FAISOmbud
Office of the Ombud for Financial Services Providers

OUR REFERENCE: FAIS 06866/10-11/ KZN 1

23 January 2018

ATTENTION: Mr Bruce Griffiths Key Individual: Midcoast Financial Services Pty Ltd

Per email: bruce.griffiths@momentum.co.za

Dear Mr Griffiths,

Mr Andrew James Allan and Mrs Suzanne Joyce Allan (complainants) v Midcoast Financial Services (Pty) Ltd (first respondent) and Mr Bruce Griffiths (second respondent): RECOMMENDATION IN TERMS OF SECTION 27 (5) (C) OF THE FAIS ACT, (ACT 37 OF 2002)

A. INTRODUCTION

1. Complainants, Andrew James Allan and Suzanne Joyce Allan are married to one another and were retiring at the age of 54 when the advice was provided. Following respondents' advice, they individually invested, at various intervals, a total of R3.7 million of their retirement savings into The Villa Retail Park Holdings Limited[1](The Villa Ltd), a public property syndication promoted by Sharemax Investment (Pty) Ltd (Sharemax), during 2009. The objective of the investment was to provide for their retirement income.

2. Income payments from Sharemax ceased in September 2010. As at the time of lodging their complaints with this Office in November 2010, complainants' income had not been reinstated. To this day, neither the income nor the capital has been repaid. Complainants hold respondents liable to repay their lost income. They blame respondent's advice for placing their retirement funds at risk and consequently, the loss.

[1] Registration number 2008/017207/06

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Delays in finalising this complaint

3. It is necessary to digress a little and explain the delays in finalizing this complaint in view of the Office's mandate to resolve complaints expeditiously. Sometime in September 2011, after the Office issued the *Barnes* determination[2], the respondent in that matter brought an urgent application to set it aside[3]. Before the fate of the application could be known, respondents sought an undertaking from this Office that it would not proceed to determine any other property syndication related complaints involving them.

4. Since no legal basis existed for respondent's demands, the Office continued to determine further property related complaints, to which respondents reacted with an urgent application for an interdict to stop the Office from filing the determinations in court, and issuing further determinations against them. The decision was finally delivered in July 2012 in favour of the Ombud. See in this regard *Deeb Risk v FAIS Ombud & Others*[4].

5. The Office continued to determine complaints involving property syndications after the High Court decision. However, in 2013, following the *Siegrist* and *Bekker* determinations[5] and the relevant appeal, a decision was taken by the Office to halt processing property syndication related complaints. The decision was not taken lightly, but was a precautionary and necessary risk management step, as the Office had, for the first time, sought to hold the directors of property syndication schemes liable for complainants' losses. The said appeal was finally decided in April 2015[6], after which the Office resumed processing complaints involving property syndications with due regard to the decision. As many as 2000 complaints had to be shelved pending the Appeals Board decision.

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2 See E Barnes v D Risk Insurance Consultants FAIS-06793-10/11 GP 1

3 Respondent claimed that section 27 of the FAIS Act was unconstitutional

4 Gauteng High Court Division, case number 50027/2014

5 See in this regard FAIS-00039-11/12 and FAIS-06661-10/11.

6 See in this regard the decision of the Appeals Board date 10 April 2015.

B. THE PARTIES

6. First and second complainants are Mr Andrew James Allan and Mrs Suzanne Joyce Allan. They are married to one another and are retired. Their full particulars are on file with this Office. The complaint was brought by first complainant, Mr Allan, who is also acting on behalf of this wife.

7. First respondent is Midcoast Financial Services (Pty) Ltd (2000/006698/07) a company duly incorporated in terms of South African laws. First respondent is an authorised financial services provider (FSP) (17641,) with its principal place of business noted in the Regulator's records as 20 Hoskins Road Wembley, Pietermaritzburg, KZN. The licence has been active since 29 September 2004 and it lapsed in April 2011 when respondent requested the regulator to remove him as a key person and representative of the first respondent as he had since become a representative of Momentum.

8. Second respondent is Bruce Griffiths, an adult male representative and key individual of first respondent. The regulator's records confirm second respondent's address to be the same as that of first respondent. At all times material hereto, second respondent rendered financial services to the complainant.

9. It appears from the Regulator's records that respondent was a representative of the now defunct Unlisted Securities South Africa (Pty) Ltd, (USSA) trading as FSP Network (Pty) Ltd which enabled him to render financial services in connection with this product.

10. I refer to the respondents collectively as "respondent". Where appropriate, I specify which respondent is being referred to.

C. THE COMPLAINT

11. The undisputed facts confirm that complainants, having retired already, were in need of financial advice as to where they should place their funds in order to generate monthly income. They engaged the services of respondent to advise them. Respondent advised them about a Sharemax product

which he described as the best for their financial needs[7]. Having known respondent since 1998, complainants took the advice without question. Relying on these representations, the complainants made the investments as detailed below[8]:

February 2009 – R500 000 - AJ Allan

February 2009 – R500 000 - SJ Allan

May 2009 – R500 000 - AJ Allan

May 2009 – R500 000 - SJ Allan

September 2009 – R1.400 000 - AJ Allan

May 2010 – R300 000 - AJ Allan = Total R3.7 million.

12. The interest rates agreed in respect of the investments varied between 10% - 12.5% from date of minimum subscription to 8% – 11% from date of occupation.
When complainants' income for the month of September was not paid, they realised that there was a problem and that their capital and income were in fact at risk. They filed their complaints against the respondents in November 2010.

Relief sought

13. The complainants have each asked this Office to order the respondents to pay their lost income which, subject to the jurisdictional limit of R800 000, should be calculated at the bank interest rate of 6 % on their investments. Complainants also stated in their complaint that they were not asking for the refund of their capital as they were still seeking legal advice on that aspect.

D. JURISDICTION

14. To satisfy the jurisdictional restrictions of this Office as provided for in the Act, complainants have confirmed in writing that save for the complaint being considered by this Office, they have never at any stage instituted legal proceedings against the respondents and do not intend to do so in the future.

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7 Respondent articulates his understanding of the product in his response of 9 February 2011, paragraphs 22- 23 as one that protected investors' capital.

8 Note: the months used are those supplied by respondent to overcome the discrepancies regarding dates.

E. PROCEDURAL FAIRNESS

15. On 23 November 2010, the complaint was referred to respondents in terms of Rule 6 (b) of the Rules on Proceedings (the Rules) to resolve it with his client. Having sought and granted postponements in order to meet the demands of informing his PI policy, the response was finally filed on 9 February 2011.

F. RESPONSE

16. The respondent's response is in the form of an application in terms of sections 27 (3) (c) and 27 (4) (c) of the Act wherein the respondents seek the following:
    a. that the Ombud determine that it is more appropriate that the matter be dealt with by a court; and
    b. decline to entertain the complaint.

17. The respondent made it clear notwithstanding the specific invitation to submit his response (in line with section 27 (4) (c), that he will only do so when it becomes necessary. The application itself is premised on the following grounds:
    (i) The complaint is pre-mature
    (ii) His right to have the dispute resolved by a court;
    (iii) The appropriateness of the procedures of the Ombud's Office;
    (iv) Whether the FAIS Ombud is a forum or tribunal;
    (v) The independence and impartiality of the Ombud

18. Before I deal with the respondent's application I note that respondent's attorneys have consistently provided the same response to almost all the complaints filed against their clients with this Office. Incidentally, respondents' attorneys are the same people who represented the applicants in the High Court application, (refer to para 20 below). Quite apart from basing their application on speculative reasons, the indiscriminate cutting and pasting of the same content word for word on the part of the respondent's attorneys amounts to abuse of process and must be condemned.

19. First, the complaint is not premature. It is now almost eight years since the complaints were first made by complainants with no cogent answers as to when their funds will be repaid. Second, the central question to be answered in these complaints is whether respondent, in discharging his obligations in terms of his contract with the complainants , acted in line with the requirements of the General Code for Financial Services Providers and Representatives (the Code), and whether such conduct could be calculated to have caused complainants loss.

20. With regard to the rest of the application in terms of section 27 (3) (c), I refer to *Raymond Deeb Risk*[9] where his Lordship, J Baqwa ruled that:

'*The section confers neither a right to the applicants to demand that the Ombud declines her jurisdiction to deal with complaints nor does it confer a duty on her to do so. The section clearly confers a discretion on the first respondent. Any other interpretation would be tantamount to stripping her of her statutory powers in terms of the FAIS Act. Absent a decision by the first respondent, she retains jurisdiction. It is not the task therefore of the reviewing court to consider whether or not the decision by the first respondent is correct in law. That is a matter for the appeal board.*'

21. The application is hereby dismissed for lack of merit.

22. I now deal with the material aspects of the respondent's response from the application. For convenience, I comment where necessary.

22.1 The complaint pertains to performance of investments totalling R3.7 million. The claim thus exceeds the jurisdiction of the FAIS Ombud.

The complaint made by the complainants is based squarely on respondent's advice and not investment performance. See rule 4 (f)[10]. It is about respondent's inappropriate advice of projecting Sharemax as the best possible product (ignoring the inherent high-risk) for pensioners who had specifically engaged his professional service for suitable advice. The

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9 and Another v The Office of the Ombud for Financial Services Providers, North Gauteng High Court, Case No. 38791/2011, para- 38 to 39.6

10 Rule 4 (f) states that the complaint must not relate to investment performance of a financial product which is the subject of the complaint, unless such performance was guaranteed expressly or implicitly or such performance appears to the Ombud to be so deficient as to raise a *prima facie* presumption of misrepresentation, negligence, or maladministration on the part of the person against who the complaint is brought, or that person's representative

complainants have pertinently stated that they are only claiming for the lost income and that they limit their claim to the jurisdiction of this Office.

22.2 Respondent refers to section 27 (3) (b) (i) and (ii)[11]. The sections do not apply as there are no legal proceedings instituted at any stage since the complaint was filed with this Office in which the same subject matter is pending.

22.3 Then respondent placed on record that the case against him is not clear. He stated that in the event the complainant is framing a case of negligence against him, he denies acting negligently. Respondent nevertheless went on to confirm that he has known complainants since 1998 and that they had built a friendship since then. His reasons for recommending Sharemax include *inter alia*, Sharemax was well structured and had an impeccable track record and investors' capital was protected. Respondent states that he had confidence in Sharemax.

22.4 Respondent thereafter refers to a number of documents which he claims evidence his compliance with the Code.

I will get to the documents in a moment, but what is important to highlight at this early stage, is that the respondent's advice was not based on fact and was materially flawed. (More on this later). Investors' capital was not safe and the series of prospectuses conveyed this much. Equally important, which the respondent also missed from the prospectus, is the fact that the very income promised was tenuous as it was dependent on the discretion of the directors.

22.5 Respondent confirms all the investments and states that the reason for moving the investments from Momentum was to counter what complainants viewed as poor performance.

The pursuit of what may appear to be attractive returns aside; there is not a single instance (according to respondent's own version) in which the material differences between the two

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[11] Section 27 (3) (b) (i) and (ii) provide:

(i) 'The Ombud must decline to investigate any complaint if, before the date of official receipt of the complaint, proceedings have been instituted by the complainant in any Court in respect of a matter which would constitute the subject of the investigation.'

(ii) 'Where any proceedings contemplated in subparagraphs (i) are instituted during any investigation by the Ombud, such investigation must not be proceeded with.'

investments (Momentum and Sharemax) were specifically canvassed and carefully incised. Respondent had a duty in terms of the Code to do so in order to satisfy himself that the complainants understood the differences and were in a position to make an informed decision[12].

Compliance documents

22.6 Throughout respondent's response, he constantly referred to the following documents as evidence of his compliance with the Code:

(i) Sharemax application form:

(ii) Statutory notice in terms of the Long Term Insurance Act;

(iii) Sharemax Risk Assessment form; and

(iv) the Record of Advice.

Despite the replication of the same set of documents in respect of each of investments made by the complainants, there is nowhere that respondent advises complainants of the true risk involved in this product. Respondent also fails to state the relevance of the Statutory Notice in terms of the Long Term Insurance Act, (which on its own is demonstrative of mindless compliance) given that the complaints being considered do not concern insurance products.

22.7 Here I only propose to deal with the records of advice and the risk profile document. The first set for the both complainants was completed in February 2009 and the need and recommendation in respect of the first complainant's record is recorded simply as, '*split income to wife for tax purposes……*'. As to why the products were recommended, this is what respondent has recorded, '*Property Risk income will be generated from a rental pool in Sept 2011… Property risk as per prospectus. Split income/growth via equity/property*.' For the second complainant, there is nothing written under need and recommendation, and to explain why the products were recommended, the following is noted, '*as per husband's planning done as on structure including a trust/growth por*t'.

[12] Section 8 (4) (d) and 8 (2) of the Code

22.8 The risk profile marked as annexure 'H' makes no reference to either of the complainants and is scored 66 which gives an outcome of moderate to aggressive. This document is followed by another document which is also marked 66 with the words 'as per James risk profile'. I have perused all the compliance records furnished by respondents, including his records of advice and there is nothing that could have assisted complainants to appreciate the magnitude of risk they were facing in the Villa Ltd investments.

G. REPLY IN TERMS OF RULE 5 G

23. Arising out of respondent's response, complainants were requested to answer some questions in terms of Rule 5 (g). Their response is provided in a letter dated 29 January 2013 to which complainants attached an e-mail they had sent to respondent following a meeting organised by the latter for Sharemax investors sometime in November 2010. Their reply is summarised immediately below:

23.1 Respondent never once advised them that the investment was high-risk.

23.2 At one point they even referred respondent to a press article about Sharemax and respondent simply brushed it off. Even when their income was not paid, respondent explained to them that their money was in bricks and mortar.

23.3 In November 2010 respondent organised a meeting of investors and invited one Dirk Koekemoer of Sharemax to address them. Complainant says it was after this meeting that he realised that something was wrong.

23.4 They were never told they were purchasing debentures.

23.5 They were told that the fault lies with the South African Reserve Bank (SARB), the Financial Services Board (FSB) and the South African Revenue Services (SARS). Apparently Sharemax and Willie Botha[13] had done nothing wrong.

[13] Willem Botha was then the managing director of Sharemax

23.6 The financial advisors were meant to raise funds to take the SARB to the Queens Court. Complainants state that they never knew such a court existed.

23.7 Respondent had presented Sharemax as a well-known and respected company to them in which he had invested his own funds.

23.8 Complainants trusted respondent completely.

Notice in terms of section 27 (4)

24. In November 2017 respondents filed their response to the Notice in terms of section 27 (4) of 19 October 2017.

25. Respondent first made a point of noting that he had initially responded in 2011 with absolutely no feedback from the Ombud, only to be notified in 2017 of the Ombud's intention to investigate the complaint. He complained that the conduct of the Ombud of allowing the matter to hang over his head violated his constitutional rights and raised perceptions of bias.
Attached to this recommendation is a copy of complainant's comments in terms of rule 5(g) dated 2013. As mentioned in the introductory section of this recommendation, the Ombud had suspended the processing of property syndication related complaints in early 2013 and only resumed processing the +/- 2000 complaints in April 2015, after the Siegrist appeal. The processing of the property syndication complaints does not relieve the Office from its business goal of resolving 80% of all complaints received in any given financial year. Respondent's comments are regrettable given the transparency about the delays and the FAIS Ombud's commitment to resolve complaints expeditiously in terms of its business goals.

26. The Notice in terms of section 27 (4) invited the respondents to explain the basis of their recommendation of the Sharemax product. Respondents were further afforded the opportunity to provide proof that they had advised their clients of the risk involved in the Sharemax products. A copy of the Notice is annexed to this recommendation.

27. I summarise respondent's response to the Notice in the immediately following paragraphs:

27.1 At the outset respondent pointed that he acted at the time as a representative of first respondent but that entity ceased to exist upon his retirement.

27.2 Respondent has never received any comment or response from the complainants.

27.3 The complainant's claim is ousted by the jurisdiction provisions of the FAIS Act as it is 3.7 million.

27.4 Complainant had advised that he intended to institute legal proceedings therefore, the claim is ousted by sections 27 (3) (b) (i) and (ii) of the Act.

27.5 Respondent complains about procedure followed by this Office and refers to the *Siegrist* decision.

27.6 He demands that the Office take into account an opinion provided by one Anton Bosman Swanepoel.

27.7 The Sharemax prospectus which complied with Notice 459 achieved the same result as envisaged in section 7 (1) of the Code. To this day, not a single statement as contained in the prospectus has been proven to be false or incorrect.

27.8 Respondent then refers to the principle of *pacta sunt servanda* and states that complainants cannot repudiate their own signatures on the documents.

27.9 He states that he advised the complainants of the risk and refers to the compliance documents, namely, the Sharemax Risk assessment form, the Sharemax application form, the Record of Advice and the Statutory Notice in terms of the Long Term Insurance Act.

27.10 He was not aware that the Sharemax structures required it to have a board.

28. With regard to what he took into account in deciding that the investments were appropriate, respondent states that the complainants wanted high returns and they were unhappy with the performance of their investments with Momentum.

29. He took into account that Sharemax was licensed by the FSB, meaning Sharemax had a stamp of approval and that it offered a registered prospectus which complied with Notice 459. Respondent ought to know that the FSB does not product regulate the industry and the approval of a category of licence does not relieve the FSP from his duty in terms of sections 2, and 8 (1) (a) to (c) of the Code.

30. The risks are fully explained in the prospectus and other compliance documents signed by the complainants.

31. The disclosures contained in the prospectus (which are in compliance with Notice 459) constitute full and frank disclosures which enabled the complainants to make an informed decision.

32. Then respondent makes the following telling statement:
'*With reference to the Government Notice 459 of Gazette N. 28690, it does not prohibit schemes where amounts would be paid prior to the transfer where the property is being developed. In this regard I also refer to the expert report of Mr Anton Swanepoel annexed hereto. Although the Villa scheme fell outside the parameters as envisaged in the said Notice, the promoters nevertheless utilised the provisions of the Notice to ensure that full and transparent disclosures were made to investors to enable investors to make informed decisions. The Sharemax prospectus complied in all these respects with the provisions of Notice 459*.'

33. Respondent sees his role as that of ensuring that investors, such as the complainants, are able to make an informed decision. He claims that his role does not extend to refusing to assist an investor who wishes to invest in a product that exceeds the investors risk profile.

H. ANALYSIS AND RECOMMENDATION

The complaint against respondent is not clear

34. It is necessary to first deal with the statements by the respondent that the case made against him by the complainants is not clear. I also note that respondent nevertheless proceeded to deal with the complaint and denied that he was negligent; this, in the event the complainants' case was based on negligence.

35. First there is no requirement in the FAIS Act that complainants formulate their complaints with the same particularity and precision as that of pleadings in an adversarial system. Second, the complainants state in their complaints that as a retired couple, they sought the services of the respondent (a long-time friend and authorised financial services provider) to advise them on where they could place their retirement funds in order to provide for their retirement income. In other words, the complainants have established the existence of a contract to render financial services.

36. In rendering financial services respondent had to align his conduct with the General Code of Conduct, (the Code). Based on respondent's, complainants invested their retirement capital.

37. Respondent on the other hand, has not denied the existence of the contract and the fact that it was his advice that led to the Sharemax investment. He has further proffered the basis of recommending Sharemax to the complainants which includes *inter alia*, the fact that investors' capital was protected under Sharemax and their impeccable track record. It is only when their income stopped that the complainants realised that their capital and income were in fact at risk and they promptly filed complaints against them. That same complaint is made in the complainants' rule 5 (g) response where they accused respondent of failing to advise them that the Sharemax product was high-risk.

38. Apart from the *ex post facto* claims of having explained risk to the complainants, there is nowhere in the documents submitted to this Office where he explained the true risk to his clients. Not in his section 3 (2) record, nor his record of advice in terms of section 9.

The opinion

39. Upfront, the opinion of Swanepoel, which was attached to the respondent's response is dealt with in detail in the *Vorster* determination[14] paragraph 31 (a) – (m). Quite simply, the opinion adds no value as Swanepoel claims that the Notice (Notice 459) did not apply to schemes such as The Villa and that the promoters of the scheme had to adapt it. Swanepoel failed to substantiate why the Notice would not apply to The Villa. The law in any event does not call for the Notice to be adapted; it is to be complied with. Overall, this Office is simply not persuaded by the opinion.

[14] Bernardus Rudolf Vorster and Magdalena Josina Vorster v Fanie du Preez Makelaars CC t/a The Meadow Group and Stephanus Johannes du Preez- FAIS 03406/03408/03409/03410/03411/12-13/ EC 1, paragraph 31 (a) – (m)

40. In the paragraphs that follow I demonstrate that the risk inherent in The Villa was extraordinary and that respondent's statements that the complainants' investment would be safe was a material flaw in his advice. In that case, respondent failed to advise his clients appropriately as required by the Code.

41. On their own, the violations of the law as conveyed by the directors, (in this respect their disbursement of investor funds in violation of Notice 459), meant that the investors were without any protection. I point out that the prospectuses confirmed that investors' funds had already been disbursed to several entities including the unexplained and gratuitous disbursement to entities like Brandberg Konsultante (Pty) Ltd, (the directors of which are not revealed anywhere, not in the Sale of Business Agreement, (SBA) and not in the prospectuses). The provisions of the prospectus and the Sale of Business Agreement (SBA), more fully dealt with hereunder, should have raised questions of investor protection on the part of respondent and should have been communicated to his clients. None of that appears in any of the respondent's responses to this Office.

The Villa Ltd Prospectus

Violations of Notice 459

42. From the onset, paragraphs 4.3 of The Villa Ltd prospectus made it plain that the directors of Sharemax, who also were directors of all the other Sharemax companies involved in the prospectus, were not going to comply with Notice 459.

43. In this regard, the prospectus made provision for disbursing investors' funds to pay for the entire shareholding of The Villa Retail Shopping Investments (Pty) Ltd, (The Villa (Pty) Ltd), from Sharemax. There is no detail of the concomitant benefit for investors and neither is the full purchase price noted anywhere in the prospectus.

44. The prospectus disclosed (in paragraph 4,3) that investor funds will be lent to the developer, Capicol 1 via The Villa (Pty) Ltd, a subsidiary of the group, Sharemax well before registration of transfer of the immovable property into the name of the syndication vehicle.

45. The movement of the funds was illegal and a direct affront to Notice 459 (see Annexure A3, which contains a summary of section 2 (b) of the Notice) which is aimed at investor protection. The respondent, even in his answers to this office, says nothing about the infringement of the Notice.

Conflicting provisions of the prospectus

46. I refer also to the conflicting provisions of prospectus; in this regard paragraphs 19.10 and 4.3. First, paragraph 19.10 states that funds collected from investors would remain in the trust account in terms of section 78 2 (A) of the Attorneys Act. Investors' returns will be paid from the interest generated by the trust account. Paragraph 4.3 however, conveys that the funds would not stay long enough in the trust account with 10% being released after the cooling off period of seven days to pay commissions. The same statement is made in the application forms that clients had to complete in applying for the investment. This payment too was in violation of the Notice.

47. There are two problems with the proposition that the investor's return was paid from the interest generated by the trust account. They are:

47.1 At the time, the interest payable by the bank on investments made in line with section 78 (2A) did not go beyond one digit. In fact, this office obtained information that the interest payable at the time was between 5.9% - 7%[15].

47.2 The prospectus is unequivocal that the funds would not stay long enough in the trust account to have accumulated any significant interest as they were withdrawn, firstly after ten days to fund commissions and subsequently, to fund the acquisition of the immovable property.

47.3 The prospectus states that the interest payable on the claim component of the unit will be determined from time to time by the directors[16].

Sale of Business Agreement (SBA)

48. The prospectus issued by The Villa refers to a Sale of Business Agreement (SBA) concluded between The Villa (Pty) Ltd and the developer, Capicol 1 (summary attached, annexure A4). Two types of

[15] http://www.fidfund.co.za/banking-options/credit-interest-rate-history/

[16] See paragraph 9.3.1

payments are dealt with in the SBA. They are: payments to the developer, Capicol 1 (Capicol) and an agent, Brandberg.

Payments to Capicol

49. According to the agreement, investors' funds were moved from The Villa Ltd to The Villa (Pty) Ltd and advanced to the developer of the shopping mall. The payments were made well before transfer of the immovable property, and thus were in violation of the provisions of Notice 459. At the time of releasing the prospectus of The Villa, Sharemax had already advanced substantial amounts to the developer in line with this agreement (see paragraph 4.23 of The Villa prospectus). A brief analysis of the business agreement reveals:

49.1 No security existed for the loan in order to protect investors, which is clear from reading the prospectus and the agreement.

49.2 The prospectus states that the asset was acquired as a going concern, but the building was still in its early stages of development.

49.3 At the time the funds were advanced to the developer, the immovable property was still registered in the name of the developer. Although the prospectus mentioned the intention to register a mortgage loan, there is no evidence that it was registered.

49.4 The developer paid interest of 14%, from which Sharemax took 2% and paid the remaining 12% to the investors of the Villa.

49.5 The agreement is devoid of detail relating to the assessment of the developer's credit worthiness.

49.6 No detail is provided to demonstrate that the directors of the Villa had any concerns about the Notice 459 violations.

49.7 There are no details regarding the economic activity that generated the 14% return paid by the developer.

49.8 The conclusion is ineluctable that the interest paid to investors was from their own capital.

50. There was also no evidence that the developer had independent funds from which it was paying interest; besides which, if the developer had the financial standing to borrow such large sums of money at 14% per annum, it would have gone to mainstream commercial sources.

Payments to Brandberg

51. An entity known as Brandberg was paid commission in advance. The commission is said to have been calculated at 3% of the purchase price of R2 900 000 000 according to the SBA. There are no details of the benefit to investors for paying the amounts to this entity. No valid business case is made as to why commission had to be advanced in light of the risk to investors. There was also no security provided against this advance to protect the interests of the investors.

52. It is plain from the response of the respondents that the high risk involved in this investment was ignored or respondent simply had no resources to identify it.

I. FINDINGS

53. On the basis of the reasoning set out in this recommendation, the respondent failed in his duty to advise complainants about the risk in the investment, thus violating Section 7 (1). The section calls upon providers other than direct marketers to 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*".

54. I add that the prospectus made it plain that the investment was far too risky, guaranteeing neither the capital nor the income. Again, respondent had no basis to invest complainants' funds into this product. His recommendation was either a result of incompetence or lack of skill, in which case respondent was negligent (*Durr v ABSA*). Either way, respondent violated his duty to act with skill, care and diligence as provided for in section 2 of the Code.

55. Respondent has provided no documentation to demonstrate that, despite having had access to all the relevant and available information pertaining to complainants, the recommendation made was appropriate to their needs and circumstances.

56. As a consequence of the breach of the Code, the respondent committed a breach of his agreement with complainants in that he failed to provide suitable advice. The respondent must have known that complainants would rely on his advice as a professional financial services provider in effecting the investment in Sharemax. Complainants also trusted respondent.

57. The representations made to the complainants were incorrect and in violation of section 3 (1) (a) (vii) of the Code. Complainants were simply not advised that the product was high risk and that they could lose their capital. There is no doubt that had the complainant been made aware of the risks involved in these investments, they would not have invested in the Villa Ltd scheme.

J. CAUSATION

58. The question that must be answered is whether respondent's materially flawed advice caused complainants' loss. In the first instance, had respondent complied with the Code and sought investments that were in line with complainant's circumstances, there would have been no investments in Sharemax. In the event the complainants had still insisted on the investment, and assuming they had been made aware of the obvious dangers, respondent was still obliged to comply with record 8 (4) (b) of the Code. Instead respondent referred this Office to a Sharemax Risk Assessment form, which form contains no useful information in so far as the risk that was contained in this product. In all, respondent failed his clients woefully in terms of his duty to provide appropriate advice. Second, respondent must have known that his clients were going to rely on his recommendations in making the investment. It stands to reason that the respondents caused the complainant's loss, which loss must be seen as the type that naturally flows[17] from the respondents' breach of contract.

[17] *Administrator, Natal v Edouard* 1990 (3)SA 581 (A); *Thoroughbred Breeders' Association of SA v Price Waterhouse* [2001] 4 All SA 161 (A), 2001 (4) SA 551 (SCA), paragraphs 46-49; Compare in this regard, *First National Bank v Duvenhage* [2006] SCA 47 (RSA).

K. RECOMMENDATION

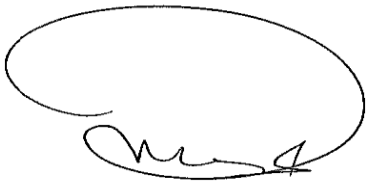
59. The FAIS Ombud recommends that respondent pay complainant's loss in the following manner:

59.1 An amount of R800 000[18] to the first complainant; and

59.2 An amount of R800 000 to the second complainant.

60. The respondents are invited to revert to this Office within TEN (10) working days with their response to this recommendation. Failure to respond with cogent reasons will result in a final determination being made in terms of Section 28 (1) of the FAIS Act[19].

Yours sincerely



NOLUNTU N BAM
OMBUD FOR FINANCIAL SERVICES PROVIDERS

[18] The lost income in respect of each of the complainant's investments since October 2010 far exceeds the amount of R800 000. Each of complainants' investment constitutes a distinct cause of action.

[19] "*The Ombud must in any case where a matter has not been settled or a recommendation referred to in section 27(5)(c) has not been accepted by all parties concerned, make a final determination, which may include-*
(a) the dismissal of the complaint; or
(b) the upholding of the complaint, wholly or partially…."