

Relevant information required to be provided within the product provider's documentation.

[39] In order to ensure a client's understanding of the provider with which they are contracting, section 4 of the General Code requires, *inter alia*, that full particulars of the following requirements be provided in writing by the provider:

39.1 Section 4(1) (a) 'Name, physical location, and postal and telephone contact details of the product supplier;'

39.2 Section 4(1) (b) (i) 'the contractual relationship with the product supplier (if any), and whether the provider has contractual relationships with other product suppliers;'

39.3 Section 4(1) (c) 'the existence of any conditions or restrictions imposed by the product supplier with regard to the type of financial products or services that may be provided or rendered by the provider;'

39.4 Section 4(1) (b) (ii) 'names and contact details of the relevant compliance and complaints departments of the product supplier;'

39.5 Section 4 (1) (d) 'Where applicable, the fact that the provider-

(i) directly or indirectly holds more than 10% of the relevant product supplier's shares, or has any equivalent substantial financial interest in the product supplier;

(ii) during the preceding 12 months received more than 30% of the total

remuneration, including commission, from the product supplier, and the provider must convey any changes thereafter in regard to such information at the earliest opportunity to the client.'

[40] In spite of the clear requirements of section 4, there does not appear to be any contractual documentation on file which properly complies with these requirements. In particular, nowhere is Polus Capital or Abante Capital mentioned, as Respondent claims as part of this contractual arrangement. It is impossible to be certain as to exactly who the product provider is, as required in terms of this section, let alone the additional details required therein.

[42] The three page application form headed '*DEED OF ADHERENCE FOR INVESTORS WISHING TO BECOME LIMITED PARTNERS OF OR MAKE FURTHER INVESTMENTS IN THE RELATIVE VALUE ARBITRAGE FUND EN COMMANDITE PARTNERSHIP*' does not contain any RVAF contact details.

[43] Returning now to the missing contact details; the first document that contains any mention thereof appears to be the acknowledgment of investment dated the 21st July 2010. This is signed off by 'Eduard Brand for and on behalf of RVAF EN COMMANDITE PARTNERSHIP'

[44] These same details are included in the investment statements which then followed. These were headed RVAF Trust IT 932/2004. Quite how the trust fitted in, is not evident from the documentation on file.

Necessary contractual documentation, or mandate required to enter into an agreement with a hedge fund.

[45] Additionally sections 5 and 8A of the Discretionary FSP's Code which relate to

the mandates and duties of hedge fund FSP's, detail the necessary documents to enter into an agreement with a hedge fund service provider and, despite these requirements, there is not a single mention of Polus Capital or Abante in any such documentation.

[46] For example, section 8A (3) requires that: '*A hedge fund FSP must, after having complied with subsection 8A (2) with the introductory provisions of subsection 5.1 and with subsection 5.2, and before rendering any intermediary services to the client, obtain an additional signed mandate from the client, in accordance with the proviso to the introductory provisions of subsection 5.1 and subsection 5.2, which apply with the necessary changes.*

[47] Subsection 5.1 is particularly important in that it requires a signed mandate which records the arrangements made between the parties, whilst setting out necessary details to be contained therein.

[48] For example, section 5.1 (a) '*authorise the discretionary FSP to act on behalf of the client, indicating whether the authorisation is given with full or specific limited discretion*'.

[49] Section 5.1 (d) thereof requires that the agreement must *'stipulate in whose name the financial products are to be registered and whether they are, for example, to be registered in the name of-*

(i) The client or a nominee company nominated by the client;

(ii) The nominee company of the discretionary FSP or a nominee company within the group of the companies of which the discretionary FSP forms part;

(iii) The nominee company of a product supplier;

(iv) …….;'

[50] Nowhere is there a signed mandate in compliance with section 5 and certainly, not with Polus Capital or Abante. I particularly point out that the mandate is required to deal with the client's investment objectives; which not only need to be contained in this document but again confirmed in terms of the requirements of the section dealt with hereunder. The lack of a nominee company is also conspicuously absent.

The requirement that there be an additional signed mandate.

[51] Following on from the requirements of section 5(1) we have section 8A (4) which requires an additional mandate from the client which must confirm that the client-

(a) approves of—

(i) the clients investment objectives, guidelines and trading philosophy of the hedge fund FSP, as disclosed and stated in the mandate;

(ii) utilisation by the hedge fund FSP of the process to be implemented in the form of strategies or positions (including leverage and/or net short positions, borrowing limits and risk management principles to be applied to mitigate interest rate, liquidity, and credit and derivative risk), risk profile and risk management (for instance a sensitivity analysis), as disclosed and stated in the mandate.

[52] What is clearly evident from a reading of the Code is that that the legislature

has made every effort to require not only that the client be appropriately apprised as to the risks inherent in, and processes and strategies followed by the hedge fund but importantly, that the client actually confirms such disclosure having taken place.

[53] Having examined the documentation, this Office is satisfied that nowhere is any mention made of either the client's investment objectives or her approval of the guidelines and trading philosophy of the hedge fund in the manner as required in terms of section 8A (4).

Written disclosure of hedge fund risks

[54] Section 8A (4) is further reinforced by section 8A (2) which requires that a hedge fund FSP must, before rendering any intermediary services to a client that requires such intermediary services in respect of a financial product governed by the Act, provide a written disclosure to the client in the format determined by the registrar, of the risks involved in a hedge fund. Section 8A (2)(b) specifically requires written confirmation of receipt of such written disclosure.

[55] The format as determined by the registrar is contained within the Notice on Hedge Fund FSP disclosures, 2008 as promulgated in Board Notice 571 of 14th July 2008. This notice requires not only the disclosure of all risks involved in investing in a particular hedge fund portfolio, but, moreover specifies that hedge fund FSP's must ensure that clients understand the risk disclosures.

[56] Respondent has provided no evidence that this board notice was actually complied with, in particular that the client actually understood the risks. The

Complainant denies having received a copy of the risk disclosure.

[57] The code itself and in terms of section 7 (1) (c) (xiii) further requires that the provider make available information about:

'any material investment or other risks associated with the product, including any risk of loss of any capital amount(s) invested due to market fluctuations'

[58] Nowhere is there any evidence that the complainant was made aware of the fact that by investing in a hedge fund she potentially placed her entire capital at risk.

Nominee Account

[59] The normal risks being magnified by the fact that without any mention of a nominee company and in contravention of section 8[6] of the Discretionary Code, monies were directly paid over to, and controlled by, RVAF. In fact, without any supporting agreement or client mandate containing limits on the manner or method of investment, RVAF exercised complete discretionary control over a client's funds. In simple terms, there was no separate distinction between the fund manager and the administrative functions. The requirement that the investment be held by a nominee account is a safety mechanism to distinguish investors' funds from those of the service provider. A failure to ensure that the investment is secured by a nominee account as occurred here robs the investors of this protection and potentially, allows the product provider to use the funds for their own ends. This is a clear breach of the Discretionary Code.

6 Section 8 requires that a nominee company be utilised by the discretionary FSP with the main object of being the registered holder and custodian of the investments of clients.

General duty of an advisor to render advice with due skill, care and diligence in terms of section 2 of the General Code of Conduct for Authorised Service Providers and Representatives, (the Code)

[60] This leads onto section 2 of the General Code; a provision which can be seen to draw together the more specific sections of the General and Discretionary codes. Section 2 of the General Code requires that '*a provider must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interests of the clients and the integrity of the financial services industry*.'

[61] Of relevance to this matter, I would expect that the Respondents be sufficiently skilled such that they diligently ensure that they invest their client's money in a reputable entity. To put it another way, that they look after the interests of their client by checking that the fund is actually what it purports to be. From what follows it will become evident that the Respondent failed in this regard.

[62] Respondent was specifically questioned on the due diligence which they conducted on RVAF which led to them deeming RVAF to be a suitable investment for their client. In reply thereto, respondent made mention of *inter alia*, the license of Abante/ Polus Capital.

[63] Respondent asserts that with Pretorius having run, '*his business successfully for approximately 10 years at that time, previously under the name of Mat Securities, together with the fact that they were registered with the FSB, I felt save (sic) in the knowledge that a proper due diligence would have been done by the FSB prior to them having granted Abante Capital a license.'*

[64] It is important to note that Respondent has chosen to be vague in its response. At no point do they deal with the glaring lack of documentation amongst which is the fact that whilst on complainant's version, Abante/Polus was the licensed FSP, there is not so much as a single scrap of paper on file supporting such assertions. There is no evidence of an enquiry with the regulator as to the license status of RVAF itself.

[65] Mention is made of the respondent having visited the trading desk and the fund managers and watching them doing the trades, yet no mention is made of the complete lack of any financials or even something as basic as a fund fact sheet[7].

[66] This Office has seen no evidence in Respondents' papers that the legal meaning of a 'partner e*n commandite*' (own italics) was explained to Complainant. Nor is there evidence indicating that Respondent disclosed the legal consequences of investing in this entity as a partner. Respondent has further failed to provide a basis for selecting this type of contractual arrangement as an appropriate mode to address the client's needs. This despite the provisions of section 7(1)(a) of the general code which requires that the provider '*provide a reasonable and appropriate general explanation of the nature and material terms of the relevant contract or transactions to a client…'* Alongside which there is section 7 (1) (b) which requires that '*the provider whenever possible provide to the client any material contractual information…..'*

7 Usually a one to two page document containing important key information about the fund, namely asset allocation, market performance, top holdings as well as the fund management company

[67] It should also be pointed out that of additional concern is the fact that the bank details utilised are those of 'RVAF Trust'. A trust is an entirely different legal entity from a partnership and yet Complainant's proof of payment reflects payment into this Trust. Again, Respondents saw no need to explain their actions to complainant in this regard. At this point, it is reasonable to conclude that Respondents were themselves ignorant of the legal implications.

F. CONCLUSION

[68] As mentioned previously, this complaint is about being advised to invest in a scheme that was not above board.

[69] The scheme itself purported to act as a legitimate hedge fund; a fact which would have made it subject to the provisions already detailed within this determination.

[70] Yet respondents either ignored, or were unaware of the legislative requirements. Instead they appear to have blindly accepted whatever they were told about RVAF without any proper attempt to verify such information; which information they then recklessly conveyed to their client. The simple fact is that Respondents were out of their depth.

[71] Therefore they could have had no understanding about the economic activity that generated the returns or the sustainability of the investment. This question was actually put to respondents by complainant's husband; who received an assurance that the investment was sustainable and performing well. This, shortly before the whole scheme collapsed.

[72] Accordingly respondents' could not have properly apprised complainant as to

the material investment or other risks associated with the product, as required in terms of section 7 (1) (c) (xii) of the General Code.

[73] That respondents failed in their duties in this regard is clear. Without complainant being advised that they were investing in an unregulated and unregistered entity without so much as a set of financials it cannot be said that Complainant made an informed choice as required by section 8 (2) of the General Code.

[74] In a nutshell, respondents as registered financial services providers failed to meet the requisite requirements as set out in the FAIS Act.

[75] In many ways the matter at hand mirrors that of the case of *Durr vs ABSA Bank Ltd and Another 1997 (3) SA 448 (SCA),* wherein the Supreme Court of Appeal had occasion to consider the duties of a broker. At 463 the following is instructive:

"The important issue is that even if the adviser himself does not have the personal competence to make the enquiries, I believe it is incumbent upon him to harness whatever resources are available to him or if necessary to ask for professional, legal or accounting opinion before committing his client's funds to such an investment".

[76] In the words of Schutz JA in the above-mentioned Durr matter, at 466 his lordship sounded the following timely warning:

'*One of the first requirements of a professional is to know when he may be getting out of his depth, so that I do not think that that is sufficient excuse. I am not able to say exactly what Stuart should have done. But I would suggest that there was a point at which he should have walked down the passage or across*

the street, or lifted the telephone, or activated the fax, and said to a lawyer, or accountant, or banker, none of which he was, in the employ of ABSA something like this: 'Look, I have been introduced to some attractive debentures (preference shares) in a group called Supreme. Would you please tell me quite what debentures (preference shares) are and how secure they are. And also, please tell me how I find out who and what Supreme is and what risk attaches to investing in it".

[77] Similarly, at 468, the words of the learned judge of appeal on what constitutes negligence are instructive. The learned judge pertinently stated the following:

"I come towards my conclusion on the subject of negligence. The basic rule is stated by Joubert (ed) The Law of South Africa First Reissue vol 8.1 para 94, as follows:

'The reasonable person has no special skills and lack of skill or knowledge is not per say negligence. It is, however, negligent to engage voluntarily in any potentially dangerous activity unless one has the skill and knowledge usually associated with the proper discharge of the duties connected with such activity."

[78] Quite simply, no adviser would have recommended this product as a suitable component of any investment portfolio had they so exercised the required due skill care and diligence (section 2 of the General Code). Complainant as a client of a registered financial adviser relied on Respondents' advice when making this investment. When rendering financial services to clients, the FSP is required to act in accordance with the FAIS Act. Respondent failed in this regard.

[79] In addition Respondents owed a duty of care to Complainant to give financial

advice with due care skill and diligence. In the circumstances, Respondents could reasonably foresee that a breach of this duty will result in loss to the Complainant. Such a breach occurred, for reasons set out above, and Complainant lost her capital.

[80] Although claim forms were submitted to the administrators of the collapsed RVAF, there is no reasonable prospect that Complainant will recover any part of her capital.

[81] For the reasons set out above, complainant's complaint must be upheld.

G. ORDER

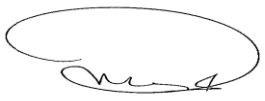
[82] Accordingly the following order is made:

1. The complaint is upheld;

2. Respondents are hereby ordered, jointly and severally, the one paying the other to be absolved, to pay to complainant the amount of R120 000.00.

3. Interest at the rate of 10,25 %, per annum, seven (7) days from date of this order to date of final payment.

DATED AT PRETORIA ON THIS THE 16th DAY OF MAY 2016.



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NOLUNTU N BAM
OMBUD FOR FINANCIAL SERVICES PROVIDERS