IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS PRETORIA

CASE NUMBER: FAIS 00119/11-12/ FS 1

In the matter between:

Rusaan Van Staden	**Complainant**
and	
Dovetail Trading 509 CC t/a Legacy Invest	**First Respondent**
Hermanus SP Lombard	**Second Respondent**

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

A. INTRODUCTION

[1] The complaint in this case arises from failed investments made by the complainant into a property syndication known as Sharemax The Villa Retail Park Holdings Limited,[1] (The Villa), following the advice of the respondent. The basis of the complaint is that the respondent advised the complainant to invest in a high-risk scheme that was incompatible with her personal circumstances at the time.

B. THE PARTIES

[2] The complainant is Rusaan van Staden, formerly Fivaz, an adult female whose full particulars are on file with the Office.

[1] Registration number 2008/017207/06

[3] The first respondent is Dovetail Trading 509 CC trading under the name and style of Legacy Invest, a close corporation duly registered in terms of South African laws, with registration number 2002/082361/23. The Regulator's records confirm first the respondent's address as 41 Niel van Loggerenberg Crescent, Universitas Ridge, Bloemfontein. The first respondent is an authorised financial services provider in terms of the Financial Advisory and Intermediary Services Act, (Act 37 of 2002) as amended, (the Act), with license number 19653.

[4] The second respondent is Hermanus Stephanus Phillipus Lombaard, an adult male representative and key individual of the first respondent. The second respondent's address is the same as that of the first respondent.

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

[6] In this determination, I refer to the first and the second respondents collectively as the respondent. Where appropriate I specify.

C. THE COMPLAINT

[7] According to the information available to this Office, the second respondent was a financial advisor to the late Mrs JM Fivaz (Mrs Fivaz), the complainant's mother. During January 2010, the second respondent assisted the late Mrs Fivaz with drafting her will. In terms of the will, the second respondent together with the complainant's sister Ms Cornel Erasmus, were nominated as co-executors of Mrs Fivaz's estate. Following the death of Mrs Fivaz in February 2010, the second respondent and the complainant's sister, Mrs Erasmus, were subsequently appointed by the Master of the High Court as executors. The second respondent was also appointed together with Mrs Erasmus, as a co-trustee in a testamentary trust that was meant to benefit the complainant.

[8] The Will of the late Mrs Fivaz stated that the complainant's inheritance must be deposited in a trust and only after the complainant, at the time a 20-year-old full-time Architecture student at the University of the Free State, had completed her studies must the balance of the inheritance be paid-out accordingly as stipulated in the Will.

[9] Despite the stipulations in the Will the respondent had instructed that the inheritance moneys be immediately be divided and paid-out to both the complainant and her sister and he had instructed the complainant that she must immediately invest her inheritance to receive an income.

[10] Subsequent to this instruction, the respondent recommended that the complainant invest her entire inheritance into the Sharemax syndication The Villa. The reason for the respondent's recommendation was that The Villa was the safest investment with the highest percentage interest, which the respondent believed suited the complainant's need to receive a high income and that there was no other investment which offered a better interest. The complainant claims that the reason provided by the respondent as to the safety of the Sharemax investment was that a big part of the property had already been developed

[11] The complainant also claims that the respondent did not provide her with any alternative investment options, and neither did he discuss any of the risks involved with the investment or in deed provide her with a record of the advice provided. The respondent had only provided her with a document recording the different interest rates available with Sharemax, and he had stressed that the complainant had a limited time to invest and that the complainant should attend to the deposits as a matter of urgency or risk losing out on a specific interest rate.

[12] Based on the respondent's insistence and assurances that an investment in Sharemax was safe, the complainant invested her entire inheritance of R1 300 000 into The Villa

syndication. The investment was made by way of three separate transactions as follows:

- Investment of R500 000 on 15 April 2010
- Investment of R500 000 on 16 April 2010
- Investment of R300 000 on 6 July 2010

[13] It is perhaps necessary to mention that the complainant's sister Mrs Cornel Erasmus, the co-executor of the estate, had been sceptical of the respondent's proposal of Sharemax, and she had even asked what would happen if the development ran into financial trouble? Mrs. Erasmus was sceptical that the Villa was still in the developmental phase and despite the respondent's assurances that it was a safe investment, she had only placed a portion of her inheritance into the syndication. As co-executor, Ms Erasmus had requested that the complainant be provided alternative investment options and that not all her inheritance should be invested into The Villa. The respondent ignored these requests and had proceeded without the knowledge of Mrs Erasmus, to deal directly with the complainant in facilitating all three investments that represented the complainant's entire inheritance.

[14] The purpose of the investment had been to generate income and capital growth, however, after the final investment was made in July 2010 the complainant only received a further two income payments where after they came to an abrupt end.

[15] At the time the investments were made the complainant was a 20-year-old student, whose parents were both deceased, meaning that the returns generated from the inheritance were her only source of income, with the exception of a three hundred Rand living annuity. Due to the loss of her inheritance, her primary source of income, the complainant was forced to forfeit her studies due to insufficient funding, which has had a negative effect on her financial wellbeing.

[16] The complainant as a result approached this Office as she is of the view that the respondent, who had been aware of her situation, and despite the explicate instructions made in the will, had still pursued the investment. The complainant is of the view that the respondent had disregarded her needs and circumstances in recommending the investments into The Villa. Recommendations she regards as having been inappropriate.

D. RELIEF SOUGHT

[17] The complainant seeks repayment of the R1 300 000 from the respondent.

[18] The basis of the complainant's claim against the respondent is the latter's failure to render financial services in line with the FAIS Act and the General Code of Conduct, which includes the respondent's failure to appropriately advise the complainant and disclose the risks involved in The Villa investment.

E. THE RESPONSE

[19] The respondent by his own admission was provided with a number of opportunities to respond to this matter in compliance with Rule 6(b) of the Rules on Proceedings of the Office of the Ombud (rules), the last being 6 June 2017. The respondent's response was received on 16 June 2017 and is summarised here below:

19.1 The respondent is satisfied that he had at all times acted in the best interests of the complainant. The claim is made that he saw himself as her financial mentor, responsible for teaching her fiscal discipline owing to her being "…reckless and fruitless in her financial disregard."

19.2 The respondent also disregards any assertions made with regard to his actions as he claims to have at all times conducted himself in accordance with the last will and testament of the complainant's late mother.

19.3 The respondent claims to have presented the complainant with numerous alternative options, all of which were rejected by the complainant in favour of the higher investment return offered by Sharemax through its prospectus. (Note: No documentation has been provided by the respondent in support of the fact that he had provided the complainant with various options, or that the complainant had rejected all other options in favour of Sharemax as her preferred investment.)

19.4 With regards to the complainant's assertion that she had been harried into making the investments, the respondent claims that he had merely informed the complainant that each prospectus has a closing date, which needed to be met to enjoy the benefits of the offer presented. It had been the complainant, who after receiving this information deposited the funds out of her own accord.

F. INVESTIGATION

[20] On 30 November 2017, the FAIS Ombud addressed correspondence to respondent in terms of Section 27 (4) of the FAIS Act informing respondent that the complaint had not been resolved and that the Office had intentions to investigate the matter. Respondent was invited to provide this Office with information on his case together with supporting documents in order for the Office to begin its investigation. The respondent's response is summarised below.

20.1 The respondent once again submits that he had been serving the complainants direct instruction to invest in The Villa syndication, after the complainant had, in his words 'overruled' any alternatives made.

20.2 The respondent goes on to state that as determined by this Office, Sharemax had been conducted as a Ponzi Scheme, which had been structurally and

according to the respondent very technically concealed in the prospectuses. Prospectuses which the respondent goes on to confirm were approved by the Department of Trade and industry. This was in addition to Sharemax, having been registered by the Financial Services Board. (Now the Financial Services Conduct Authority.) The respondent questions how the reasonable financial advisor could have pro-actively assumed that Sharemax was in fact a Ponzi Scheme.

20.3 The respondent was satisfied that the complainant had been placed in a position to make an informed decision, not only with regards to the alternative options provided but also with regards to the risks involved. As previously mentioned, the respondent maintains that it was the complainant who had insisted on the Sharemax investment as a result of her desire to maximise capital growth and income.

20.4 With regards to the prospectus and the respondent's thoughts on the governance failures contained therein together with the highlighted risks that such an investment held, the respondent merely points to the investigation conducted by the South African Reserve Bank ('SARB'), which commenced during 2008. The respondent claims that not only were the concerns with Sharemax triggered by its intervention, but that it was the SARB that had failed to act on Sharemax until 2010, despite the prospectuses being promoted under their supervision without any warning to the Financial Services Industry. The respondent is once again of the view that this was beyond the scope of the reasonable financial advisor as it took SARB investigating all aspects of Sharemax to make the finding.

G. DETERMINATION

[21] The following issues arise for determination:

21.1 Whether respondent, in rendering financial services to complainant, violated the Code and the FAIS Act in any way. The pivotal question is whether complainant was appropriately advised, as demanded by the Code.

21.2 In the event it is found that respondent breached the Code and the FAIS Act, whether such breach caused the loss complained of.

21.3 Amount of the damage or financial prejudice; and

21.4 Conflict of interest.

Whether complainant had been appropriately advised

[22] It must be appreciated that there is no evidence that the respondent presented any other options to complainant or that the complainant had rejected any other alternatives in favour of an investment into The Villa. Having had knowledge of and appreciation of the complainant's personal circumstances, in that she was a 20-year-old student who relied on these funds, the respondent in accordance with Section 8(1) (a-c) of the General Code of Conduct for Authorised Financial Services Providers and Representatives ('the Code') was required to make a recommendation that appropriate to her circumstances.

[23] Had the respondent indeed as he claims presented the complainant with a number of options, and had the complainant as alluded to rejected these options in favour of The Villa, this would in accordance with Section 8(1)(b) of the Code, have required that the respondent discuss the risks involved with not adhering to his recommendation with a record thereof maintained. This section requires that where a complainant wishes to conclude a transaction that differs from that recommended by the provider, or otherwise elects not to follow the advice furnished, the provider must alert the client as soon as reasonably possible of the clear existence of any risk to the client, and must advise the

client to take particular care to consider whether any product selected is appropriate to the client's needs, objectives and circumstances. This we know was never done.

[24] Respondent also claims to have conducted due diligence by researching statutory resources out of which he noted that Sharemax had been approved by the FSB and that its prospectus had been approved by the Department of Trade and Industry, and registered by CIPC[2]. I note for the record that the approval of Sharemax as a fit and proper to hold a licence does not mean that the product was safe and compatible with complainant's circumstances. The Financial Services Conduct Authority ('FSCA') formally the FSB, does not approve products; it authorises the provision of classes of financial services and products[3]. The approval of the prospectus b the DTI and the registration of the prospectus with CIPC likewise mean nothing in so far as risk carried by the product is concerned.

[25] The prospectus made it plain that the investment was far too risky, guaranteeing neither the capital nor the income. Again, the respondent had no basis to invest complainant's funds into the syndication. The recommendation was either a result of incompetence or lack of skill, in which case the respondent was negligent (*Durr v ABSA*). In the event, the respondent appreciated the magnitude of risk involved in the investment, and this would not appear to be the case, and nonetheless went ahead with the recommendation, even though he could see that the investment was in violation of section 8 (1) (c) of the Code, then the respondent was reckless. Either way, the respondent violated his duty to act with the required due skill, care and diligence as provided for in section 2 of the Code. In the determination issued by this Office in respect of Mrs Erasmus[4] and more specifically paragraphs 33 – 43 this Office set out a

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2 Formerly known as CIPRO (Companies and Intellectual Property Registration Office), now the Companies and Intellectual Property Commission

3 ACS Financial Management CC v P S Coetzee, Case No. FAB 1/2016, September 2016, paragraph 35.

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few aspects of The Villa prospectus to highlight the magnitude of risk involved in the product. A risk that was inappropriate to the needs and circumstances of the complainant.

[26] On the basis of the reasoning set out in this determination, the risks in the investment were not disclosed, thus violating Section 7 (1). 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*"

Conflict of interest

[27] In advising the complainant, the respondent was fulfilling yet another of his roles in terms of the will: that of a designated financial service provider to the complainant. This is where the respondent's difficulties arose. The respondent should have realised at the time of preparing the will that he could not wear two hats and inform the complainant's mother of the inherent difficulties that would come with his appointment into the two positions. Clearly, the respondent saw and still sees no problem with having occupied the two roles.

[28] As an independent provider of financial services, the respondent stood in the position of an agent to the complainant, who was his principal. From that relationship, certain legal duties arose. The implied duties arise *ex lege*. See in this regard *CF Hodgkinson v Simms* [1994] 3 SCR 377 (SCC)[5]: '. . . *the existence of a contract does not necessarily preclude the existence of fiduciary duties between the parties. On the contrary, the legal incidents of many contractual agreements are such as to give rise to a fiduciary duty. The paradigm example of this class of contract is the agency agreement, in which the*

[5] *Phillips v Fieldstone Africa (Pty) Ltd* Case No 516/02 SCA, November 2003, para 27

allocation of rights and responsibilities in the contract itself gives rise to fiduciary expectations.

There is no magic in the term 'fiduciary duty'. The existence of such a duty and its nature and extent are questions of fact to be adduced from a thorough consideration of the substance of the relationship and any relevant circumstances which affect the operation of that relationship (CF Bellairs v Hodnett and Another 1978 (1) SA 1109 (A) at 1130F). While agency is not a necessary element of the existence of a fiduciary relationship (Robinson v Randfontein Estates Gold Mining Co Ltd 1921 AD 16168 at 180), that agency exists will almost always provide an indication of such a relationship.'

[29] In terms of the provisions of the Act and the Code, the respondent owed certain statutory duties to the complainant. One of those duties is eloquently described in section 2 of the Code that '*a provider must at all times render financial services honestly, fairly, with due skill, care and diligence, and in the interests of clients and the integrity of the financial services industry*.'

[30] As executor of the estate, the respondent had access to information which is not of a public nature and had to use that information to fully discharge on his duties toward the estate and the heirs. Indeed, it would be unprofessional and a breach of his fiduciary duties towards any of the heirs and the estate for that matter, if the respondent were to use the information he accessed during the course of his execution of his duties, to identify opportunities for himself. This is exactly what happened in this case.

[31] The principles which govern the actions of a person who occupies a position of trust towards another were adopted in South Africa from the equitable remedy of English law: '*The fullest exposition in our law remains that of Innes CJ in Robinson v Randfontein Estates Gold Mining Co Ltd, supra, at 177-180. It is, no doubt, a tribute to its adequacy and a reflection of the importance of the principles which it sets out that it has stood unchallenged for 80 years and undergone so little refinement*.

'*Where one man stands to another in a position of confidence involving a duty to protect the interests of that other, he is not allowed to make a secret profit at the other's expense or place himself in a position where his interests conflict with his duty. The principle underlies an extensive field of legal relationship. A guardian to his ward, a solicitor to his client, an agent to his principal afford examples of persons occupying such a position. As was pointed out in The Aberdeen Railway Company v Blaikie Bros. (1 Macqueen 474), the doctrine is to be found in the civil law (Digest 18.1.34.7), and must of necessity form part of every civilized system of jurisprudence. It prevents an agent from properly entering into any transaction which would cause his interests and his duty to clash. If employed to buy, he cannot sell his own property; if employed to sell, he cannot buy his own property; nor can he make any profit from his agency save the agreed remuneration; all such profit belongs not to him, but to his principal. There is only one way by which such transactions can be validated, and that is by the free consent of the principal following upon a full disclosure by the agent . . . Whether a fiduciary relationship is established will depend upon the circumstances of each case . . . But, so far as I am aware, it is nowhere laid down that in these transactions there can be no fiduciary relationship to let in the remedy without agency. And it seems hardly possible on principle to confine the relationship to agency cases*[6]*'.*

[32] So oblivious was the respondent to the conflict of interest that was brought about by his occupying the two positions, that he did not even claim to have drawn the complainant's attention and notice to the conflict of interest. In advising the complainant, the respondent was obliged to act in the complainant's interest and recommend an investment suitable to her circumstances. He failed to do so and simply rushed to recommend the product, which brought him the highest commission with no claw back. The respondent had every incentive to ignore any other product that would suit

[6] Phillips v Fieldstone supra, paragraph 30

complainant for the commission paid by Sharemax was lucrative in terms of industry standards. It has not escaped me that the very idea of being nominated as executor or co-executor of one's client's estate, as a financial advisor, is sufficient to conclude possible undue influence on the part of the provider.

[33] The respondent could not have acted fairly towards the complainant. He had far too many interests to mind and was likely to put his interests before those of his client. For example, other than blaming the SARB, the respondent cannot justify why he put the complainant's entire inheritance into the high risk Sharemax investment in circumstances where he had hardly carried out any due diligence. He does not explain how the circumstances and needs of the complainant could only be matched by the Sharemax product. The respondent violated his duty to act in the interests of the complainant and the financial services industry.

[34] There is no question that between the complainant and the respondent, there existed a contractual relationship to render financial advice. In discharging these obligations towards the complainant, the respondent was duty bound to observe the FAIS Act and the General Code, (the Code) and align the standard of such service to the Code. As has been mentioned, the respondent's conduct violated the Code which amounts to a breach of the contract.

Causation

[35] The principles of causation were explained in *Standard Chartered Bank of Canada v Nedperm Bank Ltd* 1994 (4) SA 747 (AD); [1994] 2 All SA 524 (A). Causation has two legs, namely, factual and legal.

[36] In advising the complainant, the respondent presented no other options but the Sharemax product. He failed to deal with the risks involved in Sharemax when advising complainant. It thus cannot be denied that had the respondent firstly appreciated the

risk and secondly, explained it to the complainant, the latter, in all probability, would not have invested in Sharemax. The first leg of the causation enquiry, the "but for" test is thus satisfied. But for the respondent's inappropriate advice, there would be no investment in Sharemax and consequently no loss.

[37] That, as Corbett CJ[7] said, does not conclude the enquiry. It is still necessary to determine legal causation, i.e. whether the furnishing of the poor advice was linked sufficiently closely or directly to the loss for legal liability to ensue, or whether the loss is too remote. The test:

"*is a flexible one in which factors such as reasonable foreseeability, directness, the absence or presence of a legal policy, reasonability, fairness and justice all play their part*[8]".

[38] The learned judge added that:

"*the reasonable foreseeability test does not require that the precise nature or the exact extent of the loss suffered or the precise manner of the harm occurring should have been reasonably foreseeable for liability to result. It is sufficient if the general nature of the harm suffered by the plaintiff and the general manner of the harm occurring was reasonably foreseeable.*

The main factor limiting liability is the absence of reasonable foreseeability of harm. This is an objective question[9]."

[39] I refer to some, but not all, the glaring indications. The violations of Notice 459 as communicated by the directors in the prospectus, followed by the conflicting statements contained in the prospectus; the SBA, which simply explained no ordinary business proposal but something which, in effect, amounted to a pyramid scheme; and the

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7 ACS Financial Management CC v P S Coetzee, Case No. FAB 1/2016, September 2016, paragraphs 61-63

8 See footnote 19 *supra*

9 ACS Financial Management supra,

obvious poor governance practices conveyed in the prospectus, none of which appear to have caught the respondent's eye. The ineluctable conclusion is that the collapse of the scheme was not only reasonably foreseeable but, in all probability, inevitable. The precise nature of the collapse and the intricate details are not necessary.

[40] The SARB's intervention as the respondent earlier mentioned, interrupted the development. The less said of respondent's statement, the better. SARB was discharging its duties in intervening in Sharemax besides, there is no evidence that SARB ever took control of the business of Sharemax at any stage[10].

[41] The loss was inevitable.

H. FINDINGS

[42] I make the following findings:

42.1 The respondent, in complete disregard for complainant's interest rendered inappropriate and negligent advice.

42.2 The respondent rendered financial services to complainant while faced with a conflict of interest and failed to disclose the conflict of interest to complainant.

42.3 The respondent treated the complainant unfairly.

42.4 The respondent failed to disclose the risk involved in the investment, in violation of Section 7(1).

42.5 The respondent denied the complainant the opportunity to make an informed decision about the Sharemax investment.

[10] See in this regard Judgement delivered on 7 October 2014: Willem Van Zyl & Deon Pienaar v PricewaterhouseCoopers & Others HC WC Case No.: 12511/2013.

42.6 The respondent, in violation of section 2 of the Code, had carried out no due diligence. This saw him advising his client on an investment product he hardly knew anything about.

42.7 The respondent's advice caused the loss.

I. QUANTUM

[43] Complainant invested in total R1 300 000.

[44] Accordingly, an order will be made that the respondent pay to the complainant an amount of R1 300 000 plus interest.

J. THE ORDER

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

1. The complaint is upheld.

2. The respondent is hereby ordered to pay to the complainant, jointly and severally, the one paying the other to be absolved, the amount of R1 300 000.

3. Interest on this amount at the rate of 10% per annum from the date of determination to date of final payment.

DATED AT PRETORIA THIS THE 20th DAY OF NOVEMBER 2018

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NARESH S TULSIE

OMBUD FOR FINANCIAL SERVICES PROVIDERS