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Santander's Madoff Sales Mean 'Catastrophe' for Teacher, Vendor

By Charles Penty and Esteban Duarte

Jan. 21 (Bloomberg) -- Banco Santander SA sold Bernard Madoff investments to a teacher and a street vendor, not just to wealthy private banking clients in Spain and Latin America.

Branch managers channeled customers with money from property sales or inheritances to private banking salespeople, lawyers for the investors said. A retired school teacher put 300,000 euros ($388,000), half her savings, in a structured product linked to Madoff, said Jordi Ruiz de Villa, an attorney at the Barcelona law firm Jausas. The vendor invested 325,000 euros of lottery winnings in a similar product and may have to return to street sales, according to lawyers at Cremades & Calvo-Sotelo in Madrid.

"The fact that someone has a sum of money in the bank doesn't make him a suitable customer for this type of product," said Ruiz de Villa, who's representing about 30 account-holders with potential claims of 10 million euros, including the teacher. "Some retail clients have suffered true personal catastrophes because of this." He wouldn't provide the teacher's name.

Santander, Spain's biggest lender, may lose customers at the domestic branch network that accounts for a third of profit if it is found to have misled people who trusted their neighborhood bankers, said Peter Hahn, a fellow at Cass Business School in London. The bank, led by Chairman Emilio Botin, has said clients have 2.33 billion euros invested with Madoff, including 320 million euros from private banking customers in Spain.

"The model in Spain where customers just left it to Big Daddy Botin to take care of things has been broken," said Fernando Zunzunegui, a Madrid-based lawyer. He said he is taking on Madoff-related claims valued at 8.2 million euros from 20 clients who are "clearly retail." He declined to provide detailed information about his firm's clients.

'Qualifying Investors'

Ruiz de Villa and Zunzunegui said they are signing up clients and reviewing the cases in preparation for filing possible lawsuits against Santander. Javier Cremades, chairman of Cremades & Calvo-Sotelo, said he'll push for a settlement first.

New York-based Bernard L. Madoff Investment Securities LLC collapsed last month after Madoff told his sons it was a $50 billion Ponzi scheme, according to a complaint filed by the U.S. Federal Bureau of Investigation. Worldwide, the victims include banks, charities and investors such as Madrid-based billionaire Alicia Koplowitz and film director Steven Spielberg.

Santander, based in the Spanish city of the same name, on Dec. 14 said international private banking clients and institutional investors had 2.01 billion euros of potential losses in Madoff-related funds. The rest of the money is in investments sold to "qualifying investors" in Spain.

Legal Protections

Branch customers were sold products linked to Madoff through Santander's Geneva-based Optimal Investment Services hedge-fund arm, said the three lawyers representing the bank's customers. Investors were asked to sign statements that they understood what they were purchasing and met the criteria for investing.

The bank has said it won't compensate clients who invested with Madoff because the losses involve fraud. A spokeswoman for Santander said the bank had no further comment on the matter.

Selling structured products to wealthy clients has been a popular strategy in Spain and wasn't in itself wrong, because Santander believed it would yield safe and stable returns, said Fernando Luque, an analyst at Morningstar Inc. in Madrid.

"Many of these institutions like Santander are going to be protected by the documentation, but the question is how great is the business damage from all this," Hahn of Cass Business School said.

Lottery Winner

Spanish securities law requires anyone offering investment services to "suitably evaluate" a customer's experience and market knowledge and ensure that he or she understands the risks.

The criteria for being a potential private banking customer are lower in Spain than other countries, said Manuel Romera, head of financial industry studies at Instituto de Empresa, a business school in Madrid.

A 2006 study by the school showed that Spanish banks tend to start targeting clients with 500,000 euros in assets, compared with 1.5 million euros for international banks.

The lottery winner invested in a Santander structured finance product, according to Cremades & Calvo-Sotelo. The firm is representing some 80 individuals in Spain and Latin America, mostly Santander customers, who have about 35 million euros of claims. Cremades declined to provide the investor's name.

'Stable' Fund

The teacher put half the proceeds from an apartment sale in a "multi-strategy" structured product, 35 percent of which was in Optimal Strategic U.S. Equity, an Irish-registered fund whose trades were executed by Madoff, according to Santander's description of the investment, which was shown to Bloomberg by Ruiz de Villa.

The document describes the investment as "conservative" and "probably the most stable" of all funds run by Optimal. Structured products have a defined maturity date and include a mix of assets to meet investor needs in areas such as risk hedging and diversification.

'Pending Valuation'

A retired electronics executive said his private banking account manager told him losses on a 400,000-euro investment he made three years ago could be 80 percent. His bank statement now lists the product as "pending valuation," the executive said in an interview. He asked not to be identified because he may have to return to work.

Spain's anti-corruption prosecutor last week said it had opened an investigation into Madoff's alleged fraud.

M&B Capital Advisers, a brokerage founded by Botin's son Javier and Guillermo Morenes, husband of his daughter Ana Patricia Botin, has said its investors put 152 million euros in funds linked to Madoff.

Santander shares have fallen 18 percent since the bank released details of potential Madoff-related losses. The Bloomberg Europe Banks and Financial Services Index dropped 27 percent in the same period.

In a speech at the Euromoney magazine awards last July in London, Botin urged bankers not to buy products they don't understand.

'Incalculable' Damage

"The damage to reputation from all this to the Santander name is incredible, incalculable, the kind that takes years to repair," said Bernhard Bauhofer, founder of Wollerau, Switzerland-based Sparring Partners GmbH, a consulting firm that specializes in corporate image management.

Santander, which calls itself "the world's best bank," has avoided most of the fallout from the U.S. subprime lending crisis. Last February, the bank took a 737 million-euro writedown on its stake in Sovereign Bancorp after the Philadelphia-based lender plunged in value following charges for loan losses. That compares with the $49 billion of losses and writedowns posted by Zurich-based UBS AG, the largest total among European banks.

In the five years through 2007, Santander's net income tripled to more than 9 billion euros as Botin expanded in Latin America.

Spain has the world's highest density of banks, with 96 branches per 100,000 people, compared with 18 for the U.K., according to a World Bank study. Santander has about 4,840 retail branches in Spain, while Banco Bilbao Vizcaya Argentaria SA has about 3,484.

In that environment, Santander has been expanding its private banking business. The division, with almost 110 billion euros under management, targeted 18 percent growth in managed assets in 2008 and a 20 percent increase in pretax profit, according to the bank's 2007 annual report.

'Back to Basics'

"Spain is a country of salesmen, but we also need financial experts to better explain the product to clients," said Romera, at Instituto de Empresa.

The Madoff case highlights the need for Spanish banks to return to good investment practices that should preclude clients from putting more than 15 percent of their money in a single security or product, said Jose Miguel Mate, chief executive officer of Tressis SV, a Madrid-based wealth management company.

"There will be a way back to the basics and to common sense," said Mate, a former commercial director of Banif, another private bank owned by Santander.

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