IN THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

Case Number: FAIS 09446/10-11/NC 1

In the matter between

ABRAHAM HENRY ROTHBART **Complainant**

and

FREDERIK HENDRIK KOTZE **Respondent**

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

A. INTRODUCTION

[1] In 2006, the complainant invested R270 000 into a property syndication scheme managed by DIV-VEST (PTY) LTD on the advice of the respondent. At the time, the complainant was nearing retirement and was looking for an investment that would provide him with an income and capital growth. The investment was meant to subsist for a period of five (5) years from the date of investment but in 2009, the complainant stopped receiving his income and to date, has not received his capital back.

[2] Following a failed attempt to resolve the matter with the respondent, the complainant approached this Office for assistance.

B. THE PARTIES

[3] The complainant is Mr Abraham Henry Rothbart, an adult male pensioner whose full details are on record with this Office.

[4] The respondent is Frederik Hendrik Kotze, an adult male financial services provider and broker. The respondent has been registered as an authorised financial services provider (FSP) (licence number 12806) since 2004 and his license remains active. At all times material hereto, the respondent rendered financial services to the complainant in his capacity as a sole proprietor of the aforementioned FSP. The respondent's principal place of business is noted in the records of the Financial Sector Conduct Authority (FSCA), or the Regulator, as 101 De Oude Schuur Building, 120 Bree Street, Cape Town, 8000.

C. THE COMPLAINT

[5] It is common cause that the respondent rendered a financial service to the complainant in June 2006 which led to the complainant investing in a property syndication scheme known as Zambezi Business Park managed by DIV-VEST (PTY) LTD[1]. The complainant alleges that when the respondent furnished him with the advice that led to the investment, he informed him that the investment was the most appropriate. The complainant alleges that all the advice he received from the respondent was provided to him in writing and that he did not at any time receive any other advice from the respondent except the advice that is recorded in emails that were exchanged between them. The complainant attached these emails to his complaint.

[1] Registration number 2000/011419/07.

[6] The complainant alleges that the respondent did not advise him of the risks inherent in the investment and that he did not receive a ‘financial plan’ from the respondent.

[7] The complainant states that he depended on the respondent’s advice and invested a total of R270 000 on the strength of the information provided to him by the respondent.

[8] The complainant was advised that he would receive an income or interest payments from the investment during its subsistence, that he would have access to the capital he had invested in the event of an emergency and that his capital would grow and be paid to him on maturity of the investment. The investment period was said to be five (5) years.

[9] The complainant did in fact receive an income from the investment from 2006 but the income ceased in February 2009. It seems that the complainant was under the impression that his capital had been invested in Sharemax because in 2010 he wrote to the respondent and advised that from what he had seen from press releases and the internet, it seemed as though he had lost the money he had invested in Sharemax. The complainant advised the respondent that he held him personally liable for the loss of what he described as his retirement money.

[10] The complainant also, in this letter dated 22 December 2010, accused the respondent of having failed to conduct a full and proper due diligence into the financial viability of Sharemax prior to giving him advice on investing a portion of his retirement capital with ‘them’. The complainant then asked the respondent to provide him with a copy of their complainants policy and afforded them six (6) weeks within which to respond to his concerns failing which he would report the matter to ‘the Ombud’.

[11] The complainant received no response to his letter and on 3 February 2011, he addressed a further letter to the respondent reminding him that his response was outstanding. On 4 February 2011, the respondent sent a response to the complainant but did not address the matter to the complaint's satisfaction. The complainant had demanded that his capital be paid back to him but the respondent had instead provided the complainant with 'clarity' on his investment as well as an update on what had happened to the property syndication. The respondent ended his response by informing the complainant that his money has never been at risk, that he is invested in a rental generating property and that he will most probably make 'quite a bit of money when the property is sold.'

[12] The complainant, unsatisfied with this response from the respondent, lodged a complaint with this Office and indicated that he would like this Office to assist him to at least get his capital paid back to him with interest.

D. RESPONDENT'S VERSION

[13] On receipt of the complaint, this Office, in accordance with Rule 6(c) of the Rules on Proceedings of the Office of the Ombud for Financial Services Providers (the Rules), forwarded the complaint to the respondent to afford the respondent an opportunity to either resolve the complaint with the complainant or to respond fully thereto. The complaint was sent to the respondent on 14 March 2011.

[14] The respondent opted to respond to the complaint and in his response alleged that when he first met with the complainant, that the complainant had indicated to him that he had some funds with various institutions and that he was retiring soon and needed a monthly income. The respondent claims that he conducted a full needs analysis on the complainant's portfolio and that his advice was in accordance with the needs analysis.

[15] The respondent claimed that because the complainant had a number of funds that he could choose from to provide both capital growth and an income on a monthly basis, that this led him to suggest that part of the complainant's funds be paid into the Zambezi investment. The respondent claimed that he had, with the complainant, discussed at length the risk, growth potential and monthly income but did not specify if these discussions were in relation to all the investment options or if they were in relation only to the investment in question.

[16] The respondent also claimed that the complainant chose the investment with the highest monthly income and advanced that due to the fact that the complainant had various investments to draw from, in the event that one of the investments did not deliver or the funds were reduced, the complainant could subsidies his income from the other investments with the Zambezi investment.

[17] Lastly, the respondent mentioned that the management of the property syndication had been taken over in 2009 by a company known as Capital Investments and that the directors decided to enrich themselves at the expense of investors. The respondent positioned this as the reason why the rental income due to the investors had ceased and indicated that at that stage there were discussions underway with a potential new buyer for the property and that rental income would be paid to investors as soon as all arrears and other costs had been recouped.

E. INVESTIGATION

[18] After due consideration of this response, this Office found it wanting and was not satisfied that the allegations raised by the complainant had been adequately addressed by the respondent. Consequently, this Office accepted the matter for formal investigation but prior

to undertaking the investigation, issued a notice to the respondent in terms of section 27 (4) of the Financial Advisory and Intermediary Services Act (FAIS Act) informing him of its decision.

[19] In this notice, the respondent was advised that his response, as well as the documentation he submitted, where insufficient to demonstrate his compliance with the FAIS Act and the General Code of Conduct for Authorised Financial Services Providers and Representatives (the Code). The respondent was advised that the matter had consequently been accepted for formal investigation and was referred to various sections in the FAIS Act and the Code which this Office perceived he had breached.

[20] On account of these perceived breaches, this Office recommended that the respondent resolve the matter with the complainant and the respondent was advised that in the event he failed and/or refused to do so, that the complaint would be resolved by way of a determination. In the event that the respondent elected not to resolve the matter with the complainant, he was called on to submit the information and documentation necessary to support his statements.

[21] The respondent did not settle the matter with the complainant and instead submitted his response to the allegations put to him in the notice. The respondent started his response by providing this Office with information regarding how he met the complainant and what led to him providing the advice in question. The respondent then furnished this Office with details of the complainant's financial position at the time he rendered the advice and detailed his recommendations to the complainant.

[22] This information from the respondent had already been furnished to this Office in the respondent's previous response, though not in the same manner, and consequently did

not offer any new information which could address the specific allegations put to the respondent. In the same vein, the respondent maintained that the directors of the property syndication were responsible for its collapse given that they, the respondent alleged, had decided 'to enrich themselves' by accessing all available funds, creating fictitious loans and not collecting any rentals or municipal services. The respondent continued that the debt, seemingly occasioned by the aforementioned actions, mounted and could not be serviced by the small amount of capital left over in the company.

[23] The respondent stated that he was of the view that he had always had a good working relationship with the complainant and that he had always given him good advice. The respondent stated that he did not know, at the time that he rendered the financial service to the complainant that four (4) years later, the directors of the company would 'decide to enrich themselves'. The respondent ended by stating that the marketing promotion as well as the attorneys who had been appointed to the property development all seemed above board at the time.

[24] Again, this Office was unsatisfied with the response received from the respondent and issued another notice to the respondent in terms of Section 27(4) of the FAIS Act. In this notice, this Office highlighted again what it perceived to be contraventions of the FAIS Act and the Code and called on the respondent to either resolve the matter with the complainant or to file its response to the notice together with the necessary supporting documentation. This notice was sent to the respondent on 20 April 2018.

[25] In the notices sent to the respondent, he was advised that the notice was being sent to him because he had failed to resolve the matter with the complaint within the six (6) week period afforded to him to do so, when the complaint was initially sent to him. In his response to the notice of 20 April 2018, the respondent claimed that the complaint had never been

brought to his attention and asked how then he would have been able to respond to the complaint.

[26] On 14 May 2018, this Office advised the respondent of the date when the initial correspondence to which the complaint was attached and in respect of which he was afforded six weeks to respond to the complaint sent to him. This Office also confirmed that it had not received a response from the respondent to this correspondence. The respondent was also advised that this Office had no record of having received a formal response from him to the notice of 20 April 2018 and asked that he submits his response by 18 May 2018.

[27] On 15 May 2018, this Office received a response from the respondent in which he advised that he had asked his employee to forward his previous responses and asked if there was anything further that this Office required from him. In response, this Office advised the respondent that if he was satisfied with the responses he had submitted to date, that the matter would be sent to the Ombud so a determination could be issued thereon. An employee of the respondent, acting on behalf of the respondent, in turn advised that they confirm having done all that they can from their side and this Office accepted that the respondent did not intend then to submit any response to the final notice sent to him.

[28] The file was prepared for determination. However, after careful consideration of the file, this Office noted that while the respondent had consistently maintained that the documents he submitted in support of his statements proved his innocence, these documents related primarily to the other investments the complainant had made and hardly related to the investment in question. The respondent was thus asked to submit the record of advice which reflects the basis on which the advice specific to the current complaint was given

and the other documents which would support his claims, all again relating to the current complaint.

[29] In response, the respondent simply forwarded the responses and documents he had previously submitted to this Office and on receipt of this, this Office then concluded its investigation into the matter as it was evident that the respondent either did not have the documents which had been specifically requested from him or that he was unable to provide these to this Office.

F. DETERMINATION

[30] The respondent states emphatically that he is not to blame for the loss occasioned to the complainant. He maintains that there was nothing wrong with the advice that he furnished to the complainant because the product, as it was then, was appropriate to the complainant's needs and financial circumstances. To prove this, the respondent provided much detail of the other investments that the complainant had taken up on his recommendation and also detailed the advice that he had given to the complainant in respect of these investments.

[31] The respondent maintained that but for the actions of the directors that took over the management of the syndication and were entrusted with the duty to manage the syndication, the complainant would not have suffered the loss complained off.

[32] Interestingly, the respondent, in his initial responses to this Office had claimed that the complainant would not lose his capital, that because it was invested in rental property, it was not and had never been at risk and that once certain factors had been dealt with, the complainant would make a sizeable profit from the investment. The factors that the respondent referred to ranged from the removal of the liquidator who had been unlawfully

appointed to head up the liquidation of the company that managed the syndication, as well as the difficulty the syndication experienced in selling the property.

[33] The respondent barely acknowledged the facts that led to the syndication being liquidated and instead repeatedly referred to how the directors had 'enriched themselves' at the cost of the syndication and consequently, the investors. The respondent did not consider how long the mismanagement of the company had persisted and importantly, whether this was already the case when he recommended the product to the complainant.

[34] The respondent did not refer this Office at all, to his analysis of the product. its sustainability and therefore the ability to deliver what it promised to investors and also its suitability to the complainant given his needs, risk profile and financial circumstances.

[35] From the documents that the respondent submitted in support of his averments, it appeared that his consideration of whether or not the product was suitable for the complainant was premised only on the income that the product promised investors and whether the product offered any capital growth as well as the flexibility of an investor to withdraw from the investment if they elected to do so on account of an 'emergency'.

[36] There is nothing, in any of the documents received from the respondent, and from the correspondence that the complainant attached to his complaint, that shows that the respondent, as he claimed, considered the risks inherent in the product. The respondent's statement that he discussed the risks with the complainant is particularly doubtful given that he maintains that the product was suitable and seems to hold the view that it would have delivered on the promises advanced to investors had it not been for the unlawful actions of those entrusted with its management. If the respondent holds this view then it is improbable that he would have discussed risks with the complainant, and, there is no

evidence to prove such a discussion. There is no record thereof, in so far as there hasn't been any submitted to this Office despite the many requests to the respondent that they be made available.

[37] It is also important to note that the Office repeatedly requested the respondent to make the said record(s) available on the strength of the requirements of section 3(2)(a) of the Code, which states that:

'A provider must have appropriate procedures and systems in place to –

(i) record such verbal and written communications relating to a financial service rendered to a client as are contemplated in the Act, this Code or any other Code drafted in terms of section 15 of the Act;

(ii) store and retrieve such records and any other material documentation relating to the client or financial service rendered to the client; and

(iii) keep such client records and documentation safe from destruction.'

[38] Section 3(2)(b) states that the records must be kept for a period of five years after termination to the knowledge of the provider of the product concerned, or in any case after the rendering of the financial service concerned.

[39] However, notwithstanding the above duties, the respondent failed and/or refused to show that he in fact apprised the complainant of the risks by not submitting the records necessary to prove this. I am therefore of the view that the respondent, contrary to his claims, did not consider what risks the complainant would be exposed to should he invest in the syndication and he thus did not comply with section 8(1)(c) of the Code since he could not have been able to assess that a product was suitable if he did not know the risks inherent therein. Therefore the respondent's inability and/or failure to produce any records

to disprove the above, constitutes non-compliance with sections 3(2)(a) and 3(2)(b) of the Code.

[40] In addition to and as a result of the above, there is no evidence to show that the respondent, in accordance with the duty placed on him by section 8(2) of the Code, put the complainant in a position to make an informed decision since there is no evidence of him having put before the complainant, all the information the complainant required in order to understand the product and its risks.

[41] I am therefore of the view that , when the respondent rendered this financial service to the complainant, he acted negligently and that but for his actions, the complainant would not have suffered the loss complained of. The respondent is, therefore the factual cause of the complainant's loss.

G. LEGAL CAUSATION

[42] However the enquiry into whether or not the respondent must be held liable for the complainant's loss does not end there. The enquiry into negligence is a two-step process. The first part of the process deals with whether the respondent in fact caused the loss. A question that is answered by considering whether, if the actions of the respondent are removed, the loss would have occurred or not[2]. If this question is answered in the positive, then the enquiry ends there and the complaint against the respondent must be dismissed.

[43] If however, the question is answered in the negative, then we must consider whether the respondent is the legal cause of the loss. This we do by considering whether the respondent's actions were so close to the loss that without them the loss would not have

[2] Lee v Minister of Correctional Services 2013 (2) SA 144 (CC) at paragraph 40.

ensued. If the loss would have in anyway ensued, then the wrongful conduct of the respondent cannot be said to be the legal cause of the loss and the respondent cannot be held liable for said loss[3]. If however, the loss occurred as a direct result of the respondent's actions, then it follows that he is the legal cause of the loss and must be liable therefor.

[44] Despite the respondent's claims that the trouble for the syndication started only after he had furnished the complainant with advice, the evidence adduced by the liquidator appointed to attend to the liquidation of the management company suggests otherwise.

[45] The liquidator, on the same day that the liquidation application was heard, in March 2013, brought an application in terms of the Companies Act[4] in which he requested that the company that managed the property syndication, together with those managed by the same board of directors, be declared a single entity as envisaged by ss 20(9), 22, 141(2)(c) and 141(3) of the Companies Act.

[46] The Supreme Court of Appeal (SCA), summarising the evidence adduced in the aforementioned application quoted the following grounds in respect of which the application had been made:

'The five companies were part of an unsustainable syndication scheme which had engaged in reckless trading and defrauded members of the public. The use of the companies, or the acts by or on behalf of them, constituted an unconscionable abuse of their juristic personality, justifying an order that they should not be regarded as juristic persons as contemplated in s 20(9) of the 2008 Act. Members of the public had invested some R140 million into Zambezi Retail Park, whereas the property was worth only about R45 million,

[3] Ibid.
[4] Act 71 of 2008.

leaving investors with a loss of nearly R100 million. The syndication value of the property was about R125.5 million, its purchase price was some R107.3 million, and the promoter of the scheme had made a profit of more than R19 million, which immediately reduced the value of the investors' money. In addition, investors were liable for about R10million raised through a mortgage bond. The only way they would recover anything in the liquidation proceedings was if the promoter and other companies in the scheme were held liable by holding the persons behind the promoter personally responsible for the losses incurred.

Zambezi Business Park was run as a single indivisible commercial enterprise. The corporate identity of the five companies had not been maintained, their financial affairs were not kept apart, and funds flowed to and from the various companies as investors were paid dividends promised to them.'[5] (My emphasis)

[47] It is apparent from the above quoted sections of the judgement of the SCA that the mismanagement of the company existed before the income, or dividends as the court referred to them, ceased to be paid to investors and in fact at the time were investments were being collected or received from members of the public, including the complainant.

[48] The respondent did not adduce any evidence to show that prior to recommending the product to the complainant, that he satisfied himself as to its sustainability and its efficacy. He did not lead any evidence to show what else he considered, apart from the information provided by the promotors, marketers and the directors of the company, in order to ensure that the company could deliver what was promised to investors. Nor did he lead any evidence to show that he considered how the company was being run and if it subscribed

[5] City Capital SA Property Holdings Ltd v Chavonnes Badenhorst St Clair Cooper NO (85/2017) [2017] ZASCA 177 at paragraph 12 – 13.

to good governance practices, a consideration that is important since a failure in governance can, and in this case did, have a detrimental effect on the company.

[49] This was especially important given the source of the funds that the complainant invested, his age and that he was unlikely to be able to recover the funds should the investment fail. So while the respondent alleged that there was an act that intervened in the investment and that he consequently cannot be held liable for the complainant's loss, for the above reasons, I do not find this to be true.

[50] As such, I am of the view that the loss suffered by the complainant was sufficiently linked to the respondent's failure to render the financial service in the manner demanded of him and that the respondent should be held liable for such loss.

Loss suffered by the complainant

[51] When the complaint was initially sent to the respondent, he claimed that the complainant had not suffered a loss since the property could still be sold and investors' capital returned to them. Since then, the investment company has been liquidated and to date, the complainant and many other investors have not received their capital. In 2017, the SCA noted the difficulties that investors faced in recovering their capital and it seems unlikely, given the time that has passed even since then, that investors will see the relief they seek. I am therefore satisfied that the complainant has in fact suffered a loss.

H. THE ORDER

[52] In the instance, I make the following order:

1. The complaint is upheld.

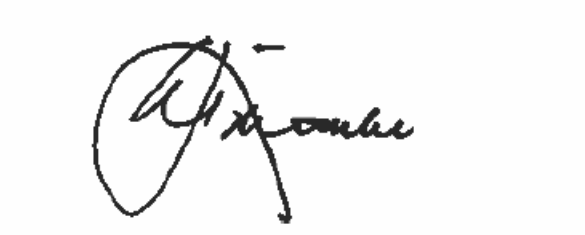
2. The respondent is ordered to pay to the complainant the amount of R270 000.

3. The respondent is ordered to pay interest on the above amounts at a rate of 7% per annum from the date of determination to date of final payment.

4. The complainant is to cede his rights and titles in respect of any further claims in respect of this investment to the respondent.

5. Should any party be aggrieved with the decision, leave to appeal is granted in terms of section 28 (5) (b) (i), read with section 230 of the Financial Sector Regulation Act 9 of 2017.

DATED AT PRETORIA ON THIS THE 5th DAY OF FEBRUARY 2021.



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ADV NONKU TSHOMBE

OMBUD FOR FINANCIAL SERVICES PROVIDERS