IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

Case Number: FAIS 01110/10-11/WC1

In the matter between

GERALD EDWARD BLACK	**Complainant**
and	
JOHN ALEXANDER MOORE	**First Respondent**
JOHNSURE INVESTMENTS CC	**Second Respondent**

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

A. THE PARTIES

[1] The Complainant is Mr. Gerald Edward Black, an elderly male pensioner who resides at 9 Avenue Orleans, Diepriver; CAPE TOWN.

[2] The First Respondent is Mr. John Alexander Moore, an adult male, an Authorised Financial Services Provider and key individual of 2nd Respondent` who resides at number 1 Rosmere Centre, 67 Rosemede Avenue Kenilworth, Cape Town.

[3] The Second Respondent is Johnsure Investments CC a close corporation registered in terms of South African Law, with its principal place of business at 1 Rosmere Centre, 67 Rosemede Avenue Kenilworth, Cape Town. At all times material hereto the First Respondent dealt with the Complainant. In this determination a reference to Respondent is a reference to the First Respondent.

B. INTRODUCTION

[4] It is now a well published fact that a property syndication scheme, Blue Zone Property Investments Pty Ltd, generally known as "Blue Zone", collapsed and investors believe that they have lost their money.

[5] On the 04th March 2009, the Financial Services Board ("the FSB") released an Inspection Report on the activities of Blue Zone Property

Investments (PTY) Ltd, Blue Dot Properties 1330 (Pty) Ltd, and Spitskop Village Limited.

[6] The report provides a helpful background to the various property syndication schemes that were run by Blue Zone Investments.

[7] The complaint relates to the role of the representative who rendered financial services in relation to the Blue Zone products to members of the public.

C. FACTUAL BAKGROUND

[8] This determination concerns the property syndication known as the Spitskop Village Properties Ltd ("the Spitskop Project"). The syndication was promoted by Blue Zone. In terms of the paperwork, investment was solicited from members of the public to raise an amount of R425 million to fund the Spitskop Project. The project entailed the development of housing intended to be sold to members of the public and in particular to people involved in mining in the immediate area.

[9] On 17 October 2005, Blue Zone was granted a licence to act as an authorised Financial Services Provider (FSP number 21227) in terms of section 8 of the FAIS Act with effect from 27 September 2005. In terms of the licence, Blue Zone is authorised as a Category 1 Financial

Services Provider to render advisory and intermediary services with regard to Securities and Instruments (category 1.8.of the licence application form).

[10] On 16 August 2006, Blue Zone applied for an amendment to its licence to also render advisory and intermediary services with regard to Securities and Instruments: Debentures and Securitized Debt (category 1.10). On 24th October 2008, the FSB granted the amendment. Blue Zone nevertheless started marketing their investment in 2006. On the 17th September 2009, the Registrar withdrew the Blue Zone licence.

[11] The Registrar's records indicate that Blue Zone had a list of about 482 representatives, and its key individual was Mr. J.J van Zyl.

[12] Loubser Du Plessis Inc ("LDP Inc") were the external auditors of Blue Zone.

[13] The Blue Zone Group consisted of Blue Zone, Blue Dot Properties, and Spitskop Village project. The directors of Spitskop, Blue Dot and Blue Zone are the same. The two directors who feature prominently

throughout the various entities are Mr Jacob Johannes van Zyl and Hendrik Christoffel Lambrecht.

[14] The Complainant invested an amount of R100 000.00, which represented a substantial portion of his life savings. According to the complainant, he and his elderly wife were dependent on these funds in their retirement.

[15] The Complaint's wife invested an amount of R250 000 through the Respondents in Sharemax, which complaint is being processed by this Office.

D. THE COMPLAINT

[16] The Complainant states that on or about January 2007 he and his wife approached the Respondent with R 350 000-00 that they wanted to invest. This was their lifesavings and they wanted it invested in a secure investment that would provide a monthly income.

[17] On the 30th January 2007 the Complainant, through the Respondent, invested R 250 000-00 into Sharemax in the Complainant's wife's name. The Respondent then invested the further R100 000-00 in

Spitskop Village Properties Limited in Mpumalanga through the Blue Zone Group, and this was in the Complainant's name.

[18] On the 17th January 2007, the Respondent conducted a Risk profile which indicated that the Complainant and his wife needed to invest in a 'moderately conservative' portfolio. Later in this determination, I deal at some length with 'risk profiling' of the complainants, and in particular, the implications of the results of the Complainant's 'risk profile'.

[19] The Complainant asserts that after investing his R 100 000-00 into the Spitskop scheme, he only received correspondence from Blue zone, but did not receive any information from the Respondent updating him on his investment.

[20] On the 10th October 2007, the Complainant received a letter from Blue Zone that was addressed to all investors. The letter advised that certain investors were starting to question the 'legality' of Spitskop's Steelpoort project. When the Complainant approached the Respondent and told him about his own concerns about the controversy surrounding the Spitskop scheme, the Respondent assured him that his investment was sound.

[21] On the 10th November 2008 the Complainant received a letter from the South African Police stating that Blue Zone Property (Pty) Ltd was involved in the contravention of a number of laws, including, the South African Reserve Banks Act; Intermediary Service Act; Unfair Business Practices Act; Restitution of Lands Act; and the Companies Act.

[22] On the 12th of December 2008, a month after receiving the letter from the South African Police, the Complainant received another letter from Blue Zone stating that the investors should ignore the concerns expressed in the South African Police's letter.

[23] In his complaint, the Complainant contends that although the warning bells started ringing as far back as 2007, the Respondent did nothing to advise him about the viability of the Spitskop Village scheme.

[24] The other aspect of the Complainant's complaint relates to what he calls the Respondent's failure to invest his money in accordance with the outcome of the Risk Profile that was conducted when he took the initial investment on the 17th January 2007. In that regard, the Complainant submits that the Respondent was negligent in advising him to invest his money in a risky investment even though it was clear from the results of the Risk profile that he was a 'moderately conservative' investor.

[25] The Complainant then points out in his complaint that the Disclosure documents of Spitskop Village made it clear that the shares in property syndication investment are unlisted and should therefore be considered as a risky investment. What lies at the heart of the Complainant's complaint is the allegation that the Respondent failed to exercise the necessary care and skill to ensure that he properly advised him to invest according to his risk profile and circumstances.

[26] The Complainant states that even when it became clear that Spitskop Village was heading for liquidation, the Respondent failed to contact him and properly advise as to the necessary steps that could be taken. On that score, the Complainant mentions that he made numerous requests to the Respondent asking him to sell his shares in Spitskop Village. These pleas, so the Complainant asserts, fell on deaf ears.

[27] The Complainant is an elderly man. He required the assistance of his daughter Nicki Conradie in contacting the Respondent, as well as in the proper formulation of the present complaint. Correspondence was exchanged between the Complainant, assisted by his daughter, and the Respondent. At about the same time, there were meetings between the Complainant, his family and the Respondent. However these efforts failed to yield any positive results. The Complainant's daughter took an active role in assisting the Complainant. The implication is that the

Respondent was reticent and did not assist the Complainant as best he could.

[28] As a result of the Respondent's failure to exercise due care and skill of a professional he held himself out to be, so the complaint goes, the Respondent lost his investment which was worth R 100 000-00.

[29] The Complainant referred the present complaint to this Office, after the parties could not resolve the matter.

E. THE RESPONSE

[30] On the 05th of August 2010, the Respondent issued a statement in which he sought to answer the Complainant's allegations. At this stage, it is convenient to deal with the response:

[31] The Respondent states that the Complainant was referred to him by a long standing client as someone who needed guidance in investing the proceeds of the sale of an immovable property.

[32] At their first meeting, the Respondent was introduced to the Complainant who was in the company of his wife. It was at that meeting that the Respondent introduced himself and gave the Complainant a detailed

background of his experience together with the Letter of Introduction. Later, in this determination, I deal at some length with the Respondent's qualifications and his letter of introduction.

[33] The Complainant and his wife needed additional income to supplement their pension income. The Respondent then conducted a risk profile on the Complainant. As mentioned above, the results of the risk profile indicated that the Complainant was a moderately conservative investor. The Complainant's subsequent answers revealed that he would prefer an investment in commercial properties, and that his final goal was to receive an income generated from his investments. According to the Respondent, the Complainant further informed him that he did not intend preserving his assets, but that he was keen to experience an annual steady growth.

[34] The Respondent further states that after explaining all the avenues of the investment, the Complainant chose to invest in unlisted commercial properties. The Respondent then mentions that he informed the Complainant that as an Independent Financial Services Broker, he had "broker contracts with various Companies and was in discussions with some others when dealing in investments with unlisted shares". In that regard, the Respondent refers to his letter of introduction. As already stated, I deal with this aspect later in this determination.

[35] The Respondent denies that he failed to send any correspondence to the Complainant. In that regard, the Respondent refers to the written correspondence which acknowledges the Complainant's investment which also contained information on shares. He further notes that in subsequent meetings he held with the Complainant and his daughter, the Complainant admitted to have been furnished with what he calls "a full set of Information Disclosure documents" from Blue Zone.

[36] As further proof of communication between himself and the Complainant, the Respondent provides several dates on which he says he had verbal conversations with the Complainant.

[37] The Respondent confirms that various meetings were held between himself and the Complainant who was in the company of his wife and daughter. The Respondent asserts that he gave the Complainant proper and professional advice.

[38] The Respondent further asserts that he was of the view that the Spitskop Village investment was sound and had every reason to succeed. He then submits that although the Spitskop Village investment was a risky investment, in his assessment the risk would have been between low and medium risk. The Respondent bases this assessment on correspondence to investors and brokers from Blue Zone itself. In particular, the Respondent refers to two letters, one signed by Mr. J.J

van Zyl, and another by Mr Lamprecht, both of whom were Blue Zone Directors.

[39] The Respondent also denies the Complainant's allegations that he received a lot of negative correspondence from Blue Zone. He further denies that Complainant asked him to sell his shares in Spitskop Village. In that regard, the Respondent states further that the Complainant may be confusing the request to sell shares in Spitskop Village with instructions to sell shares held by his wife in Sharemax's Athlone Park.

[40] The Respondent states that at the time the Complainant bought the shares, all indications were that the Spitskop Village scheme seemed set for success.

[41] The Respondent states that he could not possibly sell the Complainant's shares as at that time Blue Zone was already running into difficulties.

[42] As regards the South African police letter referred to by the Complainant, the Respondent dismisses the allegations as emotional and lacking in substance and not based on facts. The same holds true for the questions surrounding the legitimacy of the Spitskop Village investment. In this connection, the response is instructive. He states that, "To us as marketers/Brokers we could only determine the Risk by the Disclosure documents and the fact that it had been scrutinised by the Compliance

officers, Legal team and the Department of Trade and Industry". Similarly, the First Respondent relies on the letter and professional opinion sent out by Mr. J.J van Zyl. In the letter referred to by the Respondent, van Zyl advises the investors to simply ignore the concerns and the allegations raised in the South African Police's letter.

[43] In essence, in his response, the First Respondent submits that there is no merit in Complainant's Complaint against him.

F. THE ISSUES

[44] There are two crisp issues for determination:

44.1 Whether the respondent rendered the financial service herein negligently and/ or in a manner which is not compliant with the FAIS Act;

44.2 If it is found that the respondent did render the financial service negligently and/or failed to comply with the FAIS Act, whether such failure caused the complainant's loss.

[45] To do justice to the many and varied contraventions of the FAIS Act and the Code would be voluminous. As such, and in the interest of brevity, I confine myself in this determination to some of the more pertinent breaches.

G. THE LAW

The FAIS Act:

[46] It is convenient to sketch out the applicable provisions of the FAIS Act and General Code of Conduct which are relevant in the present matter.

[47] Section 7 of the FAIS Act provides the following:

> **7. Authorisation of financial services providers**
>
> (1) With effect from a date determined by the Minister by notice in the *Gazette*, a person may not act or offer to act as a financial services provider unless such person has been issued with a licence under section 8.

[48] Section 8 of the Act deals with the authorization of Financial Services Providers.

[49] Section 1 of Part I of the General Code of Conduct for Authorised Financial Services Providers ("the Code")[1], defines a 'provider' as an authorised services provider, and includes a representative.

[50] Section 2, of Part II of the General Code provides as follows:

'A provider must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interests of clients and the integrity of the financial services industry'.

[51] The specific duties of a provider as spelt out in section 3 of the General Code are apposite to the facts of this matter.

[52] Section 3 of the Code requires that when a provider renders a financial service:

(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,

[1] Published under BN 80 in GG 25299 of 8 August 2003

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;

[53] Section 8 (1) (a) of the Code provides that a provider 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.

[54] In *Durr v ABSA Bank LTD and Another 1997 (3) SA 448 (SCA)* the Supreme Court of Appeal had occasion to consider the duties of a broker. At 463 the following is instructive:

"The important issue is that even if the advisor himself does not have the personal competence to make the enquiries, I believe it is incumbent upon him to harness whatever resources are available to him or if necessary to ask for professional, legal or accounting opinion before committing his client's funds to such an investment".

[55] The First Respondent held himself out as an expert who was able to advise clients on various products including investments of different kinds. However, it is clear from his letter of introduction that the First Respondent was not qualified to render financial services in unlisted securities. As, already mentioned, the First Respondent shied away from clearly telling the Complainant that his experience in unlisted securities was extremely limited.

[56] The fact remains though that the First Respondent held himself out as a highly experienced representative who sold the products mentioned in his letter of introduction. Therefore, the Complainant was entitled to hold the Respondent to the standards of a highly experienced and qualified representative who professed the investment skills of an expert. At the very least the Complainant was entitled to assume that the Respondent would act according to the standard as contemplated in section 8 of the Code, and as reinforced by section 2 Part II of the Code. I am fortified in my view by the fact that nowhere in his response does the Respondent state that he did not understand the product or investment he sold to the Complainant. However, the objective facts indicate that the Respondent

was out of his depth in his understanding of the Spitskop investment. As stated above, the Respondent did not conduct any objective analysis or assessment of the Spitskop investment. He merely relied on the promotional material produced by Blue Zone themselves.

[57] In this regard, I refer to the determination in the matter between Dudley and Leisure Financial Services CC case number FOC 04114/08/09WC 1.

[58] There was a duty on the Respondent to conduct a check on the Blue Zone Investment scheme and its related entities. This he could have done by going through the relevant documents which would have shed light on the liquidity of the Companies. There is no indication that the First Respondent sought to establish whether any of the Blue Zone entities had issued any financial statements. Had the First Respondent checked, he would have established that Blue Zone did not own any assets of value except the piece of land it had purchased through a sister company for R 1 057 000. That should, on its own, have raised a concern in the mind of the First Respondent as to how the investors' debentures, in a subscription worth 425 million rand, could be secured. This information was readily available in the Disclosure documents.

[59] The inescapable conclusion is that the First Respondent did not read the disclosure documents. If he did, then he clearly did not understand them.

[60] Respondent suggested in his response that the rumours and newspaper reports about the legality of the Spitskop project could not be relied upon by professionals of his calibre. The Respondent might have been correct in that assertion. However, instead of verifying the correctness of these allegations by conducting an independent and objective assessment of the Spitskop project, the Respondent was content with the information from the implicated Blue Zone directors.

[61] What is clear is the fact that the First Respondent was not properly qualified to render advice on unlisted property investments. In this connection, the words of Schutz JA in the above-mentioned *Durr matter* are apposite. At 466, his lordship sounded the following timely warning:

> *"One of the first requirements of a professional is to know when he may be getting out of his depth, so that I do not think that that is a sufficient excuse. I am not able to say exactly what Stuart should have done. But I would suggest that there was a point at which he should have walked down the passage or across the street, or lifted the telephone, or activated the fax, and said to a lawyer, or accountant, or banker, none of which he was, in the employ of ABSA something like this: 'Look, I have been introduced to some attractive debentures (preference shares) in a group called Supreme. Would you please tell me quite what debentures (preference shares) are,*

and how secure they are. And also, please tell me how I find out who and what Supreme is and what risk attaches to investing in it."

[62] The First Respondent did not bother to conduct even the most basic investigation on Blue Zone. He appeared blissfully ignorant as to his duties in terms of the FAIS Act, as a representative. The First Respondent's conduct borders on gross dereliction of his duties as a representative, and shows negligence on his part.

[63] Similarly, at 468, the words of the learned judge of appeal on what constitutes negligence are instructive. The learned judge pertinently stated the following:

> "I come towards my conclusion on the subject of negligence. The basic rule is stated by Joubert (ed) The Law of South Africa First Reissue vol 8.1 para 94, as follows:
>
> 'The reasonable person has no special skills and lack of skill or knowledge is not per se negligence. It is, however, negligent to engage voluntarily in any potentially dangerous activity unless one has the skill and knowledge usually associated with the proper discharge of the duties connected with such an activity.'

[64] The FAIS Act clearly expects of providers who hold themselves out as experts in the products they sell to act with knowledge and skill they purport to have. In this matter, the Complainant was entitled to rely on the expert advice of the First Respondent as to the viability of the Spitskop investment.

[65] The facts of the present matter illustrate the importance of strict compliance with the provisions of the FAIS Act and Code by the FSP when dealing with clients. Almost all of the complaints that have come before this Office indicate that a substantial number of customers/clients are lay people in investments and insurance policies. The clients therefore are always entirely dependent on their brokers for sound advice.

H. LICENCING

[66] Since the inception of this Office we have dealt with complaints from members of the public who invested their monies in various failed investment schemes.

[67] These schemes include property syndications, bridging finance, forex, property development and various so-called ponzi or pyramid schemes. Unsuspecting South Africans have lost millions of Rand to the perpetrators of these sham investments.

[68] From experience all of these failed schemes have the following features:

68.1 Most of the schemes market the investment through independent Financial Services Providers (FSPs), most of whom are engaged as representatives in terms of section 13 of the FAIS Act. The promoters of these schemes usually apply for a licence with the FSB and thereafter engage independent FSPs in terms of Section 13 of the FAIS Act.

68.2 Having obtained a licence from the FSB and even in instances where they have been refused such licence, the providers/promoters then merely produce documentation which provides prima facie proof that the Intermediary was appointed as a representative and that the provisions of section 13 were complied with. I find that in fact there was no actual compliance on the part of these providers/promoters. In most cases, they certainly did not comply as contemplated in section 13, but merely paid lip service to the provisions of the Act.

68.3 The representatives in these investment schemes were offered and paid lucrative commissions. The commissions were paid immediately and unconditionally upon the making of the investment. The commission was

not subject to any claw back provisions. Needless to say, this created enormous incentives for the intermediary to aggressively market the investment to members of the public.

68.4 The intermediaries held themselves out to the public as licensed to sell the particular products, thus winning over the confidence of the unsuspecting public.

68.5 In most instances, after the scheme fails and after investors lose their money, the representatives often claim to have rendered financial services on behalf of their principals, and that therefore they cannot be held liable. They conveniently hide behind the promoters of the schemes.

68.6 Key to all of these schemes is the availability of a network of intermediaries to the promoters. Without the intermediaries the promoters of these sham investment schemes will not be able to mobilise and exploit the resources of the public. To put it plainly, these schemes will not be viable in the absence of a network of intermediaries.

[69] In this regard it is instructive to consider the applicable legislation. Of significance is the fact that section 13 has undergone material amendments. In particular, section 13(2)(a) read as follows:

> *"(2) an authorised financial services provider must-*
>
> *(a) at all times be satisfied that the provider 's representatives, and key individuals of such representatives, are , when rendering a financial service on behalf of the provider, competent to act,* ***taking into consideration requirements similar to those contemplated*** *in paragraphs (a) and (b) of section 8(1) and subsection (1) (b) (ii) of this section, where applicable (my emphasis); and*
>
> *(b) 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."*

[70] This section has been the subject of abuse. Unscrupulous promoters of investments merely used the section to market their toxic investments through a network of representatives who were not licensed and properly qualified to advise members of the public. There are many instances in respect of which the providers and promoters of these schemes merely paid lip service and failed to observe the requirements of section 13. It could not have been contemplated that the section would create two classes of representatives, those licensed in their own right and those

who are unlicensed but give advice and sell investments as section 13 representatives. What was contemplated was for licensed FSPs and those appointed in terms of section 13 be subject to the same high standards of competence and ethical conduct.

[71] On the wording of the section it lends itself to a wide interpretation, whereby people are appointed as representatives very easily. The present case is in point where Blue Zone appointed, according to their records, 580 representatives in terms of section 13. The Act did not call for strict compliance with the requirements as contemplated in section 8(1) (a) and (b) of the Act, but required mere compliance or substantial compliance. Such compliance being left entirely in the hands of the provider.

[72] Clearly, there was a need to address the problem, this came in the form of an amendment published in section 52 (b) of Act 22 of 2008.

[73] The legislature removed or deleted the words "**taking into consideration requirements similar to those contemplated**". This represents the much needed tightening of the legislation. It no longer provides scope for an expansive or liberal interpretation.

[74] In appointing representatives, FSP's must comply strictly with the provisions of section 8(1) (a) and (b). There is an onus on the FSP to

ensure that the representative meets the standards of fit and proper person as contemplated in section 8. It means that:

74.1 The FSP must ensure that the representative meets the requirements of competence and has necessary skills as contemplated in the provisions of the Act.

74.2 There is an onus on the representative to ensure that he or she gets the correct and necessary training and that he or she is satisfied that they have the competence and ability to serve members of the public.

74.3 There is a reciprocal duty on both the FSP and representative to ensure that the provisions of section 13 are met.

74.4 In respect of both pre and post amendment requirements of section 13 of the FAIS Act, it is clear that it was never intended that two separate standards should apply, namely; one for licensed FSPs and another for section 13 representatives.

74.5 Upon a proper interpretation of section 13, read in the context of the FAIS Act as a whole, both FSP and representative are subject to the same standards of

competence as contemplated in sections 7 and 8 of the Act.

74.6 The Act, as amended, now requires stricter regulation of the appointment and supervision of section 13 representatives.

[75] It must be made known to all representatives of FSPs that they will be held personally responsible if they recklessly or negligently market meaningless investments to their clients. If there is meaningful deterrence then the scam promoters will suddenly find that they no longer have a network of representatives that they can exploit. I believe that the current legislative framework provides adequate regulation if the FAIS Act is applied more strictly.

[76] In that regard, the Blue Zone debacle is a very good example and a case in point. According to the records of the FSB, Blue Zone utilised the services of no less than 482 (four hundred and eighty two) representative FSPs. This is indeed a startling figure. How Blue Zone could possibly address the question of competence and training in respect of this number of people in terms of section 13 of the Act is beyond comprehension. Blue Zone as a financial institution had no infrastructure, nor the capacity to train and supervise as many as 482 representatives. As I will show in this determination, the First

Respondent in this case, being one such Representative, received no training at all in respect of the Blue Zone investment he sold.

[77] Blue Zone purported to comply with the provisions of section 13 and even claims to have trained the representatives, some of whom according to Blue Zone, had to attend competency examinations. The irony is that at the time when Blue Zone started marketing the investment through these representatives, they were themselves not licensed to market the debentures.

[78] Blue Zone had a Category 1.8 license when in fact they required Category 1.10. When they appointed representatives and started marketing, their application for Category 1.10 licence was still pending. In fact, according to the FSB records they were granted the Category 1.10 licence only in October 2008. Blue Zone purported to train their representatives when they were in fact contravening section 7 of the FAIS Act.

[79] Equally, one has to question the conduct of the individual representatives themselves. A basic and simple enquiry at the FSB would have revealed that Blue Zone was not licensed to deal in Debentures and securitised debt. It appears that none of these representatives, including the Respondents, took the trouble to find out. If they did, they would have realised that Blue Zone in appointing them in

terms of section 13 was acting contrary to the provisions of the Act. The resultant financial chaos and loss to members of the public is now a historical fact.

[80] In this regard the certificate issued by Blue Zone to the Second Respondent is instructive. The certificate, duly signed by Blue Zone, records as follows:

"JOHNSURE INVESTMENTS CC T/A FINANCIAL HUB

is competent and authorised to render financial advice and intermediary services on the following of products of Bluezone Property Investments (Pty) Ltd,

Category 1/8/A/B

Being advice and intermediary services on the marketing and selling of unlisted shares in a private or public company."

(Quoted as is)

The significance of this is that the Respondents were authorized to sell category 1.8/A/B which means that they were not authorized to market debentures for which one requires a 1.10 licence. It was patently clear to the Respondents that they were not allowed to market the Blue Zone investment. The Respondents as well as Blue Zone acted in breach of the FAIS Act.

[81] Section 13 of the FAIS Act deals with the qualifications of representatives as well as the duties of authorized FSPs. Before delving into the significance of the provisions of section 13 of the Act, I consider it important to sketch out the rationale behind the provisions of section 13 of the Act.

[82] In broad terms, the rationale behind the licensing provisions as contemplated in sections 7 and 8 of the Act could be divided into two parts:

(a) First, to ensure that the provisions of the Act are complied with;

(b) Secondly, to protect members of the public and strengthen the integrity of the financial services industry.

[83] When an FSP is licensed, it conveys to members of the public that the regulating authority has satisfied itself that the FSP is qualified to render the necessary service. Once the FSP holds himself or herself out to the public as a qualified adviser, it then follows that members of the public may safely rely on the provider's services.

[84] There appears to be a legal loophole which exposes members of the public to the risk of dealing with unlicensed FSPs. These unlicensed

FSPs are let loose on unsuspecting members of the public. Significantly, this occurs ostensibly under the provisions of section 13 of the Act. What is more, judging by the number of complaints which have come before this Office, it appears that, more often than not, FSPs observe the provisions of section 13 only in their breach.

[85] As the facts of this case amply demonstrate, an undesirable practise appears to have taken hold. In terms of this practise, the perpetrators of scam investments make use of unqualified brokers in the marketing of their products. Below, I deal at some length with the practice of using unlicensed brokers.

[86] Section 13 deals with the qualifications of representatives and the duties and obligations of licensed providers. In terms of section 13 (b) no person may act as a representative financial services provider, unless such person is (1) able to provide confirmation, certified by the provider, to clients that "(a) that a service contract or other mandate, to represent the provider exists"; and that "(b) the provider accepts responsibility for those activities of the representative are performed within the course and scope of, or in the course of implementing any such other contract or mandate".

[87] The section places an obligation on the provider to ensure that the Representative complies with the requirements of fit and proper as contemplated in section 8 of the Act. Similarly, there is a duty on the provider to ensure that the representative has the necessary knowledge and training to market the product.

[88] Whilst section 13 does not specifically refer to the duties and obligations of representatives, the Act and the code clearly makes the representative equally responsible to satisfy himself as well, that he has a full and proper understanding of the provider's product and that it is an economically viable one, and further that he is qualified and competent to market it.

[89] Moreover, there is an obligation on the representative that if he does not understand the product, he cannot render financial service in relation to that product to members of the public. This is so because the representative must have the capacity and operational ability to market the product.

[90] It must have been contemplated in the Act that such a duty, as set out above, must be attributed to the representative. That being the case, the representative must be held responsible for marketing the product and cannot hide behind their status as mere representatives. If this is not the case, then clearly there is no incentive for representatives not to act recklessly.

[91] The danger of making use of unqualified representatives is illustrated by the facts of the present matter.

[92] From the complaints received by this Office, it is clear that the independent representatives marketed Blue Zone after being attracted by the lucrative commissions on offer. The respondents were paid a commission of 6% of the invested amount.

[93] This determination should serve as a warning to representatives that if they fail to comply with the provisions of the Act and General Code they will be marketing those products at their peril, and they will be held responsible. To put it plainly, the attraction of quick profit may well result in permanent financial ruin.

I. *COMPLAINANT'S RISK PROFILE*

[94] It is common cause that the Respondent did a risk profile of the Complainant. Accordingly, it is appropriate to examine the manner in which the Complainant's risk analysis was conducted so as to determine whether such 'analysis' was done properly.

[95] As already stated, the Complainant asserts that the Respondents' decision to invest his money into the Spitskop Village Investment was at variance with the results of the risk analysis. It bears repeating that the results of the risk analysis identified the Complainant as a 'moderately conservative investor'. In that connection, First Respondent requested the Complainant to complete a standard questionnaire.

[96] Significantly, First Respondent was expected to apply his mind to the results of the questionnaire. He was then expected to recommend investments that are consistent with the client's risk profile. The First Respondent merely went through the motions when he purported to be conducting the risk analysis. The First Respondent's intention from the onset was to sell the Complainant Blue Zone's investments, regardless of the outcome of the risk analysis.

[97] The respondent's conduct is in conflict with the General Code which places an obligation on the representative to identify the financial product consistent with the client's circumstances and act within the scope of his client's mandate.

[98] In his response, the First Respondent states that he acted independently and "explained all the avenues of Investment including Unit Trusts, Bank deposits, Government Retail Bonds, Five year Insurers

Income plans and Commercial property Investments both listed and unlisted". The Respondent further states that once he had given all this explanation, the Complainant chose to invest in unlisted Commercial properties. The First Respondent does not explain why an investor whose risk analysis indicated that he was a moderately conservative investor would choose to invest in a high risk investment in unlisted commercial properties. Similarly, the First Respondent does not indicate why he disregarded the outcome of the risk analysis.

[99] The First Respondent had an obligation to explain the risks involved in the Blue Zone scheme. He had a duty to specifically point out to the Complainant, the downside of investing in unlisted properties. Strangely, there is no record reflecting the Respondents' advice on the risks involved in the Blue Zone scheme. In that regard, a case in point which sets out the applicable principles is the determination in *Dudley v Lifesure Financial Services CC*[2].

[100] The Complainant is a lay person who has no in-depth understanding of commercial transactions, including investments. He relied entirely on the information he obtained from the Respondent. The Complainant's answers furnished in the risk analysis indicate that he was inclined to invest in a low risk investment. On the documents furnished, as well as the risk analysis, there does not appear any factual basis to justify the

[2] Bernard Frederick Dudley Case No FOC 04/114/08/09 WC 1

Respondent's assertion that the Complainant wanted to invest in unlisted commercial properties. On the contrary, the objective evidence as appearing in the risk profile analysis indicates that the Complainant, as a moderately conservative investor, would have opted for a low risk investment.

[101] What is more, the Complainant is a pensioner who even had to be assisted by his daughter to lodge the present complaint. It is not clear how he would have objectively assessed the merits of various types of investments, and then decide on investing in high risk unlisted shares and debentures. Judging by the answers that the Complainant supplied in the questionnaire, if properly advised, the Complainant would have preferred investing in a low risk investment. Caution should have been exercised as the complainant, being a pensioner will have no more access to capital.

[102] The question arises as to what significance should one attach to the results of a risk analysis? That the Respondent patently failed to properly advise the Complainant, is clear.

[103] The risk analysis document describes moderately conservative investors as "investors who want to protect their capital, and achieve some real increase in the value of their investments." The mind boggles at how

advising the Complainant to invest in unlisted commercial properties accorded with the results of the risk analysis.

[104] It is clear that the Respondent disregarded the significance of the results of the risk analysis. He merely went through the motions.

[105] Once a broker presents himself as an expert to the public, members of the public have no objective means of verifying the veracity of the claim.

[106] In the Respondent's "letter of Introduction and Disclosures", the Respondent does not say anything about having received training in terms of section 13 of the Act.

[107] As an authorised FSP, Blue Zone (the Respondent) has a duty to comply with the provisions of section 13 of the Act. Before he accepts an appointment as an authorised representative, the Respondent has an obligation to ensure that he receives proper training in order to market the product responsibly.

[108] The Complainant contends that he was not properly advised by the First Respondent, an allegation which is rejected by the First Respondent. However, there is, no indication that the First Respondent conducted

proper due diligence to satisfy himself of the suitability and the viability of Blue Zone's Spitskop Village Investment scheme.

J. RESPONDENT'S LETTER TO THE COMPLAINANT DATED 25th JANUARY 2007

[109] The letter, dated 25th January 2007, written by the Respondent to the Complainant merits some consideration. The letter reads as follows:

"25th January 2007

Dear Mr.& Mrs Gerald & Violet Black

408 Oakdale

66 Main Road

PLUMSTEAD

7800

RE: Your recent Applications for Investments-

Sharemax-Athlone Centre & Blue Zone Steelpoort

Firstly let me say thank you in entrusting this part of your Financial planning to me. Not only is this step mutually beneficial but it gives me a great sense of satisfaction in knowing that there are those who have felt comfortable in entrusting their financial affairs to my care.

Allow me just to summarize the salient points of this Investment to refresh your memory.

1. *The Athlone Centre is situated in the very busy city of Amanzimtoti in KwaZulu Natal. This center is of particular interest as it has just been totally re-vamped inside and out and upgraded to double in size from the original that was built 10 years ago. Pick 'n Pay have just signed a 10 year lease which shows tremendous confidence in the project. I am sure that your investment will achieve great results. Blue Zone's Steelpoort project is way ahead of schedule and again this will prove to be a winner.*

2. *You have an investment amount of R 250 000.00 in the Athlone Park shopping center and R 100 000 in Blue Zone's Steelpoort development.*

3. *As you know Income starts at a guaranteed 9.% pa and 9.5% respectively for the first year and thereafter, will increase on an Annual basis.*

4. *Your Capital should also show a profit over the years to come once, of course, the costs have all been recovered by Sharemax Investments (Pty) Ltd. And Blue Zone Investments (Pty) Ltd.*

5. *Should you wish to sell your shares in the Athlone Park Centre it can be done in one of two ways:*

   a. *By requesting Sharemax to place your shares on the market and sell them through their network (which will cost a selling fee of about 7% of the capital value) or*

   b. *By selling them privately yourself. There would be a fee of R 250.00 for the re-registration of the share certificate in that instance.*

   c. *I could also find a buyer for you at a reduced selling fee than Sharemax's 7%*

   In addition a R 250.00 re-registration fee would be recovered from the new owner.

   The Blue Zone's Steelpoort project as you know is a 3 year term after which you will have the option of taking your Investment or re-investing it into Phase 2 or another project.

   Your Documents will soon be issued and will be sent to you directly. You will be receiving them shortly.

Should you have any questions regarding your Income or the points outlined above please do not hesitate to call me and I shall be very happy to answer any questions you may have.

Once again I would like to thank you for your support.

Sincerely

(signed)

John A Moore

Authorised Financial Service Provider

Licence # 10014"

[110] The letter contains some worrying aspects in regard to the quality of advice that the First Respondent gave to the Complainant. The letter purports to "summarize the salient points" of the investment. Of particular concern, the First Respondent specifically informs the Complainant that the "Blue Zone's Steelpoort project is way ahead of schedule and again this will prove to be a winner."

[111] In reality, the assertion in the letter that the Blue Zone project was ahead of schedule was factually inaccurate. In fact, an inspection by the Financial Services Board found that no development work was ever undertaken in the Spitskop's Steelpoort project. Had the Respondent

bothered to conduct a basic and elementary due diligence, he would have realised that the statement about the Steelpoort project being ahead of schedule as contained in his letter was untrue and misleading.

[112] The optimism of the letter was not borne out by the objective reality which prevailed, which was that the project had not got off the ground. Had the First Respondent conducted a simple enquiry, he would have established the correct state of affairs. Regrettably, the First Respondent relied entirely on the glossy marketing material furnished to him by Blue Zone. Needless to say, as already pointed out above, the glossy material of Blue Zone contained many misleading assertions. The marketing material used by promoters requires skilled analysis in order to appreciate the viability or otherwise of the investment scheme. Ordinary members of the public do not possess these skills and rely on the advice of their broker.

[113] The letter of the 25th January 2007 simply regurgitates the promotional material by the marketing section of Blue Zone. There is no objective analysis of the proposed investments. The proposed schemes are not subjected to any critical assessment. There is no mention of the possible risks that are attendant to the investments. In the letter, the First Respondent seems to be entirely optimistic about the future success of the scheme, without setting out any factual basis for such optimism.

[114] One would have expected the First Respondent to have sounded some caution on the future prospects of the Spitskop Investment. Quite the contrary, the Respondent does not express the slightest concern about the volatility of the investment the Complainant had just taken. At worse, it is safe to state that the conduct of the First Respondent was negligent and possibly naive. The First Respondent had an obligation to advise the Complainant to invest in accordance with the outcome of the risk profile analysis.

K. LETTER OF INTRODUCTION AND DISCLOSURES

[115] The First Respondent's letter of Introduction and Disclosures which was shown to the Complainant during their initial consultation also warrants some comment. The letter purports to be in compliance with the FAIS legislation, and in it, the First Respondent sets out his qualifications.

[116] After stating his names the First Respondent proceeds to mention the following:

> *"A copy of the licence, which contains details of the financial services I am authorised to provide, as well as any exemptions, is available for inspection on request and is displayed in my offices."*

[117] It is not clear why the Respondents would not readily supply the Complainant with a copy of their license. It is desirable for brokers/representatives to furnish their clients with copies of their licences. This would enable clients to objectively verify the qualifications of the representatives. Since most clients who are in the same position as the Complainant are lay men, they could conceivably enquire from independent sources who can explain to them any shortcomings in the broker's qualifications. In the present matter, the letter of introduction asserts that the First Respondent is duly qualified. Yet, a careful reading of the letter reveals that the Respondent was not qualified to sell, market, or deal in unlisted shares and debentures.

[118] The letter of introduction then proceeds to mention that the First Respondent has been providing financial advice and intermediary services since June 1978 in the areas of financial planning in Life Insurance and Disability Planning, Investments Planning.

[119] As regards the Respondents' licence in marketing unlisted shares and debentures, the letter merely sets out that the Respondents' brokerage has written authority to market the products of reputable Life Companies. This list of old and reputable companies would no doubt have alleviated any concerns by any client about the Respondent's qualifications.

[120] The list of companies mentioned in the letter of introduction is indeed impressive. However, the letter proceeds to mention that the Respondents had written authority to market the investments in property syndication companies such as Sharemax Investments, Dividend Investments, and in Blue Zone Investments.

[121] As regards his authority and license to market the investments in the mentioned property syndication companies, the Respondent then indicates by means of a footnote the following:

> *"Any FSP who has applied for a Sect. 1.8 and Sect. 1.10 licence and has not had 3 years of experience in marketing of listed or unlisted shares as classified as a Representative under supervision for the remainder of the 3 year qualifying period. I am registered under their license and supervision until September 2007. Sharemax Supervision-Unlisted Securities SA-LICENSE#6152. Dividend Investments and Blue Zone Supervision-Sterling Compliance license#CO2"* (sic)

[122] I have quoted the cited paragraph from the letter verbatim. I have gone through the cited paragraph on several occasions, and it is still difficult for me to make out what it conveys. It seems to me that the paragraph is

lifted from the Act, and attempts to inform the reader that the First Respondent is not qualified and licensed to sell and market the unlisted shares. The passage is also supposed to inform the reader that the Respondent has less than three years experience in the selling and marketing of listed and unlisted shares. This would inevitably, include the dealing in Debentures.

[123] The cited passage is in technical legal language. One has to bear in mind that it is in respect of this cited passage that the Respondent was supposed to convey to the Complainant that he was not qualified to sell or market unlisted shares and debentures. Yet the important message and information is buried under the rubric of technical legal jargon. The impression created by the letter of introduction is that the Respondent is duly qualified to sell or market unlisted shares and debentures, when in fact the contrary is true. One surmises from the letter that the Respondent cannot deal in unlisted shares unless supervised. This would then ostensibly mean that the Respondent falls into the category of a Representative who is not licensed but is working under the supervision of a licensed Financial Services Provider as envisaged under the provisions of section 13 of the FAIS Act.

[124] The wording of the letter in respect of the Respondent's qualifications is vague and obscure. The letter does not expressly state that the Respondent is not qualified or licensed to market unlisted securities and

shares. By merely repeating the wording of the statute, which is in legal jargon, the Respondent failed to communicate in clear and simple language a material fact that could have influenced the Complainant's decision to invest in unlisted property.

[125] Worse still, in his response to the complaint made to this Office, the Respondent states the following:

> *"I explained to Mr. Black that as an Independent Financial Services Provider I had Broker contracts with various Companies and was in discussions with some others when dealing in investments with unlisted Shares. My letter of Introduction stated that I had signed contracts with Sharemax (Pty) Ltd, Blue Zone Investments (Pty) Ltd and Dividend Investments (Pty) Ltd."*

[126] It is clear from this response that the Respondent persists in holding himself out as qualified to deal in unlisted shares. This does nothing to disabuse the Complainant of his misapprehension that he was dealing with a highly qualified individual on whom he could pin all his hopes.

[127] Accordingly, the Respondent's failure to communicate the shortcomings in his qualifications in a clear and understandable language which might

have influenced the Complainant otherwise, was in breach of section 3 (1) (a) (ii) of the General Code of the FAIS Act.

[128] Similarly, as mentioned earlier, the Respondent does not set out the level of training he might have acquired which qualifies him to deal in unlisted shares, even if under supervision.

[129] In his response to the Complainant's allegation that his advice about the viability of the project was "contrary to the actual state of affairs", the Respondent further states the following:

> *"On Friday 19th October 2007 an article appeared in the Cape Times regarding Spitskop Property Development that was meant to allay fears that had been raised in the media."*

[130] The First Respondent then attaches the relevant document that appeared in the Cape Times. I have gone through the attached document, which apparently appeared on Friday, 19th October 2007 in the Cape Times. This document seems to be an advertorial as it bore the letterheads of Blue Zone Investments. Its entitled *"SPITSKOP PROPERTY DEVELOPMENT IS ON TRACK"*.

[131] In essence, the advertorial sought to allay the fears of investors, and informed them that the Spitskop investment scheme was commercially

and financially viable. It assured the investors that the scheme was safe and sound.

[132] The First Respondent did not bother to test the validity of these claims by Blue Zone. Had he conducted an objective and independent check, the Respondent would have realised that the claims contained in the Blue Zone's correspondence, including the advertorial in the Cape Times, were patently false. The objective evidence as appearing in the comprehensive findings of the Financial Services Board's inspection Report indicated that the project did not get off the ground. The findings of the Financial Services Board's Report were not contested by Blue Zone.

L. CONFLICT OF INTEREST

[133] Section 1 of the General Code of Conduct defines conflict of interest as:

> "Any situation in which a provider or a representative has an actual or potential interest that may, in rendering a financial service to a client, -

(a) influence the objective performance of his, her or its obligations to that client; or

(b) prevent a provider or representative from rendering an unbiased and fair financial service to that client, or from acting in the interests of that client,

Including; but not limited to -

(i) a financial interest;

(ii) an ownership interest;

(iii) any relationship with a third party".

[134] Although the definition was only inserted recently, the Act and Code nevertheless provided for a conflict of interest.

[135] The Code prohibits both actual and potential conflict of interest. The First Respondent received commission from Blue Zone. That in itself does not necessarily create any conflict of interest. The mere presence of financial interest is not prohibited by the Code. However, the representative has an obligation to disclose their financial interest.

[136] The Code enjoins the Representatives to make full and proper disclosure of their financial interest. It seems to me that what is contemplated by the Code is full and proper disclosure. This would entail mentioning to the client what the broker's commission in relation to the going rate for comparable investments in the industry is. It does not avail the broker to merely mention that he gets six (6) percent commission. However, there is an obligation to inform the client how this compares with the present industry's going rate. Thus for example, if the industry rate is three (3) percent, and the representative stands to gain six (6) percent commission, then the client is in a position to determine the broker's interest in marketing the product. However, it does not assist the client to merely mention that the broker's commission would be six percent. In addition, the intermediary is obliged to explain how the product provider intends to pay the commission. The client has to be placed in a position in which he is able to understand.

[137] In terms of Section 3 (1) (iii) The Respondent failed to identify the obvious flaws in the Investment scheme. A cursory reading of the Disclosure Documents that were sent to investors such as the Complainant reveals some worrying aspects. I mention that had the Respondent conducted a proper due diligence of the investment, he would have realised that the scheme was not commercially viable. In that regard, a glaring aspect concerns the fact that the debentures are

secured by land with an inflated value of R180 million and actual value of R1 057 000 – 00.

M. THE ROLE OF PROFESSIONALS

[138] Equally in all of these failed investments, that came through this Office we noticed another common factor. That is the use of professional people or professional practices in the process of establishing, promoting and selling the investments. These professionals include firms of accountants, attorneys, valuators and compliance officers. This is a case in point, where well established attorneys and accountants were used.

[139] The perpetrators use the names of these professionals and their practices to win the confidence of members of the public. It is these professionals that lend credibility to these schemes.

[140] The relevant professions are equally relied upon by regulators to carry out their functions professionally and independently. Unfortunately, the opposite appears to be true. The professionals either, wittingly and sometimes unwittingly become involved in the toxic scheme to the detriment of the investing public. The regulators, and other law enforcement agencies, rely on professionals to report suspicious and fraudulent transactions. These professionals, in particular, attorneys and

auditors, are public officials who have assumed the duty to report fraudulent conduct or potentially fraudulent conduct.

[141] Failure by professionals to report, or worse to become involved, results in serious consequences. Professional people are equally attracted by lucrative fees and are easily tempted into losing their independence.

[142] The most spectacular example of such failure, in recent times was the collapse of ENRON in the United States. There the accountants lost their independence and became key to defrauding investors and shareholders. This case is another good example. Professional valuators were used to blatantly inflate land values which were in turn used to swindle investors. I recommend, in respect of both the Accountants of Blue Zone and the Valuators, that their conduct be investigated by their respective regulatory bodies.

[143] Professionals must guard against being drawn into these fraudulent schemes. Those who lend their names and practices to these schemes will do so at their peril.

N. HONEY ATTORNEYS

[144] After the collapse of Blue Zone, the role of a firm of attorneys drew the attention of this office. This firm of attorneys, in documentation available to this Office, primarily drawn from complainants and the attorneys themselves, was generally referred to as Honey Attorneys, Honey and Partners, Honey Group and Honey & Partners (Johannesburg) Incorporated.

[145] Honey and Partners (Johannesburg) Inc were appointed as attorneys for the Blue Zone/Spitskop and were represented by Mr. H.E Van der Walt and G.S Goodes who are both directors/partners in the firm.

[146] In all Blue Zone documentation in our possession, there appears reference to Honey and Partners and/or Honey Attorneys. The Blue Zone documentation refers to Honey and Partners as part of the professional team to facilitate the investments processes. In the Blue Zone Disclosure Documents Honey and Partners is described as follows:

"Honey and Partners-this well established law firm was founded in 1962 and now has offices country wide. They will be acting as the transferring attorneys and will be in charge of all legal matters".

[147] As pointed out, one of the master minds behind the Blue Zone scheme was a director Mr. J.J van Zyl. Of significance is that JJ van Zyl was also

a director/partner in Honey Attorneys. This fact was not disclosed to both representatives and investors. Clearly, a conflict of interest had arisen. I shall say more about this in the paragraphs that follow.

[148] In terms of paragraph 3.8 of the disclosure document, all funds from investors were deposited into a trust account managed and held by Honey & Partners (Johannesburg) Incorporated until such time as the relevant units were allotted and issued. The investment documents carefully point out that investors were not expected to pay any money directly to brokers or a Blue Zone company. The money would be paid into Honey Attorneys trust account.

[149] This Office engaged Honey Attorneys in correspondence wherein the questions raised herein were asked. The responses received can only be described as evasive. On being questioned about the firms' involvement, van der Walt pointed out that in fact there were three separate law firms, one in Cape Town, one in Bloemfontein and another in Johannesburg. He submitted that Honey and Partners (Johannesburg) Incorporated had nothing to do with the Bloemfontein office. In all the documentation before this Office, no distinction was drawn between three separate firms of attorneys. Van der Walt was merely trying to distance his firm from JJ van Zyl. According to records kept at CIPRO, when the firm was incorporated van Zyl was indeed a director of Honey & Partners (Johannesburg) Inc. He subsequently resigned.

Nevertheless, notwithstanding the resignation of van Zyl, Honey and Partners (Johannesburg) Inc found themselves in a conflict of interest.

[150] In terms of the disclosure document Spitskop Village Properties Limited was offering for subscription 425 000 units that if fully subscribed would raise 425 million rand in funding for the company. This also means that if the subscription was not fully subscribed then Honey Attorneys, in terms of their mandate, had to repay the money to investors.

[151] The document then states that the project comprises the purchase of immovable property which is registered in the name of Blue Dot Properties 1330 (Pty) Limited. It is further stated that Spitskop would use investors' funds in order to purchase and develop the property.

[152] The acquisition price of the immovable property is disclosed as R 118 300 000 million. A fatal non-disclosure is the failure to point out, to investors, that the purchase price was being paid to a sister company which acquired the property for only R 1 057 000, 00. Clearly the whole transaction smacked of a scam.

[153] Of concern is that the disclosure document was prepared by Honey attorneys, in particular Mr Hugo van der Walt, who was aware of the conflict of interest between van Zyl, Lamprecht, Blue Dot, and Spitskop. To make matters worse, van Zyl was a partner/director of Honey

attorneys. Even more alarming is the fact that the conveyencing attorneys were also Honey and Partners. On the documentation available to me, the conclusion is inescapable that Honey Attorneys knew that Blue Dot acquired the property for only R1 057 000, 00.

[154] The valuation of the property, as represented in the disclosure document was patently a sham valuation designed to swindle investors of their money.

[155] On the facts before this Office Honey Attorneys were in a conflict of interest in that:

(1) They were part of an independent professional team in respect of the project, and this is according to the disclosure documents.

(2) The same attorneys acted for the promoters of the scheme, the seller of the property, the purchaser of the property and carried out the conveyencing.

(3) Van Zyl, a director, key individual and the mastermind behind the whole Blue Zone/Spitskop scheme was also a director/partner in this firm of attorneys, which fact was never disclosed to the investors. His subsequent resignation did not absolve Honey & Partners from disclosing the fact of his previous directorship to the investors.

(4) The same firm of attorneys also accepted investors' funds into their trust account.

[156] The purchase and sale agreement of the property from Blue Dot to Spitskop was not at arm's length. The agreement was signed by Lamprecht on behalf of Spitskop and Van Zyl on behalf of Blue Dot. The Board resolutions to buy and sell were taken by both men in their respective capacities as directors of Spitskop, on the one hand, and Blue Dot, on the other. The investors were never made aware of these circumstances.

[157] To the detriment of the investors the directors sold the property to themselves. The investors were not aware of the situation in respect of which van Zyl and Lamprecht sold the property, using the investors' money, to themselves at a highly inflated price.

The investors simply had no protection.

SECTION 78(2A) of the Attorneys Act

[158] The investors signed a document entitled "client authorization letter" that was part of the investment documents. The standard letter, which is common to all complainants in the Spitskop project, including in this matter, reads as follows:

> "I hereby instruct Honey& Partners (Johannesburg) Inc. ("Honey") to invest, subject to the provisions of section 78 (2A)

of the Attorneys Act. 53 of 1979, as amended, in a separate interest bearing call account at First National Bank the amount of R 100 000 (one hundred thousand rand) constituting an amount paid to reserve my participation in the Steelpoort Spitskop Village (the "Project"), which amount is to be held on my behalf and any interest accrued will be for my benefit".

[159] This was effectively a mandate from the investor to Honey attorneys to deal with the money in terms of section 78(2)(A) of the Attorneys Act. The money had to be invested in an interest bearing account for the benefit of the investor. With the exception of one complainant, this Office is not aware of any of the complainants receiving any interest from Honey Attorneys. This is obviously a matter of concern.

[160] In correspondence with this Office questions were asked about interest payment to investors. There was a legal duty on Honey Attorneys to deal with the trust funds strictly in accordance with their mandate. I deal with the scope of this mandate below.

[161] If the funds were paid to Spitskop, who were clients of Honey Attorneys, then they acted contrary to their mandate. If the money was not paid to Spitskop, then Honey Attorneys have to account for the interest to individual investors. In correspondence with Honey Attorneys, this question was also addressed to them. Again, this Office was treated to

an evasive response. In this regard, I make certain recommendations later in this determination.

[162] As already set out above, in all of the Blue Zone documentation, the investors were informed that all monies would be deposited into the trust account of Honey and Partners. It is clear that the attorneys' firm of Honey and Partners was a vital cog in the entire Blue Zone Investment scheme. In this regard I would like to quote from what the former sales manager of Blue Zone, Mr Riaan van Zyl, had to say about Honey Attorneys:

> *"Mnr Hugo van der Walt van Honey and Partners prokureursfirma (wat n gerespekteerde prokureursfirma is sedert 1962 en verskeie takke nasionaal het) was n sleutelpersoon in die vertroue wat bemarkers in die projek gehad het en hy was ook by baie van die projek-en bestuursveragderings betrokke (indien nie almal nie). Hy was ook die person wat n sleutelrol gespeel het in die daarstelling van die projek en waarvolgens hy n professionele fooi daarvoor gekry het. George Goodes die ander vennoot by Honey & Partners was ook ten nouste by die projek betrokke, volgens my kennis, en dit het gerusstelling by die bemarkers gelaat."*

[163] Once a firm of attorneys is appointed, the promoters of the scheme readily and freely go around throwing about the words "trust" and "trust account" in order to win the confidence of investors.

[164] The information before me is that the targeted subscription in the amount of R 425 million was not reached. That being the case, then Honey Attorneys were not mandated to pay the funds received into their trust account to Spitskop. The funds had to go back to investors. In a letter to all investors dated 3rd August 2009, Mr. JJ van Zyl acting in his capacity as director of Blue Zone, states that, "*It is not true that an amount of R 425m was raised. As already communicated to shareholders only an amount of R361m was raised.*" If this is true, this is indeed a cause for alarm. The investors may well have a claim against Honey Attorneys and possibly the Fidelity Fund

[165] The conduct of this firm of attorneys raises the following questions:

(a) why did Blue Zone and Honey and Partners fail to disclose to the investors the relationship between van Zyl and Honey and Partners?

(b) How did Honey and Partners fail to notice the blatant fraudulent misappropriation of investors' funds by van Zyl and Lamprecht through various means including contracts

drafted by Honey and Partners themselves? In particular, the sale of the land from Blue Dot to Spitskop;

(c) How did Honey and Partners transfer the hundreds of millions of Rands of investor's funds from the trust account to Spitskop and various Blue Zone entities? Did they comply with their mandate and the law in respect of these funds?

(d) What steps did Honey and Partners take to ensure that the investors' funds in its trust account were not used for purposes other than those they were intended for?

[166] There are serious questions which arise as a result of a potential conflict of interest between Blue Zone, Lamprecht, van Zyl and Honey & Partners. In this regard I make the following recommendations:

(1) That this determination be referred to the Law Society;

(2) That, in respect of the Spitskop project, Honey and Partners (Johannesburg) Inc's trust account be subjected to a full audit; and

(3) That a copy of this determination be referred to the Attorneys' Fidelity Fund.

(4) That investors be advised to approach Honey and Partners (Johannesburg) Inc to account for interest earned in terms of the latter's mandate.

(5) That a copy of this determination be referred to the NPA.

O. THE DISCLOSURE DOCUMENT

[167] For investors to make a decision to invest they not only require professional assistance from credible providers, but require a full and proper disclosure of all the material facts regarding the investment scheme. This requirement was recognised by the legislature in *General Notice 459 of 2006* issued by the *Department of Trade and Industry Consumer Affairs (Unfair Business Practices) Act*, 1988, published in *Government Gazette* number 28690 dated 30 March 2006 (the DTI Notice). The DTI Notice was aimed, inter alia, at promoters of investments in property syndication. In an annexure to the DTI Notice, the legislature set out the prescribed information which must be presented to investors in the disclosure document.

[168] Blue Zone Property Investments (Pty) Limited, as promoter and through Spitskop Village Properties Limited (Spitskop) presented their disclosure documents to members of the public through Blue Zone's representatives.

[169] In the event that Respondent applied his mind to the Disclosure Document, the following would have become apparent and he would have been obliged to draw the Complainant's attention to it:

169.1 The investment scheme involved the purchase of immovable property known as portion 6 of the farm Spitskop in Mpumalanga (the property).

169.2 The property was to be developed into residential erven to be sold at market value.

169.3 Blue Dot Properties 1330 (PTY) Limited (Blue Dot), a Blue Zone sister company which shares the same directors as all the Blue Zone entities, purchased the property from a farmer Mr. J.N Joubert for an amount of **R 1 057 000,00**.

169.4 According to the scheme, Spitskop, being the syndication vehicle, would purchase the property from Blue Dot. Spitskop and Blue Dot are sister companies having the same directors as Blue Zone, namely Hendrik Christoffel Lamprecht and Jacob Johannes van Zyl.

169.5 The property was sold by Blue Dot to Spitskop for a purchase price of **R 118 300 000**.

169.6 The same property which was purchased by Blue Dot for **R 1 057 000**, 00 was valued, for purposes of the scheme, at between **R 170 000 000,00** and **R180 000 000,00.**

169.7 The valuations were carried out by certified valuators. How a property that changed hands, in an arm's length transaction, for a purchase price of R1 057 000, 00 became valued at R 180 000 000, 00 was unexplained.

169.8 In effect Blue Dot sold the property to its own sister company for R 118 300 000, 00. This is a property that they acquired for a mere R 1 057 000, 00. It was the investors' money that was used to fund this sale to Spitskop.

I have no doubt that if this information was conveyed to the Complainant by the Respondent the former would not have invested. A provider acting with due care, skill and diligence would have asked the questions. Regrettably, in this case, the respondent did not.

[170] It is abundantly clear that the disclosure document did not comply with the express terms of the DTI Notice, and as a result investors were swindled of millions of rand.

[171] Of grave concern is the fact that the disclosure documents were prepared by professional people, including attorneys, both of whom were partners in the same firm, one of whom was also a director of all the Blue Zone entities.

[172] Upon a proper reading of the disclosure document, coupled with the undisputed facts, the irresistible conclusion is that the whole Blue Zone/Spitskop scheme was a fraud from the start.

P. CONCLUSIONS

[173] On the undisputed facts before this Office, the following conclusions are made:

173.1 The Respondent failed to make an independent and objective assessment of the Blue Zone/Spitskop product.

173.2 The respondent as a representative held himself out as an expert on the product he sold to the Complainant.

173.3 The Complainant was dependent on the Respondent for professional and sound advice on the appropriate investment he needed to make.

173.4 The Respondent conducted the necessary needs and risk analysis of the Complainant.

173.5 The results of the risk analysis indicated that the Complainant was a "conservatively moderate investor".

173.6 The Respondent invested the Complainant's money into the Spitskop project, which was a high risk investment.

173.7 The Respondent was not qualified to deal in unlisted shares and debentures, nor was he licensed to do so.

173.8 The Respondent relied almost exclusively on the glossy marketing material of Blue Zone and did not conduct any independent analysis in making his assessment of the Spitskop project.

173.9 The Respondent breached various provisions of the FAIS Act and General Code, and is therefore liable to the Complainant.

In the premises, the complaint is upheld, and the Respondents are ordered to pay the complainant's claim.

Q. QUANTUM

[184] The First Respondent invested an amount of R 100 000.00 of Complainant's money in the Spitskop Project. There is no prospect of recovering any amount from Spitskop or Blue Zone.

[185] Accordingly an order will be made that Respondents pay to complainant an amount of R100, 000.00, and interest will be awarded on this amount.

THE ORDER

I make the following order:

1. The complaint is upheld.

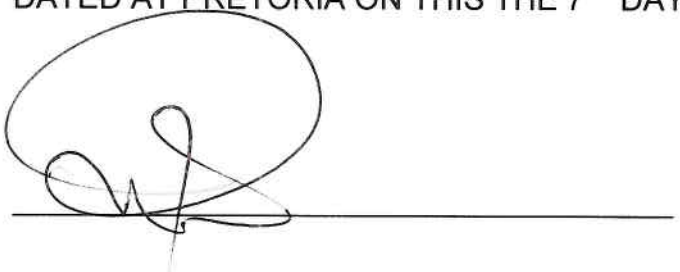
2. The respondents are ordered to pay the complainant, jointly and severally, the one paying the other to be absolved:

   2.1 The amount of R 100, 000.00

   2.2 Interest on the amount of R100, 000.00 at the rate of 15, 5% per annum from the 25th January 2007 to date of payment.

3. Respondents are ordered to pay the case fee of R1000, 00 to this office within thirty (30) days of date of this determination.

DATED AT PRETORIA ON THIS THE 7th DAY OF MARCH 2011.



NOLUNTU N BAM

OMBUD FOR FINANCIAL SERVICES PROVIDERS