IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

CASE NUMBER: FAIS 06416/10-11/KZN 4

In the matter between:-

JANNET ANN SCOTT BUJOK **Complainant**

and

D RISK INSURANCE CONSULTANTS CC **1st Respondent**

DEEB RAYMOND RISK **2nd Respondent**

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

A. THE PARTIES

[1] Complainant is Janet Ann Scott Bujok, a female, retiree of Westdene, Johannesburg, Gauteng Province.

[2] First Respondent is D Risk Insurance Consultants CC, a close corporation duly incorporated in terms of South African law, with its principal place of business at 60 Van Riebeeck Avenue Edenvale, Gauteng Province. First respondent is an authorised financial services provider in terms of the FAIS Act, with license number 12806. The license was issued on 25 November 2004.

[3] Second Respondent is Deeb Raymond Risk, a male of adult age, a key individual and authorised representative of the 1st respondent. At all times material hereto, complainant dealt with 2nd respondent. In this determination, for the purposes of convenience, I refer to 1st and 2nd respondent as respondent. Where necessary, I have specified.

B. INTRODUCTION

[4] This complaint involves investments made by the complainant in two Sharemax property syndication schemes known as 'The Villa' and 'Zambezi'. The Sharemax group has been offering investments to the public through several broker networks for the last decade. They own several shopping centres country wide. To understand the way the group operated and the legal implications of what members of the public were actually involved in, one would have to carefully study the prospectuses of the various shopping centres. A cursory glance will not do. In a sense, the way these schemes have been crafted are beyond the reach of the average broker. At least thus far, this Office has only come across brokers who had no clue what they were marketing to the investors. Clearly, those who could comprehend the legal implications of what the prospectuses contained kept their distance from the product.

General description of how the group operated

[5] A simple way of describing the way the Sharemax group operated would be: The group would set up a public company and invite investors to the scheme

through the issue of the prospectuses. Brokers would be invited to fancy lunches by the group where the scheme is marketed by the promoters to them. It is the brokers that contacted members of the public and offered the Sharemax products. In many instances, new or existing clients would be offered the products, but mainly the products would be offered to the elderly.

General description of the structure

[6] After the Sharemax group set up a public company, a private company would also be set up which would receive funds by way of a loan from the public company. It is the private company that will eventually own the immovable property, (the shopping centre). The directors of the promoters, the public company and the private company that owns the immovable property would essentially be the same people. The public would be told that they are investing in immovable property and that their investments were low risk. But, as has been seen in several Sharemax determinations issued by this office, the investment was by no means a low risk investment. The convoluted structure on its own conveyed a level of risk.

The Villa and the Zambezi

[7] It is now a known fact that the two schemes, the ‘Villa’ and ‘Zambezi’ did not develop as planned. Investors have not received income since August 2010. Whilst the group have been known for purchasing shopping centres, these two ventures were concerned with the purchasing of land with a view to building the

shopping centres. While there were no income generating activities, interest was still paid to the investors. As to what economic activity generated the income paid to the investors, so far, no broker has proffered any plausible explanation. It is at this point that the Registrar of Banks stepped in. The Registrar was of the view that Sharemax's funding model was in contravention of the Banks Act. As a result of the intervention of the Registrar, Sharemax could no longer continue to accept deposits from members of the public. As a result, in relation to the two schemes, the 'Villa' and 'Zambezi', no investor has been paid income since August 2010.

C. THE COMPLAINT

[8] Complainant first met with respondent on 9th of September 2008 after she was introduced to him by one of his clients. She states that she is not an experienced investor in that she has only invested in Stanlib and Momentum before. Her complaint is as follows:

a. Respondent invested her full amount of R815 000 into the Sharemax property syndication schemes;
b. He told her that the investment was low to medium risk;
c. Respondent also promised her that there would be high gains when the centre was sold during May/June 2010;
d. She questions promises made, especially because the 'Villa' was still under construction.

[9] According to the complainant, respondent advised she could improve her income by investing in Sharemax. Complainant appointed respondent as her

financial advisor. Monies were moved from existing investments with Stanlib, Momentum and Glacier International for investment into Sharemax. On the 18th of September 2008, Complainant signed forms for an investment in 'Zambezi' and gave the respondent a cheque for R575 000.00. According to complainant, no other products were discussed or offered.

[10] On the 2nd of November 2009 the complainant, in an effort to increase the income she was receiving from the 'Zambezi' investment, invested a further R20 000. This amount was invested in the 'Villa'. No other products were discussed or suggested.

[11] On the 14th of May 2010 complainant and respondent met again at the offices of Glacier International. Complainant had decided to dissolve her offshore trust and transfer R220 000.00 of the trust money for additional investment in South Africa. On the 21st of May 2010, yet another meeting took place at Glacier International Offices when the respondent suggested adding the R220 000.00 to the 'Villa'. This complainant did. The cheque according to complainant was handed over to the respondent on 11th of June 2010. Complainant contends she did this because she had confidence in the respondent.

[12] Alarm bells rang at the end of August 2010, when Sharemax failed to pay her monthly interest. Not only did the income stop; complainant states that respondent was not able to offer her any plausible explanation about what was happening.

[13] Complainant is of the view that respondent failed to follow procedures according to the FAIS Act. In this regard, complainant alludes to the promises made by the respondent of high gains upon the sale of the centres, including the advice that Sharemax is a low to medium risk investment.

D. THE RELIEF SOUGHT

[14] The complainant seeks to recover her entire capital of R815 000 together with interest from August 2010 to date of payment from respondent on the basis that respondent failed to adhere to the provisions of the FAIS Act when he advised her.

E. RESPONDENT'S VERSION

[15] The complaint was referred to the respondent in terms of Rule 6 of the Rules on proceedings of the FAIS Ombud, (the Rules). Respondent filed his response in the form of an application in terms of section 27 (3) (c) of the FAIS Act. The response can be divided into two sections. One section deals with the merits of the complaint and the other deals with whether the Ombud is the appropriate forum to deal with the complaint. In this application, respondent also attached supporting documents relating to the rendering of the financial service. It is noted that respondent states that the complaint pertains to the performance of three investments and that the Ombud should not entertain this complaint as the complainant's claim is in excess of R800 000. The submissions will be dealt with later in the determination. The respondent further states that he does not deal with the merits of the complaint in the application but reserves '*the right to do so if and when it may become necessary to do so*.' However, as will become

apparent, respondent does deal with the merits of the complaint. I summarise the response to the merits:-

[15.1] According to the respondent, one of his clients referred him to the complainant on 9th of September 2008.

[15.2] The respondent met with the complainant at her home to discuss her finances and investments. On the same day, the complainant appointed him as her financial advisor.

[15.3] After the respondent met with complainant again on 18 September 2008, she requested that he switch funds in her Momentum Life Annuity to Allan Gray's money market fund as there was a lot of volatility in the stock market. At the request of the complainant, the respondent also completed an application in Sharemax (Zambezi Prospectus no. 6) for an investment in the amount of R575 000.00. During the course of the meeting, a Life and an Investment Client Advice Record and Risk Profile Questionnaire were completed. According to the respondent, these documents were fully discussed and explained to the complainant.

[15.4] According to the respondent, he was satisfied that the complainant was an experienced investor who held a number of investments. The respondent contends that the complainant appears to be fairly knowledgeable on the product she was investing in. This he says is evident from Annexure E of his response, i.e. a Life and Client Advice Record completed on 18 September 2008 on which it is stated that the complainant is fairly knowledgeable in respect of the Sharemax product. According to the respondent the complainant also advised him

on this date that the amount she was invested constituted between 5% and 10% of her current net worth.

[15.5] He states that he met with the complainant again on the 2nd of November 2009. They had a follow up meeting on the 6th of November 2009 where they finalised switches in her Momentum Life Annuity and decided to invest a further R20 000 into Sharemax (The Villa Prospectus no. 14)

[15.6] On the 4th of May 2010, they met again as complainant wished to discuss her off shore investment. It was decided that the complainant would transfer R220 000 to her South African bank account and to invest the said amount into Sharemax (The Villa prospectus 2). The balance of the off shore investment would be administered by Glacier International.

[15.7] The respondent contends that the complaint against him was made after Sharemax stopped paying interest. He refers to the complainant's contention that he placed too much of her portfolio into property syndication, which according to her is a high-risk investment not suited to her circumstances. What the complainant in essence alleges, says the respondent, is that he '*acted dishonestly- thus fraudulently – or negligently'*. The respondent denies this allegation.

[15.8] Sharemax, according to the respondent, was authorised to act as a financial services provider by the Financial Services Board ('FSB'). He submits that the complaint against him is simply that the complainant believed that she was purchasing a product that was guaranteed, when

it was not. He denies the complainant's allegations that he was negligent by not properly understanding the product that he was selling or that he intentionally misled her.

[15.9] He states that it is apparent from the documentation signed by complainant that she must have been aware that she selected an investment which projected higher income (i.e. Option A), but did not guarantee such income. In terms of the prospectus, Option B guarantees income for at least five years, but at a lower rate.

[15.10] The complainant signed all the relevant documents clearly indicating that she accepted and understood the context and importance of the documentation. Furthermore, the complainant is an experienced investor who has an investment portfolio extending over numerous investments as set out in the Glacier Portfolio Breakdown.

[15.11] Respondent states that there are obvious discrepancies and disputes between the versions of the complainant and his on essential events. These factual disputes cannot be determined on unattested and untested conflicting versions of events made on paper. Oral evidence on oath and cross-examination are required in order for the finder of fact to determine the truth.

[15.12] Regarding the legality of the Zambezi/ Sharemax model and the events surrounding 'The Villa', respondent avers that when he assisted complainant, he was not aware of any questions regarding the solvency and the legality of the business model of the investments. It was only in about August / September 2010 that he learnt through the

public media that The Villa and Zambezi had defaulted on the interest payable to investors. He then followed the events surrounding the two in the press.

[15.13] He believes that the South African Reserve Bank, (SARB) has appointed judicial managers for 'The Villa' and 'Zambezi' and that eminent persons, Justice Hartzenberg and well respected economist Mr Dawie Roodt have been appointed to its board of directors. His understanding is that every attempt is made to complete the projects to prevent losses. At this point, it is unknown whether 'The Villa' and 'Zambezi' will recommence payment of interest and complete the projects or whether the two will fail or even be liquidated. Whether or not any investor will lose his or her investment and if so what the loss may be are questions to which the answers are unknown. In respondent's view, no decision concerning any compensation claimed by complainant from him may be made before it is determined whether the 'Zambezi' and 'The Villa' will fail.

[15.14] Respondent finally submits that no decision can be made concerning his negligence on the grounds alleged by the complainant, unless it is established whether or not the Sharemax model was legal, what the causes of the non-payment of interest were and what was in the public domain when he discussed the investments with complainant.

F. ISSUES

There are three issues:-

(i) Jurisdiction of this Office;

(ii) Whether respondent in rendering financial services failed to comply with the Code and/or acted negligently.

(iii) In the event it is found that the respondent failed to comply with the Code and/or acted negligently, whether such conduct caused financial prejudice.

(i) Jurisdiction

[16] Respondent has raised the point that there are obvious discrepancies and disputes between the versions of the complainant and his, on essential events. These factual disputes cannot be determined on unattested and untested conflicting versions of events made on paper. Oral evidence on oath and cross-examination are required in order for the finder of fact to determine the truth. Respondent raised the same defence in the first Barnes determination[1], which defence was dismissed. For essentially similar reasons, which may be summed up as, all the allegations made by complainant are matters of compliance with the Code, which can and are answerable by records maintained by the financial services provider. This defence is therefore dismissed'.

[17] Moreover, respondents' application to the North Gauteng High Court wherein he challenged the jurisdiction of this Office has now been disposed of. The High Court dismissed the application with costs[2].

[1] FAIS 6793/10-11/GP 1 para 18-24

[2] Risk Deeb Raymond v The Ombud for Financial Services Providers and Others CASE NO. 38791/2011

(ii) Whether in rendering the financial service to complainant, respondent failed to comply with the Code and/or negligently.

Complainant made the following investments on the advice of the respondent:

1. R575 000.00 in Zambezi on 18 September 2008
2. R20 000.00 in The Villa on 06 November 2009
3. R220 000.00 in The Villa on 11 June 2010

It is noted that in rendering the financial services to complainant, respondent's conduct infracted the General Code of Conduct in several respects. The purport of these violations simply point to the fact that complainant could not have made an informed decision at the time she decided to invest in Sharemax. I shall not mention them all, as to do so would result in an unnecessarily long determination. For example, it is not in dispute that in order to make the first investment of R575 000, complainant surrendered her Stanlib investment. On respondent's own version, he advised the complainant to invest in Zambezi. On the respondent's own admission the source of the R220 000.00 invested in The Villa was the complainant's off shore investment.

Although the complainant's investments were replaced by the respondent, I could not find anything from his papers in support of the requirements of Part VII, section 8 (i) (d) of the Code. The section provides that a provider must, where the financial product is to replace an existing financial product wholly or partially, fully disclose to the client the actual and potential financial implications ,costs, and **consequences of such a replacement**, (own emphasis) including, where applicable, full details of-

(i) fees and charges in respect of the replacement product compared to those in respect of the terminated product;

(ii) .....

(v) the material differences between the investment risk of the replacement product and the terminated product,

(vi) penalties or unrecovered expenses deductible or payable due to termination of the terminated product,

(vii) to what extent the replacement product is readily realisable or the relevant funds accessible, compared to the terminated product.

I have perused all documents submitted by respondent to this Office and nowhere are the consequences of the replacement disclosed. I have also seen no comparison in respect of liquidity and risk as the section demands.

[18] Most importantly though, the essence of the complaint is about the failure to properly advise the complainant, in particular, the suitability of the investment to complainant, a 69 year old (pensioner at the time of rendering the financial services). Complainant contends that the true risk of the product was not disclosed her. It has not been denied by respondent that he advised complainant that the Sharemax Villa and Zambezi investments were low to medium risk. Respondent failed to appreciate that Sharemax product, because of the risk inherent in it, was not disclosed to her.

Risk inherent in the Sharemax (Zambezi and The Villa) investments

[19] The Sharemax product was anything but low to medium risk. This is confirmed by the Sharemax prospectuses issued in respect of the Zambezi and the Villa. Right at the beginning of each of the prospectuses (i.e. page 4 of prospectus 6 (Zambezi), pages 6 of prospectuses 2 and 14 (The Villa) open with the warning that the shares on offer are unlisted and should be considered as a 'risk capital investment'. Investors are therefore at risk as unlisted shares and claims are not readily marketable and should the company fail this may result in the loss of the investment to the investor. I have not seen anywhere in respondent's papers that he warned complainant that she was investing in an investment where she could potentially lose her capital.

[20] It is stated in the prospectuses (i.e. page 4 of prospectus 6 (Zambezi), pages 6 of prospectuses 2 and 14 (The Villa) that the offer by Sharemax Zambezi and The Villa is for a subscription for linked units. Each unit consists of 1 ordinary par value share of 0,00001 and one unsecured floating rate claim with a value of R999,9999 linked together in a Unit at R1000 per unit by way of a public offer. There is no indication or record to suggest that complainant was made aware, as the Code demands, of the legal implications of investing in such investment.

[21] According to the complainant, Sharemax was marketed to her as a low to medium risk investment. Annexures M and R of the respondent's file of papers give credence to this allegation as it describes the risk profile of Zambezi and The Villa as 'medium' and 'low to medium risk'. The respondent's description of the Sharemax investment as a low to medium risk investment is a clear

indication that he did not understand what he was selling and could not have appreciated the danger to which he exposed the complainant. I have no doubt complainant would not have made the investments if she was told she could lose her capital of R815 000.00.

Complainant's risk profile

[22] The respondent's file of papers includes a Risk Profile Questionnaire used to assess the complainant's risks profile. The assessment was conducted on 18 September 2008 (Annexure F), at the time that the first investment was made. According to the assessment conducted, the complainant was categorised as an 'aggressive to assertive investor'. On closer scrutiny of the assessment, the following appear from the risk profile questionnaire:

Question 1 of Section A of the questionnaire reads as follows:

'What is the primary purpose of this investment?'

Out of the seven possible alternatives, the following answer was chosen:

'Wealth accumulation over the long-term (time horizon over 10 years)

Question 5 of Section B of the questionnaire reads as follows:

'**Based on your investment goals, which of the objectives profiled below best describes your investment approach?'**

Out of the five possible alternatives, the following answer was chosen:

'Seeking growth and capital over the medium-term and prepared to accept only **moderate levels of risk'** (own emphasis)

Question 8 of Section B of the questionnaire reads as follows:

As an investor, where would you place yourself on the following scale?

Out of the five possible alternatives, the following answer was chosen:

'**Low to medium risk'** (own emphasis)

[23] According to the assessment, complainant was only prepared to accept 'moderate levels of risk' and considered herself a 'low to medium risk' investor. Given the clear indication by the complainant of the level of risk she was willing to take, the respondent must have realised that his conclusion that complainant was an 'aggressive to assertive profile' was inaccurate. In other words, the risk profile questionnaire is fundamentally flawed in that it disregards the client's express needs and objectives.

Appropriateness of advice

[24] Although it is reflected in the Life and Investment Client Advice Record (Annexure E) that the complainant is fairly knowledgeable in respect to Sharemax investments, there is no basis for such conclusion. The point is, given respondent's own questionable appreciation of the product, his pronouncement of complainant as an experienced investor must be tempered with. I have already mentioned the complicated nature and the language used in the prospectuses in the Barnes determination[3] (and many other

[3] FAIS 6793/10-11/GP 1

determinations concerned with Sharemax) and pointed out that it was not possible for ordinary citizens like complainant to appreciate what exactly they were buying into when they bought the Sharemax investment. The labelling of the complainant as fairly knowledgeable in respect of Sharemax investments without any basis points to paucity of skill to render financial services in relation to this financial product on the part of the respondent.

[25] In terms of Section 8(1) (c) of the General Code a provider must identify the financial product or products that will be appropriate to the client's risk profile and financial needs. Complainant was 69 years old at the time the investment was made. It is common cause that the monies invested in Zambezi and The Villa needed to generate post retirement income. These factors, coupled with the fact that complainant was only prepared to accept moderate levels of risk and considered herself a 'low to medium risk' investor, should have alerted the respondent that complainant is not an aggressive investor. Clearly, she could not afford to risk her retirement funds. Not only did the high risk investments not correlate with her circumstances, complainant could not have understood the risk associated with the investment in Zambezi and The Villa as it was incorrectly described as low to medium risk by the respondent. There is no doubt that the investments in Zambezi and The Villa were inappropriate.

Causation

[26] Respondent failed to properly advise complainant of the true risk inherent in the Sharemax investments. Had he done so, complainant would not have bought the investment. Importantly, even if complainant had insisted on the investment,

(of which there is no such evidence), respondent was still duty bound to disclose the risk and dissuade complainant against the investment as it was way out of kilter with her circumstances.[4] There is no such description of risk or warning in any of the respondent's papers.

G. FINDINGS

[27] I am satisfied that respondent failed in his duty to comply with section 8 (1) (d) of the Code, given that the transaction involving the Zambezi and Villa investments were replacements.

[28] Respondent was negligent by failing to apply his mind as to how much risk complainant could tolerate, given her circumstances and the risk she was willing to take. He failed to recommend a product appropriate to the complainant's risk tolerance and her financial needs.

[29] By marketing the high risk Sharemax investments as low to medium risk investments, the respondent failed to act with due skill, care and diligence in the interest of his client and the integrity of the financial services industry.

[30] Respondent's contention is that no decision can be made on the question of his being negligent until the question of the legality of Sharemax funding model has been decided upon. None of the issues ventilated in this determination are dependent on that enquiry. The duty imposed on respondent by the provisions of the FAIS Act to appropriately advise his client have everything to do with the

[4] Part VII, section 8 (4) (a) to (b) of the Code

nature of the investment as detailed in the prospectuses. Respondent's contention in this regard must fail.

[31] Respondent's contention that the complaint is premature must also fail. The issue is not whether some monies will be recovered by complainant at some future unknown date. The test is whether the advice, given complainant's circumstances, was appropriate. I may add that it is now two years since respondent made this statement. Clearly, the prospects of complainant recovering her investment are becoming bleaker by the day. As the respondent is aware, Sharemax conceded to the illegality of their funding model the day they stopped collecting deposits from members of the public.

[32] Respondent has failed to point out the material disputes of fact. What is clear in this complaint is respondent's failure to abide by the Code. None of the documents submitted by respondent to this Office support his claims to have complied with the Code in so far as the disclosures of risk and liquidity are concerned. It is clear that there is no material dispute of fact in the matter.

H. QUANTUM

[33] According to the respondent the Ombud should not entertain this complainant as the complainant's claim is in excess of R800 000. The complaint relates to three investments made on the advice of the respondent on three different occasions. These are in effect three different causes of action. Each claim in respect of each cause of action is less than R800 000. Therefore, all three claims fall within the jurisdiction of this Office.

[34] The complainant invested a total amount of R815 000 in Sharemax Zambezi and Sharemax The Villa. She has not been paid any income since August 2010 and has by all indications lost her capital. There can be no question that it is respondent's inappropriate advice that led to the investments.

I. ACCOUNTABILITY

[35] I deem it appropriate that I deal with the issue of joint and several liability of the respondents herein. I have held that the 2nd respondent failed to comply with the Code in the rendering of the financial service herein. 2nd respondent is a member and key individual of 1st respondent. If I were to hold 1st respondent solely liable this would not be in line with what the legislature intended as evidenced by section 8 of the FAIS Act. I say so for the following reasons:-

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

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

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

[39] The fact that where the key individual does not meet the legislative requirements of fit and proper, the corporate entity's license can be withdrawn simply means the intention of the legislature is to hold both persons accountable. The General Code of Conduct for Authorised Financial Services Providers and Representatives (the Code) clearly envisages that the general and specific duties of a provider of financial services are those that are performed by a natural person as opposed to an artificial persona. This is evident in:-

(i) the definition of provider includes a representative;

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

(iii) the various specific duties regarding the rendering of a financial service set out in section 3 require human intervention. So too are all the requirements set out in Parts III, IV, V and VI;

[40] First Respondent is the licensed provider under whose name the financial service was rendered. Second Respondent is an authorised financial services

provider and key individual of 1st respondent. Therefore, it is necessary that I hold both respondents liable jointly and severally, the one paying the other to be absolved.

J. ORDER

In the premises the following order is made:

1. The complaint is upheld;
2. Respondents are hereby ordered, jointly and severally, the one paying the other to be absolved, to pay to complainant the amount of R815 000,00;
3. Interest at the rate of 15.5 % , per annum, effective from seven (7) days from date of this order to date of final payment;

DATED AT PRETORIA ON THIS THE 13th DAY OF NOVEMBER 2012.

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NOLUNTU N BAM

OMBUD FOR FINANCIAL SERVICES PROVIDERS