IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS PRETORIA

CASE NUMBER: FAIS 00536/13-14/ FS 1

FAIS 09212/12-13/ FS 1

In the matter between:

AMANDUS TOBIAS VILJOEN **Complainant**

and

DAWIE JOUBERT VERSEKERINGS MAKELAARS BK **First Respondent**

DAWIE JOUBERT **Second Respondent**

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

A. INTRODUCTION

[1] Sometime during 2008, complainant, then aged 51, followed the advice of second respondent and invested his life savings in Sharemax Zambezi Retail Park Holdings Limited, (hereinafter referred to as Zambezi Ltd) and Highveld Syndication 20 Ltd (hereinafter referred to as PIC or HS). The funds invested came from a pension pay-out following complainant's exit from a former employer.

[2] The Zambezi Ltd offer was promoted by Sharemax (Pty) Ltd (Sharemax) and the HS offer by PIC Syndications (Pty) Ltd (Picvest).

[3] Following the much-publicised financial challenges that the two schemes (Sharemax and PIC) experienced, resulting in the substantial reduction of complainant's income, complainant came to the conclusion that he had lost his capital and lodged the present complaint. At the time of lodging, complainant had not been paid his capital.

B. THE PARTIES

[4] Complainant is Amandus Tobias Viljoen, an adult male whose full particulars are on file with this Office.

[5] First respondent is Dawie Joubert Versekerings Makelaars BK, a close corporation registered in terms of South African law with registration number 1998/036065/23. The regulator's records confirm first respondent's address as 19 Bukes Street, Kroonstad, 9499. First respondent was authorised as a financial services provider on 26 August 2004 with license number 3368. The licence is still valid.

[6] Second respondent is Dawie Joubert, an adult male and key individual of the first respondent whose address is the same as that of first respondent. At all material times second respondent rendered financial services to complainant.

[7] I refer in this determination to first and second respondents collectively as "respondent". Where necessary, I specify which respondent.

C. BACKGROUND TO SHAREMAX

[8] Sharemax, a private company known as a promoter of public property syndication schemes, (property syndication schemes) was incorporated in 1998

and was based in Pretoria. Sharemax managed and provided administration services in connection with the immovable properties aassociated with the Sharemax group of companies. Although very little was highlighted about its role as a provider of secretarial services and manager of investor funds in relation to the companies within the group, the last two functions were at the heart of Sharemax's business operations. Essentially, Sharemax controlled most if not all the companies that fell within its group.

[9] On 13 September 2005, Sharemax was granted a licence as an Authorised Financial Services Provider (FSP) in terms of section 8 of the FAIS Act. In terms of the licence, Sharemax was authorised as a Category 1 FSP to render advisory and intermediary services with regard to securities and instruments, shares (1.8) and debentures (1.10).

[10] From time to time Sharemax promoted and issued prospectuses regarding various property syndication schemes. The prospectuses were purportedly registered with the Registrar of Companies in terms of section 155 of the Companies Act 61 of 1973, as amended. This complaint concerns Zambezi Ltd number 3 and Picvest prospectuses.

[11] The Zambezi Ltd prospectus states that the directors of Sharemax and Zambezi Ltd at the time were Johannes Willem Botha, Andre Daniël Brand, Diederick Rudolph Koekemoer, and Dominique Haese, all described in the prospectus as businessmen and business woman.

[12] Although the Zambezi Ltd prospectus made provision for the election of a new board by shareholders at the company's first annual general meeting, after registration of the prospectus, the promoter reserved the right to have three directors on the board[1] for the first five years. The number of directors could not be less than three and not more than five.

[13] There is no evidence that there was ever an independent board of directors, audit, risk, nor remuneration committees in place within the Sharemax group's business. (I expand more on this later in this determination)

[14] During the course of 2010 news of Sharemax's financial troubles surfaced. It was said that Sharemax was experiencing difficulties in paying income to investors. At around the same time, news that the South African Reserve Bank (SARB) was conducting an inspection followed. Not long thereafter the Registrar of Banks concluded that the Sharemax business model offended the Bank's Act. Directives were issued by the Registrar of Banks during September 2010 to Sharemax for the repayment of funds collected from individual investors.

[15] It would appear that funds were not repaid and during 2012 the court sanctioned schemes of arrangement[2] in respect of several schemes within the Sharemax group. These schemes were taken over by an entity known as Nova Property Group Holdings Limited 2011/003964/06 (Nova). Sharemax investors were issued with either debentures or shares in Nova. Nevertheless, Sharemax's FSP license lapsed in October 2012.

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1 Paragraph 3.3 of the Zambezi Ltd prospectus

2 As contemplated by section 311 of the Companies Act 61 of 1973

D. BACKGROUND TO PICVEST[3]

[16] PIC Syndications (Pty) Ltd (commonly known as Picvest) then an authorised financial services provider,[4] marketed shares through a well-established network of investment consultants and financial advisers.

[17] Investors were invited to invest in a number of public companies that formed part of the property syndication structures established and promoted by Picvest. Each company was established to acquire certain properties which typically comprised small shopping centres around the country.

[18] The intended syndication structure was that the investor would buy a share coupled with a loan account (referred to as a unit in the prospectus) in a public company and the immovable properties were meant to be registered debt free in the name of the same public company.

[19] The capital raised was to pay off and procure an unencumbered title for the properties specified in the prospectus. The net rental income would be distributed on a monthly basis to investors. It was further intended that a head lease and buyback agreement with a company known as "Zephan Properties (Pty) Ltd" would ensure a stable monthly income over a specific period and secure capital growth.

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3 For more reading on Picvest and its Highveld Syndications, refer to the matters of Geldenhuys and Others v Orthotouch Limited and Others, case number 42334/2014 (para 1-9) (High Court, Gauteng Local Division, and Zephan (Pty) Ltd (para 5) and Others v De Lange, case number 1068/2015 (SCA)

4 Picvest with Licence number 20878, has since been withdrawn, according to the Registrar of Financial Services.

[20] On 4 September 2008, the South African Reserve Bank (SARB) appointed inspectors to investigate the activities of Picvest to establish whether it was conducting the business of a bank. The intervention of SARB saw a reduction in the income provided by some of the syndications and the subsequent collapse of the schemes. Some of the Picvest companies were placed under business rescue[5] during December 2011, and a company known as Orthotouch Limited (Orthotouch), which was meant to purchase the syndicated properties and pay interest to investors, failed to do so. The result of which, a scheme of arrangement (in terms of section 155 of the Companies Act) was proposed between Ortotouch and its creditors on 7 October 2014. Picvest lost its licence as an FSP sometime in 2014 following the Registrar's decision to withdraw same.

E. INFRACTIONS OF NOTICE 459

[21] On 30 March 2006 the Minister of Trade and Industry, acting in terms of section 12(6) of the Unfair Business Practices Act, published Notice 459 of 2006 (Notice 459 or simply, Notice) in Government Gazette No 28690. The Notice declares the Minister's opinion (having considered a report by the Consumer Affairs Committee) that terms of the Notice are necessary to combat unfair business practices in property syndications. The Notice came into effect on 30 March 2006. The Notice further provides for penalties and imprisonment in the event of transgressions.

[22] Section 2 (a) of Annexure "A", which deals with **investor protection,** states as follows: "*Investors shall be informed, in writing, that all funds received from them*

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5 See paragraph 7 of the Ortotouch matter, reference in footnote 5

prior to transfer/finalisation shall be deposited into the trust account of a registered estate agent, a legal practitioner or a certified chartered accountant and provided that such trust account is protected by legislation. Individual investors are to be given written confirmation thereof. ***It shall be clearly stated who controls the withdrawal of funds from that account****. Such an account shall be designated " XYZ Attorneys/auditors/estate agents Trust Account- the xyz syndication*"....."

[23] In terms of section 2 (b) investor funds shall **only** be withdrawn from the trust account **in the event of registration of transfer of the property** into the syndication vehicle; **or underwriting by an underwriter whose details shall be disclosed; or repayment to an investor in the event of the syndication not proceeding**.

[24] Against the background of the Notice, the prospectuses of the two schemes, will be analysed.

Zambezi Ltd

[25] In the prospectus[6] issued by Sharemax, the promoter uses the words 'Zambezi Retail Holdings' or the 'Company' when referring to the public entity (Zambezi Retail Park Holdings Limited), into which investors' funds were paid and Zambezi when it refers to Zambezi Retail Park (Pty) Ltd (the entity that would eventually own the immovable property after transfer). For ease of reading, Zambezi Ltd in this determination refers to the public company to distinguish it from Zambezi (Pty) Ltd.

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[6] Zambezi Ltd prospectus 3

[26] The Zambezi Ltd prospectus offered units (to prospective investors) comprising one ordinary par value share at the issue price of R1000 per unit. The share was linked to an '*unsecured floating rate claim*'. In order to effect investments, investors were directed to complete the relevant application form and deposit funds into the trust account of attorneys Weavind and Weavind Inc. The prospectus[7] further conveyed that investor funds will be retained in the attorneys' trust account in terms of section 78 2 (A) of the Attorneys Act (Act 53 of 1979) until registration of transfer into the name of the syndication vehicle. In this respect the prospectus complied with Notice 459.

[27] In violation of the notice however, the same prospectus[8] made provision for the withdrawal of funds from the trust account prior to registration of transfer to fund, *inter alia*, commissions, directors' travel expenses, office and other expenses[9]. The prospectus further made provision for the advancement of large amounts of money as loans to the developer of the land, Capicol 1 (Pty) Ltd.

[28] The relevant paragraphs of the prospectus are quoted below:

28.1 Paragraph 4.3:

'The Company will operate as a holding company and intends utilising the proceeds of this offer to:

4.3.1. pay part of the Purchase price being R10 481 955……in respect of the entire shareholding in Sharemax Zambezi Retail Park (Pty) Ltd purchased from Sharemax for an amount equal to 16.64% of the

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7 Paragraph 19.10

8 Paragraph 4.3.1

9 The application form used to effect this investment notes that upon payment of the amount into the Attorneys' trust account, Sharemax will deduct 10% of the funds to pay marketing costs.

Purchase price to be paid by Sharemax Zambezi Retail Park (Pty) Ltd ***for the business referred to in 4.3.2 below……***

28.2 Paragraph 4.3.2:

to advance *loan funding in the amount of R50 000 000….. to Sharemax Zambezi Retail Park (Pty) Ltd for the purpose of paying part of the purchase price which is to be paid to purchase the Immovable Property from Capicol (Pty) Ltd (2007/010860/07) for a projected amount of R930 000 000 (excluding VAT) which purchase will be a purchase of an income generating undertaking as a going concern. The expected date of transfer is 1 November 2009. The actual Purchase Price will only be calculated and adjusted thirty days after date of occupation, once the income stream (rental) has been determined. The income generating business comprising, inter alia, the Immovable Property was purchased for an amount equal to an agreed cap rate of 9.80% per annum return on investment as at date of transfer of the Immovable Property in the name of Sharemax Zambezi Retail Park (Pty) Ltd. It has further been agreed that in the event of the actual income generated by the business as at the said date being more or less than as anticipated, the Purchase Price would be adjusted to equate the agreed cap rate of 9.8%.*

28.3 Paragraph 4.3.3:

Creating a cashflow shortfall fund for the Company in the amount of R2 518 045…..

28.4 Paragraph 4.8.1 reminds investors that '*All monies received from investors of the Company will be deposited in a trust account with the*

Attorneys who shall control the withdrawal of funds from that trust account.'

[29] The Sale of Business Agreement (SBA) was not attached to the prospectus but was, according to the prospectus, made available at the promoter's business premises. The SBA reveals a pyramid scheme. (This shall be further discussed later in this determination.)

Picvest

[30] According to the prospectus[10] and contrary to Notice 459 of Government Gazette 28690 of 2006, investor funds were to be held in the trust account of attorneys Eugene Kruger & Company Inc. until the syndication company took occupation of the properties mentioned in the prospectus.

[31] Following on the undertaking made in the prospectus, Picvest withdrew the funds from the attorneys' trust account well before the properties were transferred into the syndication companies and paid it to the sellers. Without reference to the investors, Picvest cancelled the sale agreements between the syndication companies and various sellers and brought on board an entity known as Orthotouch Limited (Orthotouch). The syndication companies and the various sellers then entered into agreement with Orthotouch in terms of which Orthotouch would buy the syndication companies. Nothing of substance appears to have materialised from the agreement[11]. Investors in a similar situation to complainant ended up filing complaints with this Office.

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10 The prospectus for HS 20

11 See in this regard the decision of the FSB Appeals Board in the matter of Picvest (Pty) Ltd v The Registrar of the Financial Services Board, https://www.fsb.co.za/appealBoard/Pages/fsd.aspx

F. THE COMPLAINT

[32] According to the complaint, complainant was advised by respondent to invest in HS 20 and Zambezi Ltd. An amount of R450 000 was paid into the bank account of each syndication as designated in the respective prospectuses. Both investments were effected on 23 April 2008.

[33] Complainant received interest payments from Sharemax[12] from April 2008 up to and including 30 July 2010, where after payments abruptly ceased. As far as the Picvest investment was concerned, complainant was to receive monthly income calculated at the rate of 10% on the investment of R450 000. Complainant indicated that he was initially paid about R4000, however this amount withered over time. Complainant is still receiving monthly income of R750 from the HS20 investment[13]. Complainant confirmed he has not been repaid his capital, notwithstanding maturity[14] of both investments.

[34] At the time the investments were made, complainant was 51 years old and unemployed. Prior to his retirement, he was employed as a train driver. Respondent knew that the funds came from complainant's retirement savings and that complainant had no capacity to risk his capital. Hence it is alleged by complainant that respondent had assured him then that the investment guaranteed his capital.

G. RELIEF SOUGHT

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12 In respect of the Zambezi investment.

13 Confirmed on 15 March 2017

14 According to the PIC documentation, the maturity date of the investment was 30 April 2014, in line with the buy-back agreement of 5 years. The Sharemax investment was set to mature in 5 years, thus also payable to complainant during April 2014

[35] Complainant seeks repayment in the amount of R900 000 from respondents. The basis of complainant's claim against respondent is the latter's failure to render financial services in line with the FAIS Act and the General Code of Conduct, which includes respondent's failure to appropriately advise complainant and disclose the risk involved in both investments.

[36] In so far as jurisdiction is concerned, each investment represents a separate and distinct cause of action. Thus, the Office has jurisdiction to consider the whole amount of R900 000.

H. RESPONSE

[37] In compliance with Rule 6 (b) of the Rules on Proceedings of the Office of the Ombud, (rules) the Office referred the complaints to respondent, advising respondent to resolve same with his client. Respondent duly responded on 31 May 2013 stating that the matter could not be resolved.

[38] On 30 June 2015, the FAIS Ombud addressed correspondence to respondent, in terms of Section 27 (4) of the FAIS Act, informing him that the complaint had not been resolved and that the Office intended to proceed with an investigation. The letter invited respondent to deal with the question of appropriateness of advice taking into account the risk involved in the investment and respondent's duty to recommend financial products that are suitable to complainant's circumstances. Respondent was advised, *inter alia*, that in the event the complaint was upheld, he could be held liable. Instead of dealing with the merits of the dispute, respondent, through his attorney, brought an application supported by a lengthy declaration for the following relief:

38.1 That this Office should find, in terms of section 27 (3) (c) of the Act that it is more appropriate to refer the complaint to a court and that this Office decline to entertain the complaint.

38.2 That, in the alternative, this Office should afford the respondents a "formal hearing", which had to include the exchange of pleadings, requests for further particulars, discovery, oral evidence from experts and oral evidence from witnesses who had to be subject to cross-examination, a public hearing and legal argument before determination.

[39] Respondents were effectively requesting that this Office afford them an adversarial procedure as it is applied in the high court. In plain language, they wanted a trial.

[40] Respondent filed two lengthy responses in terms of Section 27 (4) (c). The first response raised a number of legal points which, according to respondent, militated against consideration of the complaint by this Office. Respondent urged that the complaint be dealt with by a court of law. The declaration contained legal arguments that:

a) the processes of this Office were unconstitutional;

b) the procedure in this Office was inappropriate for this case;

c) the process "lacks transparency"; and

d) this office is not independent and is biased.

Finally, respondent's legal argument questioned whether this office was "a forum or a tribunal".

[41] In the matter of *Deeb Risk v The Ombud for Financial Services*[15], Baqwa J dismissed a similar application based on the same legal submissions as in this declaration. Accordingly, and for reasons that appear in the Deeb Risk judgement, respondent's motion is dismissed.

[42] I add that respondent's grounds do not disclose any special or exceptional circumstances that warrant the referral of this complaint to court. Respondent's submission has no merit.

[43] The rest of the response can be summarised as follows:

43.1 Respondent stated that he had informed complainant that there were risks associated with investments in unlisted securities. Respondent did not elaborate on what those risks were.

43.2 Respondent further states he recommended the two investments so that complainant diversify (or spread the risk). Picvest and Sharemax were both property syndication schemes offering above inflation returns; there was, in reality, no spreading of risk.

43.3 Respondent further stated that he had conducted due diligence on both Picvest and Sharemax.

43.4 Respondent relied on complainant's signatures on both the Sharemax and Picvest application forms and suggested that after explaining the various options, complainant accepted and signed the application forms. Respondent's record of advice was annexed to the response. A cursory

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15 Deeb Risk v The Ombud For Financial Services & Others (38791/2011)[2012]ZAGPPHC 199 (7 September 2012)

glance at the record of advice gives no information such as required by section 9 of the Code[16].

I. DETERMINATION

[44] The following issues arise for determination:

44.1 Prescription.

44.2 Appropriateness of advice: the question is whether complainant was appropriately advised, as demanded by the Code.

44.3 Causation: in the event it is found that respondent breached the FAIS Act and the Code, the question that must be answered is whether such breach caused the loss complained of.

44.4 Quantum.

J. PRESCRIPTION

[45] Respondent raised, perhaps opportunistically, the question of prescription. In so doing respondent pointed only to the provisions of section 27 (3) (a) (i) and conveniently, left out sub section (a) (ii), which reads as follows:

"Where the complainant was unaware of the occurrence of the act or omission contemplated in subparagraph (i), the period of three years commences on the date on which the complainant became aware or ought reasonably to have become aware of such occurrence, whichever occurs first" [own emphasis].

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16 Section 9 enjoins providers to set out a brief statement regarding the financial product/s considered, and note reasons for concluding that the recommended product would suit the client's circumstances. Such record must be maintained by providers.

[46] It is correct that the advice was rendered during 2008. What is relevant however, is when complainant became aware that something was wrong with the investments. Complainant became aware that there was a problem with the Sharemax investment when he did not receive his monthly income during or about 31 August 2010. In respect of the PIC investment, complainant is still receiving income, but at a reduced rate since approximately 2011. He submitted his complaint to this Office on 28 February 2013, well within the three-year period required by the law. The argument with regard to prescription is thus settled.

Whether complainant had been appropriately advised

[47] Before I deal with respondent's declaration, it is necessary to state what was expected of respondent, bearing in mind the issues. In terms of the Code, read with the Act, the duty rests on the FSP to appropriately advise his/her client and in so doing, disclose the material aspects of the transaction in order for complainant to make an informed decision.

[48] In responding to the complaint, respondent was required to explain:

48.1 how he satisfied himself that Zambezi Ltd was able to pay the promised monthly returns, given that it had not traded, had made no profits of its own and the syndicated property was still under construction;

48.2 whether he considered that the returns were being paid out of the investors' own funds;

48.3 why respondent did not regard the investments as highly risky; and

48.4 why and on what basis respondent concluded that the products were appropriate for complainant, bearing in mind the latter's financial circumstances and his capacity and tolerance for risk.

[49] Respondent's version is that he conducted due diligence on the two investments, Zambezi Ltd and Picvest. In advising complainant, respondent discussed the risks involved in both investments, leading to complainant accepting his recommendation. I mention at this point that disclosures and the advice must take into account the client's reasonably assumed level of familiarity and understanding of financial products. Notwithstanding the disclosures, the provider is not relieved from his duty to act in the interests of the client[17] and recommend a product(s) that are commensurate with the client's circumstances[18].

How Sharemax paid the returns (This is inextricably linked to the violations of Notice 459)

[50] Respondent says he satisfied himself of Sharemax's ability to pay income to investors by looking into the affairs of the respective syndications, utilizing the contents of the prospectus. In respect of Zambezi Ltd, respondent explained that investors received income from the promoter, initially funded from interest earned on the pooled funds in the attorney's trust account. Thereafter, income was obtained from interest received from the developer on the loan funding provided by the promoter to the developer and ultimately, from the rental income received from tenants of the shopping centres.

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17 Section 2 of the Code

18 Section 8 (1) (a) to (c) of the Code

[51] Respondent did not explain how it was possible to pay investors from interest earned on the call account in the attorney's trust account, bearing in mind the rate of interest paid by the bank on this account. Respondent deliberately fails to state what interest was paid by the bank. The rate at that time was between 4 - 5%[19] during August 2009. This interest was entirely inadequate to cover payments to investors when one takes into account the payment of commissions on the capital invested, calculated as 6 %; 10 % administration fees[20] and 3% to Brandberg Konsultante (Pty) Ltd as "agent fees". Yet, Sharemax was able to pay "*12% from the interest earned on call accounts*"? This was simply impossible. If respondent did not understand the flaw in the prospectus, then how did he possibly explain this to complainant?

[52] I refer to the commentary in *CC van Zyl v JC Mostert*[21] paragraphs 51-60, regarding the same question of how Sharemax paid the return to investors and note that same applies to this case, *mutatis mutandis*.

How did Picvest pay the return to Investors?

[53] The prospectus issued by Picvest carried a clear message of how the directors intended to deal with investors' funds. Respondent, being aware of the regulations pertaining to this investment, still went ahead and recommended it.

[54] The message contained in the prospectus made it clear that funds would remain in the attorneys' trust account up until the syndications took occupation of the

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19 http://www.fidfund.co.za/banking-options/credit-interest-rate-history/ (accessed on 16 November 2016)

20 Refer to the Zambezi application form

21 FAIS-02955-11/12 KZN 1

properties. Instead, Picvest accessed investors' funds prior to registration of transfer into the names of the syndication vehicles and paid it as they pleased.

[55] It is noted in paragraph 6, schedule 3 of the HS20 prospectus that the company had never conducted any other business before the purchase of the mentioned properties on 26 July 2007. The question that arises is how investors were paid income, if not from their own investment? Again, interest was supposedly paid from the attorney's call account. As argued in paragraph 50, this was simply not possible.

Risk

[56] Despite respondent's claims of conducting due diligence and discussing the risk involved in the two schemes, I demonstrate in the following paragraphs that respondent had no appreciation of the magnitude of risk involved in either scheme and could not have disclosed same to complainant.

Zambezi Ltd

[57] Upon reading the prospectus, the following poor governance red flags were manifest. When considered cumulatively, the red flags point to one conclusion: the way the investment was promoted was a lie. Each one of the flaws I will point to were sufficient to have seriously discouraged respondent from investing his client's funds.

57.1 The directors of Zambezi Ltd were the same as the directors of Sharemax[22] and Zambezi Pty Ltd. An interesting point to note in respondent's response is his failure to recognize the obvious conflict of

[22] Note that Sharemax was the company secretary, property administrator and fund manager.

interest that the directors faced as they went about their daily duties. Respondent, for example, had no clue of the costs claimed by Sharemax from investors' funds for rendering secretarial services, fund management and property administration. This aspect of the investment alone posed high risk to investors. A basic knowledge of corporate governance[23] would have alerted respondent to the inherent risks.

57.2 There is no evidence (and this was patently clear from the prospectuses) that an independent board of directors ever existed in the entire group of Sharemax entities at the time, nor were there independent audit, risk and remuneration committees. With no evidence of independent oversight, it is fair to conclude that investors would have no protection whatsoever and were at the mercy of executive directors who were accountable only to themselves. The fact that a business operation of the size of Sharemax, funded by investors' monies, did not see the need to have an independent board of directors is quite telling. This particular risk factor was not seen by the respondent.

57.3 Flowing from the lack of oversight arrangements by means of an independent board of directors, respondent did not know whether there were any internal controls, and the extent to which such controls would support reliance on financial statements.

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[23] Reference is drawn to the King II report where one of the seven characteristics of good corporate governance is independence. It is explained as: "*Independence is the extent to which mechanisms have been put in place to minimise or avoid potential conflicts of interest that may exist, such as dominance by a strong chief executive or large shareowner. These mechanisms range from the composition of the board, to appointments to committees of the board, and external parties such as the auditors. The decisions made, and internal processes established, should be objective and not allow for undue influences*".

57.4 It is evident from respondent's version that he had not seen a set of audited financial statements of any of the entities within the Sharemax stable. Respondent could not know whether the assets of the entities within Sharemax were properly recorded and expenses accurately accounted for, so as not to inflate profits or understate losses.

57.5 Each share sold comprised an unsecured floating rate claim. The prospectus states that the interest payable on the claim component of the unit, **will be determined from time to time by the directors**[24]. There is no evidence that this was explained to complainant.

57.6 Paragraph 4.2 of the prospectus notes that the company had never traded prior to its registration and has not made any profit whatsoever. The question that should have immediately arisen in respondent's mind is the source of the income from which investors will be paid.

57.7 From the projected financials in the prospectus[25], there were going be significant shortfalls. Respondent does not explain how the entity intended to make up these shortfalls and why, notwithstanding this information, he still went ahead with advising clients on the investment.

[58] According to respondent he considered that there was risk in the investment, but he did not see the risk as too high after reading the prospectus. He supports his contention by pointing out that there was a bond in favour of Sharemax

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[24] See paragraph 9.3.1 of the prospectus

[25] Paragraph 5.12 of the prospectus

"*which secures the investment against the underlying property. This constitutes "real" security, being the same type of security taken by banks when lending funds to a property developer.*" This is entirely misleading and not supported by any facts.

[59] The prospectus stated that there was no registered bond in place (it was in the process of being registered). Why respondent viewed the alleged bond as security is unexplained. Respondent also failed to deal with the valuation of the immovable property, compared to the debt intended to be secured. The total amount invested by investors far exceeded the value of the property, if one considers the circumstances around the business agreement, the payment of administration and commissions. Even if there was a registered bond over the property, it was quite useless to investors.

[60] Respondent then states that the high court holds divergent views from this Office regarding risk relating to property syndication companies. To support this startling statement, respondent refers to a judgement in the case of *Anne-Marie de Lange vs Zephan (Pty) Ltd and others*[26]. This judgement certainly does not support respondent's submission. The judgment concerns a class action brought by investors who lost their funds in the Picvest property syndication. Respondent quotes from the judgement to make the submission that bonds and buy-back agreements render this investment risk free. The learned Judge said no such thing; the learned Judge was quoted out of context.

[61] The full quotation is as follows:

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[26] (82322/14) [2015] ZAGPPHC 540 (22 July 2015)

"The plaintiffs [investors] purchased the shares because of the security of the buy-back agreements. That made the investment ostensibly risk-free. The investors were made to believe that contracts in that form had in fact been signed. It is highly probable that such contracts had in fact been entered into, at least orally,"

[62] Respondent only quoted the first two sentences. The learned Judge did not suggest that buy-back schemes and bonds made the investment risk free. His Lordship was referring to how investors were lured into making an investment in Picvest on the understanding that a buy-back contract was signed. In this case, the investors brought an application for summary judgement where the plaintiffs enforced the terms of the buy-back agreement. The defendants unsuccessfully defended the application on the basis that the buy-back agreement was of no force and effect. Judgement was granted in favour of the plaintiffs against the masterminds behind the scheme.

HS 20

[63] In respect of the prospectus issued by Picvest, I need not look any further than the affront to the law as Picvest had communicated its intention on how it would deal with investors' monies. (See paragraph 29 of this determination).

What the Code demands when providers render financial services

[64] The complaint in this case centres on the appropriateness of advice. Complainant relied on, and trusted the advice of respondent.

[65] The record of advice provided by respondent dated 23 April 2008 deals with both investments and explains the basis for recommending them.

[66] It is stated in the document that complainant did not want to invest with banks, as he required income and capital growth. The record of advice provides no further details in respect of the types of products that were evaluated, in violation of section 9 of the Code. In fact, there is reference only to PIC and Sharemax. The only reasonable deduction to be made under the circumstances is that respondent did not provide any other options, apart from the two property syndications. It boggles the mind as to why banks are mentioned with the conclusion that they were rejected by complainant. No reference is made and certainly no information is recorded to establish complainant's risk capacity and what in complainant's circumstances matched the high risk in the two investments. Respondent does not state what he considered and why he concluded that these two investments were the most appropriate to suit complainant's needs.

[67] Section 9 (1) of the Code provides:

"A provider must, subject to and in addition to the duties imposed by section 18 of the Act and section 3(2) of this Code, 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 brief summary of the information and material on which the advice was based; the financial products which were considered; the financial product or products recommended with an explanation of why the products selected, is or are likely to satisfy the client's identified needs and objectives; [own emphasis]"

[68] It is worth noting that complainant had informed respondent that he could not afford to lose his funds as they represented his pension. At any rate, the

financial circumstances of the complainant objectively indicated that he did not have the capacity to absorb high risk. I am therefore not persuaded by respondent's submission that there was a thorough discussion of the products selected. The record demonstrates that respondent failed to carry out investigations of complainant's circumstances and without appreciating the risks involved in this product, recommended the products to the unsuspecting complainant.

[69] Bearing in mind that respondent had concluded that complainant was a conservative investor, according to his risk profile analysis, I am persuaded that the investment in the two property syndications had to do with respondent's interests. In this regard, the 6% commission with no claw-back provisions comes to mind. Accordingly, the advice could not have been in the interests of complainant. Respondent's conduct undermined the Code.

[70] Respondent notes in his response that the recommendation of a suitable product is often a balancing act between the client's needs and circumstances. Correct, except that this is half-truth. The client's circumstances and needs, according to the Code, must be matched with the risk inherent in the product. Respondent cannot rewrite the law.

[71] A professional provider would not rely on the claims of a return when analysing a financial product. If it is true that complainant insisted on high income and returns, after a proper discussion of the risks involved in the two products, respondent was obliged to comply with the provisions of section 8 (4) (b) of the Code. In any event, on the basis of what has been pointed out in this

determination, respondent was not in a position to explain the risks to complainant.

[72] On a balance of probabilities, had complainant been fully aware of the risks inherent in these products, he would not have made them. Respondent's reliance on complainant's signature as proof that he understood the risk is untenable, as I have already demonstrated. Simply informing a client that the investment is not guaranteed or that there are risks in unlisted securities does not explain the risk to a lay person. Nor does it absolve respondent from his duty to appropriately advise and act in the client's interest.

[73] What complainant needed to know is that he stood to lose his capital because of, amongst other reasons:

73.1 the directors of both schemes, Zambezi Ltd and Picvest, had chosen to disregard the law, see in this regard discussion regarding Notice 459;

73. 2 showed no regard for the interest of investors; and,

73.3 showed no interest in conducting their business along sound corporate governance principles.

[74] The Code requires that the nature of the risk is to be disclosed to the client in unambiguous terms, in a language that the client can understand, so that clients make informed decisions. Complainant could not have made an informed decision about the Sharemax or PIC transactions.

Whether respondent's conduct caused complainant's loss

[75] The facts in this case point to the conclusion that the investments in Sharemax and PIC were made as a result of respondent's advice. The test for factual causation is satisfied.

[76] The next step is to establish whether, as a matter of public and legal policy, it is reasonable to impose legal responsibility on respondent for the failure of the investment. In other words, could respondent have reasonably foreseen the collapse of respective syndications?

[77] The reasonable foreseeability test did not require that the precise nature, or the exact extent of the loss suffered, or the precise manner of the harm occurring should have been reasonably foreseeable for liability to result; it was sufficient if the general nature of the harm suffered by complainant and the general manner of the harm occurring was reasonably foreseeable.

[78] Both prospectuses were patently in violation of Notice 459; add to that the poor governance practices that permeated throughout the businesses of the two schemes; the conclusion is inescapable that the loss was inevitable.

[79] If respondent had only done his work according to the Act and the Code, no investment would have been made into the two property syndications, bearing in mind complainant's personal circumstances.

[80] It may be easy and convenient to impute loss to director mismanagement or other commercial causes. In this case however, complainant's loss was not caused by management failure of either schemes, it was caused by respondent's inappropriate advice. That the risk actually materialised, for

whatever reason, is not the issue. Otherwise the whole purpose of the Act and the Code would be defeated. Every FSP can ignore the Act and Code in providing financial services to their clients and hope that the investment does not fail. Then when the risk materialises and loss occurs they hide behind unforeseeable conduct on the part of product providers. This will defeat the purpose of the Act and Code.

[81] The loss suffered by complainant was as a result of respondent's inappropriate advice. I refer in this regard to *Standard Chartered Bank of Canada v Nedperm Bank Ltd*[27] where the Court held that:

"as to the issues of loss and causation, that although the untrue report issued by the respondent had been a factual cause of the appellant's loss, the test to be applied to the question whether the furnishing of the untrue report had been 'linked sufficiently closely or directly to the loss for legal liability to ensue was a flexible one in which factors such as reasonable foreseeability, directness, the absence or presence of a novus actus interveniens, legal policy, reasonability, fairness and justice all played a part."

[82] The financial red flags were patently clear from the onset and these were sufficient to stop respondent in his tracks. He carried on nonetheless. Predictably, when the house of cards came tumbling down, respondent would have nothing to do with it, claiming he could not have foreseen the collapse.

M. FINDINGS

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[27] 1994 (4) SA 747 (AD)

[83] In the premises, based on the reasons set out in this determination, I make the following findings:

83.1 Respondent failed to render a financial service fairly with due skill, care and diligence and in the interest of client and integrity of the financial services industry, thereby contravening Section 2 of Part II of the General Code of Conduct.

83.2 Respondent advised complainant to invest in the risky Sharemax and PIC property syndication schemes without taking into account the needs of complainant or the risk involved in the product in contravention of section 8 (1) (a),(b) and (c), as well as section 8 (2) of the General Code of Conduct.

83.3 In advising complainant to invest in Sharemax and PIC, respondent contravened sections 2; 3, 7 (1), 7 (2) and 9 of the Code. I also find that respondent's conduct was the cause of complainant's loss.

N. ORDER

[84] In the result, I make the following order:

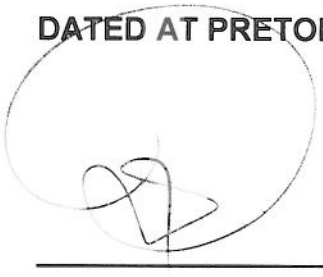
1. The complaint against respondent is upheld.

2. Respondents are ordered to pay complainant, jointly and severally, the one paying the other to be absolved, the combined amount of R900 000 to complainant.

3. Interest on the amount of R900 000 shall be calculated at the rate of 10.25% per annum from the date of determination to date of final payment.

4. Complainant's rights in terms of the PIC claim is ceded to respondent following payment of the capital and interest.

DATED AT PRETORIA THIS THE 24th DAY OF APRIL 2017.



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OMBUD FOR FINANCIAL SERVICES PROVIDERS