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

**PRETORIA**

**Case Number: FAIS 08280/11-12/ GP 1**

**In the matter between:**

**BRENDA BARRABLE** **Complainant**

**and**

**NEVILLE GERHARD** **Respondent**

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**DETERMINATION IN TERMS OF SECTION 28 (1) OF THE FINANCIAL ADVISORY AND INTERMEDIARY SERVICES ACT 37 OF 2002 ('FAIS ACT')**

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## A. INTRODUCTION

[1] During March 2012, the complainant approached this Office for assistance. She complained that she made a number of investments with Sharemax and PIC, on advice of the respondent. Since July 2010, she has not received income on any the investments, and despite attempts to resolve the matter with the respondent and have her capital withdrawn, she has not been successful.

[2] The complainant invested approximately R1.6 million in the respective property syndication schemes, and fears that her money is now lost.

## B. THE PARTIES

[3] The complainant is Ms Brenda Jean Barrable, an adult female whose particulars are on file with the Office.

[4] The respondent is Mr Neville Gerhard, an adult male sole proprietor. His last known address is 103 Monument Road, Allen Grove, Kempton Park. The respondent was an authorised

financial services provider with licence number 7003. The licence has lapsed on 29 September 2014. The respondent is currently a representative of IFSA (FSP 43337).

## C. THE COMPLAINT

[5] The complainant knew the respondent for more than 20 years. During this time, she purchased a number of endowment policies and retirement annuities and also made several investments with Sharemax and PIC, on the respondent's advice.

[6] The earlier Sharemax investments in the amount of **R293 000** are set out below:

| | | |
|---|---|---|
| 6.1 | Flora Centre (August 2005): | R 43 000 |
| 6.2 | Mont Rouge (May 2006): | R 38 000 |
| 6.3 | Parkside Plaza (April 2007): | R112 000 |
| 6.4 | Zambezi Retail Park (November 2008): | R100 000 |

[7] During December 2008, the complainant was retrenched from her employer, for whom she had worked for 20 years, and the respondent advised her to invest her retrenchment package in Sharemax The Villa. The respondent said that it would provide a good monthly income, that the interest would be most beneficial to her, and that the investment was safe. The complainant was skeptical, because she had so much money invested with Sharemax already, but the respondent assured her that things were going well with the company.

[8] The complainant's mental health deteriorated from 2009 onwards, and she suffered from severe anxiety and depression. Her father had to step in and deal with her financial affairs, for which he sought advice from the respondent.

[9] From 2008 to 2010, the following investments totaling **R1.4 million** were made:

| | | |
|---|---|---|
| 9.1 | PIC HS 22 (Jan 2009): | R100 000 |
| 9.2 | The Villa (Oct 2009): | R200 000 |
| 9.3 | The Villa (March 2010): | R300 000 |
| 9.4 | The Villa (March 2010): | R150 000 |
| 9.5 | The Villa (May 2010): | R300 000 |

9.6 The Villa (June 2010): R250 000

9.7 PIC HS 22 (June 2010): R100 000

[10] The funds for the aforesaid investments came from the sale of the complainant's property, as well as an inheritance from her deceased mother. Available information also indicates that the respondent surrendered a number of the complainant's endowment policies to invest in Sharemax.

[11] The income on all her investments stopped during July 2010, and this has caused the complainant severe distress. The older Sharemax investments have reached their maturity dates, however, the capital has also not been returned. The complainant made various attempts to resolve the matter with the respondent, however, he continuously advised her to wait until the issues at Sharemax are resolved.

[12] The complainant stated the following:

12.1 She was not advised of the risks in respect of property syndication investments.

12.2 She was not provided with any alternative investment options.

12.3 The respondent did not explain the difference and cost implications of the products he replaced with Sharemax products.

12.4 She was not advised that the investments were medium to long-term, and that she would have difficulty withdrawing the capital.

12.5 She was not advised of the commission that the respondent would receive.

12.6 She never received any prospectuses to read, and claim that some of the investments made were signed on her behalf.

12.7 The complainant is also of the view that the respondent "took advantage" of her health condition, and knew that she had limited chances to be gainfully employed.

12.8 The respondent knew that she was a conservative investor that did not want to take any risks. Therefore, he did not act in her best interest by investing all of her money in one basket.

## D. RELIEF SOUGHT

[13] The complainant seeks repayment of the capital amount of R1 693 000 from the respondent. Since each investment represents a distinct cause of action, the jurisdictional limit is not applicable here.

[14] The basis of the complainant's claim against the respondent is the latter's failure to render financial services in line with the FAIS Act and the General Code of Conduct, which includes the respondent's failure to appropriately advise the complainant and disclose the risk involved in the Sharemax and PIC investments.

## E. THE ISSUES

[15] The issues for investigation and determination amount to the following:

15.1 Did the respondent in advising his client, conduct himself in terms of the General Code, in particular section 2; and

15.2 Did the respondent comply with the provisions of the following sections of the Code: Section 3 (1) (a) (i) and (iii), section 7 (1) (a), section 8 (1) and (2), as well as section 9.

15.3 Did the respondent act in breach of his contract with the complainant; and

15.4 Did the complainant suffer loss and if so, what was the cause of the loss and the quantum thereof.

## F. THE RESPONDENT'S REPLY

[16] During April 2016, a notice in terms of rule 6 (b) was issued, referring the complaint to the respondent to resolve it with his client. No response was received.

[17] Notices in terms of Section 27 (4) of the FAIS Act was sent during July 2016 and December 2017 respectively, informing the respondent that the complaint had not been resolved and that this Office had intention to investigate the matter. The respondent was invited to provide the Office with his case, including supporting documents, in order for the Office to begin its

investigation. The respondent was also requested to answer specific questions regarding the advice rendered to this client.

[18] The respondent replied during January 2018, advising as follows:

18.1 That he acted as a representative of Unlisted Securities South Africa (USSA), t/a FSP Network[1], under supervision.

18.2 That the complainant's father approached him and suggested that owing to her state of mental health at the time, that some of her endowment policies be surrendered so that the proceeds could provide a monthly income. The idea was that it would be similar to the complainant receiving a salary, and would therefore aid in restoring her mental health. The respondent by his own admission, saw "merit" in this idea.

18.3 The primary concern, according to the respondent, was the complainant's health, and not her wealth. The recommendation was therefore to invest in Sharemax, who had been very successful since its inception in 1999 and from where the complainant would receive monthly interest or income.

18.4 The respondent then blames the former Financial Services Board (now the FSCA) for not having done proper due diligence on Sharemax stating that the same institution that was established to protect investors, was the one that caused investors the biggest losses.

18.5 In response to the question of Sharemax being a high risk investment, the respondent merely replied that if that was the case, why the former FSB granted Sharemax a license.

[1] Unlisted Securities South Africa was established by Gerhardus Rossouw Goosen while he was a director of Sharemax. Independent brokers like the respondent - who were licensed in their own right as Financial Services Providers, but lacked the correct license type - were able to market unsecured debentures as representatives of FSP Network Ltd, trading at the time as USSA. FSP Network was finally liquidated in 2013

18.6 The respondent stated that the investors knew that their funds were being used to construct the actual property and that it was "normal business practice". The investors however had shares in the actual building itself, and could sell those shares upon completion of the building.

***Representative of USSA***

[19] The respondent claimed that at the time of rendering the advice, he acted in the capacity as a representative of USSA[2], thus implying that he cannot be held accountable for the advice rendered. I refer in this regard to the definition of a representative[3]. The definition assumes that a person acting as a representative has to exercise the relevant final judgment, decision making and deliberate action inherent in the rendering of a financial service to a client[4].

[20] The question of whether a representative [and not the provider] should be held liable was dealt with by the former Board of Appeal in the second *Black v Moore* Appeal[5]. The appellants, relying on Board Notice 95 of 2003 argued that the responsibility lay not with the appellant as a representative, but rested solely with the financial services provider. In dismissing the argument, the Board concluded that, *'the effect of the Exemption Notice thus allows a representative (due to his minimum experience) to market products subject to a supervisor's guidance. Apart from this exemption, he has to comply with the Code of Conduct.*'

[21] Section 13 (2) (b) of the Act[6] states:

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2 Despite this contention, the respondent completed the Sharemax application form with his own FSP number, and not that of USSA. There is thus no indication that the complainant was even aware that the respondent was not licensed to sell the respective categories of products.

3 According to Section 1 of the FAIS Act 37 of 2002, a 'representative 'means any person, including a person employed or mandated by such first-mentioned person, who renders a financial service to a client for or on behalf of a financial service provider, in terms of conditions of employment or any mandate, but excludes a person rendering clerical, technical, administrative, legal, accounting or other service in subsidiary or subordinate capacity…

4 Nell v Jordaan FAIS 05505-12/13 GP 1

5 Decision handed down on 14 November 2014, paragraphs 18 to 23

6 Financial Advisory and Intermediary Services Act 37 of 2002

*"An authorised financial services provider must take such steps as may be reasonable in the circumstances to* ***ensure that representatives comply with any applicable code of conduct*** *as well as with other applicable laws on conduct of business*" [my emphasis].

[22] It is clear that there is a duty imposed not only on the provider, but also the representative to comply with the provisions of the FAIS Act and Code of Conduct. The complaint is thus directed against the correct party, being the respondent.

***Risk***

[23] It is evident from the onset that the respondent did not understand or appreciate the risks inherent to the Sharemax and PIC investments. Contrary to the respondent's explanation, the complainant did not hold shares or invest in the property itself. What the respondent failed to understand and explain to his client, was that she was lending her money to a company that did not own a property yet, and the complainant's money was subsequently lent to a developer to build the properties (Zambezi and The Villa).

[24] What the complainant acquired, was nothing other than debentures[7] or as captured in the Sharemax prospectus a claim. A "claim" is defined in the Sharemax prospectus as an "*unsecured subordinated floating interest rate acknowledgement of debt made by the company in favour of the shareholder".*

[25] The test here is whether or not the respondent provided the complainant with adequate and appropriate advice, wherein the considerable risks in the syndication products were explained to her. There is no independent record of advice which shows that the respondent made a full disclosure to the complainant, so that she could make an informed decision. On a reading of the Sharemax prospectuses, it does not guarantee the promised income and describes the

[7] A debenture is used by companies to borrow money, at a fixed rate of interest. The debenture is a document that either creates a debt or acknowledges it. A debenture is a certificate evidencing the fact that the company is liable to pay a specified amount with interest. Although the money raised by the debentures becomes a part of the company's capital structure, it does not become share capital.

investments as "*capital risk".* Similarly, the PIC prospectus states that shares on offer are noted as unlisted and should be considered as a business enterprise capital investment.

[26] The Tribunal had the following to say in the *C S Makelaars*[8] decision:

*"Each property syndication scheme must be assessed on its own merits and demerits and with reference to the risk profile of the client. Terms such as low, moderate and high are relative and should be gauged in the circumstances of the case. It is the duty of the FSP to inform the client of inherent risks in the particular product. The client may be prepared to accept the risk which many are, who are looking for a higher return and the possibility of special growth."* (My emphasis)

[27] On a balance of probabilities and on the peculiar facts of this case, it is unlikely that the complainant would have agreed to invest if the risks were disclosed to her. The complainant was reluctant to invest more money in Sharemax, but only did so because of the reassurances made by the respondent that the money was safe.

***Due diligence***

[28] The respondent has not conducted any due diligence on the products he recommended his client to invest in. This much is clear from e-mail correspondence sent by the respondent to the complainant on 4 February 2013, wherein he stated that the reason he recommended Sharemax was because they had been authorized by the FSB, and accredited with a license to market the product, which gave him the confidence to recommend the product.

[29] The attached summaries of the prospectuses, provides a clear indication why these products were simply not appropriate, and highlights non-compliance with the law (notice 459) and lack of governance. This information was available to the respondent at the time, which he failed to observe or act on.

8 FAB 5/2016

[30] The Act and Code requires an FSP to act with due diligence. This one finds in a collective reading of sections 2, 7 and 8 of the Code, read with Section 16 of the Act. "Due diligence" in law means the care that a reasonable person exercises to avoid harm to other persons, or their property. Here, the test is of a reasonable FSP. I refer to the findings of the Tribunal in the matter of *Prigge*[9]:

*"The liability of a provider to a client is usually based on a breach of contract. The contract requires of a provider to give advice with the appropriate degree of skill and care, i.e., not negligently. Failure to do so, i.e., giving negligent investment advice, gives rise to liability if the advice was accepted and acted upon, that it was bad advice, and that it caused loss. And in deciding what is reasonable the Court will have regard to the general level of skill and diligence possessed and exercised at the time by the members of the branch of the profession to which the practitioner belongs."*

[31] I also refer to the judgment of Daffue J, in the matter of *Oosthuizen v Castro*[10] where the following was noted:

*"……according to the pleadings defendant admitted informing plaintiff that she did not have to be concerned as he had spoken to Sharemax as well as his consultant. This was not good enough. Defendant should have spoken to independent auditors, attorneys or financial analysts. He should have insisted on financial statements, such as income and expenditure accounts, cash flow analyses and a balance sheet. He should have inspected the shopping complex. If he did that, he would know that the investment could not possibly have an income stream at that stage or even in the foreseeable future". (my emphasis)*

[32] It is disingenuous of the respondent to blame the FSCA for his failure to observe the Code. The FSCA does not regulate products. It remains the duty of the FSP to satisfy himself of the risks attendant in a particular product, and to match the product with his client's risk profile and needs, in line with section 8 (1) (a) to (c) of the Code.

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9 Case number FAB 8/2016 at paragraph 42

10 2858/2012, High Court, Free State Division, paragraph 53

***Replacement products***

[33] Section 8 (1) (d) of the Code provides that where a financial product is to replace an existing financial product, wholly or partially, that the FSP has to fully disclose to the client the actual and potential financial implications, cost and consequences of such a replacement. The respondent has not provided any evidence that he complied with this section of the Code.

[34] By the respondent's own startling admission, he replaced existing products the complainant had with property syndication investments because he thought there was "merit" in the suggestion made by her father. In his own words, the concern was for her health, not her wealth. This offends the very essence of what a financial services provider is licensed and obliged to do.

[35] The respondent should have shown concern with the financial wellbeing of his client and exercised his duties in accordance with the Code, especially in light of her ongoing medical problems and inability to secure employment at the time. Section 8 (1) (a) is prescriptive, in that when advice is rendered, the FSP must take reasonable steps to seek from the client appropriate an available information regarding the client's financial situation and objectives, to enable him to provide her with appropriate advice.

[36] The respondent has further not demonstrated what informed the choice of property syndication products, and why the objective of a monthly income could not be achieved by any other, more traditional options. What is evident from the facts, is that there was no incentive for the respondent to recommend any other products, *in lieu* of the attractive commission that he received on each investment. The need for a higher income alone is not sufficient to recommend high risk products where an investor could lose their entire capital.

## G. FINDINGS

[37] On the facts before me, I find as follows:

37.1 The respondent failed to render financial advice with the necessary skill, care and diligence required.

37.2 The respondent, in providing financial advice, failed to provide his client with information that was factually correct.

37.3 He failed to provide information about the products that were adequate and appropriate.

37.4 The respondent failed to provide full and frank disclosure of information to the complainant enabling her to make an informed decision.

37.5 He failed to ensure that his client invested in products that were appropriate for her needs and consistent with her tolerance for risk; and

37.6 The respondent failed to take reasonable steps to ensure that the complainant understood the advice and was in a position to make an informed decision.

[38] I find that the respondent also contravened the following sections of the General Code: Sections 3 (1) (a) (i) and (iii); Section 7 (1) (a); Sections 8 (1) and (2); and section 9 (1).

[39] On his own version, the respondent confirms that he rendered financial services to the complainant, and had done so for many years. What cannot then be disputed is the existence of a contract of rendering financial services, and that in rendering financial services to the complainant, the respondent had to align his conduct with the Code. In contravening the Code, the respondent committed breach of his contract with the complainant. On this basis alone, the respondent must be held liable for the consequences of such breach.

## H. CAUSATION

[40] On the respondent's own version, factual causation was established. But for his advice, the complainant would not have invested in Sharemax and PIC, and her capital would not have been lost.

[41] As for legal causation, this too has been established, and in this regard, I refer to the determination *in ACS Financial Management vs Coetzee*[11].

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[42] I also refer to the Tribunal's decision in *J G Financial Service Assurance Brokers (Pty) Ltd and another vs Robert Prigge*[12].

## I. THE ORDER

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

1. The complaint is upheld.

2. The respondent is ordered to pay the combined amount of R1 693 000, as stipulated in paragraphs 6 – 9 of this determination.

3. Interest on this amount at a rate of 10% per annum from the date of determination to date of final payment.

4. The complainant is to cede her rights in respect of any further claims to these investments to the respondent.

**DATED AT PRETORIA ON THIS THE 16TH DAY OF AUGUST 2018.**

**NARESH S TULSIE**

**OMBUD FOR FINANCIAL SERVICES PROVIDERS**

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