**THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS**

**PRETORIA**

**CASE NUMBERS: FAIS 07274/10-11 GP1**

**In the matter between:**

**JOYCE SUSANNA LOUWRENS N.O.** **Complainant**

**AND**

**CHARLES N BOTES**

**t/a HAMILTON SOLUTIONS KEMPTON PARK** **Respondent**

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

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## A. INTRODUCTION

[1] Carel Christian Engelbrecht was 65 years old when respondent advised him to invest his savings, in an amount of R800 000 in Sharemax The Villa Retail Park Holdings Limited (The Villa).



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[2] Mr. Engelbrecht (the deceased) passed away on the 1 January 2012 after the complaint was made, and the complainant was appointed as a joint executor of his estate. The deceased was her father.

[3] Sharemax stopped making interest payments and eventually it was finally liquidated. Complainant believes that the deceased's capital and accumulated interest is lost. Various communications with respondent failed to result in any settlement between the parties. A complaint was filed in this office. Thereafter this office wrote to respondent requesting that he attempt to settle the matter with complainant. Respondent did not believe that the matter was capable of being settled by him.

## B. THE PARTIES

[4] The complainant is Joyce Susanna Louwrens who represents the deceased in this complaint. She was appointed as a joint executor in the deceased's estate by the Master of the High Court on the 1 January 2012. A copy of her letters of executorship was delivered to this office and is on record.

[5] The respondent is Charles N Botes an FSP who traded under the name and style of Hamilton Solutions Kempton Park. At the time of advising the deceased, respondent was licensed under FSP Number: 6678. This licence did not authorise respondent to advise on shares and debt instruments. In other words, respondent was not licensed to sell Sharemax investments. However, respondent's license has since lapsed, according to the records of the FSCA.

## C. THE COMPLAINT

[6] The investment was made by the deceased on the 22 October 2009. Respondent met with deceased on the 22 October 2009 and advised him to invest R800 000 of his retirement funds into Sharemax The Villa. Respondent emphasised the good interest to be earned in 2009 and advised that this will increase in 2010. Respondent even said that he invested his own funds in Sharemax.

[7] Deceased was a panel beater by profession and only had a standard six education. Deceased trusted respondent to have given him good advice and the right choice of investment. On the 22 October 2009, deceased signed the forms to invest in The Villa. According to complainant, the deceased was not handed a prospectus but was merely told about the investment being excellent and the interest he will get. Respondent met with deceased at the bank on the 24 October 2009 when the funds were transferred into the investment.

[8] Complainant states that the broker “did not give correct advice to my dad, a pensioner with 80% of his funds” being placed into “this high-risk investment”.

[9] In August 2010 deceased stopped receiving interest and also read about Sharemax in the newspapers. Complainant, on behalf of her father, sent an email to Sharemax on the 26 October 2010, but received no reply. On the 1 November 2010 complainant sent a letter to respondent. The latter responded to this and I will discuss this below. On the 6 November 2010 the deceased received a circular letter from Sharemax detailing what steps were being taken and a promise to keep the investors informed.

[10] Complainant holds respondent liable for the loss of the investment; “due to incorrect advice”. Complainant claims, from respondent, payment of the accumulated interest from August 2010 to date as well as return of the capital.

[11] There was some relevant correspondence between complainant and respondent and I deal with it immediately. On the 1 November 2010 complainant wrote to respondent requesting the following information:

a) Was a needs analysis done for Mr Engelbrecht? If so, a copy was requested; and

b) Was a prospectus handed to Mr Engelbrecht?

[12] On the 5 November 2010, respondent responded to the letter as follows:

a) “In terms of the FAIS ACT, under certain circumstances, not do a full needs analysis (sic), and Mr Engelbrecht said it was not necessary”.

b) “We had a meeting on Thursday the 22 October 2009 and I told Mr Engelbrecht to think it over before we come to an agreement and on Saturday 24 October 2009 the application was signed.”

c) “The prospectus was handed to Mr Engelbrecht attached and signed, **SHAREMAX INVESTMENTS RISK ASSESSMENT ON PRODUCT INFORMATION”;**

d) Respondent then states that 3 independent directors were appointed to all Sharemax companies. They will start the communication process in the near future.

I will refer to this letter in more detail below.

## D. THE RESPONSE

[13] On the 7 December 2010, this office referred the complaint to respondent and requested a response. Respondent was also requested to provide a statement of how the investment

was entered into; proof of financial planning conducted for deceased and why this product was recommended bearing in mind deceased's financial needs and risk profile.

[14] Respondent was also required to explain why he was eligible to market Sharemax, bearing in mind his license status. Respondent was requested to provide this office with his record of advice and any other document he wishes to use to support a claim that he had complied with the General Code of Conduct for FSPs (The Code).

[15] Respondent made a written response to the complaint and the letter. This office was not entirely happy with the response and on the 14 August 2011 another letter was written to respondent requesting a response to a number of queries directed at his decision to advise a pensioner to invest 80% of his retirement funds in Sharemax. To this letter came a more comprehensive response from respondent. I will deal with both responses below.

[16] Respondent was contacted by the deceased's sister in law who requested him to give advice regarding his provident fund pay out. Of significance is that prior to meeting with the deceased, respondent was instructed that "the money should be fixed to receive a regular income and to preserve the capital and not be easily withdrawn." This is confirmed by respondent who knew that deceased did not want to lose his capital. Respondent had to explain why he then decided that Sharemax, a high-risk investment was found to be appropriate for deceased's needs. This issue will be dealt with in more detail below.

[17] Respondent states that a full needs analysis was not done. He advised deceased that it was not recommended that he put his entire pension into one fund and that he should split his investment. I find nothing wrong with this advice save that it is inconsistent with what respondent actually did. Respondent had to explain why he then, invested 80% of the

pension funds into a single, high risk investment where the capital was at risk of being lost.

[18] At the time of providing the advice, apparently Respondent presented deceased with a Sharemax prospectus along with quotes for income. The quotes are relevant and it is necessary for me to deal with them immediately:

a) The quotes appear in a document prepared by respondent in his own hand writing. Quotes were provided from Sharemax, Sanlam and AIMS. The manner in which the quotes are arranged on this document is significant. It begins with Sharemax and a quote on a R1 million is presented at 12.5% providing a monthly income of R10 416 – 67. An interest rate of 11.8% is also quoted for Sharemax providing income of R9166.67 per month. The next quote is also for Sharemax, but on an investment of R800 000 at 12.5% per annum providing income of R8333.33 per month. This quote also presented "capital growth" at 11.0% per annum of R7333 – 33 per month.

Then follows an investment of R200 000 in Sanlam, described as a "guaranteed investment over 5 years". This provides income of R1244.72 per month. This was followed by another quote on a Sanlam investment of R400 000, providing income of R2 533. 72 per month. However, the rate of interest is not stated. Immediately below the Sanlam quote, there follows another Sharemax quote for R600 000 which provided a return of 12.5% in an amount of R6 250 – 00 per month, there is also a quote of 11.0% per annum for capital growth. Then follows what is described as "Aims guaranteed investment" for R400 000 providing income of R2 566 – 17 per month, the rate of interest was not provided. Finally, there appears another Sharemax quote for an investment of R400 000 providing income of 12.5% per

annum with a monthly payment of R4 166 – 67 and the quote included capital growth of 11% per annum of R3666 – 67 per month.

b) What is patently clear from this quotation, it was designed to persuade the client to invest in Sharemax. A lay client will take one look at this and will see that Sharemax, is by far, the best performing investment. The quotation was made to mislead the unsuspecting lay client. The Sanlam and Aims investments are described as “guaranteed investments” but there is no indication of what kind of investments they represent and how it differs from Sharemax.

c) The immediate question is how Sharemax can outperform the likes of Sanlam and Aims. Respondent was under a duty to explain this to client. There is no record that respondent did so, to enable client to make an informed decision.

[19] Respondent then advised deceased to split his investment between Sharemax, Sanlam and Aims. Deceased “opted “to invest R800 000 in Sharemax, to get the highest income and R200 000 in Sanlam 5-year guaranteed investment plan with income. A further R53 000 was invested in a 5-year savings plan with Sanlam, no income.

The advice to spread one’s investments is sound, however respondent advised deceased to invest just over 80% of his funds in Sharemax. This does not amount to any mitigation of risk. In fact, respondent did the opposite by investing most of the funds in a risk capital investment that is Sharemax. Respondent also knew that Sharemax warned that investors ran the risk of losing their capital and income. Respondent also did not explain why he believed that Sharemax was an appropriate investment for deceased’s needs, bearing in mind that respondent was mandated to invest with capital preservation.

[20] Respondent submitted that his presentation took place on the 22 October 2009 and he told the deceased to “think it over”. The parties then met on the 24 October 2009 to “sign up and pay the money”.

[21] Respondent dealt with his license status and admitted he was not licensed, in his own right, to market Sharemax products. He acted as a representative of USSA, a Sharemax front company. When he advised deceased to invest, he did so as a Section 13 representative of USSA.

**The Documentation**

[22] Respondent attached a number of documents to his response; these comprise application forms for the Sharemax and Sanlam investments. There is also a document to show compliance with Section 8(4) of The Code. I deal with the relevant documents below.

**Section 8(4) of The Code**

[23] Respondent provided a document titled “Advice Record in Terms of Section 8 (4) of The General Code”. Section 8 (1) (b) of The Code provides that a FSP must conduct an analysis, for purposes of the advice, based on information obtained from client. Section 8 (4) provides for circumstances where client does not give the necessary information or where client declines an analysis. Respondent relies on this section for not carrying out a full needs analysis. This form, created by respondent, serves the purpose of recording that respondent proceeded to advise client subject to Section 8 (4). However, the form contains certain relevant information. The form was filled in by respondent in his own hand writing.

a) The document records that client chose not to provide full information because "client wanted only to invest his retirement funds so as to earn an income".

b) The document records that client said that it was not necessary to carry out a full analysis.

c) The document records the information on which the advice was based. This is stated as "to provide for retirement";

d) Client risk profile is recorded as "moderate";

e) Client's investment objective is recorded as "to protect pension funds".

f) It is recorded that client considered the Sharemax investment because of "best interest income";

g) It is recorded that Sharemax was recommended because of "highest income".

This document confirms that respondent was aware that client wanted to protect his pension funds and to obtain an income from it. It is surprising that client was considered to be moderate in terms of his risk profile. In fact, on the information presented to respondent, it was clear that client was a conservative investor. But even as a moderate investor, the Sharemax investment was entirely inappropriate.

**Sharemax Application Form**

[24] Respondent attached a copy of the Sharemax application form, which was also filled out by himself. This form contains important information which I detail below:

a) Under the heading "Instructions" the following "Notice" appears: investors' attention is drawn to the fact that on payment of the purchase price for the unit and once the cooling off period has lapsed, an amount equal to 10% of the invested amount will be released to the promoter for payment of commissions. Further that the promoter "will eventually pay all the commissions".

What this means, is that Sharemax will deduct 10% of investor's funds to pay commissions and other costs. But undertakes to repay it at some future unknown date. In effect, Sharemax borrowed out of investors capital to fund commissions and other payments. It was important for deceased to know this. I must assume that respondent was certainly aware of it.

b) Then the form contains a list of Schedules to the prospectus. An important document for investors is schedules H1 to H3, which is the business agreement entered into with Capicol 1 (Pty) Ltd, the developer. This document was not annexed to the prospectus but was available on request. The reason this document is so crucial to investors is because it records that Sharemax was going to use investor funds to make a loan to the developer. The latter was going to pay interest on the loan at 14% per annum. Sharemax then paid 12.5% interest to investors. Effectively investor funds were also used to pay them their monthly interest.

There is no evidence that respondent obtained this contract and drew deceased's attention to it. This is highly relevant information which respondent was obliged to disclose to his client, before the funds were invested. It made no sense just leaving a copy of the prospectus with client, knowing that important schedules accompanied the prospectus.

c) The form provides for a "Client Mandate" which was signed by deceased and respondent. The importance of this document lies in the fact that it contains a number of explicit warnings that the investment is high risk. The following warnings appear:

Firstly, under a heading "General Risk Disclosures" there is a reminder that there is inherent risk of capital loss and the document sets out some of the factors determining the levels of risk;

Secondly, that Sharemax does not guarantee capital growth or capital preservation in respect of investment in unlisted securities in unlisted property investments;

Thirdly, there is a risk with unlisted property investment that capital and income could not materialise, repayment of capital and income is not guaranteed, the performance of the investment is not guaranteed and the investment should be considered a “risky capital investment”; and

Fourthly, that investors may not get back the full amount invested and run the risk of financial loss.

d) What strikes one on considering this document is that it is presented in the smallest font possible. There is no spacing and more than 22 lengthy clauses are crammed onto a single page. The investor is not likely to read this document. Certainly, the deceased, a 65-year-old panel beater, was not likely to read and understand this. However, the respondent, as a reasonably competent and trained FSP, will be familiar with the contents of this document. There is a duty on him to explain these warnings to client so that the latter can make an informed decision. There is no evidence that respondent did so. On the probabilities, had he made the disclosures, deceased would not have invested in such a high-risk investment. Respondent knew that his client wanted to preserve his capital and wanted a monthly income. Notwithstanding a warning in the prospectus and application forms that this was a high-risk investment, respondent still deemed the investment to be suitable for his client.

**Sanlam Documentation**

[25] Respondent also attached copies of the documentation for the investments made in Sanlam. These documents are not relevant to this complaint and I will not deal with them

in any detail. However, it is worth noting that the Sanlam documents reveal the names of the funds in which deceased's money was invested. Firstly, 50% of the available funds were invested in Allan Gray Stable Fund where the risk level is stated as "conservative". Secondly, 50% of the funds were placed in Allan Gray Balanced Fund where the risk level is stated as "moderate". I must add that this information was filled in by respondent.

[26] The point to be made is as follows with respect to the Sanlam investment:

a) Respondent demonstrates that deceased was a conservative or moderate investor. This is perfectly compatible with deceased's financial and risk profiles.

b) The funds selected by respondent are also perfectly suitable for an investor of deceased's financial profile and needs.

c) Yet, having such knowledge, respondent still decided that Sharemax, a risk capital investment, was suitable, for most of the investment, for the deceased who wanted to preserve his capital. He then proceeded to advise deceased to invest 80% of his funds in Sharemax. How can deceased be a conservative investor for the Sanlam investment but at the same time a risk taker for the Sharemax investment. Respondent simply failed to explain this bizarre conduct.

**Response to letter of 14 April 2011**

[27] This office was concerned, having considered respondents response, that the latter did not explain his decision to invest 80% of client funds in a high-risk investment. Therefore, a further letter was written to give respondent another opportunity chance to explain his conduct. I deal with his response below:

a) The first issue addressed was the absence of a risk profile analysis. Respondent admits that no analysis was done but explains that deceased did not want to

provide him with the relevant information and had elected not to have a full analysis. He refers to the document signed by deceased, discussed above.

b) It may be so that respondent was not provided with *all* the information. But that is not to say that he had *no* information. He knew the following:

Firstly, that deceased was investing his retirement funds;

Secondly, deceased was 65 years old and about to retire;

Thirdly, deceased instructed respondent that he wanted to preserve his capital; and

Fourthly, respondent must have been aware that deceased was not able to replace lost capital.

It is abundantly clear from the information that was available to respondent that deceased was a conservative to moderate investor who had absolutely no tolerance for risk.

c) Respondent then relies on the fact that deceased clearly understood that he was under an obligation to take particular care to consider "on his own" whether the advice was appropriate. Respondent reminds us that he did not put pressure on deceased to invest and even gave him time to consider the advice. The respondent was engaged as an FSP and was expected to provide a service according to the applicable codes of conduct and the Act. Respondent cannot abdicate his responsibilities to the very client who engaged his services. The duty was on respondent to make a full and frank disclosure to deceased about the high risks inherent in the Sharemax investment. Neither can respondent rely on deceased's own reading and understanding of the prospectus. It must have been obvious to respondent that deceased was an elderly person, not familiar with financial transactions and quite simply unable to read and understand the Sharemax prospectus on his own. Bearing in mind that it was respondent who introduced Sharemax to deceased in the first place.

d) Respondent disagrees that deceased was a “moderate” investor. He submits that respondent wanted a higher income and was “willing to take on a higher risk than moderate”. There is no substance in this submission. Deceased was convinced to choose Sharemax by the respondent who demonstrated that the income from Sharemax was so much higher than any other options. There is no evidence that respondent explained the risks in Sharemax and how Sharemax intended to pay the generous income. Respondent cannot rely on deceased’s own understanding of the risks. It is not in dispute that respondent promised deceased that Sharemax will pay 12.5% interest and 11% capital growth. Respondent accepted this advice, on the undisputed facts before me, respondent did not explain to deceased that Sharemax did not guarantee capital growth nor the income. Respondent certainly did not explain that Sharemax was going to pay commissions and returns from investors own funds.

e) The next issue related to respondent’s duty of care towards his client as contemplated in Section 2 of The Code. Respondent, for the first time submitted that he gave deceased “limited advice”. This is not persuasive as respondent must decide if he gave advice or not. On respondent’s own version, deceased was advised by *him* to invest 80% of his funds in Sharemax. It is equally not disputed that but for respondent’s advice, deceased would not have invested in Sharemax. Respondent’s advice was the cause of the investment. There is no basis for calling this “limited advice”. I note that respondent did not limit his commission from Sharemax.

f) Respondent submits that he was not expected to reasonably foresee that the SARB will intervene. He claims that he had no knowledge of any problems with the investment. Firstly, this investment was made in October 2009; at this time the print media was already questioning the legality and viability of the Sharemax Zambezi

and The Villa investments. Many financial journalists and experts in financial advice were expressing reservations about the schemes. Surely respondent must have read at least some of these articles and as a competent FSP, should have been concerned about advising his clients to invest. At the very least he should have alerted his client to these media reports. It appears that respondent happily turned a blind eye to everything and was firmly focused on the lucrative commission Sharemax was about to pay him. He received 6% on the capital, paid within two weeks of the investment with no claw back. Respondent was paid R48 000 by Sharemax for his "limited advice". Further, that commission was paid out of client's own funds; and respondent knew it.

g) Respondent claims that for 10 years Sharemax had been promoting "registered prospectuses" yet the registrar of companies, DTI, FSB and SARB did not raise any objections. There is no substance in this. The regulatory institutions do not carry out product approval and only check on compliance requirements. They do not pronounce on the risks inherent in the product, it is up to the FSP to determine if a product is suitable for client; Section 8 (1)(c) of The Code.

h) Respondent cannot rely on Sharemax's record over 10 years because in the past, Sharemax had never promoted a scheme such as Zambezi and The Villa. Previously, Sharemax acquired and syndicated developed property with an established income. Respondent presents eight examples of previous successful syndications by Sharemax. All of which were completely different to the scheme employed in The Villa. With the Villa, Sharemax did not own any property and it had no income from which to pay extravagant commissions and returns. The obvious question to be answered is; just where did respondent think Sharemax was going to find the funds to pay commissions and interest? Respondent does not answer this question, nor did he offer his client any explanation.

Respondent concludes that he complied with Section 2 of The Code. For reasons stated above, this submission must be rejected. Respondent knew that he was marketing a highly risky investment, his knowledge of the prospectus and application forms would have informed him and warned him of the risks inherent in The Villa investment. Still, and inexplicably, he found the investment to be suitable for a 65-year-old pensioner who had no tolerance for risk.

i) Respondent then refers to a document signed by complainant;

this is another Sharemax standard document titled “Sharemax Investments Risk Assessment On Product Information”. This document was signed by the parties. The document is drafted by Sharemax and supplied to all its brokers. The document is nothing more than a sham. It purports to be some form of risk assessment. It comprises of 6 questions which must be answered by ticking off “yes” or “no”. All the questions have absolutely nothing to do with risk in the product. The document also contains the following declaration from deceased: “ *I hereby confirm, that the financial forecasting presented was done from the information in the prospectus and that no other projections were presented to me”.* To this deceased marked “yes”. In fact, it was respondent who filled in this document for his client. The significance of this declaration is as follows:

Firstly, although there are projections in the prospectus, no further information is given that can assist the prospective investor to authenticate the projections. There are no financial statements and no financial information about the developer who received all of the investors remaining funds in the form of a loan.

Secondly, the prospectus in various places, from page one to the application form, warns of the risks in the investment, yet there is absolutely no reference to this in this form. For instance, the obvious question to ask is: Can you afford to lose your capital or any part thereof? There is no such question.

One thing is clear, respondent did not explain the risks in this type of investment to complainant. Still less did he explain the risks in this particular product. There is absolutely no evidence that respondent explained to complainant that this product represented a risk capital investment.

Respondent was under a duty to explain the risks to complainant.

j) Then respondent makes a startling submission. He states that this office "tagged" the Villa investment as high risk so that this office can conclude that it did not fit in with a moderate risk profile. This is absurd, the prospectus itself warns that this is a high-risk investment; only, respondent did not seem to notice.

k) Respondent submits that the prospectus was left with deceased for him "to scrutinise". Then respondent admits that the prospectus warns, in bold, that investors are warned that this must be considered "risk capital" investment. Indeed, such a warning appears. However, respondent assumes that his 65-year-old panel-beater client will know what "risk capital" means. There is no evidence, on respondent's own version, that he referred his client to the myriad warnings in the prospectus and what the investment meant in terms of risk to capital and income. Respondent's only response is that deceased had all the information and could "clearly" understand the higher risks disclosed to him. Respondent again relies on his clients own reading of the prospectus. This does not amount to compliance with the code.

l) Here, respondent admits that the prospectus warns that The Villa has never traded prior to the registration of the prospectus and has not made a profit "whatsoever". I must assume that respondent knew this when he gave deceased advice to invest. Respondent does not state how he satisfied himself that Sharemax had the means to pay commissions and returns other than from investors' own funds.

m) Respondent also admits that the prospectus states that there is a “substantial risk that a shareholder would not be able to sell his shares should he wish to do so at a specific time in the future”. Indeed, this is one of the many warnings to be found in the prospectus. However, respondent does not state that he drew deceased’s attention to it and explained what it means. Respondent again attempts to escape responsibility by relying on deceased’s own reading and understanding of the prospectus.

n) The next aspect pertains to a question from this office requesting details of any due diligence carried out by respondent in respect of The Villa investment. Respondent immediately challenged this office to show where in The Code does it call for a performance of due diligence. The Code specifically deals with it in Sections 7 and 8. Respondent was under a duty to find out all the information about a product in order to make full and frank disclosure to client so that the latter can make an informed decision.

Section 7 (1)(a) provides as follows:

*“(a) provide a reasonable and appropriate general explanation of the nature and material terms of the relevant contract or transaction to a client, and generally make full and frank disclosure of any information that would reasonably be expected to enable the client to make an informed decision;”*

This requirement clearly expects the provider, in the first place, to become familiar with the product, have a firm understanding of it, so that an explanation can be given to the client. The Code does not expect that the client himself must study the prospectus and rely on his own understanding.

On respondent’s own version, he did not refer deceased to the warnings in the prospectus that this is a high-risk investment, instead he relied on deceased to

read and understand the complex 52-page prospectus, after receiving “limited advice” from respondent. This is a breach of The Code.

o) Respondent then refers to Section 2 of The Code and makes the following pertinent submission; “*it encompasses the degree of prudence and caution required of an individual who is under a duty of care and is closely dependent on circumstances. It is in other words, whether the individual proceeded with such reasonable caution as a prudent man would have exercised under such circumstances”.* Respondent then questions this offices requirement that an FSP is expected to carry out due diligence on the product. Respondent questions what is “due diligence”? Then suggests this answer: “*the correct interpretation would be whether the individual proceeded with such reasonable caution as a prudent man would have exercised under such circumstances”.* Firstly, I agree with these submissions and they appear to have been taken from a judgement. Secondly, I will consider respondents conduct in terms of what one would expect a reasonably competent FSP to do under similar circumstances.

Respondent submits that he acted reasonably by leaving the prospectus with deceased and by not placing any pressure on him to invest. Deceased had all the available information and was in a position to make an informed decision. I cannot accept this as, on respondent’s own version, he did not explain the risks in the investment to his client but left him to read the prospectus for himself. A reasonably competent FSP would have realised that his 65-year-old lay client was not capable of reading and understanding the prospectus and would have done his duty as an FSP and explained the risks in plain language. Thereafter as a reasonably prudent FSP, he would have kept a written record of his advice and explanation. Respondent did not conduct himself as a reasonably competent FSP, nor did he take care to comply with The Code. Respondent failed to proceed with caution

notwithstanding that the prospectus warns the investor that there is a real risk of losing one's capital and income. In fact, respondent makes the following admission: "*I advised him that he had to consider on his own or with help from others, whether the products were suitable to his needs."* (emphasis added). This is reckless conduct and an attempt to distance himself from his own poor advice. Deceased engaged respondent as his FSP, respondent accepted the mandate and was therefore obliged to act in terms of The Code. The Code does not envisage that an FSP can leave it to client to decide "on his own".

p) Respondent submits that "*it was common knowledge that the investor is buying an unlisted product. It is common knowledge that there are risks associated with unlisted investments".* There is absolutely no factual basis for respondent to attribute such "common knowledge" to his aging panel beater client. It is highly unlikely that deceased knew what "unlisted investments" were and the risks associated with such investments. It was not reasonable, in the circumstances, for respondent to attribute such knowledge to deceased.

q) Respondent then makes the following, nonsensical statement: "*as the complainant chose not to provide me with complete and full information in respect of his situation, I could not know that 80% of his investment was going to be invested in The Villa".* This is misleading, respondent was told that deceased had received payment from his provident fund of an amount of R1million and wanted to preserve the capital. Respondent then proceeded to provide quotations where he placed R800 000 in Sharemax. Respondent knew exactly what he was doing, he went to deceased to sell the latter the Sharemax investment. The commission was just too tempting.

r) Respondent ends his response by needlessly, and without any factual basis, accusing this office of a bias and that he is not being treated with impartiality.

**The Case Law**

[28] Finally, respondent attached a copy of the judgment in **Shane Allison Symons N.O. vs The Rob Roy Investments CC t/a Assetsure.** This judgment is distinguishable on the facts and is not persuasive, nor is this office bound by it. A more appropriate judgment is **Oosthuizen v Castro 2018 (2) SA 529 (FS),** which was approved by the SCA in **CENTRIQ INSURANCE COMPANY LTD v OOSTHUIZEN AND ANOTHER 2019 (3) SA 387 (SCA) .**

[29] Appropriate to the complaint herein, are the findings of the SCA in respect of the Sharemax investment. The court stated as follows:

*"The scheme required investors to transfer their money to Sharemax's chosen company. The company or Sharemax would then pay their investors interest on this investment without the underlying investment — the property development — having earned anything — and where it was unlikely to do so for years, pending the purchase of the land and the construction of a shopping centre. Only upon the completion of the construction centre would rental income be realised. Yet the prospectus previously mentioned held out to investors a projected rate of return equal to a 10% after tax dividend from the date of full subscription to the occupation date in September 2011. The 'investment' in fact had all the hallmarks of a Ponzi scheme in which money placed by later investors pays artificially high interest or dividends to the original investors, thereby attracting even larger investment. When there are no longer new investors, which inevitably happens, the scheme collapses. Mrs Oosthuizen was one of the later investors. On any objective analysis the investment was not viable, certainly not having regard to her needs.* (emphasis added)

*[15] As the learned judge trenchantly observed:*

*'It is amazing that [Mr Castro] could think for one moment that interest could lawfully accrue from the investment from the first month. I wonder where he thought the magical origin of the income stream would derive from. . .. (A) simple investigation or even an inspection of the half-built shopping complex would have been an eye-opener. He would have realised that enormous costs would have to be incurred to complete the project [and that the] half-built shopping complex could not earn any income for some time . . . but the investment provided for income to be paid to investors from the start.'*

*[16] It was, to be kind to Mr Castro, an investment that he himself did not properly understand. He dismissed the adverse criticism circulating in the media without satisfying himself as to whether there was any substance in it. He quite clearly failed to explain the risks of the investment so as to allow Mrs Oosthuizen to make an informed decision."*

*"The finding by the court a quo that Mr Castro was in breach of his fiduciary duty to his client because he had not taken reasonable steps to satisfy himself of the safety of the investment and to give her adequate financial advice to meet her needs is therefore unassailable."* (emphasis added)

[30] On the facts of this case, respondent failed to explain the risks of the investment to deceased so as to allow him to make an informed decision. This conclusion can be made on the respondent's own version.

**E. THE ISSUES**

[31] Having considered the facts as stated above, the issues here are the following: in giving deceased financial advice:

a) Did respondent comply with the provisions of the Act and Code;

b) If respondent failed to comply, was his conduct and advice, in the circumstances, negligent;

c) If respondents conduct was negligent, did that negligence result in loss to deceased.

[32] By all accounts, the Sharemax investment was high risk. It cannot be disputed that respondent advised deceased to invest in Sharemax. Nor is it in dispute that these were high risk investments. The issues then are:

a) Were these investments suitable for deceased's needs;

b) What motivated respondent to give this advice;

c) Did respondent place deceased in a position to make an informed decision; and

d) Was there negligence on the part of respondent in providing the advice?

[33] For purposes of this determination, a finding need not be made that Sharemax was a "Legal or illegal investment". The legality of the investment is not the test nor is it an issue; it is the suitability of the investment for deceased and his financial circumstances that is in issue.

**Negligence**

[34] A reasonably competent FSP, at the time of providing financial advice to client, can be expected to do the following:

a) ensure that he read and understood the Code;

b) understands that he is obliged to comply with the code in providing financial advice;

c) understands the nature of the financial product/s he is recommending to client;

d) understands the product so that he is in a position to explain it to client in plain language;

e) accepts that he is obliged to make a full and frank disclosure of all the available information about the product;

f) understands that he is obliged to ensure that his client will be in a position to make an informed decision; and

g) accepts that he must recommend a product that is suitable for client bearing in mind the latter's financial circumstances and tolerance for risk.

[35] Respondent is vague and lacking in detail as to what he explained to deceased regarding the suitability of the Sharemax investment. he fails to state that he explained the myriad warnings in the prospectus to client.

[36] Respondents conduct in not explaining the risks is exacerbated by the fact that he had received training in the products and had even read and understood the prospectus. We assume he received training in terms of Section 13 of the FAIS Act. Yet he failed to tell deceased the following:

a) Neither his capital nor monthly income were guaranteed;

b) That the investments were considered risk capital;

c) That in fact he was not investing in property, Sharemax did not own any property and that the shopping mall was not built;

d) His funds were not going to enjoy the safety of a trust account, but was going to be paid out to the promoters who could use it at their discretion;

e) That his funds were being lent to a developer to construct the building, before the promoter took transfer of the property and that the loan was not subject to any security;

f) That Sharemax was not going to comply with the requirements of Notice 459;

g) That Sharemax had no independent financial resources from which to pay agents' commissions and interest on the capital to investors; and

h) That their interest was going to be effectively paid from their own capital and from the investments of other investors.

[37] None of the above was a secret, this information appears in the prospectus and was available to respondent at the time when he gave client advice to invest. Respondent admits to have read the prospectus. There can be no doubt that had this information been disclosed to client, he would not have invested. Respondent failed to comply with the Code and negligently advised client to invest 80% of his retirement funds in Sharemax.

**Application of Law**

[38] Bearing in mind the facts found to be proved and the conclusions to be drawn from them, the following findings can be made:

a) Respondent failed to act honestly, fairly, with due skill, care and diligence;

b) Respondent failed to act in the interests of client and by his conduct compromised the integrity of the financial services industry. Respondent contravened section 2 of The Code;

c) Respondent failed to provide full and frank disclosure of all the material information about the Sharemax product;

d) Respondent failed to enable client to make an informed decision. Respondent contravened section 7 (1) (a) of The Code; and

e) Respondent failed to seek relevant information from client and failed to provide appropriate advice. This office rejects respondent's version that deceased "refused" to provide him with information. Respondent failed to identify a product that was appropriate to client's risk profile and financial needs. Respondent contravened section 8 (1) (a), (b) and (c) of The Code.

[39] The fact that respondent was in breach of the Act and The Code does not mean that he is therefore liable for deceased's loss. There is a breach of contract as well as a claim in delict.

[40] Further, this office as well as the Board of Appeal has consistently found that there existed a contract between FSP and client. It was an express, alternatively implied term of the contract that respondent, in carrying out his obligations, will comply with the provisions of the Act and The Code. For reasons already stated, respondent was in breach of this term. A consequence of this breach was the loss of deceased's capital.

[41] In a number of recent judgements in the high court, it was found that complainants claim is one in delict based on negligence. Once it is established that the respondent gave financial advice, two questions arise:

a) did respondent comply with their legal duties towards client; and

b) whether in terms thereof the respondents acted wrongfully and negligently.

[42] A reasonably competent FSP in the position of respondent would have done the following:

a) Carried out diligent research to become familiar with the nature of the Sharemax product he intended to sell;

b) Would have found out that the investment in Sharemax was an investment in debt instruments and that there was no underlying asset;

c) As a basic step respondent was expected to read and understand the prospectus and the annexures thereto and explain it to client in plain language;

d) Made a point of understanding how Sharemax intended to pay his commission and investors returns bearing in mind that the latter owned no assets and enjoyed no trading history and did not have any independent means of making these payments

(these facts are stated in the prospectus and in the disclosure documents). Significantly, respondent had a duty to explain this to deceased;

e) Would have noticed that contrary to what was initially stated in the prospectus, it then informs that investor funds will not be kept in trust but will be paid out to the developer at the discretion of the promoter (this too is stated in the prospectus), this had to be explained to client;

f) Would have noticed that the shares will not be easy to dispose of, the promoter offered no assistance in disposing of the shares and the onus was placed on the investor to find a buyer (also stated in the prospectus).

g) Would have explained the risks as enumerated in the client mandate signed by respondent and client as part of the application form.

Clearly by failing to draw deceased's attention to the above information, respondent failed in his legal duties to his client.

[43] The respondent also acted wrongfully and negligently; he was under a legal duty to make a disclosure of these facts to deceased. Respondent acted negligently in not making full and frank disclosure thereby depriving deceased of the right to make an informed decision.

[44] Respondent must be judged by the standard of a reasonably competent FSP in the same circumstances. Then the inquiry must progress to the next question: would a reasonably competent FSP have advised deceased differently. It is overwhelmingly clear that a reasonably competent FSP would have read and understood the prospectus and would not have advised deceased to invest his retirement funds in a manifestly high-risk investment where there was a prospect of losing all the capital. The SCA in **Durr v ABSA Bank,** Schutz JA stated 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 an activity."*

"Liability *in delict arises from wrongful and negligent acts or omissions. In the final analysis the true criterion for determining negligence is whether in the particular circumstances of the conduct complained of falls short of the standard of the reasonable person."*

Respondents conduct fell short of this standard and was the factual and legal cause of deceased's loss.

[45] Accordingly, and in the circumstances, the respondent was under a legal duty of care to comply with his obligations. An omission to comply, in the circumstances, amounts to a negligent breach of the duty of care. A reasonably competent FSP, at the time of providing advice, should reasonably be expected to foresee that in the event of a breach of the aforesaid legal duty of care client will suffer harm. That harm will be the possible loss of client's capital. The precise or exact manner in which the harm occurred need not be foreseeable, the general manner of its occurrence had to be reasonably foreseeable. For example, advice to invest in a risky investment must result in a reasonable foreseeability that the investment could be lost in the near future. It is not a question of performance of the product but the realisation of existing risks in the product. The reasonable foreseeability must become even more clear where the product provider actually warns the FSP of the risks in the product. As in this matter, the prospectus and disclosure documents stated the risks in the Sharemax investments. The respondent was aware of these risks; but nevertheless, advised deceased to invest their funds.

[46] Respondent's conduct fell short of a reasonably competent FSP and respondent was the factual and legal cause of deceased's loss.

See **Sea Harvest Corporation (Pty) Ltd and Another v Duncan Dock Cold Storage (Pty) Ltd and Another 2000 (1) SA 827 (SCA).**

I refer to the following decisions:

**OOSTHUIZEN v CASTRO AND ANOTHER 2018 (2) SA 529 (FS);**

**CENTRIQ INSURANCE COMPANY LTD v OOSTHUIZEN AND ANOTHER 2019 (3) SA 387 (SCA)** – approved of the Castro judgement.

**ATWEALTH (PTY) LTD AND OTHERS v KERNICK AND OTHERS 2019 (4) SA 420 (SCA) at p529.**

[47] For all of the reasons stated above, I find that respondent acted negligently and such negligence was the cause of complainant's loss.

**The Loss**

[48] Respondent submitted that deceased's funds were not lost and until the loss was established, he cannot be held responsible. No factual nor legal basis was made for this submission. Respondent must know that Sharemax went into final liquidation and The Villa, a partially built shopping centre, has stood as a derelict building for many years. There is no prospect that funds will be found to complete the building and pay back investors funds. Deceased's funds in an amount of R800 000 is lost.

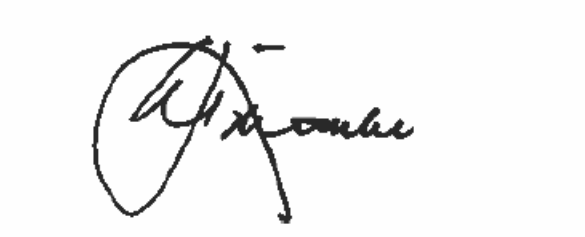
## F. THE ORDER

[49] The following order is made

1. The complaint is upheld;

2. The respondent is ordered to pay to the deceased estate of the late C. C. Engelbrecht an amount of R800 000;
3. Interest on the amount of R800 000 at the rate of 7%, seven days from the date of this order to date of final payment.
4. Should any party be aggrieved with the decision, leave to appeal is granted in terms of section 28 (5) (b) (i), read with section 230 of the Financial Sector Regulation Act 9 of 2017.

**DATED AT PRETORIA ON THIS THE 25th DAY OF MAY 2021.**



**ADV NONKU TSHOMBE**

**OMBUD FOR FINANCIAL SERVICES PROVIDERS**