IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

Case Number: FAIS 03045/09-10/WC/(1)

In the matter between:-

Vinolia Ntombekaya Bam-Mgugunyeka	**Complainant**
and	
U C PRIVATE WEALTH T/A	
LIBERTY MOON INVESTMENTS	**1st Respondent**
MOUNTAIN BROKERS CC	**2nd Respondent**
MOUNTAIN BROKERS TRUST	**3rd Respondent**
BERNARD MARC EDGCUMBE	**4th Respondent**

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

A. INTRODUCTION

[1] This complaint concerns investments made with companies known as Genesis Property Partners (Pty) Ltd ('GPP') and Cedar Falls Properties 30 (Pty) Ltd ('Cedar'). Both companies are part of an entity generally referred to as the Genesis Property Group of Companies ('Genesis').The background information on the Genesis Property Group of Companies was comprehensively dealt with in the determination of LOUISE ELLEN DANIELZ and ANOTHER v U C PRIVATE WEALTH and OTHERS, FAIS Reference No's: FOC 3593/09-10 WC (1) and FOC 3594/09-10 WC (1)

('Danielz')[1]. It therefore follows that this determination must be read with that of Danielz.

B. THE PARTIES

[2] The Complainant is Vinolia Ntombekaya Bam-Mgugunyeka, an adult female, residing in Goodwood, Western Cape.

[3] The first respondent is U C Private Wealth, Registration number 2001/016812/07, trading as Liberty Moon Investments with its registered address being 17 The Pavilion, Central Park, Esplanade Road, Century City, Western Cape. The first respondent was licensed in terms of the FAIS Act with licence number 22015, however according to the regulator's records; the first respondent's licence lapsed on 6 April 2011.

[4] The second respondent is Mountain Brokers CC, a close corporation duly incorporated in terms of the company laws of South Africa with its registered address being 4th Floor, Long Street, and Cape Town, Western Cape registration number 1995/017669/23. According to the respondents' documents, Mountain Brokers CC was issued the licence, its number being 12248, as a financial services provider. The registrar's records indicate however, that the same licence number was issued to an entity noted as "Lucre, the Financial Collective CC", and that this licence has since lapsed.

[1]The underlying facts in the current matter are exactly the same as in Danielz. As in Danielz, all 4 respondents are respondents in this matter.

[5] The third respondent is Mountain Brokers Trust, a trust duly registered in terms of the Trust Property Laws of South Africa with its registered address being Lonpre House, Loerie Park, Paul Kruger Street, Durbanville, Western Cape, registration numberIT1518/2004. The third respondent was also an authorised financial services provider with licence number 12906, which lapsed on 6 April 2011.

[6] The fourth respondent is Bernard Mark Edgcumbe, an adult male financial services provider of 10 Morea Street Vierlander, 7550, Western Cape.

[7] Complainant argues that she was under the impression that she was dealing with second respondent. Her impression was formed as a result of the fourth respondent's representations during the course of rendering financial advice to her. However, Fourth respondent states that, at the time he rendered financial advice to the complainant, he was only acting on behalf of the first and third respondents.

[8] Notwithstanding the fourth respondent's assertions, he was unable to proffer any evidence supporting his claims. There is no evidence that he disclosed to complainant that he was only representing the first and third respondents. What is more, the disclosure documents do not bear out any of the fourth respondent's claims that he made the required disclosures. In this connection, Section 5 (b) of the Code requires financial services providers to confirm in writing:

'concise details of the legal and contractual status of the provider .....to be provided in a manner which can reasonably be expected to make it clear to the client which entity accepts responsibility for the actions of the provider or representative in the rendering of the financial service involved.....'

[9] On the facts before the office, the fourth respondent was at all relevant times, the key individual, authorised representative and clearly a mover and shaker behind the first, second and third respondents.

[10] The investigations in both the present complaint and that of Danielz point to fourth respond having operated the first, second and third respondent interchangeably. Having failed to meet his obligations in terms of section 5 (b) of the Code, fourth respondent cannot now be allowed on his own accord to decide which entity is responsible for rendering financial services to respondent. The fact remains that at different times, and without making the required disclosures to the complainant, the fourth respondent made use of the first, second and third respondents when advising the complainant.

[11] In the instance I have no option but to cite all four respondents, whom I hereafter refer to collectively as 'the respondent'. This is a reference to the fourth respondent who was also a representative of the first, second and third respondents, and was accordingly acting on behalf of these entities when he rendered financial advice to the complainant.

C. COMPLAINT'S VERSION

[12] When she needed to invest her retrenchment benefits, complainant was referred to the respondent who recommended Genesis as a low risk investment. Genesis focused on investments in undeveloped sites just outside Cape Town and the Water Front. The respondent advised the complainant that she would receive her initial investment and 25% interest after a period of six months.

[13] The respondent recommended to the complainant the benefits of investing in Genesis and emphasised how well it had been performing over the years. In addition, he showed the complainant a list of Genesis investors and the numbers of years they had invested with Genesis to further reaffirm its impressive reputation.

[14] Acting on the respondent's advice, the complainant invested an amount of R120 000.00 in GPP and R160 000.00 in Cedar. On 20th March 2008, the complainant's total investment in Genesis amounted to R280 000.00.

[15] Sometime in September 2008, when the complainant contacted the respondent with the view to reinvesting the interest payment due to her, the respondent informed her that Genesis was experiencing problems and that a number of investors had not received their interest payments since March 2008. The respondent further advised her to attend a meeting of Genesis' investors. It was then that the respondent accused Genesis management of the theft of funds and mismanagement.

[16] Subsequently the complainant contacted the respondent on numerous occasions, only to be advised that he could not be of any assistance. In August 2010, the complainant received confirmation that Genesis was in final liquidation.

[17] Complainant received neither her interest nor capital payment, and consequently lodged a complaint with the office.

[18] The complainant asserts that the respondent violated the provisions of the FAIS Act in that he failed to conduct proper due diligence on the financial product prior to recommending it to his client. The complainant submits that given her personal profile and circumstances, the respondent should not have sold her such a high risk product.

[19] Accordingly the complainant attributes her financial loss squarely on the respondent's failure to properly advise her. In that regard, the complainant seeks compensation for her lost investment.

D. RESPONDENTS' VERSION

[20] Before dealing with the respondent's response in detail, it is perhaps apposite to note that in all complaints against the respondent that have come before this office, the common thread running through his responses amounts to the following:-

20.1. the product sold to the complainant is not a financial product and that the complainant was aware of this fact;

20.2. the complainant is a well-educated person;

20.3. the Office lacks jurisdiction.

[21] Of concern though, is the respondent's seeming failure to appreciate his statutory duties as a provider rendering financial services to clients. However, since each complaint turns on its own peculiar facts, in this matter, I simply confine myself to its own set of facts as furnished by the parties.

Due Diligence

[22] The respondent stated that when he advised the complainant, he had been dealing with Genesis since 2002. He submits that Genesis and its directors had a good reputation and history of successful developments.

[23] The respondent states that he physically inspected the properties, and assessed the prices, location, views and measured the physical size of those properties, comparing them with those of surrounding developments in the same geographical areas.

[24] The respondent further asserts that the 2006 financial statements of Genesis appeared healthy, and that this was borne out by the substantial loans granted to Genesis by large banks which are notoriously risk averse and conservative. This assertion is not entirely accurate. The respondent

conveniently fails to mention that the loans granted by the banks were secured by the immovable property.

[25] I have had occasion to go through the financial statements of Genesis as submitted by the respondent. Closer inspection of these and other Genesis' documents reveal a somewhat different picture than the one respondent sought to paint. Contrary to the respondent's claims of Genesis's financial soundness, the fact remains, investors' unsecured loans made up the bulk of Genesis financial liabilities.

[26] As a result, whilst the banks were able to call up their secured loans amounting to R43 497 740.00 when Genesis collapsed, unsecured investors, such as the complainant, enjoyed no such protection.

[27] Unsecured loans together with interest amounted to R113 475 770.00. These loans had to be repaid to investors within 4 to 18 months; yet a perusal of Genesis' financial statements reveals that their revenue was a mere R9 208 213 for the period ending February 2006.

[28] Even more disturbing are the loans to the directors in the same financial year (2006) which amounted to R16 612 607.00. An amount far in excess of Genesis' turnover, which would indicate a contravention of the Companies Act of 1973 as amended.

[29] Given Genesis' huge debt and low turnover, it is incomprehensible how the respondent could conclude that Genesis was in sound financial form.

[30] Perhaps, what is even more astounding about respondent's claims of financial stability and soundness is that he at no stage claims to have personally satisfied himself as to the legality of Genesis' activities. It is common cause that Genesis was collecting money from the public. To this end, they made use of licensed intermediaries who acted as a link between Genesis and the broader public. It is clear that the respondent failed to make elementary enquiries about the legal status of Genesis. Thus for example, the respondent as a financial provider should have verified from the regulator whether Genesis was licensed or authorised as financial services providers, as was required by law. As it turns out, they were never licensed. Needless to say, this constituted a material breach of the FAIS Act.

[31] In terms of chapter III of the Financial Advisory and Intermediary Services Regulations:

'no person may in any manner or by any means, whether within or outside the Republic, canvass for, market or advertise any business related to the rendering of financial services by any person who is not an authorised financial services provider or a representative of such a provider.'

[32] Quite simply respondent breached the law. He showed flagrant disregard of various provisions of the FAIS Act by failing to even ascertain whether the

entity in which he invested the complainant's money was authorised or licensed. In my view, the respondent's claims of financial soundness of Genesis merely serve to illustrate the extent of his lack of appreciation of, and insight into the inner workings of the kind of financial product he recommended.

Complainant is highly educated

[33] The respondent submitted that the complainant was employed by Old Mutual for a number of years. She had significant exposure to the traditional and regulated products marketed by Old Mutual. Complainant readily admitted that she indeed worked for Old Mutual, but asserts that her experience was limited to group life.

[34] Respondent claims that the complainant made it clear that she was not interested in investing in unit trusts or endowments. She wanted a property related transaction which would provide her with higher returns.

[35] According to the respondent the complainant was not risk averse. She was prepared to relend her capital to Genesis. The respondent however claims to have cautioned the complainant that should property values decline so would the security of her loan. These claims by the respondent are however not supported by any documentary evidence or record of advice. The respondent could not furnish any evidence to substantiate his claim that complainant was aware of the risks which she faced in relending to Genesis. I pause to mention that section 8 of the Code enjoins the financial provider to maintain a record of

advice furnished to a client which must provide the basis on which the advice was given. The requirements of section 8 were clearly meant to prevent fabrication of latter day defences; as such records serve as objective account of how and what advice was rendered.

The FAIS Ombud lacks jurisdiction to entertain the complaint

[36] The respondent states that the product sold to the complainant constituted a loan agreement which does not qualify as a financial product. He therefore argued that the present complaint falls out of the ambit of the FAIS Ombud. In that regard, the respondent submitted a document he claimed was a legal opinion supposedly from the Financial Services Board ('FSB'). It is significant however that the alleged opinion that the respondent is referring to is something that he stumbled upon long after he had sold the financial products to the complainant. Contrary to the impression that the respondent sought to create, it is clear from the facts he submitted that he did not go out of his way to establish the legality of the operations of Genesis. At any rate, nothing really turns on the so-called Opinion. It could never have assisted the respondent at the time he rendered advice to the complainant, as he only obtained it purely fortuitously long after he had rendered financial services to the complainant. In my view, the respondent's production of the opinion can only be seen as a self-serving move.

[37] Moreover, in dismissing the respondent's defence, I can do no better than refer to the reason set out in Danielz. In the latter matter, the Ombud had occasion to remark as follows:

'The FSB legal 'opinion' respondent is referring to is a page with the regulator's logo, written in poor English, with no author. The regulator had no knowledge of the 'opinion'. When the respondent was asked where and when he obtained the 'opinion', he pointed to the directors of Genesis but could not remember the time. Clearly, any provider who would accept such a document as an opinion must be questioned as to his fitness to advise the public.'[2]

[38] Put simply, the FSB had nothing to do with this document. As pointed out in Danielz, this so-called Opinion was clearly contrived to mislead the investors. On his own version, the respondent did not purport to have personally enquired from the regulator about Genesis. Quite the contrary, he later attributed the so-called Opinion to the directors of Genesis.

[39] An additional submission made by the respondent which in his view deprives this Office of jurisdiction is that the resolution of this matter will involve, amongst other things, an investigation into how and why the Genesis group collapsed and the timing thereof, which investigation would require expert evidence in order to determine whether or not respondent acted negligently.

[40] There is no substance to the latter submission. The issues to be determined by this Office are essentially issues of compliance with the provisions of the FAIS Act, at the time financial advice was rendered. The substance of the complaint is that the respondent failed to appropriately advise complainant in accordance with the Code. This is rebuttable by mere production of the

[2]Quoted from paragraph 58 of Danielz.

records of advice which the respondent as a provider ought to have maintained in terms of section 9 of the Code. As pointed out already, such requirements of maintaining records of advice were meant to prevent unnecessary disputes of facts. Where a financial services provider has kept such records of advice, whether in writing or electronic form, they serve as an important and often reliable source of evidence. In the present matter, the respondent failed to maintain any record evidencing how and what financial advice was rendered.

Impartiality

[41] The respondent's response also alludes to what he calls the lack of impartiality of this Office. There is no basis to the respondent's allegations of bias. In my view, these assertions are not borne out by any supporting evidence, and should be rejected without more.

E. DETERMINATION AND REASONS

The records maintained by the respondent

[42] After taking reasonable steps to seek from the client appropriate and available information, there is a duty on respondent to identify the financial product that will be appropriate to the client's risk profile and financial needs. That these requirements as encapsulated in section 8 (1) of the Code were indeed met must be evidenced by the record of advice, which is required to be maintained in terms of section 9 (1) of the code.

[43] As pointed out already, the respondent's failure to comply with section 9 means that he is unable to proffer any evidence in support of his allegations. In fact, there is simply no record kept in terms of the Code. The respondent could not provide this Office with his record of advice. His response when asked for his records is worth quoting at some length:

'I do not have the complainant's files in my possession. IRRES Wealth Management (Spotlight/X-plan) has an offsite and triple on-line back-up service that they offer. Being 100% FAIS compliant in terms of their back-ups and due to the fact and they are the most respected and widely used insurance industry data base company both Nationally and with International operations as well, we were assured that we could safely and securely convert all our files into an electronic format and store the latter with them. Please refer to the emails (Annexure 6) addressed to IRESS Wealth Management (Spotlight/X-plan), which expressly indicates my frustration in getting all the relevant compliance documentation form their data base. It appears as though when downloading our information, somewhere in their process they practically corrupted our database to the extent that their own internationally acclaimed professionals were not able to resolve this matter as yet. Due to the technical problems encountered we are currently not able to provide your office with any other documentation. I would however request that your office view the numerous documents supplied with the complaints of Mr & Mrs Germishuys 03593/09-01 and 05322/08-09 and ..... 03353/08-09 & 04040/08-09 all of which clearly indicate that, from a documentation perspective I conduct business according to the FIAS Code of Conduct'.[3]

[3]Quoted with errors.

[44] During the course of investigation, IRESS confirmed to this Office that they could not find any records relating to financial services rendered to the complainant. It therefore goes without saying that the respondent failed to maintain the required record of advice.

Inherent investment risks

[45] According to investment agreements entered into with GPP and Cedar, the complainant agreed to lend money to the companies for a period of six months. In return, the companies agreed to pay the complainant simple interest calculated at a guaranteed rate of 25% per annum on the loan amount, with interest running from the date of the loan up until the date of full repayment.

[46] The respondent argues that most of Genesis' financing came from banks and other financial institutions and that paying returns of 25% 'did not in itself indicate risk'. Furthermore, so the submission goes, investors' loans formed a very small percentage of Genesis' total development costs. The financial statements paint a different picture.

[47] These submissions are factually incorrect and misleading. As previously pointed out, Genesis had unsecured loans which amounted to R113 475 770.00 when interest of 25% per annum was added. These loans had to be repaid to investors within a period of four to eighteen months and made up the bulk of Genesis liabilities. The astronomical return of 25% was way above

the average market rates offered at the time. What is more, this rate was supposedly guaranteed.

[48] This alone should have been a red flag to the respondent. The respondent is an authorised financial services provider. He should have known that investments that offer extravagant claims of returns invariably come with a very high level of risk. He should have investigated how it was possible for Genesis to generate such huge returns for investors when the markets were offering single digit returns. Needless to say, he failed to do so.

[49] Apart from the questionable high returns offered, Genesis was not an authorised financial services provider. They were unlicensed and unregulated. The lack of regulatory oversight meant that Genesis offered very little, if any protection, to investors. When companies are not regulated, mismanagement and/or fraudulent activities are generally not detected or if so detected, it is usually too late. The respondent's failure to make these disclosures marks a contravention of Section 7(1)(a) of the Code which requires a provider to

'make full and frank disclosure of any information that would reasonably be expected to enable a client to make an informed decision.'

[50] The respondent was not perturbed by the fact that at a time when the revenue of the entity appeared to have been less than its liabilities, according to its financial statements dated 23 November 2006, the company had no problem lending money to directors. What should have alarmed the respondent even

further is the fact that the investment agreements entered into with the investors stipulate that capital invested would, *inter alia,* be utilised to repay investors or other interim funders. The payment of purported returns to investors from funds contributed by new investors should have raised alarm bells with respondent and dissuaded him from investing complainant's funds in Genesis. The payment of later investors by new investors' funds made the scheme illegal. The respondent had access to the financial statements of Genesis, but could not appreciate or discern these unlawful activities.

[51] The respondent submitted that he was alerted to the financial difficulties faced by Genesis in January 2008 when one of his clients drew his attention to an Afrikaans newspaper article. According to the respondent, he made enquiries but was assured by Genesis that the client who featured in the article had already been paid. That same client, so the respondent was told, did not understand the maturity date and the notice period of the investment. Despite all the warning signs about Genesis, the respondent accepted Genesis' explanation and two months later he advised the complainant in the present matter to invest in Genesis. A few months later, Genesis investors had to deal with the news of its demise. The respondent's conduct does not accord with the conduct expected of an adviser exercising the requisite due skill, care and diligence.

Appropriateness of advice

[52] At the time the complainant was advised to invest in Genesis, she was unemployed and could not tolerate high risk. The fact that she was

unemployed is in itself indicative of a need for capital preservation, unless records indicate the contrary. Yet as already mentioned, the respondent could not produce evidence which contradicts this need for capital preservation.

F. CAUSATION

[53] In light of the aforegoing, there can be no question that the recommendation of such a high risk product was wholly inappropriate to complainant's needs.

[54] Had it not been for the respondent's advice, the complainant would not have invested in Genesis and would not have lost her capital. It does not avail the respondent to argue that he could not have foreseen the alleged theft or mismanagement in Genesis. As already detailed in this determination, all the warning signs that the scheme was a high risk one, were there. The scheme was clearly unsustainable, and this simple fact was evidenced by the blatant use of investors' capital to pay other investors. This was disguised by Genesis as returns, but any person in the position of the respondent who had access to the financial statements, should have detected this impropriety. It was glaring and readily identifiable from the financial statements. Whilst not making any imputation of dishonesty to the respondent, the facts however amply illustrate his failure to appreciate even the most basic aspects of the Genesis scheme. On his own version, the respondent could not see anything wrong with Genesis financial statements. At worst, the inescapable conclusion one draws from these facts is that the respondent was simply incompetent.

[55] As it turns out, the respondent believed a mere physical inspection of properties and visits to the offices of Genesis was sufficient to constitute proper due diligence. He had no idea who was behind the company and what measures were in place to protect the investors from incidents of theft and fraud. He had no idea whether there was a board and what skills the individual members of that board possessed. He was content with putting the complainant's money into an entity he knew nothing about. Clearly, the respondent's own negligence led to the investment and complainant's subsequent loss.

[56] The complainant has informed this Office that of the R160 000.00 she invested in Cedar, she has received R17 000.00 from the liquidators. I therefore intend to make an order in the amount of R280 000.00 less the R17 000.00.

G. ACCOUNTABILITY

[57] It is perhaps convenient and appropriate that I deal with the issue of the joint and several liabilities of the respondents. The fourth respondent was a key individual of the first, second and third respondents. On the facts of this case, if I were to hold the first, second and third respondents solely liable, this would not be in line with the intention of the legislature , as encapsulated in various provisions of the FAIS Act. In a nut shell, the following illustrate the desirability of holding the fourth respondent jointly and severally liable alongside the three other respondents:-

57.1. In terms of section 8 (1) (c) of the FAIS Act in instances where a financial services provider is, amongst others, a juristic person or a corporate body, the applicant for licensing must satisfy the registrar that any key individual in respect of such applicant complies with the requirements of personal character qualities of honesty, integrity competence and operational ability. It is only when the registrar is satisfied that an applicant meets these requirements that a licence will be granted.

57.2. Additionally 'no such person may be permitted to take part in the conduct of, management or oversight of a licensee's business in relation to the rendering of financial services unless such person has on application been approved by the registrar.'

57.3. Section 8 (5) (ii) additionally requires that upon the change in the personal circumstances of a key individual, the registrar may impose new conditions on the licensee. From the obligations imposed on the key individual it is clear that it is the key individual himself that is personally responsible to satisfy the registrar that he is fit and proper. Authorisation of the entity is approved through the key individual himself.

57.4. The fact that where the key individual does not meet the legislative requirements of fit and proper, the corporate entity's licence can be withdrawn means the intention of the legislature is to hold both persons

accountable. The General Code of Conduct for Authorised Financial Services Providers and Representatives (the Code) clearly envisages that the general and specific duties of a provider of financial services are those that are performed by a natural person as opposed to an artificial persona or juristic person. This is evident in the following:-

(i) the definition of 'provider' includes a representative;

(ii) the general duty of a provider in Section 2 of the Code requires that financial services be rendered with due skill, care and diligence, in the interests of clients and the integrity of the financial services industry. This can only be performed by a natural person;

(iii) the various specific duties regarding the rendering of financial services as set out in section 3 require human intervention. The same holds true for all other requirements set out in Parts III, IV, V and VI of the Code;

H. ORDER

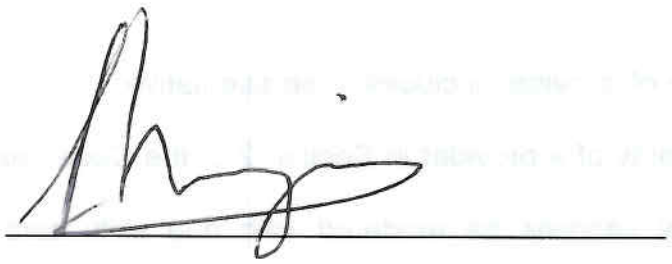
[58] In the premises, I make the following order:

1. The complaint is upheld;

2. Respondents are hereby ordered to pay, jointly and severally, the one paying the other to be absolved, to complainant the amount of R263 000.00;

3. Interest at a rate of 15,5%, seven(7) days from date of this order to date of final payment.

DATED AT PRETORIA ON THIS THE 21st DAY OF MAY 2013.



SYDWELL SHANGISA

DEPUTY OMBUD FOR FINANCIAL SERVICES PROVIDERS