IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

Case Number: FAIS 03323/13-14/ KZN 1

In the matter between

DEBBIE GIRONI **Complainant**

and

MIDCOAST FINANCIAL SERVICES (PTY) LTD **First Respondent**

BRUCE EARL GRIFFITHS **Second Respondent**

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

A. INTRODUCTION

[1] This determination follows a recommendation made in terms of section 27 (5) (c) of the Act on 27 July 2017. This determination shall be read in conjunction with the recommendation and the latter shall form part of this determination.

B. THE PARTIES

[2] The complainant is Mrs Debbie Gironi, an adult female whose full particulars are on file with this Office.

[3] The first respondent is Midcoast Financial Services (Pty) Ltd, registration number 2000/006698/07, duly registered in terms of South African law. The

Regulator's records indicate the first respondent's last known address as 20 Hosking Road, Wembley, Pietermaritzburg, 3201. The first respondent was an authorised financial services provider (FSP) with licence number 17641, which licence lapsed during April 2011, following a request by the second respondent to the regulator.

[4] The second respondent is Bruce Earl Griffiths, a representative of the first respondent. The second respondent's address is the same as that of the first respondent. The Regulator has confirmed that the second respondent is currently not associated with any FSP.

C. THE RESPONDENT'S REPLY TO THE RECOMMENDATION

[5] The respondents refused the recommendation and provided the response summarized here below.

[6] I note at this early stage that notwithstanding the response, the essence of the recommendation is not disturbed by the respondents. The recommendation upheld the complaint of inappropriate advice and found that a sufficient link between the inappropriate advice and the loss suffered by the complainant existed.

[7] Without repeating what is set out in the recommendation, it is evident from the response that the respondents had no answer for advising complainant to invest her funds in schemes where clear violation of the law and poor governance practices were manifest from the prospectuses. The respondents provide no cogent reasons as to why the Sharemax investments were appropriate for the

complainant's needs, notwithstanding the gratuitous payment of investors' funds to the likes of Brandberg and other parties, in violation of the law.

Points in limine

Prescription

[8] The respondent contended that the complaint has prescribed on the basis that the complainant failed to comply with the provisions of rule 5 (b)[1]. The complainant became aware of the problem during August 2010, but the notice in terms of rule 6 (b) was only sent during September 2013, argues respondent. The respondent argued that he did not receive any letters from this Office, and only became aware of the complaint when he was contacted by his attorneys of record on 27 July 2017.

8.1 The facts, however, will show that the complainant corresponded with the respondent and his office on several occasions during the year 2010 to 2012, enquiring about the status of her investments and expressing dissatisfaction with the state of affairs. It is evident from the trail of e-mails that the complainant continued to rely and act upon the information provided to her by the respondent. I quote from one e-mail[2] wherein the complainant noted that:

"I am not entirely happy with a few things, especially since the back-dated articles that I am only reading now (stupidly), gave very clear indications that there was trouble on the water, long before we even considered this investment. Had we taken heed, I might not be writing this letter. I

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[1] Rule 5 (b) on Proceedings of the Office of the Ombud for Financial Services Providers which provides that:
(*b*) *Before submitting a complaint to the Office, the complainant must endeavor to resolve the complaint with the respondent.*
(c) *The complainant has six months after receipt of the final response of the respondent, or after such response was due, to submit a complaint to the Office.*

[2] Dated 23 February 2011 at 09:43 am addressed to bruce.griffiths@momentum.co.za

remember talking to you specifically about these concerns and you told me emphatically not to believe what I read since the journalists were out to get Sharemax…."

8.2 Rule 5 (b)[3] is a step that precedes official receipt of a complaint in this Office. It was in fact respondent's duty to inform the complainant to firstly, direct her complaint to this Office, and secondly, the applicable time frames. There is no evidence that respondent discharged this duty.

8.3 The Appeals Board in the matter of *Mostert v Landman*[4] dealt with the issue of non-compliance with Rule 5 (b):

"[16]……We therefore conclude that non-compliance by the complainant with rule 5 (b) does not render the lodging of a complaint a nullity, if the complaint qualifies as a complaint. With the use of the word "otherwise" in section 27 (c), the legislature intended to give discretionary powers to the Ombud and the word otherwise should not be construed in any limited sense as meaning or only referring to the condition provided for in rule 5 (b) amongst others…"

8.4 It is axiomatic from the referral in terms of Rule 6 (b) that the respondent was afforded ample opportunity to resolve the complaint with the complainant. Had the respondent intended to resolve the complaint, he could have done so from the time of the complainant's letters. Even in these papers, the respondent proffers no information whatsoever about

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3 Please refer to footnote 2 for the full quotation of the rule

4 FAB 12/2017, paragraphs 13-17

his efforts to resolve the complaint with the complainant. I see no reason to make the point portentous by parading several authorities, save to say the notice sent by this Office in terms of Rule 6 (b), afforded respondent ample opportunity to resolve the complaint with the complainant independently of this Office. The respondent failed to do so.

8.5 Even though the respondent denied receiving the various notices informing him of the complaint, he still had the opportunity to resolve the matter, following receipt of the recommendation. He elected not to do so. The Office previously conceded that an error was made with the respondent's e-mail address in earlier correspondence[5]. This was subsequently rectified and does not deter from the fact that the respondent has since had an opportunity to resolve the complaint.

8.6 The complaint has not prescribed, contrary to respondent's claims. See in this regard section 27 (2)[6]. Official receipt of a complaint by the Ombud suspends the running of prescription, for the period after such receipt until the complaint has either been withdrawn, or determined. The sending of the relevant notices have no bearing on prescription.

Jurisdiction and Conflict of interest

[9] The respondent argued that this Office lacks jurisdiction to adjudicate on matters where there are material disputes of fact. Furthermore, it is conflicted to adjudicate on its own conduct of non-compliance with the rules and the Act,

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5 See in this regard correspondence addressed to the respondent's attorney dated 7 August 2017

6 *Official receipt of a complaint by the Ombud suspends the running of prescription in terms of the Prescription Act, 1969 (Act No. 68 of 1969), for the period after such receipt of the complaint until the complaint has either been withdrawn, or determined by the Ombud or the board of appeal, as the case may be.*

with reference to prescription of the complaint. The respondent argued that the matter be referred to court as provided for in section 27 (3) (c).

9.1 The respondent's argument in respect of conflict of interest is now irrelevant, considering the findings of the Appeals Board in the *Landman* matter. This point has been comprehensively responded to.

9.2 As far as the material factual disputes are concerned, the respondent is of the view that the complainant's allegations are contradicted by the documents she signed. The respondent claimed that the principle of *pacta sunt servanda*[7] applies. This argument however is misplaced. The complainant is not disputing the validity of the contract she entered into to make the investment, but rather the appropriateness of the advice that persuaded her to conclude the contract.

Response to the merits of the complaint

[10] The respondent disputed the quantum, claiming that only the R600 000 investment was complained of. Supplementary documentation received from the complainant (and provided to the respondent) nonetheless confirmed that her complaint encompasses all three investments.

[11] The respondent stated that even though the complainant was set on investing in Sharemax, he fulfilled his duties as an FSP with the view of ensuring that his client could make an informed decision before proceeding with the investments. He provided her with a registered prospectus and discussed the contents thereof in detail. The complainant's signature on the relevant document, in respondent's view, is proof that she has read and understood the content,

[7] The common law principles that agreements are binding and must be enforced.

including that the investment was medium to long term and that the complainant had to retain an emergency fund.

[12] The respondent claimed that not a single representation made in the Sharemax prospectus has been proven to be false or incorrect.

[13] The complainant's circumstances were considered, stated respondent. Her husband was employed and earned a good income. She was a 37 year old stay-at-home mother generating income from small businesses, with many years available to accumulate wealth and recoup losses, should it occur. She therefore had an appetite for risk. The respondent described the investments as "single needs", simply requiring the highest possible income with capital growth. The income was utilized for school fees.

[14] The respondent submitted that he would have utilized the necessary compliance documentation, prepared a client advice record, as well as a needs analysis. I pause to note that a record to this effect was never provided by the respondent[8].

[15] The respondent claimed that in light of the complainant's occupation as a teacher, she had the ability to read and understand the prospectus in its entirety. The risks were detailed (that it is risk capital and could be lost); therefore the complainant had an opportunity to make an informed decision. She accepted the risks owing to the higher returns she sought. The respondent therefore considered the investments to be appropriate.

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[8] What the respondent included with the response, is an example of such a record which belonged to another client of his. The particulars of the client was blacked out.

[16] Any allegation to the contrary, in respondent's view, is contradicted by the complainant's signature on the documentation. The complaint does not contain a single allegation of negligence of misconduct, nor did the complainant blame him for the loss.

[17] In response to the questions raised in the notice in terms of the section 27 (4) letter of March 2017, the respondent stated that:

17.1 He did not confirm the valuation figures shown in the prospectus, as he was entitled to rely on the contents of the registered prospectus. Expecting an FSP to confirm the figures, is setting the bar too high.

17.2 The respondent disputes that there was an "overwhelming conflict of interest" in the way the Sharemax investment is structured and presented in the prospectuses. Owing to Sharemax's track record, he had no reason to suspect dishonesty.

17.3 The respondent relied on the "expert" opinion of Mr Anton Swanepoel who concurs that requiring FSP's to take cognizance of the King Reports and anticipate director misconduct, is placing too high a standard on FSP's.

17.4 The respondent perceived the risks in the Sharemax investment not to be too excessive, according to his reading of the prospectus.

17.5 The respondent denied the statement that the Sharemax directors had intention to violate Notice 459, and that the movement of the funds from the attorneys' trust account was illegal. The respondent claimed in this regard that Notice 459 did not apply to The Villa and Zambezi. He

neglected to explain why it did not apply. In this assertion, the respondent's view is bolstered by Swanepoel, who also failed to substantiate why the Notice would not apply to The Villa and Zambezi.

17.6 The respondent relied on the approval of the prospectuses by the relevant authorities, and that Sharemax was licensed by the FSB. The respondent blames the South African Reserve Bank (SARB) for the failure of the syndication.

17.7 The respondent denied the allegation that he had no appreciation for the risks, because he maintained that these risks were set out in the prospectus, and were explained to the complainant.

[18] The respondent stated that his conduct ought to be tested against that of a reasonable FSP in similar circumstances, including the question of whether he acted negligently. It was therefore incorrect for this Office to, *ex post facto*, analyze the prospectus and pick holes in it. In addition, it should be established that such negligence caused the alleged loss of the complainant. In the respondent's view, negligence does not lie in the "simple breach of an administrative requirement" in the Code. In the respondent's view, non-compliance with the Code can only lead to liability if the non-compliance was the direct consequence or cause of the alleged loss.

D. FINDINGS

[19] Despite the overwhelming evidence provided in the recommendation letter which included a summary of the relevant prospectuses, the respondent is still

of the view that none of the representations in the prospectus have been proven false or incorrect.

[20] The respondent fails to appreciate the risk inherent in the said investments. He relied on the "track record" of Sharemax and blames the SARB for the failure of Sharemax.

[21] The respondent (through the opinion of Mr Anton Swanepoel) incorrectly interprets "due diligence" to be an expert investigation typically encountered in corporate mergers and acquisitions. This interpretation is not correct. The Act and Code requires an FSP to act with due diligence. This one finds in collectively reading sections 2, 7 and 8 of the Code, read with Section 16 of the Act. "Due diligence" in law means the care that a reasonable person exercises to avoid harm to other persons, or their property. Here, the test is of a reasonable FSP. This Office did not in any way unreasonably raise the standard; it only called for the standard which is required by the Act and the Code[9].

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

[9] See the decision of the Board in Prigge; case number FAB 8/2016 at paragraph 42

possessed and exercised at the time by the members of the branch of the profession to which the practitioner belongs."

It cannot be argued that this standard is too high.

[22] The respondent did not comply with section 9 of the Code, in that he failed to keep a record of advice[10], despite his contention that he completed such a record for all his clients. The respondent relied on the prospectus and application forms signed by the complainant to form part of his compliance documentation. This is not compliance with Section 9 of the Code. The Appeals Board have found that the Ombud would in appropriate circumstances be entitled to draw an adverse inference against an FSP who failed to keep such a record[11].

[23] Section 9 of the Code must be read with section 8 (1) and (2). This latter sub-section places a duty on an FSP to ensure the investor is in a position to make an informed decision. Section 9 requires that the provider, after collecting relevant information from the client and analysing it, identify a product that will suit the client's risk profile and circumstances. The provider has to record the financial products that were considered, as well as a summary of why the recommended product is most likely to suit the client's circumstances.

[24] Standard documentation prepared by a product provider that are merely presented to clients for signature, cannot meet the requirements of section 9. The record in section 9 requires evidence that section 8 (1) was adhered to.

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[10] What the respondent provided with his response, was an example of a record of advice of another client, on which he removed the particular client's name.

[11] ACS Financial Management CC and Others v PS Coetzee and Others (FAB 1 / 2016)

Advice is relative to the circumstances of each client, and the prospectus and forms that the respondent is referring to, can hardly be the record contemplated in section 9 of the Code.

[25] I also refer to the respondent's non-compliance with section 8 (1) (d) of the Code, which deals with the replacement of an existing financial product held by a client. From the respondent's own version, the complainant was not satisfied with the returns she was receiving on her money market account, and was not interested in unit trust investments. None of the aforesaid was noted in a record of advice, nor was there an explanation or comparison of the different products or a disclosure of the actual and potential financial implications of moving from a money market fund to a product of the nature of a Sharemax property syndication. The advice can hardly be said to be appropriate.

[26] The respondent further relied on a statutory notice[12] signed by the complainant, which contains the following warnings under point 6:

- *It is very important that you are quite sure that the product or transaction meets your needs and that you have all the information you need before making a decision.*
- *It is recommended that you discuss with the intermediary or insure the possible impact of the proposed transaction on your finances, your other polices or your broader investment portfolio…..*

[27] The respondent does not state the relevance of the statutory notice, given that the products were sold to complainant.

[12] The notice is entitled "Statutory Notice to long-term insurance policyholders". Interestingly, the notice refers aggrieved parties to the FSB and the Long Term Insurance Ombud, but not to the FAIS Ombud.

[28] What the section in the statutory notice seems to seek, is to absolve the respondent from liability of the provisions of the Code. This statement is in itself reckless and offensive to several provisions of the Code (sections 2, 3 (1) (a), 7 (1)[13] 8 (1) (a) to (c), and 9). This statutory notice is a futile attempt to transfer the duties placed on the provider by the Code on to the complainant.

[29] The complainant relied on the expertise of the respondent to guide her. On a balance of probabilities, had the complainant been fully aware of the risks inherent to the investments, she would not have placed such a substantial amount of money at risk. The respondent has not provided any evidence to suggest that the complainant was knowledgeable in financial products, nor did he demonstrate that the complainant had previously indulged in risky investments of similar nature. It is disingenuous of the respondent to rely on the assurance the complainant allegedly had knowledge of the risk, because her father previously invested in the same scheme.

E. CAUSATION

[30] The respondent stated that ordinarily legal liability must be proven, namely that the FSP acted not only negligently, but caused the complainant's loss and that the negligence does not lie in the breach of a simple administrative requirement.

[31] The principles of causation were explained in *International Shipping Co (Pty) Ltd v Bentley*[14]*:*

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[13] The section calls upon providers other than direct marketers to provide (a) '*reasonable and appropriate general explanation* of *the nature and material terms of the relevant contract* or transaction to a client, *and generally make full and frank disclosure* of any information *that would reasonably be expected to enable the client to make an informed decision*.

[14] 1990 1 SA 680 (A) [700 E-G]

"The enquiry as to factual causation is generally conducted by applying the so-called 'but-for' test, which is designed to determine whether a postulated cause can be identified as a causa sine qua non of the loss in question".

[32] As was explained by the court in *Minister of Finance & others v Gore NO*[15], "*Application of the 'but for' test is not based on mathematics, pure science or philosophy. It is a matter of common sense, based on the practical way in which the ordinary person's mind works against the background of everyday-life experiences".*

Or, as was pointed out in similar vein by *Nugent JA in Minister of Safety and Security v Van Duivenboden*[16]*:*

"A plaintiff is not required to establish the causal link with certainty, but only to establish that the wrongful conduct was probably a cause of the loss, which calls for a sensible retrospective analysis of what would probably have occurred, based upon the evidence and what can be expected to occur in the ordinary course of human affairs rather than metaphysics[17]*".*

[33] Had the respondent truly appreciated what he was advising the complainant to invest in, he would have steered her in a different direction. Not only was the loss to investors reasonably foreseeable, it was inevitable.

[34] The complainant's loss was not caused by the intervention of the Reserve Bank or the FSB, but by the respondent's inappropriate advice. If the respondent had adhered to the Code, no investment would have been made in Sharemax.

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15 Minister of Finance v Gore NO 2007 (1) SA 111 (SCA) para 33.

16 Minister of Safety and Security v Van Duivenboden 2002 (6) SA 431 (SCA) ([2002] 3 All SA 741) para 25.

17 Crafford v South African National Roads Agency Limited (215/2012) [2013] ZASCA 8 para 7

There was a substantial risk that the complainant could lose her money. This risk was always evident from the prospectus. That the risk actually materialized for whatever reason, is not important. Otherwise the whole purpose of the Act and the Code would be defeated. Every FSP can ignore the Act and Code in advising clients and hope that the investment does not fail. When the risk materializes and results in loss, they can hide behind unforeseeable conduct on the part of product providers.

[35] The findings made in the recommendation letter are hereby confirmed.

F. THE ORDER

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

1. The complaint is upheld.

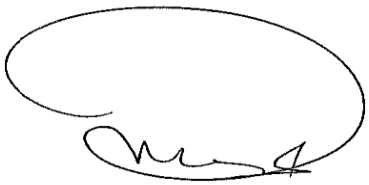
2. The respondents are ordered to pay the complainant, jointly and severally, the one paying the other to be absolved, the combined amount of R1 200 000[18].

3. Interest on this amount at a rate of 10.25% per annum from the date of determination to date of final payment.

4. Complainant, upon full payment, is to cede her rights, title and any further claims in respect of this investment to respondent.

[18] This amount comprises of three investments in The Villa of R300 000, R300 000 and R600 000, which individually make different and separate causes of action.

DATED AT PRETORIA ON THIS THE 28th DAY OF MARCH 2018.



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OMBUD FOR FINANCIAL SERVICES PROVIDERS