

IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

CASE NO: FAIS 04269/12-13/ WC 1

In the matter between:

STEPHANIE NEETHLING

Complainant

and

VAIDRO 173 CC t/a Vaidro Investments

1st Respondent

ANDREA MOOLMAN

2nd Respondent

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

A. THE PARTIES

[1] Complainant is the Mrs Stephanie Neethling, an adult female whose full contact details are on file with the Office.

[2] First respondent is VAIDRO 173 CC t/a Vaidro Investments, a close corporation duly incorporated in terms of South African laws, with its principal place of business situated at 2 Elkie Drive, Wilro Park, Roodepoort. First respondent is an authorised financial services provider, (FSP 38693) in terms of the FAIS Act.

[3] Second respondent is Andrea Fredericka Moolman, key individual, sole member and authorised representative of first respondent who shares the same address as first respondent. Both respondent and respondents must be read to mean the

same thing.

B. THE COMPLAINT

[4] On the 9th and 16th of September 2011, complainant invested R100 000 and R136 000 respectively in the now defunct Relative Value Arbitrage Fund, (RVAF). These investments were made in consequence of the recommendation and advice of the second respondent who acted as complainant's financial adviser.

[5] Following the demise of RVAF and the death of Herman Pretorius, complainant claims she has lost her capital.

[6] Having failed to resolve the complaint with the respondent, complainant resorted to lodging the present complaint to this Office.

[7] In her complaint, complainant states:

7.1. She and her husband were having difficulty in keeping up with monthly payments on their endowment and life policies, so they came to the conclusion that they were paying too much;

7.2. Having been referred to respondent, they had a second meeting in August 2011 where complainant and her husband were advised to cancel existing Old Mutual and Sanlam policies and invest the surrender proceeds in RVAF;

7.3. Complainant was assured that respondent had done sufficient investigations regarding the company and its owners. In other words, respondent had carried out the necessary due diligence;

7.4. The couple were advised by respondent that the interest rate inherent in

the investment was high and so was the risk. There were however, no risks to the capital as the fund had performed extremely well even during the downturn, to the extent of winning an award. Additionally complainant states they were given to understand that whilst one did not get the full advantage of the interest rate when it was at its highest, equally one did not lose as much when it was at its lowest with the risk being absorbed somewhere in the middle;

- 7.5. Having invested as complainant puts it, a 'substantial amount of money in the RAAF (ABANTE)' this fund has subsequently turned out to be a scam;
- 7.6. Complainant therefore contends that respondent did not conduct sufficient due diligence on the company or product;
- 7.7. Up till then complainant claims they had only invested in endowment and life policies. They believed that RAAF was the name of the vehicle through which they invested in shares on the JSE. They were advised by respondent that these shares were made up of, 'property, cash etc (like most shares are)'
- 7.8. Aside from their pensions the investment in RAAF was essentially their only investable capital.
- 7.9. Complainant never attended any meetings or presentations of Herman Pretorius.

[8] The complainant was provided by this Office with copies of respondent's client advice records as well as the RAAF application form and invited to comment thereon. Complainant advised as follows:

- 8.1. Whilst acknowledging that she indeed signed the records, she asserts that some of the details were added later. To this end she argues that with the

meetings having been held in the evening, dinner to prepare and children to be put to bed, there was insufficient time for such detailed notes;

- 8.2. In this regard she takes issue with what she terms the excessive mention of high risk as contained in records; arguing that had she understood this to be a high risk investment she would have reconsidered;
- 8.3. As to her appreciation of 'Hedge Fund Trading Strategies,' which the minutes refer to, complainant states that she does not know what that means and does not recall any discussions or explanations about this;
- 8.4. Complainant acknowledges that she signed the R VAF application form but states that she did not read same nor was it explained to her by respondent;
- 8.5. Additionally and in support of the allegations she makes against respondent (as contained in the preceding paragraphs), complainant argues that she never received copies of any of the documentation she signed.

[9] Complainant states that, having been referred to respondent by her employer, 'an accomplished businessman', she in turn placed her trust in respondent. However, respondent misled her. She claims that had she known she was investing in a partnership and not shares she would not have entered into the transaction. Accordingly she holds respondent accountable for the loss.

[10] As to the quantum of the loss; whilst R236 000 was initially invested complainant made a withdrawal of R21 000, which was paid into her bank account on the 9th June 2012. Accordingly she claims the capital balance of R 215 000.00.

C. SUMMARY OF COMPLAINT

[11] Complainant's claim is based on failure by the respondent to properly advise her in terms of the FAIS Act and the Code, with the complainant claiming that, had the respondent conducted herself in the manner that the Code demands (of providers when they render financial services to clients), she would not have entered into the transaction with RVAF. In this regard, complainant mentions the failure on the part of the respondent to appropriately disclose risk and carry out the necessary due diligence.

D. RESPONDENTS' REPLY

[12] With identical key concerns in all RVAF complaints pertaining to the respondent before this Office, similar notices in terms of section 27(4) of the FAIS Act were forwarded to respondents in respect of each complaint. In turn and with the necessary references to individual complainants, respondent provided a comprehensive reply applicable to all its matters before this Office.

[13] Commencing first with the aspects pertaining to the complainant, respondent had the following to say:

13.1. The complainant and her husband were referred to the respondent by a friend, a Mr Pringle;

13.2. They met with respondent on or about the 27th August 2011, at which meeting they informed respondent that they had a cash flow problem due to the escalating premiums of their current investments;

13.3. Having attended a presentation by one Herman Pretorius, complainant 'wanted to invest in the RVAF fund'.

13.4. According to respondent the complainant wanted to withdraw pension

fund monies to make this investment. However, she persuaded them otherwise and informed them that RVAF was a risky investment;

- 13.5. A comprehensive needs and risk analyses were conducted with the risk analysis resulting in a moderately aggressive outcome.
- 13.6. Respondent states that ‘the client insisted that monies are placed in the RVAF’;
- 13.7. The existing policies were replaced by the RVAF investment and a comprehensive replacement form completed. In this regard the couple were made aware of the penalties they were paying as well as the risks they were taking. In this regard respondent points out that that the original reason for surrendering the policies was to save on monthly expenses;
- 13.8. Respondent makes the point that complainant works at a bank and is well aware of this type of product.

[14] In summary respondent’s version is that complainant, having been properly apprised of the high risks, made an informed decision; a fact which respondent contends is supported by her records.

[15] In this regard documentation pertaining to the complainant was also provided and from which the following was extracted:

- 15.1. The minutes relating to meeting with the complainant reflect a decision to surrender endowments and invest in Abante Hedge Fund for maximum growth. In addition to the statement that this is high risk and can lead to capital loss the document goes on to remark that the reason is,
‘supplementing pension fund with aggressive high risk portfolios for maximum growth – whilst using hedge funds strategies to reduce volatility

in market movements associated with equity portfolios;

15.2. Mention is made of the fact that *'client wants to reduce portfolios as affordability has become an issue...Client wants aggressive growth on savings portion and reduction of premiums.'*

15.3. A document headed 'LETTER OF ADVICE/RECOMMENDATION' states *'cash surrender to invest for capital growth in a high return fund - equities,'*

[16] Proceeding on to the general response, respondent states that in terms of the record of advice the risks attached to this product are explained in plain language and that the record states that no forms were signed which were not fully completed.

[17] The point is also made that the application forms signed by complainant explain in plain language that the structure of the investment involved becoming a partner in the RVAF.

[18] Specifically questioned as to the due diligence she conducted, respondent advised that having been introduced to Abante Capital she visited the premises where Herman Pretorius explained the strategies and how the risk was managed. Respondent then proceeded to ascertain from the trading team whether Abante Capital was registered with the FSB. In addition thereto respondent confirmed with Momentum and Old Mutual and spoke to their fund managers about Abante Capital and their use of the fund in their portfolios.

[19] Respondent goes on to state that having a reasonable knowledge of Hedge Funds she concluded that the strategy and the fund were sound because most of top 40 JSE companies were invested therein. According to respondent, Mr

Pretorius explained that the way that the RVAF fund operated made the risks relatively low.

[20] Respondent reasons that she was satisfied that persons investing in the fund were fully appreciative and aware of the risks involved, both in that they attended presentations by Herman Pretorius but also in that respondent further explained the process and operation of the fund as she understood it. In this regard a written explanation of Board Notice 571¹ was provided and explained to each client.

[21] As to the basis upon which respondent deemed RVAF to be a suitable investment for her clients, respondent advised as follows:

21.1. Many clients need a higher return on their investment to ensure that they reached their investment goals, and as an adviser it was her duty to ensure that all products and all investment avenues are explored on behalf of clients;

21.2 Given the various market crises hedge funds could both act as a defensive strategy and outperform traditional investments in a downturn;

21.3 Researching the different hedge funds available in the country respondents' research showed that Abante Capital was one of three hedge funds in South Africa;

21.4 In 2008 Abante Capital won a hedge fund award. With regards thereto respondent provided a Symmetry multi manager document showing the market neutral category winner as 'Abante Statistical Arbitrage.'

¹ Hedge Fund FSP Risk Disclosures Notice

[22] Respondent further adds that the portfolio was explained to clients as a hedge fund, which invested in shares on the JSE. It was explained that as in any investment involving shares, the risk is of a high nature, however, historically the loss in downside markets is lessened when hedge trading strategies are used.

[23] In this regard respondent states that hedge funds may actually have lower risk than traditional investments as the target is to protect capital, increase defensive strategies, and obtain absolute returns under all market conditions as explained by Herman Pretorius.

[24] As to commission she was paid, respondent advised that she was paid 7.5% but with no trail commission. From the documents submitted by respondent, this does not appear to have been disclosed to the client as required in terms of section 3.(1) (vii) of the General Code.

E. DETERMINATION

[25] Reference is made to the determinations of *Inch vs Calitz*² and *The Trustees of Johnnie Pringle Investment Trust vs Vaidro/Moolman*³ where this Office dealt with the key issues, which pertain to the rendering of advice to invest in RVAF. Principally the issues pertain to the respondent's failure to understand the entity, (RVAF) and the risks to which she was exposing her clients whilst advising them to invest therein.

2. **Graig Stewart Inch v Impact Financial Consultants CC and Michal Johannes Calitz FAIS 0497/12-13/MP1.**

3. **The Trustees of the Johnnie Pringle Investment Trust IT1280/2004 v Vaidro 173 CC t/a Vaidro Investments and Andrea Moolman FAIS 0379512 – 12/13 EC 1.**

[26] Evident therein are the material deficiencies in the application forms which lack in substance or form to the extent that it is difficult to understand who or what the complainant was dealing with. Yet in spite of these failings, funds were transferred directly into RVAF without even the protection afforded by a nominee account.

[27] In attempting to support her version, and as part of the their investigations into the investment vehicle, respondent contends that they were shown an FSP license no 874 in the name of Abante Capital (Pty) Ltd and accordingly they were satisfied that Abante with whom they had an intermediary agreement was correctly licensed. Yet there is not so much as a single mention of Abante or its license number⁴ within the contractual documentation. This points to respondent having failed to understand the contracting entity.

[28] Furthermore there were no financials or even so much as a fund sheet. Respondent claimed that the fund invested in mostly the top 40 companies on the JSE, yet provided no documentation supporting such a belief. Ergo, without the financials or so much as a fund fact sheet respondent could not have understood the economic activity that generated the returns.

[29] Furthermore respondent was unable to explain to the office just why Abante was nowhere to be found in the very documentation which respondent used in support of recommendations she made to invest in RVAF.

4. 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.

I refer here to the Symmetry multi manager South African Hedge Fund Survey, which as its name suggests lists numerous hedge funds including those of Abante. RVAF is conspicuous by its absence.

[30] The inescapable conclusion is that respondent knew nothing about the fund or its underlying investment and accordingly was in no position to advise her clients to invest in it.

[31] As referred to in both the Inch and Pringle Investment Trust determinations, the case of *Durr vs ABSA Bank Ltd and Another 1997 (3) SA 448 (SCA)* is instructive. In this regard 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 se 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.’”

[32] In light of what I have stated in the preceding paragraphs respondent has breached section 2 of the General Code which 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.’

[33] In this regard the client was in no position to understand the ‘any material

investment or other risks associated with the product' as required by section 7. (1) (c) (xii) of the Code.

[34] Quite simply the client did not make an informed decision as required by section 8 (2)⁵ of the code. In contrast to respondents' statement, the real risks are not explained in plain language.

[35] Whilst complainant acknowledges the need to take risk in order to achieve high returns, she claims she would never have taken the kind of risk that is involved in RVAF had she known what she now knows. As fully set out in the determination, with respondent's narrative of the steps she took to conduct due diligence and what she believed about the company's association with Abante and the latter's alleged winning of the fund manager of the year award, complainant had no chance of appreciating the real risk she was confronted with. At the very least, complainant needed to know that:-

- 35.1 she was investing in an unregulated entity;
- 35.2 in a partnership where she would become a partner in *commandite* and the legal implications of that;
- 35.3 she stood the risk of losing her capital as there was no regulatory body to which Pretorius and his team were accounting to;
- 35.4 that there were no financials, fund fact sheets or even a license number on any of the documentation.

[36] No sensible person having been given the correct material information would have invested in RVAF.

5. Section 8 (2) The provider must take reasonable steps to ensure that the client understands the advice and that the client is in a position to make an informed decision.

Whilst complainant herself acknowledges the need to take on greater risk in order to achieve growth; where her version differs is in the extent of the risk and knowledge of the underlying investment and structure.

[37] There is a world of difference between making a calculated and informed decision to invest in a high risk fund as opposed to an unregistered ponzi scheme without any proper documentation. It is concerns such as these that respondent should have alerted their client to. Respondent's notes show no indication of this having occurred.

[38] Given the circumstances the recommendation to invest in RVAF cannot be justified.

[39] Whilst perhaps immaterial in the light of what has already been covered, this also leads this Office onto the issue of complainant having denied receiving a copy of the record, a requirement of section 9 (2) of the General Code. Indeed there is no correspondence indicating that such a copy was ever provided.

[40] As to complainant's allegation that the forms were never fully completed, nothing turns on it given that in any event respondent was never in a position to properly disclose the real risks.

[41] Regarding respondent's comment that complainant worked at a bank and is well aware of this type of product; nothing in respondent's file supports this conclusion. On the contrary complainant's personal circumstances and investment history indicate otherwise.

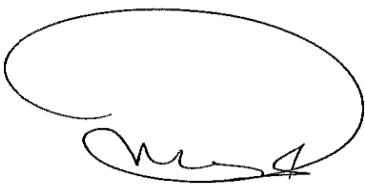
[42] Finally it needs to be mentioned again that the disclosures as to fees do not appear to have been made in accordance with section 3.(1) (vii) of the Code. In particular the amount is not reflected in specific monetary terms.

F. ORDER

[43] Accordingly the following order is made:

1. The complaint is upheld;
2. The Respondents are hereby ordered, jointly and severally, the one paying the other to be absolved, to pay to complainant the amount of R215 000.00.
3. Interest at the rate of 9 %, per annum, seven (7) days from date of this order to date of final payment.

DATED AT PRETORIA ON THIS THE 16th DAY OF MARCH 2015.



NOLUNTU N BAM
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