IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

Case Numbers:	**FAIS-04182-12/13 FS 1**
	FAIS-04183-12/13 FS 1
	FAIS-04184-12/13 FS 1
	FAIS-04185-12/13 FS 1
	FAIS-04186-12/13 FS 1

In the matter between:

MARTHINUS CORNELIS BIERMAN **Complainant**

and

HENDRIK JOHANNES ROSSOUW **Respondent**

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

A. INTRODUCTION

[1] During 2005, the complainant approached the respondent for investment advice. The complainant had funds available which stemmed from the proceeds of the sale of his farm. Since the complainant had no other investments or pension provision, the available funds represented his life savings.

[2] Following the advice of the respondent, the complainant made his first investment in Sharemax Silverwater Crossing (Silverwater) during October 2005. The complainant continued to receive the promised monthly interest of 9%, until it stopped a few years

ago[1]. The complainant also made an investment in Sharemax Zambezi (Zambezi) during December 2008 on advice of the respondent. The monthly interest on the Zambezi investment ceased during September 2010.

[3] The complainant indicated that the respondent was aware of his circumstances at the time and that he required safe investments.

[4] The complainant wants the respondent to be held liable for the loss he suffered.

[5] The complainant has since confirmed that the capital he invested in Silverwater Crossing has been refunded, owing to the sale of the building[2]. This determination will therefore deal with the investment in Zambezi only.

B. THE PARTIES

[6] The complainant is Mr Marthinus Cornelis Bierman, an adult male pensioner, whose particulars are on file with this Office.

[7] The respondent is Hendrik Johannes Rossouw, an adult male and sole proprietor. The regulator's records confirm the respondent's principal place of business as 12 Bauman Street, Frankfort, 9830. The respondent was an authorised financial services provider with licence number 7192. The licence lapsed on 6 July 2016.

[8] The respondent is currently conducting business as Rossouw Finansiële Dienste BK, a close corporation with registration number 2004/005153/23. The license number is 46212 and has been active since September 2015.

[9] According to the regulator's records, at the time that the respondent rendered the advice, he was only licensed to sell products in respect of categories 1.8 (shares), but

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1 The complainant cannot recall the date, but communication from the Nova Property Group seems to indicate that all interest payments were stopped during the middle of 2013 (Nova Communique of 20 June 2016)

2 The complainant confirmed that he received two payments of R177 000 each during end 2017 / beginning 2018

not in respect of category 1.10 (debentures). As a result, the respondent acted as a representative of Unlisted Securities South Africa (USSA)[3] in terms of section 13 of the FAIS Act.

[10] At all material times, the respondent rendered financial services to the complainant.

C. DELAYS IN FINALISING COMPLAINTS OF THIS NATURE

[11] We have taken long, admittedly, to attend to the matter. However, as previously communicated, there were a number of legal challenges that prevented this Office from proceeding with complaints relating to property syndication matters. Since the pronouncement of the Appeals Board in the matters of *Siegriest* and *Bekker* (which saw the Office halt the processing of property-syndication-related complaints), we resumed with the processing of these complaints with the objective of finalising the outstanding matters.

D. THE COMPLAINT

[12] At the time of making the first investment, the complainant was 62 years of age. The complainant had been a farmer all his life and his ailing health necessitated the sale of his farm. He subsequently bought a property in town and sought advice on how to invest the remainder of the funds. The complainant indicated that his highest qualification was grade 8. He had no investment experience whatsoever, and therefore relied on the respondent for advice.

[13] Based on this advice, the complainant invested an amount of R450 000 during October 2005 in Silverwater Crossing. The respondent assured the complainant of the safety of the investment and that there were no risks involved.

[3] Unlisted Securities South Africa, (USSA) 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 and sell unsecured debentures as representatives of FSP Network Ltd, trading at the time as USSA. FSP Network was finally liquidated in 2013.

[14] The complainant indicated that he was satisfied with the returns from the Silverwater Crossing syndication. During December 2008, he had an additional R180 000 available. On advice of the respondent, he invested this amount into the Zambezi syndication. The respondent again assured the complainant that the investment was safe and that he would not lose his money.

[15] The complainant indicated that no prospectus was provided to him and even if he did receive it, he would not have understood the content. The complainant stated that the respondent merely advised him where to sign on the papers, and never offered him any alternative investment products.

[16] When the interest payments from the Zambezi investment stopped, the complainant made various attempts to resolve the matter with the respondent. Despite all the bad publicity that surrounded Sharemax, the respondent continued to assure the complainant that his investments were safe.

[17] The complainant asked this Office for assistance to recover his capital in respect of the Zambezi investment from the respondent. The complainant indicated that he followed the advice of the respondent which he believed was sound, and seeks repayment of his capital amount of R180 000.

E. THE RESPONDENT'S VERSION

[18] During 2012, notices in terms of Rule 6 (b) were issued, referring the complaint to the respondent to resolve the matter with his client. The complaint was not resolved. The respondent's reply is summarised as follows:

18.1 The respondent does not dispute that he advised the complainant to make two investments in the Sharemax Property Syndication schemes.

18.2 The respondent further stated that he sold a product to the complainant that was approved by the Financial Services Board (FSB), and that he would not have

marketed it otherwise. The respondent also said that he presented the complainant with a prospectus that complied with the Company's Act.

18.3 The respondent confirmed that during December 2008, the complainant approached him to invest an amount of R180 000. He said that he, in conjunction with Mr Anton Hay from Sharemax, explained the Zambezi investment to the complainant, as well as the 11% interest payable. The respondent stated that the complainant elected to proceed with the Zambezi investment, because he was satisfied with the performance of Silverwater Crossing. The respondent further noted that the complainant insisted on receiving the higher interest rate.

18.4 The respondent stated that he was not negligent in rendering advice, and believed that he acted in his client's best interest at the time.

[19] During 2015 and 2016 respectively, the Office addressed correspondence to the respondent in terms of Section 27 (4) of the FAIS Act, informing the respondent that the complaint had not been resolved and that this Office had the intention of investigating 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.

[20] The respondent replied during June and August 2015 respectively. The responses are summarised below:

20.1 The respondent is of the view that this Office cannot make a determination on the matter because more than three years have passed since the investment was made. In other words, the complaint has prescribed.

20.2 A "single need" was addressed after which the complainant elected to invest in Sharemax, because of the higher income he would receive on the Zambezi investment, and the performance of the investment in Silverwater Crossing at the time.

20.3 The risks relative to unlisted shares were noted in the prospectus and explained to the complainant, who also received a copy of the prospectus, or so says the respondent. The guarantees were also explained to the complainant.

20.4 The complainant was advised that he had a 7 days cooling off period to cancel the investments.

20.5 The complainant has not lost his investment. Because of the name change of Zambezi Mall to Tshwane China Mall, clients would start receiving interest on the aforesaid investment again.

20.6 The respondent persisted that he would not have marketed products that were not approved by the FSB. Furthermore, he acted under the license of USSA[4] at the time that the advice was rendered.

[21] During November 2017[5], the respondent was provided with a further opportunity to address this Office in terms of section 27 (4) of the FAIS Act. This Office sent a list of questions to the respondent in an effort to establish if the latter explained the risks to the complainant.

[22] The salient points of the respondent's reply can be summarised as follows:

22.1 The respondent is of the view that property syndications cannot be seen as high risk investments, because it is a building that was registered in the name of the investors. The buildings were purchased in cash, without any mortgage bond. Furthermore, a value was placed on the building as per the prospectus. They were never required to check the valuation of the property.

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[4] Unlisted Securities South Africa, (USSA) 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 and sell unsecured debentures as representatives of FSP Network Ltd, trading at the time as USSA. FSP Network was finally liquidated in 2013.

[5] Letter attached for ease of reference.

22.2 The client was made aware that shares cannot be traded immediately and he accepted that it was a termed investment.

22.3 The respondent trusted the Sharemax directors, as well as the information that was provided in the prospectus.

22.4 The respondent further stated that brokers accepted that funds would be advanced to a developer as noted in the prospectus, and that investors would only own the building after construction was completed.

22.5 The respondent maintained his view that no investors has lost their money thus far.

F. DETERMINATION

[23] The following issues arise for determination:

23.1 whether respondent, in rendering financial services to the complainant violated the FAIS Act and the General Code, (the Code) in any way. Specifically, the question is whether the complainant was appropriately advised, as demanded by the Code;

23.2 in the event it is found that respondent breached the FAIS Act and the Code, whether such breach caused the complainant's loss.

The law

[24] Before I deal with the points raised by the respondent, I find it imperative to set out the sections of the General Code of Conduct that are relative to the issue of advice:

24.1 Section 2, part II of the Code states that a provider must at all times render financial services honestly, fairly, with <u>due skill</u>, <u>care and diligence</u>, and in the interests of clients and the integrity of the financial services industry.

24.2 Section 3 (1) (a) of the Code states that when a provider renders a financial service, that:

(a) representations made and information provided to a client by the provider –

(i) must be factually correct;

(ii) must be provided in plain language, avoid uncertainty or confusion and not be misleading;

(iii) must be adequate and appropriate in the circumstances of the particular financial service, taking into account the factually established or reasonably assumed level of knowledge of the client;

(iv) must be provided timeously so as to afford the client reasonably sufficient time to make an informed decision about the proposed transaction.

24.3 Section 8 (1) (a) to (c) of the General Code states that:

A provider other than a direct marketer, must, prior to providing a client with advice –

(a) take reasonable steps to seek from the client appropriate and available information regarding the client's financial situation, financial product experience and objectives to enable the provider to provide the client with appropriate advice;

(b) conduct an analysis, for purposes of the advice, based on the information obtained;

(c) identify the financial product or products that will be appropriate to the client's risk profile and financial needs, subject to the limitations imposed on the provider under the Act or any contractual arrangement…

24.4 Section 8 (4) (b) states that where a client "*elects to conclude a transaction that differs from that recommended by the provider, or otherwise elects not to follow*

the advice furnished, or elects to receive more limited information or advice than the provider is able to provide, the provider must alert the client as soon as reasonably possible of the clear existence of any risk to the client, and must advise the client to take particular care to consider whether any product selected is appropriate to the client's needs, objectives and circumstances".

24.5 Lastly, section 9 provides for the keeping of a record of advice which must reflect the following:

"(a) a brief summary of the information and material on which the advice was based;

(b) the financial product [sic] which were considered;

(c) the financial product or products recommended with an explanation of why the product or products selected, is or are likely to satisfy the client's identified needs and objectives; and

(d) where the financial product or products recommended is a replacement product as contemplated in section 8(1)(d) -

(aa) the comparison of fees, charges, special terms and conditions, exclusions of liability, waiting periods, loadings, penalties, excesses, restrictions or circumstances in which benefits will not be provided, between the terminated product and the replacement product; and

(bb) the reasons why the replacement product was considered to be more suitable to the client's needs than retaining or modifying the terminated product..."

G. PRESCRIPTION

[25] In response to the claim that the complaint has prescribed, I refer to section 27 (3) (a) (ii)[6] of the FAIS Act that deals with prescription. What is relevant in terms of this provision is not when the advice was rendered, but when the complainant became aware of the occurrence of the act or omission. In this instance, the complainant realised there was a problem with the investment, when he did not receive his monthly income.

[26] The argument put forward by the respondent with regards to prescription is thus incorrect, and is therefore rejected.

H. LIABILITY AS A REPRESENTATIVE OF USSA

[27] The respondent stated that at the time of rendering the advice, he acted in the capacity of a representative of USSA, thus implying that he cannot be held accountable for the advice rendered.

[28] To determine whether respondent may be held liable, attention should be paid to the definition of a representative[7]. 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[8].

[29] The question of whether a representative [and not the provider] should be held liable was dealt with by the Board of Appeal in the second *Black v Moore* Appeal[9]. 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, *'the effect of the Exemption Notice*

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

7 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...

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

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

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.'

[30] Section 13 (2) (b) of the Act[10] states:

"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].

[31] 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.

The Code

[32] The respondent does not deny that he had an agreement with the complainant in terms of which he rendered financial services to him. The specific form of financial service that this complaint is concerned with is advice[11]. That advice, undoubtedly, had to meet the standard prescribed in the General Code. The complainant acted on this advice; this issue is not disputed.

[33] The respondent has not provided any evidence that he conducted proper due diligence (despite his insistence that he did) on the investments, prior to recommending them to his client. The respondent claimed that he would not have recommended a product that was not approved by the FSCA[12]. The FSCA however does not regulate or approve products. It remains the duty of the FSP to satisfy themselves of the risks attendant in

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[10] Financial Advisory and Intermediary Services Act 37 of 2002

[11] The definition of a financial service in section 1 includes an intermediary service.

[12] Formerly known as the Financial Service Board. Effective 1 April 2008, the Financial Sector Conduct Authority

a particular product and match the product with his client's risk profile in line with section 8 (1) (a) to (c) of the Code.

[34] Notwithstanding the complainants' circumstances, the respondent still recommended Sharemax as an appropriate investment for his client. The record of advice (which falls short of the requirements set out in section 9 (1)) provides no explanation of the complainant's needs or personal information, and why the need could only be addressed by means of property syndication products. All that the record noted, was that the client had a "single need" that had to be addressed, which he identified himself.

[35] The respondent's lack of understanding of the investment, is demonstrated by his response that property syndications cannot be considered high risk investments. This despite the warning in the prospectus (which the respondent claimed he read) that the shares are unlisted and considered as a risk capital investment. If the respondent truly appreciated the risks inherent to the investment, he would have realised that the investment was not suitable for his client. To this extent, I refer to the attached annexures providing summaries of the prospectus of Zambezi Ltd and Government Notice 459 (Notice 459), as published in Government Gazette 28690.

[36] Because of the respondent's perception of the risk inherent in the investment, there is no information evidencing that the respondent was concerned with the complainant's capacity to absorb high risk. Equally, there is no evidence that the respondent was open to consider other types of investments with less risk than property syndications. The respondent's conduct failed to meet the requirements of section 8 (1) (c).

[37] Assuming that the complainant chose the Sharemax products on the basis of high returns, the respondent had a duty to advise his client of the consequences of chasing high income and to complete the record of advice as required by section 8 (4) (b). As already alluded to, there is no such record in the respondent's papers. The probability

favours the complainant's version that he was not advised of the risk involved in these products.

[38] Section 7 (1) 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 a full and frank disclosure of any information that would reasonably be expected to enable the client to make an informed decision.* The complainant from the onset informed the respondent that he required a safe investment. In his response, the respondent alluded to the fact that he explained the guarantees and the risks to the complainant. If the respondent understood the prospectus, he would have realised that there were no guarantees on the investments he steered his client to.

[39] The respondent is of the view that the complainant has not lost his investment. Whilst the complainant was fortunate to receive back his capital in respect of the Silverwater Crossing, the prospects for the Zambezi investment are bleak. I refer in this regard to the communique circulated to share and debenture holders by Nova during May 2016, confirming that the Nova Board made a decision in 2013 to reduce and / or cease the projected monthly return payments, and utilise these funds for repairs and maintenance. The letter also points to the ongoing litigation between Zambezi and Capicol.

I. CAUSATION

[40] The questions that must therefore be answered is whether the respondent's materially flawed advice caused the complainants' loss, and secondly, whether the non-compliance of a provision of the Code can give rise to legal liability, whether in contract or delict.

[41] I refer in this regard to the decision of the Appeals Board[13] in the matter of *J&G Financial Service Assurance Brokers (Pty) Ltd and another v RL Prigge*[14]. The Board noted the following:

"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.3

In the case of a provider under the Act more is required namely compliance with the provisions of the Code. Failure to comply with the code can be seen in two ways. The Code may be regarded as being impliedly part of the agreement between the provider and the client and its breach a breach of contract. The other approach is that failure of the statutory duty gives rise to delictual liability.

In both instances the breach must be the cause of the loss……"

[42] In the matter of *Smit v Abrahams*[15] two tests were identified: the direct consequences test and the reasonable foresight test. The former was explained as follows[16]:

"The presence or absence of reasonable anticipation of damage determines the legal quality of the act as negligent or innocent. If it be thus determined to be negligent, then

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13 Effective 1 April 2018, the Board is now called the Financial Sector Tribunal

14 FAB 8/2016, paragraphs 41 – 44

15 1992 (3) SA 158 (C)

16 See also in this regard *Foundational Principles of South African Medical Law* Carstens P and Pearmain D (2007), pages 509 – 515 in respect of causation

the question whether particular damages are recoverable depends only on the answer to the question whether they are the direct consequence of the act".

Farlam AJ pointed out in the *Smit* case that the principle upheld in the matter of *Overseas Tankship (UK) Ltd v Morts Docks & Engineering Co Ltd*[17] is subject to two qualifications. As long as the "kind of damage" is foreseeable, the extent need not be. Furthermore, the precise manner of occurrence need not be foreseeable.

[43] Had the respondent complied with the Code and sought investments that were in line with the complainant's circumstances, there would have been no investments in the above mentioned syndications. The respondent must have known that his client was going to rely on his recommendations in making the investments. It stands to reason that the respondents caused the complainant's loss, which loss must be seen as the type that naturally flows[18] from the respondents' breach of contract.

[44] The respondent failed to appropriately advise his client in violation of sections 2, 3 (1) (a) (vii), 7 (1), 8 (1) (a) to (c), 8 (2) and 8 (4) (b).

J. THE ORDER

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

1. The complaint is upheld.

2. The respondent is hereby ordered to pay the complainant the amount of R180 000.

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

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17 1961 AC 388 (PC); 1961 1 All ER 404

18 *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).

4. Upon full satisfaction of this determination, the complainant is to cede his rights and title to the Sharemax investments to the respondent.

DATED AT PRETORIA ON THIS THE 15th of JUNE 2018.

NARESH S TULSIE

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