THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

CASE NUMBER: FAIS 00039/11-12/GP 1

In the matter between:-

Gerbrecht Elizabeth Johanna Siegrist	**Complainant**
and	
Cornelius Johannes Botha T/A	
C J Botha Finansiële Dienste	**1st Respondent**
Sharemax Investments (Pty) Ltd	**2nd Respondent**
FSP Network (Pty) Ltd	**3rd Respondent**
Gerhardus Rossouw Goosen	**4th Respondent**
Johannes Willem Botha	**5th Respondent**
Dominique Haese	**6th Respondent**
Andre Daniel Brand	**7th 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] The complainant is Gerbrecht Elizabeth Johanna Siegrist, an adult female pensioner, who resides at Tigerpoort.

[2] First Respondent is Cornelius Johannes Botha Trading as C J Botha Finansiële Dienste, of 212 Camellia Avenue Murrayfield. First respondent is a licensed Financial Services Provider (FSP nr: 24152).

[3] Second respondent is Sharemax Investments (Pty) Ltd ("Sharemax"), a company registered in accordance with the laws of South Africa with registration number 1998/019038/07. Sharemax is a licensed Financial Services Provider (FSP nr: 6153) and its registered address is 105 Club Avenue, Waterkloof Ridge, Pretoria. Sharemax is the product provider and promoter of the investments in question.

[4] Third respondent is FSP Network (Pty) Ltd t/a Unlisted Securities South Africa ("USSA"), a company registered in accordance with the laws of South Africa with registration number 2002/021751/07. USSA is a licensed Financial Services Provider (FSP nr: 6152) and its registered address is 993 Swaartbaars Street, Garsfontein.

[5] Fourth respondent is Mr Gerhardus Rossouw Goosen ("Goosen"), an adult male and Director of Sharemax and USSA. Goosen is joined in this matter as a Director and compliance officer of Sharemax and USSA and the Key Individual of the latter. He resides at 18B Vlakvoëltjie Street, Rooihuiskraal.

[6] Fifth respondent is Mr Johannes Willem Botha ("Botha"), an adult male and Director of Sharemax. Botha is joined in this matter as a Director of Sharemax. He resides at 36 Glendower, Woodhill Estate, Pretoria.

[7] Sixth respondent is Ms Dominique Haese ("Haese"), an adult female and Director of Sharemax. Haese is joined in this matter as a Director, Key Individual and representative of Sharemax. She resides at 10 Oxford Street, Lynnwood, Pretoria.

[8] Seventh respondent is Andre Daniel Brand ("Brand") an adult male and director of Sharemax. Mr Brand is joined in this matter as a Director of the second respondent. He resides at 150 Langenhoven Street, Constantia Park, Pretoria.

[9] The fourth to seventh respondents are also interested parties as they are directors of Sharemax Zambezi Retail Park Investments (Pty) Ltd ("Zambezi Investments") and Sharemax Zambezi Retail Park Holdings Ltd ("Zambezi Holdings").

B. INTRODUCTION

[10] It is now a well published fact that the property syndication scheme, Zambezi Holdings and The Villa Retail Park Holdings Limited ("The Villa") , promoted by the second respondent collapsed and that investors believe that they have lost their invested capital.

[11] The complaint relates to the role of all the respondents in relation to the financial services rendered in promoting Zambezi Holdings as an investment

to members of the public. The principal complaint is that the investment in Sharemax was inappropriate for the profile and needs of the complainant and there was a failure to comply with the Act and the Code.

C. THE ISSUES

[12] The following are issues for determination:

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

12.2 If it is found that the first respondent did render the financial service negligently and/or failed to comply with the Act and Code, whether it was such conduct that caused the complainant loss; and

12.3 What is the role and consequences of the second to seventh respondents conduct in this investment as licensed FSPs, product providers and principals in terms of section 13 of the Act?

12.4 What are the consequences of any breach of the law by the second to seventh respondents?

Summary of Findings

[13] Due to the length of this determination, I deem it necessary to set out, briefly, the main findings. They are as follows:

13.1 The first respondent provided financial services to the complainant as defined in section 1 of the Act.

13.2 In providing such service the first respondent committed breach of the Act and Code. The Sharemax investment was inappropriate for the complainant.

13.3 Such breach caused the complainant loss.

13.4 In providing such service the first respondent was not licensed to do so and at all material times was acting as a representative of FSP Network, as contemplated in section 13 of the Act.

13.5 FSP Network was set up to market Sharemax products through a network of brokers, most of who were acting as section 13 representatives of FSP Network.

13.6 FSP Network is responsible for the consequences of the conduct of their representatives who almost without fail targeted pensioners.

13.7 Sharemax was a licensed FSP and subject to the Act and Code.

13.8 In marketing the Sharemax investments, Sharemax provided financial and intermediary services as defined in section 1 of the Act.

13.9 FSP Network was nothing more than an extension of Sharemax. FSP Network did not conduct its business of marketing Sharemax's products as an independent broker acting at arm's length.

13.10 Sharemax failed to make a full disclosure of the scheme in the prospectus and investors were misled.

13.11 Investors' funds were lent to the developer in terms of an agreement that was not disclosed to investors, which agreement contravened provisions of the GG.

13.12 The effect was that Investors were paid interest out of their own funds.

13.13 The directors of Sharemax and FSP Network were aware of the fact that the scheme was both illegal and not commercially viable and yet they recklessly took investors' funds. Investors whom within their knowledge were almost without exception pensioners who could ill afford the inevitable loss.

13.14 The directors of FSP Network and Sharemax must be held personally liable for the complainant's loss.

D. FACTUAL BACKGROUND

[14] This determination concerns the property syndication known as Zambezi Retail Park. The syndication was promoted by Sharemax, the second respondent, through the services of USSA, the third respondent, and independent brokers. On 13 September 2005, Sharemax was granted a licence to act as an Authorised Financial Services Provider in terms of section 8 of the FAIS Act. In terms of the licence, Sharemax is authorised as a Category 1 Financial Services Provider to render advisory and intermediary services with regard to Securities and Instruments, shares (1.8) and debentures (1.10).

[15] In terms of the documents furnished, Sharemax issued prospectuses regarding the Zambezi investments. These prospectuses were registered with the Registrar of Companies in terms of section 155 of the Companies Act 61 of 1973.

[16] According to the prospectus, the appointed Directors of Zambezi are Botha, Brand, Goosen and Haese. These individuals are also the Directors of the promoter and product provider, Sharemax. In addition, Goosen being a Director of Sharemax and Zambezi was also the Director, Key individual and compliance officer of USSA. Rinate Goosen also served as compliance officer of USSA.

[17] USSA was established to enable independent representatives in the financial services industry to market and sell the unlisted shares of Zambezi to members of the public. Most of the representatives listed under USSA did not have a licence to render advice or intermediary services in respect of unlisted shares in their own capacity. Hence USSA facilitated this for them under its licence at a monthly contribution.

[18] The appointed attorneys of Zambezi are Weavind and Weavind. According to the information contained in the prospectus all investments are paid to the attorneys and will be retained in an interest bearing account. Ten per cent of the invested amount will be released to the promoter in order for them to pay commissions. This office recommends that the Law Society should investigate the trust account of this firm of attorneys in order to establish how and under what instructions the funds were paid out of trust. We also believe that it

would be prudent to keep the fidelity fund informed. I deal with this issue in more detail later in this determination.

[19] The first respondent is a licensed financial services provider, licensed by the FSB with license number FSP 24152. The license was issued on the 9th February 2006. The significance of the license is that the first respondent was only authorised to sell and give advice in respect of Category 1 financial products and related services which excludes category 1.8 and 1.10. This means that the first respondent did not have a license to sell or provide intermediary services in respect of the type of product the latter sold to the complainant, namely, unlisted securities in Sharemax property syndication.

[20] The first respondent marketed the Sharemax financial product as a representative of the third respondent; trading as Unlisted Securities South Africa (USSA).USSA was licensed by the FSB to market category 1.8 and 1.10 products. USSA in turn authorised brokers such as the first respondent to market such a category, in terms of section 13 of the Act.

E. THE COMPLAINT

[21] The complainant is 67 years old and describes herself as a pensioner. She is suffering from poor health and is unemployable. Her late husband left her an amount of money which was intended to provide her with an income. The amount of money available to her was modest and all of it was invested with institutions such as Sanlam. An amount of approximately R648 000 was invested for her. She received a small income from these investments which

appeared to be inadequate for her needs. The complainant has no other source of income; she does not receive any pension.

[22] The complainant was introduced to the first respondent who told her about the Sharemax investment. What attracted the complainant to the Sharemax investment was the prospect of receiving a higher monthly income. The first respondent informed her that she could receive between 10% and 12%, which was substantially more than what her current investments were providing.

[23] It must be said that the complainant's funds were invested in long term investments such as Sanlam Stratus, Sanlam Glacier, ABSA money market and a small offshore investment.

[24] By all accounts the complainant was not a person who could take any risks with her capital; it was all she had. She states that she made this very clear to the first respondent. A basic financial profiling and needs analysis will show that the complainant was a conservative investor who had no tolerance for loss of any portion of her capital.

[25] The complainant states that she informed the first respondent in no uncertain terms that she wanted capital growth and a guarantee that her capital will be safe. This is borne out by the first respondent's documentation, such as the advice record which identified her needs as "*vereis 'n belegging met a*

gewaarborgde inkomste van 10% en 4% kapitaalgroei"[1]. The first respondent does not dispute that his instructions were that the "capital must be safe"

[26] The first respondent advised the complainant to withdraw all her existing investments and to invest in Sharemax. As a result of this advice the complainant, through the first respondent, invested R460 000 in Sharemax Zambezi Retail Park – prospectus 2, on the 2nd April 2008. On the 15th July 2008 complainant invested a further R120 000 in Sharemax Zambezi Retail Park – prospectus 4. In less than 2 years later the complainant stopped receiving income from her investments and has now learned that her capital was never guaranteed.

[27] The complainant is now without income and is destitute. She survives on the charity of her children. It is also her complaint that the first respondent withdrew her existing investments and "put all her eggs in one basket".

[28] The complainant states, in her formal complaint to this office, the following about the conduct of the first respondent:

" 1. Die bepalings van die FAIS wet is oortree of nie nagekom nie;

2. 'n Finansiele diens is opsetlik of nalatig aan my gelewer waardeur ek skade gely het of waarskynlik sal ly; en

3. Ek is onregverdig behandel."[2]

[1] Translation - requires an investment with a guaranteed income of 10% and capital growth of 4%.

[2] Translation – 1. The provisions of the FAIS Act were contravened or not adhered to;
2. A financial service was wilfully or negligently rendered to me which has caused damage or is likely to cause damage;
3. I was treated unfairly.

[29] The complainant states that the first respondent advised her that the Sharemax option was in her best financial interest as :

- Ten per cent guaranteed income and 4% growth on capital was payable on the investment;
- The shares could be sold whenever she wanted if sold through Sharemax;
- If she wanted to withdraw capital after one year then no penalties will apply; and
- She will make money if she sells after 3 to 4 years.

Of significance, is that the first respondent does not actually dispute that he gave her this advice. As will appear later, Sharemax did not actually promise this and the advice was entirely inappropriate.

[30] The complainant was impressed with the first respondent who persuaded her that he is a well-qualified and experienced financial services provider. She was convinced that she could rely on his advice as he pointed out to her that he was registered and approved by the FSB. She was further impressed that the first respondent, according to him, was a specialist in retirement investment and that he had a special interest in pensioners.

[31] The complainant believes that she is now financially destitute due to the first respondents conduct and seeks compensation in terms of the Act.

F. FIRST RESPONDENT'S RESPONSE

[32] In response to the complaint, the first respondent provided this office with the contents of his file and gave a written explanation. His immediate reaction was that:

32.1 the complainant was merely complaining because she was unhappy with the performance of her investments;

32.2 the complainant "specifically instructed" him to invest in Sharemax;

32.3 the complainant was informed of the risks and signed the necessary contracts in terms of the Code;

32.4 the complainant is trying to show that she is a victim by making false accusations against him; and

32.5 he did his work according to the Code and the complainant's accusations are false.

In amplification of this the first respondent referred to various documents in his file.

[33] The first respondent dealt with the allegation that he inappropriately took existing investments and placed them with Sharemax. He explained that the complainant personally withdrew these funds and understood the applicable penalties. The respondent however did not deal with the possible noncompliance with the provisions of section 8 (1) (d) of the Code. This office was unable to find, in the records of the first respondent, evidence of such compliance. The first respondent however denies that he advised the complainant to invest all her money in Sharemax.

[34] The issue of financial profile is important. In his response the first respondent refers to a document prepared by his office which is a questionnaire on client risk profile. The document tells the following about the complainant:

34.1 she was looking for post-retirement planning and not just investment planning;

34.2 the complainant's expectation was for a 10% income guaranteed, with 4% capital growth;

34.3 she indicated that she did not want to risk any portion of her capital and was rated "konservatief" in the form.

[35] In keeping with this profile the complainant, in a form called "client instructions", gives the following as "specific instructions":
*"Bele my vrywillege fondse waar **kapitaal veilig is** en 'n inkomste van 10% gewaarborg is. Daar moet ook 4% **kapitaalgroei wees**"*[3](my emphasis).

[36] The first respondent states that the complainant knew about the Sharemax product from her sister. The complainant's income was not adequate and she specifically instructed him to invest in Sharemax. In the same breath the first respondent admits that the complainant wanted an investment where her capital will be safe.

[3] Translated – Invest my voluntary funds where capital is safe and income of 10% is guaranteed. There must also be capital growth of 4%.

[37] The first respondent submitted that the complainant had all the necessary information in order to make an informed choice. In this regard the first respondent points out that the complainant was provided with the disclosure document and the prospectus. The disclosure document was signed by the complainant; this is dealt with in more detail later. The prospectus is a 94 page document containing complex and detailed financial information. This is not a document that a lay person, in particular a pensioner, will understand. Equally it is unlikely that the complainant read both the disclosure document as well as the prospectus before signing. All the documents were signed on the same day ie 13th March 2008 (for the first investment). There is no evidence that the complainant was given an opportunity to read and understand these complex documents. Nor is there any evidence that the first respondent took the complainant through these documents. The mere handing over of documents to a client does not meet the requirements of the code to make proper disclosure. As will appear later, the first respondent himself did not understand these documents in the first place.

[38] The fact that the complainant signed the disclosure document indicates that she had no understanding of the Sharemax investment. She probably did not read the document, as the disclosure records that capital is not guaranteed, nor did it guarantee income. To confuse matters even further, page one of the prospectus appears to contradict the disclosure document. The prospectus, under the heading "investment summary" states; "initial income yield: 10% guaranteed" and "Guarantee plan (option B): Capital guaranteed after 5 years".

[39] The first respondent does not appear to have explained this to the complainant. The first respondent concludes that the complainant had all the necessary information to make an informed choice. He states that the complaint was "false and unfair".

[40] Predictably the first respondent did not offer the complainant any other comparable product. He admits that only Sharemax was offered and explains this on the basis that only Sharemax complied with complainant's instructions.

G. RESPONSE FROM USSA

[41] The complainant's complaint was forwarded to USSA and a response was received from Goosen who, according to the records of the FSB, is one of the key individuals of USSA and he was also its compliance officer and director. The reason the complaint was directed at Goosen and not the liquidators of FSP Network is because the complaint relates to a financial service that was rendered in 2008.

[42] Goosen's response was to place on record that the complainant was not a client of USSA but a client of the first respondent. Goosen also points out that the complaint was lodged against the first respondent and not against USSA. However in the same breath Goosen makes the following statement: *"Mr C J Botha, with id number 730213 5048 083 was a representative on the register of FSP 6152 from 4 May 2006 to 30 September 2010".* This simply means that first respondent was a representative of USSA in terms of section 13 of the Act. This in turn means that USSA was responsible for the conduct

of the First respondent where the latter was marketing Sharemax products. The consequence of this is that USSA cannot escape liability on the basis that the complainant is not their client. First respondent did not have a licence to market this product and was only able to do so legally through being appointed as a representative of USSA; which did have a licence.

[43] Goosen also refers to the disclosure document and relies on it to escape liability. Indeed, as Goosen points out, this document makes it very clear that the Sharemax product is considered a risk to capital, that income is not guaranteed and the shares are unlisted. Goosen relies on the disclosure to suggest that the complainant went into this investment having been informed of the risk.

[44] Goosen does not appear to appreciate the provisions of section 13 of the Act. USSA was responsible for training the representatives in the product so that the latter could give competent advice to the investing public. The representative is also supervised by USSA. There was therefore a clear duty on USSA, in terms of the Act and Code, to train representatives that the Sharemax product represents risks that cannot be tolerated by conservative investors. In plain language, USSA was under a duty to train representatives that Sharemax was not suitable for pensioners or any other investor who cannot afford to lose any part of their capital.

[45] Equally there was a duty on USSA to inform their representatives to persuade pensioners that Sharemax was not for them. None of this was done; on the contrary it appears that the representatives were encouraged to target these

vulnerable pensioners with promises of income between 10% and 12 %. It comes as no surprise that USSA did not comply with section 13 as there was a clear conflict of interest. USSA was set up as an arm or extension of Sharemax and was done with the sole purpose of enabling the marketing of Sharemax products. Again, contrary to the Code, this conflict of interest was not disclosed to the investors. Nor were the representatives instructed to disclose to investors that they were unlicensed to market Sharemax and that they were under the supervision of USSA which was an extension of Sharemax, the product provider. This office could find no record that the first respondent made a disclosure of this conflict of interest to the complainant.

[46] Goosen also points out that complainant was not a client of USSA and the latter rendered no financial services to complainant. He also argues that the complainant did not file a formal complaint against USSA and therefore this was not a complaint against USSA. There is no substance to this as section 13 renders USSA responsible for the conduct of their representatives. In addition, the definition of "complaint" in section 1 of the Act includes both FSPs and representatives. It also comes as no surprise that the complainant did not include USSA in her complaint. She simply did not know that she could do this. In any event section 27 (4) of the Act requires this office to inform all interested parties to the complaint.

In any event one would have expected USSA's own representative, first respondent, to refer this complaint to Goosen.

[47] Goosen also complains that Rule 5 (d) of the Rules on Proceedings of this Office was not complied with. He states that there was no proof that the complainant endeavoured to resolve the matter with the first respondent. Again there is no substance in this. USSA in terms of section 13 was supervising the representative and at all material times knew that there was no prospect of resolving the matter.

[48] As far as USSA itself is concerned, there was equally no prospect of them resolving the matter with any of their clients introduced through their own supervised representatives. On Goosen's version, *"FSP Network is dormant, has closed its doors and has no staff and has no contract with either Mrs Siegrist or Mr Botha."* In addition, as from the 30th September 2010, FSP Network's licence lapsed in terms of section 11 (1) (c) of the Act. This Office has also learned that the company is in liquidation.

[49] It is worth noting that USSA conveniently closed its doors and disappeared without complying with the provisions of section 38 of the Act. This section provides :

"No-

(a) application for the acceptance of the voluntary surrender of the estate, in terms of section 3 of the Insolvency Act, 1936 (Act No. 24 of 1936), of;

(b) special resolution relating to the winding-up, as contemplated in section 349 of the Companies Act, 1973 (Act No. 61 of 1973), and registered in terms of that Act, of;

(c) written resolution relating to the winding-up, as contemplated in section 67 of the Close Corporations Act, 1984 (Act No. 69 of 1984), and registered in terms of that section, of; and

(d) voluntary closure of business by,

any authorised financial services provider, or representative of such provider, and no special resolution in terms of the constitution of such a provider or representative which is not a company, to close its business, have legal force -

(i) unless a copy or notice thereof has been lodged with the registrar and the registrar has, by notice to the provider or representative concerned, as the case may be, declared that arrangements satisfactory to the registrar have been made to meet all liabilities under transactions entered into with clients prior to sequestration, winding-up or closure, as the case may be; or

(ii) if the registrar, by notice to the provider or representative concerned, as the case may be, declares that the application, resolution or closure, as the case may be, is contrary to this Act."

It is time that this section was applied by regulators and by our courts It is currently too easy for FSPs to close up and avoid investors, creditors and regulators.

H. USSA

For purposes of this determination, it is important to deal with USSA and the role the latter played in this investment.

[50] A company called FUTURE INDEFINITE INVESTMENTS 188 (PTY) LTD T/A GR GOOSEN FINANCIAL SERVICES, by special resolution, changed its name to FSP NETWORK (PTY) LTD on the 21st October 2004. This was Goosen's company. It is this company that began trading as USSA. According to the records of the regulator, Goosen was the contact person, compliance officer and one of the key individuals of FSP NETWORK (PTY) LTD. Goosen was a director of the first company that changed its name, he also at that time happened to be a director of Sharemax. The compliance officer for USSA was also a Mrs C G Goosen also known as Rinate Goosen.

[51] USSA, it turns out, was nothing more than a marketing arm of Sharemax. It was set up for the sole purpose of marketing Sharemax products through a network of brokers. This company did not market any other financial product. Equally interesting is that both Sharemax and USSA applied for their respective licences with the FSB at the same time. The FSP number for Sharemax is FSP 6153 and USSA is FSP 6152. It is also worth noting that the application for compliance officer forms for both Sharemax and USSA was

filled out in the same handwriting. USSA was by no stretch of the imagination an independent financial services provider. The directors, who are respondents in this matter, of both USSA and Sharemax cannot now hide behind a corporate veil.

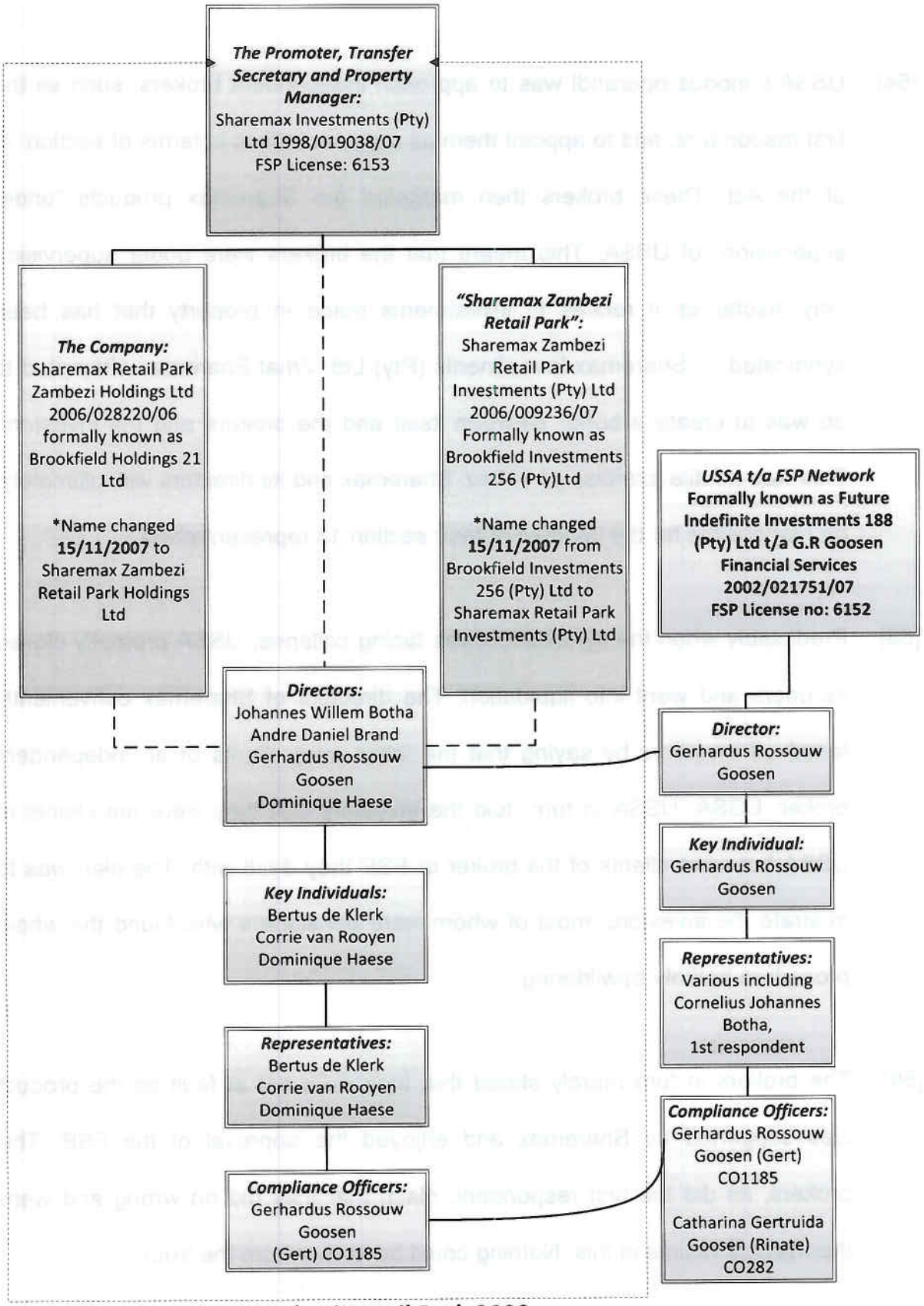
Sharemax Corporate veil

[52] The second to seventh respondents submitted that Sharemax and USSA were separate entities and conducted business at arm's length. For reasons already stated, I found that this was not the case and that USSA was merely an extension of Sharemax. The objective, and undisputed, facts are as follows:

- The two entities, Sharemax and USSA, applied for their Compliance Officer applications together and the FSB 6 form was filled in by the same person. The same hand writing appears in both application forms. This is too much of a co-incidence.
- Goosen is a director and compliance officer of both Sharemax and USSA he is also the key individual in USSA;
- Goosen joined Sharemax in August 1998 and was the latter's Provincial Marketing Manager.
- At the time of marketing this investment, Goosen was the Compliance Director of Sharemax responsible for implementing, establishing and maintaining a risk management framework which included the establishment of a compliance function at all offices of Sharemax.

- At no time, since the incorporation of Sharemax and USSA, did Goosen even attempt to sever ties with either Sharemax or USSA. On the contrary, he was very much a part of the management structure of both.
- Since its inception, USSA marketed only Sharemax products and offered no other financial product.
- All of USSA's registered representatives were only allowed to market Sharemax products.
- All of USSA's representatives were bound in terms of a contract to market only Sharemax products.
- All the USSA representatives were furnished with a "Sharemax Compliance Manual" which stated how the product should be sold.
- In marketing the Sharemax product, representatives of both Sharemax and USSA, made joint presentations at seminars and road shows.
- The section 13 representatives of USSA treated USSA as part of Sharemax.
- Marketing costs of 4% was also paid to Sharemax and not to USSA, notwithstanding that the bulk of the investments came from USSA representatives.
- There was a clear community of interests between Sharemax and USSA.

[53] I set out here an organogram which demonstrates that USSA and Sharemax were not separate entities working at arm's length; in fact they were joined at the hip.



Sharemax Zambezi Retail Park 2008

[54] USSA's modus operandi was to approach independent brokers, such as the first respondent, and to appoint them as representatives in terms of section 13 of the Act. These brokers then marketed the Sharemax products "under supervision" of USSA. This meant that the brokers were under supervision only insofar as it relates to investments made in property that has been syndicated by Sharemax Investments (Pty) Ltd. What Sharemax attempted to do was to create a buffer between itself and the brokers and the investors. This was a futile exercise as in law, Sharemax and its directors will, ultimately, be responsible for the conduct of their section 13 representatives.

[55] Predictably when the syndication was facing collapse, USSA promptly closed its doors and went into liquidation. The directors of Sharemax conveniently faced off investors by saying that the latter were clients of an independent broker, USSA. USSA in turn, told the investors that they were not clients of USSA but were clients of the broker or FSP they dealt with. The plan was to frustrate the investors, most of whom were pensioners who found the whole procedure entirely bewildering.

[56] The brokers in turn merely stated that they were not at fault as the product was supported by Sharemax and enjoyed the approval of the FSB. The brokers, as did the first respondent, claim that they did no wrong and were themselves victims in this. Nothing could be further from the truth.

[57] On a proper application of the Act and Code both USSA, in terms of section 13, and Sharemax, as licensed FSP, product provider and the controlling spirit

behind USSA are responsible for the conduct of the brokers who cause loss through their "supervised" activities. Sharemax, it must be remembered, also provided intermediary services as defined in section 1 of the Act in respect of this investment.

[58] Significantly, Goosen, in his response to this office stated the following about USSA:

"When the FAIS Act became effective on 30 September 2004, USSA was created as a vehicle through which brokers could obtain the necessary experience for financial products 1.8 and 1.10 (specifically / exclusively in respect of unlisted investments promoted by Sharemax Investments (Pty) Ltd) with the ultimate aim that once the broker meets the experience requirements, they could submit an application to the FSB to have financial products 1.8 and 1.10 added to their own FSP license. Once they have obtained financial products 1.8 and 1.10 on their own license, they would resign from USSA and carry on rendering financial services to their clients under their own FSP license. The clients always belonged to the representative and never to USSA. USSA provided the brokers with a vehicle through which they could conduct their business within a legal framework and it gave them the advantage of earning income and providing their clients with an additional range of financial products."

I must assume that when Sharemax set up USSA, they, including Goosen, were familiar with the provisions of section 13 of the Act. I must equally assume that both Sharemax and USSA were aware of their responsibilities

and obligations as principals. The time has come for USSA and Sharemax to accept that responsibility.

I. THE DISCLOSURE DOCUMENT

USSA provided each of its "supervised" brokers with a disclosure document which each investor had to sign as part of the procedure in making an investment in Sharemax. The content of this document is significant.

[59] The disclosure document records that the broker or FSP is a representative of USSA and that the former is "*rendering financial services under guidance/instruction/supervision of a key individual or other representative until the minimum prescribed level of experience has been obtained*". This can only mean that the FSP in question, who does not have a license to market Sharemax financial product, is acting as a duly appointed representative of USSA as contemplated in section 13 of the Act.

[60] The disclosure document notes that the compliance officer is "Gert Goosen", the same Goosen who is a director of Sharemax. This fact is not disclosed to the investor.

[61] There is a disclosure that the representative will receive 6% commission from Sharemax on the investment.

[62] The document records that USSA "*is responsible for those activities performed by the representative...*" This is compliance with the Act; however

the actual effect of this was not explained to investors. In particular the extent of this responsibility was not explained nor was it accepted by USSA.

[63] The disclosure makes it very clear that the representative and USSA are marketing only Sharemax products.

[64] Significantly, under the heading "*GENERAL INVESTMENT RISK...*" the document states that "*with property syndication investments there is a risk that both the capital and the income could not materialise.*" The document further warns that the investment "*is not liquid as the ability to transfer the units is restricted by the absence of a market for those units/shares.*"

[65] This document describes Sharemax as *"a newly formed company without any trading history which can be used to evaluate the likely performance of the product supplier and its ability to achieve its objectives."*

[66] The disclosure makes it very clear that *"an investment in unlisted shares / units / debentures is not a liquid investment.*"

[67] Thereafter the document provides for the investor to sign an acknowledgement that the latter understands the risks in the investment. The terms of this acknowledgement are significant.

[68] This document begins with the investor declaring that he/she is "*comfortable*" investing in a property syndication structure. The investor then agrees that

"there is a substantial risk that I may not be able to sell my shares / debentures should I wish to do so in future"

[69] The investor is then expected to acknowledge the following fact; "*USSA representatives are NOT authorised to render advice or intermediary services in respect of any other financial product, as defined by the FAIS Act."*

[70] The investor then states that *"in view of the aforementioned limitation on the financial products, a full needs analysis in respect of my financial needs could not be undertaken. There may be limitations on the appropriateness of the advice provided."*

[71] The investor then confirms the following: *"the repayment of the capital and or the income is NOT GUARANTEED, UNLESS IT IS EXPLICITLY STATED IN THE PROSPECTUS THAT IT IS GUARANTEED. The performance of the property syndication investment is NOT GUARANTEED. The units / shares of the property syndication investment are unlisted and should be considered as a risk capital investment".*

[72] The significance of the disclosure document is that it states in no uncertain terms that the Sharemax investment is a high risk investment not suitable for pensioners and anyone who cannot afford to lose their capital.

[73] The document is also a stark reminder to all representatives that the Sharemax product is not appropriate for investors who cannot afford to lose

their capital and who have no means to replace lost capital. This is also not a product that can guarantee capital growth.

[74] Any competent FSP who reads this document will understand immediately, even if they do not possess a license to sell this product, that Sharemax is a high risk investment. In the light of this document, there can be no basis for any representative to consider the Sharemax investment as anything other than high risk. At the very least, any broker will have to apply the basic advice that one should not risk capital for higher income, especially for those investors who have nothing other than the invested capital.

[75] The Code requires an FSP to recommend a financial product that is appropriate for the investor and is compatible with such investor's needs and financial risk profile or tolerance. Sharemax is certainly not a product that is appropriate for a pensioner who cannot afford to lose their capital and who has no prospect of replacing any lost capital. This, on Sharemax's own assessment of risk in their product.

[76] It must equally be said that it is inappropriate for product providers who market high risk investments to recklessly accept investments from people who should not be purchasing such high risk products.

[77] Sharemax was at all material times, a licensed FSP with a license to market unlisted shares and debentures. I must assume that they appreciated the provisions of the Code and in particular the responsibility of assisting investors to invest in a product that is appropriate. At all material times Sharemax,

through its directors, key individuals and compliance officers, were aware that investment in their property syndication was entirely inappropriate for pensioners and people who were looking for their capital to be guaranteed. Nevertheless Sharemax recklessly, and without any concern for the provisions of the Code, accepted money from the most vulnerable investors in society. They found themselves in a conflict of interest and failed to manage this according to the Act and Code.

[78] Of serious concern to this Office is that it must have been clear to the directors of both Sharemax and USSA that the Zambezi and Villa projects were not commercially viable, yet they continued to rake in money from unsuspecting investors. This is nothing short of reckless conduct, both at common law and in terms of the Companies act. Again, the directors of these companies cannot hide behind a corporate veil.

[79] An aspect that is of concern to me is the manner in which Sharemax marketed the investment through USSA and the latter's network of brokers. Most of the brokers were not licensed in their own right to sell the Sharemax product. They were only authorised to do so as section 13 representatives of USSA. In both the contract with the representatives and in the disclosure document, USSA, correctly, made it very clear that the agent is not allowed to market any other product, of the same category, while under their supervision. The representative, the respondent in this case, could market only Sharemax investments. The effect of this is that when the representative advises a client, the representative is bound to offer the client only one product, i.e. Sharemax. The representative then contravenes the Code by not offering the client an

appropriate choice of products. This is exactly what happened in this case. There is no incentive for the broker to direct client's attention to comparable investments from other product providers. If the broker did direct the client to another product provider, the broker is likely to lose commission and will contravene the Act. Thus most of the USSA representatives were effectively compelled to sell only Sharemax investments, within that category. There was absolutely no incentive to introduce clients to other investments. They were on their way to breaching the Code; Sharemax paid a commission of 6% of the whole investment amount with no claw-back provision. The actual interest of the client was no longer an imperative. Again the representatives found themselves in a conflict of interest which they either did not appreciate or simply chose to ignore.

[80] Before the Zambezi and Villa investments were marketed, the registrar of Companies attached the following note to the prospectus of property syndication companies:

"The Registrar of Companies has scrutinised the information disclosed in this prospectus. The Registrar of Companies does not express a view on the risk for investors or the price of the share. However, the attention of the public is drawn to the fact that the shares on offer are unlisted and should be considered as a risk capital investment. Investors themselves are therefore at risk, as unlisted shares and debentures are not readily marketable, and should the company fail this may result in the loss of the investment to the investor."

Indeed this cautionary note appears in the Sharemax prospectus. It also appears in the disclosure document. The significance for this determination is that there appears to be no evidence that USSA trained the representatives as to what this note means and how this affects the advice to be furnished to investors. Nor is there an explanation from the respondents as to why, in the light of such caution, they nevertheless saw it fit to advise the complainant and many other pensioners to invest in Sharemax.

[81] It must be said that the test for any FSP is not whether or not the investment is successful or proven, but whether or not the investment is suitable for a particular investor bearing in mind the latter's needs, profile and tolerance for risk. This appears to be ignored by all of the respondents, including the first respondent.

J. LICENSING

[82] It is unfortunate that the pattern this office observed with other failed property syndication schemes has emerged here again. The financial product provider, Sharemax in this case, marketed their product through a network of independent brokers. It is clear that the broker network was an essential part of the whole scheme. Without the brokers, Sharemax would not be able to access the investors in the desired numbers.

[83] This Sharemax did through USSA and the provisions of section 13 of the Act. A full explanation of the licensing provisions of the Act and in particular the requirements of section 13 is dealt with in the case of GERALD EDWARD BLACK vs JOHN ALEXANDER MOORE and another, case number FAIS

01110/10-11/WC1 paragraphs 66 to 93. A copy is available on this office's website, www.faisombud.co.za.

[84] In the disclosure document, the first respondent points out that he is rendering financial services "*under guidance/instruction/supervision of a key individual or other representative...*". It is common cause that the first respondent did not possess a licence to sell the Sharemax product and this disclosure tells one that he was a representative of USSA in terms of section 13 of the Act. This is not in dispute.

[85] As stated in the BLACK determination, both USSA and the first respondent were under a duty to ensure that the provisions of the Code were adhered to when providing financial services to members of the public.

[86] It was also the duty of USSA to ensure that the "fit and proper requirements" of the Act were met in respect of all the representatives they appointed.

[87] Proper compliance with section 13 of the Act and the Code means:

87.1 that USSA was responsible for training and supervising the first respondent in the marketing of the Sharemax product;

87.2 that USSA had to ensure that first respondent understood the product and was competent to give responsible and relevant advice to members of the public;

87.3 that first respondent had a duty to satisfy himself that he understood the product and was competent to render financial services;

87.4 that USSA was responsible for any activities of the first respondent which was performed within the latter's mandate as a representative; and

87.5 that USSA was under a duty to ensure that their representatives did not breach the Code.

[88] The provisions of section 13 were meant to be taken seriously and must be complied with. What is required is actual compliance and not mere compliance or lip service. At one point USSA had registered no less than 1376 representatives in terms of section 13. How so many representatives could be trained and supervised by USSA is unexplained. Especially when one considers that there was only one compliance officer. This compliance officer at one stage was also the key individual, viz Goosen, later Mrs Rinate Goosen became the sole compliance officer. It is also worth pointing out that Goosen was also a director of Sharemax. In his response to this office, Goosen gives no explanation as to how USSA managed to train and supervise over a thousand agents from all over the country. Certainly there is no evidence that any representative was supervised to advise a pensioner that Sharemax was not an appropriate investment for their risk profile and financial needs.

[89] What is clear is that the first respondent showed a lack of understanding of the Sharemax product and appeared to have enjoyed no supervision. Both Sharemax and USSA were responsible for first respondent's conduct. All the respondents were licensed FSPs or represented licensed FSPs and held themselves out to be capable and competent financial services providers and

product providers. The representatives, key individuals and directors of Sharemax and USSA cannot now escape liability through spurious technical arguments. Goosen tries to escape liability by saying that neither he nor USSA and Sharemax had anything to do with the rendering of financial services to the complainant. There is no substance in this as Goosen completely ignores the provisions of section 13 of the Act. In his application for approval as compliance officer for Goosen Financial Services ie USSA, (form FSP 6 page 2), Goosen, significantly, stated the following:

"At this point in time, I am the sole director, key individual and representative, and it is therefore not possible to indicate how independence and objectivity will be maintained from the company. I would like to confirm that as a responsible person I intend to attend to my compliance officer responsibilities in a professional manner, with due consideration to the fact that I am ultimately responsible to the FSB and the Ombud for FSPs".

[90] It is abundantly clear that the first respondent, and most of the section 13 representatives like him, did not have the capacity to even understand this financial product. The training they receive is inadequate, if they received any training at all. These are people who were actually unlicensed in terms of the act and were let loose into the public only because USSA saw fit to certify them in terms of section 13. It is plainly impossible for any company, with one compliance officer, to train **and** supervise well over 1000 representatives spread throughout the country. None of the respondents tendered any details of the extent of the training and supervision received by the representatives. It appears that USSA merely gave the representative a "Sharemax Compliance

Manual" and a pack of promotional materials. Surely this is inadequate and not in keeping with section 13 of the Act. It was simply too easy for Sharemax and USSA to set up a network of representatives. On the interpretation of section 13 as applied by USSA, there appears to be absolutely no barriers to entry. Anyone armed with a certificate from a licensed FSP can go out and sell financial products. This was not intended by the legislature. Certainly it was not intended that the provisions of section 13 should in any way compromise the requirements of section 8 of the act and the code. This is confirmed by the fact that section 13 (2) (a) specifically provides that a representative must comply with the provisions of section 8(a) and (b) of the act.

[91] Sharemax was a licensed FSP in its own right. This means that they were subject to the provisions of the Act and Code. Sharemax was under a duty to ensure that their investment did not attract people who had no tolerance for risk. Equally both Sharemax and USSA were under a duty to train their many representatives not to market this investment to people who could not afford to lose any part of their capital. This is what compliance with the Act and Code requires. However both Sharemax and USSA, through their representatives, acted in reckless disregard for the Act and Code.

[92] As a licensed product provider, Sharemax must take responsibility for the manner in which their product was marketed. At all material times Sharemax knew that many, if not most, of their investors were pensioners. In fact they appeared to actually target pensioners. They recklessly accepted these

investments. They were equally reckless in not training their representatives to comply with the Act and the Code.

Sixth Respondent's (Haese) Response

[93] The sixth respondent, on the 12th September 2012, submitted a written response to this Office. She responded in her capacity as financial director and key individual of Sharemax. She states that she realised that she was responsible for ensuring that Sharemax complies with the "applicable Acts and subordinate legislation applicable to FSP". She however states that she did not directly oversee representatives nor gave advice to any client.

[94] The sixth respondent then sets out the details of her duties at Sharemax. This was not helpful as the respondent did not deal with the complaint itself. The suggestion is clear that the sixth respondent did not have anything to do with USSA and the broker network and the investors. Her only reference to investors comes in an explanation that prospectuses were registered "for the procurement of funding from the general public". She then states that the prospectus contained a cautionary statement that there can be a loss of the investment. She concludes by stating that she executed her functions and responsibilities as key individual "within the guidelines as stipulated in the Sharemax Compliance Manual".

[95] The sixth respondent is silent on the key question as to how Sharemax managed the relationship between itself, USSA and the representative brokers and the investors. On her own version, sixth respondent knew that the

Sharemax investment product was a risky investment not suitable for people who had no tolerance for risk. The sixth respondent gives no explanation as to why Sharemax stood by and took money from investors, via their **"supervised"** broker network, who were clearly investing in a product that was not suitable for them.

[96] Equally the sixth respondent was silent regarding how Sharemax ensured that USSA properly trained and supervised over 1000 brokers in terms of section 13. The sixth respondent must have realised that there was a conflict of interests and failed to deal with how this was managed in the interests of the investor and the integrity of the industry.

[97] The sixth respondent is merely trying to escape responsibility, as a representative of a licensed FSP, for accepting money from investors knowing that this was inappropriate. The sixth respondent must have known that the majority of the investors brought in by the representatives were pensioners.

Further Response

[98] On the 21st December 2012, this office received a further response from the sixth respondent. This was in response to three questions that were directed to the respondents. She states as follows;

"33.1 USSA could not have been characterized as "an extension of Sharemax, set up to create a broker network to market Sharemax

investments", at the time of or in relation to the investments which form the subject matter of the complainants complaint;

33.2 There is no basis upon which I could be held responsible in terms of section 13 of the FAIS act for the advice given to complainant to invest in Zambezi Holdings (Prospectuses 2 and 4);

33.3 The source of income paid to investors has been fully explained."

Haese provided written motivation for her stance and I will deal with the substance of this. In respect of the first question relating to the relationship between Sharemax and USSA, Haese at the outset declared that she was a director of Sharemax Zambezi Retail Park Holdings LTD but was never a director, shareholder officer or employee of USSA. She states that she was not connected to USSA and had no business relationship with it.

[99] Haese points out that there was no agreement in existence between USSA and any of the Sharemax entities. She sets out a similar explanation as Goosen regarding the historical facts of USSA. Haese explained that USSA representatives were mandated to sell Sharemax group related products exclusively but were "not in any manner part of, nor employed by the Sharemax group and/or Sharemax Investments".

[100] The point Haese makes is that at the time when the complainant made her investments, USSA was an independent company that sold Sharemax products on an "arm's length basis". It was only in July 2010 that Sharemax became a 60% shareholder of USSA.

[101] Haese repeatedly points out that USSA was independent of the entire Sharemax group of companies. It was only in 2010, after this investment was made, that Sharemax "became the owner of 60% of USSA".

[102] Haese is the only director who, in her response to this office, dealt with the provisions of section 13. Her main submission is that neither Sharemax Zambezi Retail Park Holdings Ltd nor any other Sharemax entity, nor Haese in her personal capacity ever purported to carry on the business of rendering financial services or acted as a representative of an authorized FSP. For this reason, according to Haese, section 13 (1) and 13(2) to 13(5) are of no application to the present inquiry.

[103] Accordingly, Haese submits that neither she nor the directors of Sharemax and/or Zambezi can be held responsible for the advice given to the complainant to invest in Zambezi.

[104] Finally Haese gives an explanation of how investors were paid 12% interest by a company that had no trading history. Haese quotes extensively from the prospectus which details how loans were made to Zambezi Holdings which in turn entered into an agreement with Capicol. The latter paid interest to Zambezi Holdings which in turn paid interest to the investors.

[105] Haese concludes by pointing out that "the interest paid to investors emanated from income received by Zambezi from Capicol" in terms of the business

agreement that the parties had entered into. Haese must have been aware that this business agreement with Capicol was not included in the prospectus.

[106] I now deal with Haese's submissions. I can understand that USSA was an independent company. However, for reasons stated herein, I reject the notion that USSA was independent of the Sharemax group and that it sold Sharemax products independently and at arm's length. Having pierced the corporate veil, I find that USSA was very much a part of the Sharemax group of entities.

[107] The conclusion is inevitable, and justified by the undisputed facts stated above, that USSA was set up by Sharemax to establish a network of brokers to market its products. As stated above, Sharemax could not possibly even get off the ground without these brokers and representatives.

[108] It is equally clear that Sharemax was aware of the provisions of section 13 of the Act and therefore decided to establish their network of unqualified and unlicensed brokers through an "independent" company, USSA. This in order to circumvent the provisions of section 13. I am therefore not persuaded by Haese's submission that section 13 does not apply to the present inquiry.

[109] I am equally unimpressed with her submission that the payment of 12% interest to investors was explained. If one looks at the relevant prospectuses then it certainly does not explain, in plain language that an investor can understand, how the interest was being paid. There is a confusing reference to multiple transactions and the actual interest or income generating transaction is the "business agreement" that was entered into with Capicol. I

will deal with the terms of this agreement in more detail later. This agreement was fundamental to the whole scheme.

[110] All the directors, in their response to this office, mention this "business agreement". Yet all of the directors, including Haese, failed to explain why such an important document was not disclosed and attached to the prospectus. As I have stated below, full disclosure of this agreement would have substantially changed the risk profile of an already risky investment.

[111] Haese, in her response, does nothing to avoid the reasonable conclusion that the investors were being paid interest from their own funds.

Compliance officer

[112] Having found that both Sharemax and USSA had acted in breach of the code and were reckless in their conduct, one must look at the role of the compliance officer. The records of the FSB indicate that fourth respondent and Mrs Rinate Goosen served as compliance officers of USSA. Mrs Rinate Goosen is still reflected as the compliance officer of USSA in the records of the FSB.

[113] The provision of financial services is highly regulated and is subject to legislation, regulation, notices and codes of conduct. This is why FSPs require the services of a compliance officer; a fact which is recognised in the Act, and supported by the FSB. In this regard I refer to Board Notice 127 of the 9th

September 2010 – "Notice on Qualifications, Experience and Criteria for Approval of Compliance Officers, 2010".

As it appears in this determination, the compliance officers of Sharemax and USSA did not carry out their functions as contemplated in the Act. In particular they failed to properly manage and maintain the representatives USSA appointed in terms of section 13 of the Act.

K. THE FIRST RESPONDENTS CONDUCT

[114] On the facts before me, the first respondent failed to comply with the most basic provisions of the Code. In particular:

114.1 he failed to apply his mind to the fact that the complainant was a pensioner and by all objective accounts was not an investor who could tolerate any risk;

114.2 he ignored the outcome of his own risk assessment and needs analysis which clearly informed the first respondent that the complainant wanted her capital to be guaranteed, with some growth, and an income of between 10% and 12%. The first respondent knew that the Sharemax investment was entirely inappropriate for the complainant;

114.3 the complainant's funds were already invested in conservative investments. The Sharemax investment was a replacement investment, this means that the provisions of section 8 (1) (d) of the Code applies. The first respondent failed to comply. Quite simply, had the first

respondent complied, then the complainant's investments would not have been withdrawn in favour of Sharemax. Nor can the first respondent rely on any "specific instruction" from the complainant. The latter is a lay person and requires competent advice from the broker. I saw no recommendation from the first respondent that the complainant should avoid Sharemax;

114.4 there is no evidence that the first respondent took any time to actually explain to his client the nature of the Sharemax investment. First respondent merely relies on the fact that the complainant was handed a copy of the Sharemax prospectus. I have no doubt in my mind that even if the complainant read this lengthy 90 page document, she did not have the capacity to understand it. She relied on the FSP to advise her;

114.5 he failed to provide the complainant with other choices and different quotes. The first respondent's response was that there "were no other product that would comply with the client's instruction". There is no substance in this as it smacks of being a convenient excuse. There is no evidence that the first respondent even attempted to consider other options for the complainant. The first respondent gives no explanation as to why he advised the complainant to invest **all** her funds in the same asset class and how this impacts on the liquidity of her overall investment strategy; and

114.6 he failed to properly manage the conflict of interests between himself, Sharemax, USSA and his client.