IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

Case Number: FAIS 02156-09/10 GP(1)

In the matter between:-

GERT CORNEULIS JOHANNES VAN VUUREN	**1ST Complainant**
SUSARA JACOBA VAN VUUREN	**2ND Complainant**

and

KAMPSTONE FINANCIAL SERVICES CC	**Respondent**

DETERMINATION IN TERMS OF SECTION 28(1) OF THE FINANCIAL ADVISORY AND INTERMEDIARY SERVICES ACT NO. 37 OF 2002 ('FAIS ACT')

A. PARTIES

[1] The 1st complainant is Gert Corneulis Johannes van Vuuren who is married in community of property to 2nd complainant, Susanna Jacoba van Vuuren. The complainants reside in Springs, Gauteng province.

[2] The respondent is Kampstone Financial Services CC (Registration no. 1994/036556/23), a close corporation duly incorporated in terms of South

African Law, with its principal place of business at 6 Bessie Lanser Street, Jordaan Park, Heidelberg, 1438. The respondent is a licensed financial services provider (license no. 1994) and represented herein by its sole member and key individual, Gerda Dafel ('Gerda'). For convenience, and where appropriate, I refer to the respondent and Gerda collectively as respondent.

B. INTRODUCTION

[3] This complaint is about the alleged failure by a former representative of the respondent one Charlene van Niekerk ('Charlene') to act in the interests of the complainants. Although the complainants were close to retirement and needed unrestricted access to capital, Charlene invested their funds in fifteen year Max Investments Committed Plans ('Investment Plans') with Old Mutual[1]. When the complainants subsequently learnt from Old Mutual that fees ('penalties') were payable for early termination of or withdrawals from the Investment Plans, they complained to the respondent. Due to the respondent's failure to satisfactorily address their complaint, the complainants turned to this Office for assistance.

C. COMPLAINTS' VERSION

[4] The complainants' complaint may be summarised as follows:

a. According to the complainants they approached the respondent in early 2008 for assistance with investment advice. This was after being referred to the respondent by a family friend. At the time, they were 69 and 66 years of age, respectively. When the respondent visited the

[1] Plan numbers 15346497 and 15346455. See paragraph 7 for explanation of the products.

complainants at their home she was accompanied by Charlene who ultimately effected the investments in question and received commission.

b. The complainants assert that they requested that their funds be invested for a period of two years. They also wanted unrestricted access to capital in case of emergencies. Charlene however failed to adhere to their instructions to invest in accessible investments. Instead, she misled them into purchasing 2 **fifteen year** Investment Plans. The monthly premiums payable on the Investment Plans amounted to R2 000 and R5 000, respectively[2].

c. The complainants contend that given their advanced age they should not have been locked into agreements for fifteen years, especially in the light of their circumstances. The consequence of Charlene's failure to adhere to complainants' request is that complainants had to pay penalties on all withdrawals from their Investment Plans. They also had to pay penalties when they reduced premiums and prematurely cancelled the Investment Plans due to affordability. According to the complainants, the penalties were not disclosed to them at point of sale of the Investment Plans.

D. RELIEF SOUGHT

[5] The complainants claim the total amount of all penalties paid as a result of withdrawals and early termination of the Investment Plans in question.

[2] Monthly premiums were subsequently increased to R3 000 and R10 000, respectively.

E. RESPONDENT'S VERSION

[6] The respondent's response is contained in a ten page letter submitted to this Office. What follows is a summary of the salient points of the response:

a. According to the respondent, she accompanied Charlene to a meeting at complainants' home following a request to invest their funds with Old Mutual, Max investments. During the meeting, 2nd complainant who was alone at home made it known that she made all her and her husband's investment decisions. She also stated that they were financially stable and had no debt.

b. According to the respondent, various investment options were discussed with 2nd complainant. A money market investment was rejected by 2nd complainant who cited low interest rates as the reason. Charlene presented 2nd complainant with a quotation for a four year retirement annuity ('RA'). The basis for the suggestion according to respondent was 1st complainant's age, and possible tax benefits. The four year RA was rejected by 2nd complainant as she felt that her husband (1st complainant) needed to work for another ten years as they had no retirement savings.

c. Second complainant ultimately opted for Investment Plans as the best option. The terms of the Investment Plans were ten years with monthly premiums of R2 000 and R5 000, respectively. According to the respondent, 2nd complainant was informed of the penalties payable on withdrawals and early termination. On that basis, 2nd complainant agreed to not make unnecessary withdrawals from the investments. She

assured the respondent that the premiums payable on the Investment Plans were affordable and that they intended to increase the premiums at a later stage. Charlene recorded the advice.

d. The respondent asserts that she was not involved in all discussions between Charlene and the complainants. She subsequently learnt that Charlene had increased the investment period from ten to fifteen years.

e. The respondent also contends that the complainants approved the investments in question by signing investment quotations. Furthermore, 2nd complainant signed the ROA confirming that she understands the 'results of disinvestments, cancellations and reduction in premium'.

Investigation by office

[7] Upon request, Old Mutual provided the Office with a Max investments reference guide which provides an overview of the mechanics of the savings vehicle (Committed Investment Plan) in question. According to the reference guide the Committed Investment Plan provides a contractual savings vehicle where clients commit to invest a schedule of premiums for a specified term and frequency. The guide states that a reduction fee will be charged if the contractual commitment is altered during the premium payment term.[3] Old Mutual Max Investments gives clients access to wrappers which include LISP Pure Investments, Life Pure Investments or Retirement Annuities. The LISP

[3] As a result of a reduction in premiums (including making a Plan paid-up) during the premium paying term, disinvestments or plan cancellation made during the premium paying term.

wrapper[4] gives contracting parties access to (multiple) Unit Trust Funds as underlying investments.

[8] Old Mutual also provided the Office with the following breakdown of penalties which were levied upon reduction in premiums, disinvestments and cancelation of the Investment Plans:

8.1 *First complainant*

'policy 15346497…

- On 23 October 2008, an amount of R1,738.23 was deducted from R48,069.76, representing 3.61% of the Contract Value;
- On 23 January 2009, an amount of R3,409.67 was deducted from R65,109.15, representing 5.23% of the Contract Value;
- On 13 March 2009, an amount of R7,101.29 was deducted from R53,203.67, representing 13.34% of the Contract Value;
- On 13 August 2009, an amount of R23,499.05 was deducted from R78,329.99, representing 30% of the Contract Value; and
- On 15 June 2010, an amount of R10, 622.11 was deducted from R60, 064.17, representing 17.68% of the Contract Value.

The Plan Amendment Charge of R23,499. 05 was recouped by Old Mutual because premium payments ceased and the plan became fully paid-up.'

8.2 *Second complainant*

'policy 15346455 …

- On 16 March 2009, an amount of R2,215.57 was deducted from R24,901.07, representing 8.89% of the Contract value;

[4] Type of wrapper used by the complainants.

- On 1 April 2009, an amount of R3,837.10 was deducted from R18,209.69, representing 21.07% of the Contract value;
- On 18 August 2009, an amount of R6,014.69 was deducted from R28,023.33, representing 21.46% of the Contract value;
- On 15 June 2010, an amount of R4,300.33 was deducted from R23,814.44, representing 18.05% of the Contract value'

F. DETERMINATION AND REASONS

There are four issues here:-

1. Whether respondent's representative[5] acted in a manner, which is not in compliance with the FAIS Act and / or the General Code of Conduct ('the Code');
2. Should it be found that the representative's conduct was not in compliance with the FAIS Act and / or the Code, whether such conduct caused the complainants to suffer damage or financial prejudice;
3. The amount of such damage or financial prejudice; and
4. Whether the respondent should be held liable for the conduct of its representative.

The respondent's records

[9] The gist of the respondent's version is that the complainants were presented with different investment options; they chose to purchase the Investment Plans. Complainants were also informed of all potential penalties payable on the Investment Plans; they were therefore in a position to make an informed decision. In support of her version, the respondent provided the office with

[5] Charlene van Niekerk.

documents which include a ROA containing *inter alia* the following information[6]:-

Name of client: SJ van Vuuren[7]

Date of Advice: 05-02-2008

Section A

Client's goals: Capital growth

Section B

Needs (Post retirement): Client has insufficient retirement capital and must save for retirement on a monthly basis as a matter of urgency. There is a huge capital shortage.

Section C

Products considered: Client has a shortage of retirement capital and wants to put away as much as possible as soon as possible.

Section E

Important information: It is a high risk investment. Costs are applicable in the event that the contract is stopped before the term has ended. Client may withdraw in case of emergency; however, we do not recommend it.

[6] Translated as is from Afrikaans
[7] Second complainant

Section G:

General Comments: Client will increase premiums over time.

[10] I will now consider whether the ROA and other records measure up to what is required by the Code? In terms of Section 9[8] of the Code:

A provider must....maintain a record of the advice furnished to a client as contemplated in section 8, which record must reflect the basis on which the advice was given, and in particular-

(a) a brief summary of the information and material on which the advice was based';

(b) the financial products which were considered;

(c) the financial product or products recommended with an explanation of why the product or products selected, is or are likely to satisfy the client's identified needs and objectives.'

[11] On analyses of the ROA, it is evident that although the complainants expressed a specific need to be addressed, the ROA does not reflect the products allegedly considered[9] by the respondent to address the need. There is also no explanation as to why the recommended products were likely to satisfy complainants' needs and objectives. In fact, there is no reference whatsoever to the Investment Plans that were ultimately chosen, nor is there a time frame.

[12] Having scrutinised the respondent's file of papers, I do not accept that the information provided to the complainants was adequate in the circumstances to place them in a position to make an informed decision. Given the fact that potential penalties payable on the products were of such a material

[8] As the section read when the financial service was rendered.
[9] See paragraph 6(b) and (c).

consideration, respondent was duty bound to make full and frank disclosure.[10] The only document in the respondent's records that alludes to early termination penalties is the ROA. However, it merely stipulates that costs are applicable in the event of early termination. It is silent on the investment term of the contracts which has a direct correlation to the severity of penalties payable should the contracts be prematurely cancelled. I could also not find any record of disclosure of the extent of withdrawal penalties and penalties payable on the reduction of premiums.[11] I am convinced had complainants been made aware of the severe consequences of altering the contractual commitments they would not have purchased this product.

[13] Notwithstanding a request from this Office, the respondent failed to provide proof that commission earned was disclosed to the complainants.[12] She also failed to provide proof of that an analysis had been carried out for the purposes of furnishing advice.[13] Given the lack of information in the respondent's records, it appears that Charlene merely paid lip service to the provisions of the Act and the Code to create an illusion of compliance.

Suitability of the products

[14] The respondent argues on the one hand that the complainants were aware of what they were signing for and that the fifteen year Investment Plans were suitable for their needs and circumstances. In contrast, she makes the following statements[14]:

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[10] See section 7(1)(a) of the Code.
[11] See section 7(1)(c)(x) of the Code.
[12] See section 3(1)(a)(vii) of the Code.
[13] See section 8(1)(b) of the Code.
[14] Errors not omitted.

'I told my office client relationship manager....not to allow Charlene to increase this plan on the committed plan because it would definitely result in a **lapse** and problems.....I also spoke to.....,our Old Mutual consultant and told her that I would not allow Charlene to write another committed plan to Mr. & Mrs. V. Vuuren.....Charlene told me about the R5 000 p.m investment but not about the **15-year term**. I told Charlene that she could be sure that this would be a **lapse**.' (own emphasis)

[15] It is evident from these statements that the respondent herself had concerns about Charlene's conduct, in particular her recommendation to complainants. In an attempt to divert attention from Charlene's advice, the respondent argues that the complainants were aware what they were signing for when the investments were made. I disagree that complainants were aware of the consequences of what they were signing for and this is evident from respondent's records.

[16] First complainant is a draughtsman and 2nd complainant a housewife who does needlework to supplement their income. By all accounts the complainants are not sophisticated investors and were dependent on Charlene to act in their interests and to advise them appropriately. When the Investment Plans were purchased complainants were 69 and 66 years of age, respectively. At the time, the maturity dates of the Investment Plans were beyond the complainants' actuarial life expectancy.[15] Because of their circumstances, the complainants needed unrestricted access to their funds to pay for living expenses and emergencies. However, the penalties payable on the Investment Plans severely restricted the complainants' access to their funds, as such, the fifteen year Investment Plans were entirely unsuitable to them. It needs

[15] The South African Financial Planning Handbook 2009, M Botha et al.

mentioning though that the commission received by Charlene is correlated to the term of the Investment Plans, which must have been the incentive behind the recommendation that complainants invest for fifteen years, even though respondent had not satisfied herself with their means.

Cause of loss

[17] Charlene invested complainants' funds in unsuitable products without paying attention to the interests of the complainants as required by section 2 of the Code. Her conduct ultimately led to the complainants having to pay unnecessary penalties when they altered the investment plans due to affordability. There is no question that Charlene's conduct caused complainants to suffer financial prejudice.

Quantum

[18] Initial figures provided by Old Mutual show that 1st complainant and 2nd complainant respectively paid penalties totalling R46 370.35 and R16 367.69. The Office subsequently requested Old Mutual to confirm the correctness of the penalties levied. There was a concern that the complainants might have been double charged penalties (a practice commonly referred to as double dipping). Old Mutual responded as follows:

'The Contract Values[16] that were confirmed in my email below is incorrect because it was not, as initially thought, the Contract Values determined on the respective disinvestment dates; Therefore, the Plan Amendment Charges applied to the correct

[16] Contract values provided by Old Mutual as set out in paragraphs 8.1 and 8.2.

Contract Values.....The following additional amounts are payable to the Complainants –

Contract 15346497: **R30,827.46, plus interest**;

Contract 15346455: **R10,163.79, plus interest**.'[17]

[19] Old Mutual has since paid the additional amounts of R30 827.46 and R10 163.79 plus interest to the complainants[18]. The complainants informed the Office that the respondent reimbursed a portion of the penalties charged by Old Mutual. All of these amounts must be taken into consideration in quantifying the actual loss suffered by the complainants.

1st complainant

R46 370.35 (total penalties)

minus R30 827.46 (Old Mutual refund)

minus R 3 500.00 (Respondent refund)

= **R 12 042.89** (difference)

2nd complainant

R 16 367.69 (total penalties)

Minus R10 163.79 (Old Mutual refund)

= **R 6 203.90** (difference)

Liability

[20] When Charlene rendered financial services to the complainants, she was acting in her capacity as a representative of the respondent. By respondent's own

[17] See annexure A for Old Mutual's breakdown of how amounts were determined.
[18] The rate of interest was not mentioned in the e-mail.

admission, Charlene failed to follow office protocol by not obtaining her approval when making the inappropriate investments. Notwithstanding, the ease with which Charlene was able to bypass office protocol suggests that the respondent did not have sufficient control measures in place to eliminate as far reasonably possible, the risk that clients will suffer financial loss through the professional misconduct of her representative.[19] Charlene's lack of record keeping, non-disclosure of material information and unsuitable advice given to the complainants, are all indicative of the respondent's failure to maintain the operational ability to fulfil the responsibilities imposed by the Act on FSP's, which includes oversight of the financial services provided by its representative.[20] For these reasons, I am compelled to hold the respondent liable for the losses suffered by the complainants as required by section 13(1)(b)(i)(*bb*) of the FAIS Act which stipulates that '....the provider accepts responsibility for those activities of the representative performed within the course and scope of, or in the course of implementing, any such contract or mandate....'

G. ORDER

In the premises, the following order is made:

1. The complaint is upheld;

[19] See section 11 of the Code.
[20] See Part VIII of Determination of Fit and Proper Requirements for Financial Services Providers – BN 106 in *GG* 31514 of 15 October 2008.

2. Respondent is hereby ordered to pay 1st complainant the amount of R12 042.89 and 2nd complainant the amount of R6 203.90;

3. Interest at the rate of 15.5%, per annum, seven (7) days from date of this order to date of final payment.

DATED AT PRETORIA ON THIS DAY OF 12 AUGUST 2013

NOLUNTU N BAM

OMBUD FOR FINANCIAL SERVICES PROVIDERS