**THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS**

**PRETORIA**

**CASE NUMBERS: FAIS 04988/12-13/ GP1**

**FAIS 04986/12-13/ GP1**

**In the matter between:**

**ALIDA CHRISTINA WILKEN** **First Complainant**

**LOUIS PHILLIPUS WILKEN** **Second complainant**

**AND**

**CHARLES PETRUS MALHERBE T/A**

**CHARLES MALHERBE MALELAARS** **Respondent**

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

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## A. INTRODUCTION

[1] The complainants are pensioners who are married to one another. Both filed a complaint in this office and although separate complaints were lodged and accepted by this office, for convenience, we deal with both complaints in one determination. This is equally convenient for respondent who also treated the complaints as one. The complaints relate to investments made in the now defunct Sharemax property syndication.

[2] The complaints were forwarded to respondent who, through his attorneys, responded to the complaint fully and provided the relevant supporting documentation.

[3] The respondent is Charles Petrus Malherbe, a licensed financial services provider (FSP) in terms of the Financial Advisory and Intermediary Services Act of 2002 ("The Act") with FSP No 14326 who traded as Charles Malherbe Makelaars. He was licensed in his own right to market the Sharemax product, under license categories 1.08 and 1.10.

## B. THE COMPLAINT

[4] The complainants saw advertisements in the media from Sharemax. They responded to the advertisements by calling Sharemax who referred them to respondent as he was an FSP close to where complainants were located. Second complainant received an amount of R345 000 from his pension (the municipal workers pension fund). He and his wife were close to 70 years old and wanted to invest the money so as to receive a monthly income. Second complainant decided to take an amount of R45 000 from his pension and invest it in first complainant's name.

[5] They consulted respondent and were advised to invest their funds in Sharemax The Villa Retail Park. First complainant invested R45 000 and second complainant R300 000. The investments were made as a result of advice given by respondent.

[6] Complainants had two meetings with respondent who advised them to invest in Sharemax. Respondent assured them that there was no risk associated with Sharemax investments. Respondent placed a prospectus in front of them and showed how financially strong Sharemax was and that they owned a number of buildings. Complainants point out that they told respondent that the funds were their pension funds and they required a monthly income from an investment. Complainants emphasised that this was their pension and it had to be invested in a "*very safe*" investment providing a monthly income. Complainants explained to respondent that they were absolutely dependant on the monthly income from the investment. Respondent assured them that without doubt, Sharemax was the investment for them.

[7] Respondent only presented the Sharemax product and did not offer complainants any alternative choices. Complainants are certain that respondent did not explain nor inform them of any risks in the Sharemax investment. Nor did respondent explain the contents of the prospectus to them. Complainants did not read the prospectus before making the investment and respondent was aware of this.

[8] Complainants own a house and a car which are both paid for. First complainant also receives a monthly pension from Old Mutual in an amount of R1556. She has no other fixed income. She earns a modest amount from baking for a local home industry and she does some needle work. Complainants also receive some assistance from their children. Complainants do not have any other investments.

[9] On 29 September 2009 complainants made their investments in Sharemax. Initially all was well as the promised monthly payments were made. On 31 August 2010, they realised something was wrong as the payment was not made. First complainant called Sharemax head office and was informed that her payment had been loaded onto the magtape and payment will be reflected in her account the next day. This promise did not materialise.

[10] Complainants then made an appointment with respondent who informed them that there is a problem, but they need not worry as their funds were safe and payments will resume. Various further calls were made to Sharemax, but there was no response.

[11] Complainant's received two letters from respondent, on 11 March 2011 and 27 May 2011. These letters were attached to the complaint. The letters contained information about the Section 311 compromise and the role of Frontiers Asset Management. Respondent also wrote about the restructuring of the company. Both letters struck an optimistic note and gave complainants hope that their investments might be recovered. Again, none of the promises materialised and complainants decided to file a complaint with this office. Both complainants want respondent to pay them back their investments. The delay in filing a complaint was due to the fact that complainants were in constant touch with the Sharemax office and respondent. Many promises were made about resolving the matter, but none of the promises materialised.

[12] After the complaint was lodged, respondent contacted complainants and requested that they sign a letter that their complaint was not against him, but against Sharemax. Complainants refused to do this. Then respondent suggested they accompany him to his attorney and agree to launch an action against Frontier Asset Management. Complainants refused to do so.

[13] Complainants state that the invested funds was all they had. They are now in their 70s and describe themselves as “financially destitute”.

## C. THE RESPONSE/RESPONDENT’S DECLARATION

[14] Complainants’ written complaint with the documents attached, was delivered to respondent. This office also requested respondent to provide his supporting documentation, including his record of advice.

[15] Respondent was also required to attempt to settle the matter with complainants. Respondent failed to settle the matter and filed a comprehensive response, in the form of a declaration, duly assisted by his attorneys. The response is the same in respect of both complaints.

### Applications by Respondent

[16] It is a matter of routine for respondent’s attorney to do the following; all of which this office consistently rejected in a number of determinations:

a) Bring an application in terms of section 27 (3) (c), that this office should refuse to deal with the complaint and to refer the matter to the High court; and

b) Secondly, that respondent has a right to a full adversarial hearing including pleadings and discovery.

[17] Respondent’s attorney has acted on behalf of a number of respondents in these complaints, involving Sharemax investments. Notwithstanding this office’s consistent dismissal of the above applications, the attorney merely persists in doing the same thing

in each response. Thus, much of respondent's declaration is nothing more than a copy and paste from other responses.

[18] I deal with each of these points immediately:

a) Regarding the application in terms of section 27(3)(c), the Act provides as follows:

*"The Ombud may on reasonable grounds determine that it is more appropriate that the complaint be dealt with by a Court or through any other available dispute resolution process, and decline to entertain the complaint."*

This is not a matter that cannot be determined in terms of the rules and processes of this office. There are no irreconcilable disputes of fact which require an adversarial hearing. As will be demonstrated in this determination, the issues between the parties can be resolved on the undisputed facts.

It will defeat the whole purpose of the Act if parties to a complaint can, merely by application to this office, elect to refer a matter to a court. There are no reasonable grounds on which this office can determine that it is more appropriate that the complaint be dealt with by a court. This point has never succeeded before the erstwhile FSB Appeal Board; neither has it succeeded before the Tribunal. This is a matter for my discretion, and after considering all the factors, I decided to dismiss the application. Accordingly, respondent's application to refer the matter to a court was dismissed.

b) As for the second point, I refer to Section 20 (3) of the Act, which provides as follows:

*"The objective of the Ombud is to consider and dispose of complaints in a procedurally fair, informal, economical and expeditious manner and by reference to what is equitable in all the circumstances, ..."*

It was not intended by the legislature that this office should afford parties the choice of an adversarial hearing. This type of hearing would take too long, become unaffordable to most complainants and would require this office to find resources it does not have. The Office treats both parties fairly and the High court has already ruled that the processes of this office do not deprive the parties of a fair hearing neither are they unconstitutional.

See **Deeb Risk and others v The Ombud for Financial Services and others Case no 38791/2011 Gauteng Provincial Division Baqwa J judgement date – 07/09/2012.**

The second application for an adversarial hearing is dismissed.

**Respondent's Version**

[19] Here I deal with respondent's version of the events leading up to the investment in Sharemax The Villa. In doing so I will also make comment about his version and deal with complainant's version of events.

[20] Respondent confirms that complainants were referred to him by Sharemax as he was the closest FSP to complainants. He met with them on 22 September 2009. Complainants explained that they were looking for an investment to provide them with a monthly income, but required an investment which could offer a better rate of interest than the banks.

[21] Respondent then discussed various investment vehicles and also consulted the Moonstone Investment Indicators. In this discussion, they also discussed Sharemax. Respondent was under the impression that complainants "had a fair knowledge of how investments work". He also found out that first complainant had worked for Old Mutual. I must state immediately that complainants were not knowledgeable about investing. Even if they did have some knowledge about investing, they certainly knew nothing about investing in property syndications.

[22] Complainant's deny that they discussed various investment options. Their version is that only Sharemax was presented. This is likely as respondent was contacted by Sharemax to assist complainants. Respondent was not likely to promote or advise complainants to invest in any other product. Besides, respondent does not produce any record of advice recording that alternative investments were also presented.

[23] Respondent states that he explained to complainants, "*in detail*", the Sharemax investment. He even used the example of two local shopping centres in Vereeniging. Respondent also "*fully discussed*" the risks of investing in the Sharemax investment. He pointed out the "*many factors*" which contribute to risk; such as if the building stood empty and did not generate rental income; or in the event of the shopping centre burning down etc.

[24] Respondent discussed the liquidity of their capital and the penalties applicable if they withdrew their funds early. Respondent even contemplated the "*scenario"* that should Sharemax disappear, complainants' money would be deposited into Weavind and Weavind's trust account "*as at that time Sharemax did not own the building in question*".

Respondent states that he discussed the content of the prospectus *"in detail*" with complainants.

[25] Based on the facts before me, the following is undisputed:

a) Respondent created the impression that complainants were investing in property, yet he was aware that Sharemax did not own any property;

b) Respondent created the impression that complainants will be paid from rental income, when respondent knew that Sharemax did not own any rental income producing property;

c) Respondent informed complainants that their funds will be safe in an attorney's trust account and will be paid out once Sharemax took transfer of the property. Respondent knew this was entirely untrue as the very prospectus he explained to complainants tells investors that their funds will not be held in trust but will be paid out to Sharemax who intend to use the funds to make an unsecured loan to the developer, Capicol. It was crucial for complainants to know this. Respondent was aware of this and deliberately misled complainants into believing that their funds were safe in an attorney's trust account.

d) Respondent does not dispute that complainants wanted a monthly income and capital preservation. Yet he did not point out to complainants that the prospectus warns that this is "*risk capital*" investment and monthly income is not guaranteed. There was a duty on respondent to disclose what was to become of complainants' funds and that this was a high-risk investment. Plainly, and on respondent's own version, he did not make full and frank disclosure of all the information about the investment to complainants.

[26] Respondent emphasises the fact that complainants reiterated their desire for a monthly income higher than what was offered by the banks. Respondent then points out that "*this was thus a single need investment*". I must immediately state that neither the Act nor the Code provides for a so called "single needs investment" and such a description does not feature in The Act or the Code and therefore does not exempt respondent from complying with any particular provision of the Act and Code.

[27] Of importance is respondent's statement that complainants "*found the risks associated with investing in Sharemax as acceptable*". Respondent is extremely vague about this and provides no detail. He does not say what risks in Sharemax complainants found to be acceptable. He has no record of advice documenting the risks complainants were willing to accept. Two risks in Sharemax stand out, firstly that it is a risk capital investment and an investor's funds could be lost; and Secondly, the income of 12.5% was not guaranteed. There is no record that complainants appreciated these risks and were willing, nevertheless to invest. On the probabilities, complainants would not have invested if these risks were understood buy them. There can be no doubt that these risks as well as the fact that their funds did not enjoy any protection from a trust account and Notice 459 compliance, were not disclosed to complainants. If respondent had explained these risks, as a prudent and competent FSP, he would have recorded such explanation in a record of advice. There is no such record of advice.

[28] Respondent then attaches to his declaration a number of documents signed by complainants in the process of making the investment. This was done on 30 September 2009. Respondent relies on an acknowledgement by complainants that they received a prospectus. However, the fact that the complainants received a prospectus is not important, what is relevant is whether or not they read and understood it. In the

respondent's version, he does not allege that complainants read and understood the prospectus, in fact he states that he explained the prospectus to his clients "*in detail*" but respondent is unable to demonstrate such a detailed explanation. It cannot be disputed that even if complainants attempted to read the prospectus, they did not have the capacity to understand it. They relied on respondent to place their investment in a safe product producing a monthly income and where there was capital preservation. Sharemax was certainly not that type of product and that much is made clear in the prospectus.

[29] Another Sharemax standard document, relied on by respondent, is "Sharemax Investments Risk Assessment on Product Information". This document was signed by the parties. The document is drafted by Sharemax and supplied to all its brokers. The document is nothing more than a sham. It purports to be some form of risk assessment. It comprises of 6 questions which must be answered by ticking off "yes" or "no". All the questions have absolutely nothing to do with risk in the product itself. One thing is clear, respondent did not explain the risks in this type of investment to complainant, neither did he explain the risks in this particular product. There is absolutely no evidence that respondent explained to complainant that this product represented a risk to their capital. Respondent was under a duty to explain such a risk to complainant.

[30] Respondent also attaches the application form signed by each of the complainants; which contains terms and conditions. In particular I refer to paragraph 6.1.2; this is an important term and one would expect a reasonably competent FSP to explain it to client. This provides that the investors funds will remain in an attorney's trust account but that the investor "*hereby" authorises the promoter to use the funds to invest in any property syndication and at the discretion of the promoter*. This contradicts the undertaking to hold

investor funds in trust until the promoter takes transfer of the property. It is also illegal in terms of Notice 459. Respondent did not point this out to complainants.

[31] Significantly, respondent quotes from various sections of the prospectus which make it clear that this is a high-risk investment where investor funds could be lost and that the promised returns may not materialise. Respondent merely relies on complainants own reading of the prospectus. However, on his own version, he gave complainants a "*detailed*" explanation of the prospectus; I therefore assume he explained these risks to complainants. The latter deny they received such explanation. Respondent himself can provide no record of advice that these peculiar risks, as stated in the prospectus, were explained to complainants. On the probabilities, if the risks had been fully disclosed by respondent, the investments would not have been made. It cannot be disputed that complainants had absolutely no appetite for risk. They were pensioners with no prospect of ever replacing lost capital.

[32] Respondent also attaches the quotations he prepared for complainants; which they signed. I note that the quotation contains "*Important Notes*"; one such note informs the investor as follows: "*Your investment will be deposited into the attorneys trust account of Weavind and Weavind, and preserved until the monies are cleared with your bank and the property transfer and registration process is finalised".* Respondent, who had studied and understood the prospectus, must have been aware that this was a completely misleading notice calculated to maintain the illusion that there will be compliance with Notice 459 and that investors funds were safe. Respondent knew that this statement was untrue as the prospectus disclosed that the funds were to be released to Sharemax who intended to use same to make an unsecured loan to the developer. By not explaining this to complainants he had, in truth, actively deceived them.

[33] It is further significant that respondent refers to the Code and correctly interprets it regarding the duties of an FSP. He then concludes that he fully complied with all his obligations as an FSP in terms of the Act and the Code. In support of this respondent states that he "*determined the risk in investing in Sharemax was within the risk profile of Mr and Mrs Wilken*". He further concludes that if complainants, with full knowledge and understanding, selected the Sharemax product, he had not failed in his duties as an FSP. I make the following findings:

a) Respondent admits that the Sharemax investment "*may not correspond with the investors' risk profile*". He nevertheless made an assessment of the risks and was satisfied that Sharemax was a suitable investment for them.

b) By any objective standards, the Sharemax investment was high risk. This much is not disputed by respondent. Neither can it be disputed that no investment, where there was a risk of capital loss, could be deemed to be suitable for pensioners who were investing all of their available funds and were dependant on income from the investment for their future financial maintenance.

c) Respondent can provide no rational reasons, having understood the risks stated in the prospectus, as to why he deemed this investment suitable for complainants. The only conclusions to be drawn are; firstly, that respondent actually did not understand the prospectus and/or the risks in the investment; or Secondly he did understand the risks but wanted to sell this product without offering the complainants any alternative products; or thirdly, respondent was out of his depth and was not competent to give financial advice for investing in property syndications and in particular Sharemax. In respect of any or all three possible scenarios, respondent did not comply with the Code and, in the circumstances, acted negligently in advising complainants to invest in Sharemax.

**Submissions regarding the Complaint**

[34] Respondent made important submissions regarding complainant's complaint against him. Respondent makes the following points:

a) That complainants never intended to make a complaint against him, but against Sharemax; complainants do not blame him for what happened to their investment;

b) Complainants only filed a complaint against him as a result of what they had read in the media;

c) Complainants wanted to withdraw the complaint but were influenced by a case manager in this office not to do so;

d) Whilst respondent accepts that this office may assist lay complainants with their complaints, respondent requests that all communications between this office and complainants be disclosed. The submission is that this did not happen;

e) That this office plays the role of a prosecutor rather than an independent and fair tribunal;

f) That complainants had seen an advertisement by Sharemax and had made up their own minds to invest in it. Respondent was referred to them by Sharemax and he was merely the facilitator.

[35] Respondents submissions are disputed. I deal with them as follows:

a) It cannot be disputed that respondent was appointed as complainants' FSP for the purpose of making this investment. The investment was made on his advice. Even if complainants wanted to invest in Sharemax, respondent had to carry out his duties as contemplated in the Code. Respondent was not a mere facilitator assisting complainants to merely place the investment. On his own version, he offered them other investments and explained the prospectus to them in detail. He

also advised them about the risks in the investment. He was not a mere facilitator. Respondent does not dispute that he received a commission of 6%, at no stage did he refuse the commission. I cannot make a finding that complainants were acting on their own decision and did not require financial advice from respondent.

b) Complainants were not influenced by the media nor by a case manager in this office. Complainants responded to respondent's allegations in a letter dated 8 January 2013, a copy of which was forwarded to respondent. That letter makes clear that the investment was made on respondent's advice after he was repeatedly informed that complainants could not afford to risk their funds and required a safe investment with monthly income and capital growth. Respondent never disputed this, instead it is his version that after he explained the risks to complainants, he considered the investment to be suitable for complainants and advised them as much. This defence is not sustained even on his own version.

c) This office is consistently accused by respondent's attorney of holding investigations "in secret" and not conveying all the information to respondents. This has been consistently refuted. This office keeps a record of all the information it obtains and such record is made available to respondents. There is no relevant information or facts which have been withheld from respondent by this office.

d) Equally, respondent's attorney consistently makes the spurious allegation that this office sees itself as a prosecutor and enforcer of discipline amongst FSPs. This office is an independent and fair Tribunal. This office carries out its duties strictly according to the empowering legislation and the Constitution.

**Due Diligence**

[36] Respondent states that before he advised complainants to invest in Sharemax he carried out a due diligence to the best of his ability. He then sets out the facts he took into account. I deal with them below:

a) Sharemax was licensed by the FSB and respondent saw this as a "stamp of approval". Respondent was misdirected; a licence by the FSB is not a stamp of approval. Besides the FSB made itself clear that granting a license does not amount to product approval.

b) Respondent considered Sharemax's impressive track record over 12 years. This is more misdirection. Sharemax had never before promoted anything like The Villa and Zambezi. In the past, their promotions involved purchasing and taking transfer of income generating property. Investors were in fact investing in property. With the Villa, investors were purchasing unlisted shares and debentures. Sharemax had no assets and no means to pay commissions and interest. It was up to respondent, as a reasonably competent FSP, to understand the current Sharemax model and to be able to work out that it was different and far more of a high-risk investment than any other investment they may have promoted in the past. Sharemax's performance over the years was no indication of the possible success of the Villa. In fact, the prospectus itself warns that this is a risk capital investment and that investor funds can be lost and the promised returns may not materialise.

c) Respondent claims that he strives to comply with the Act and Code. In support he points out that he was registered with Masthead, a compliance company. He also claims that Masthead "audits" his files. This is not relevant, Masthead is a compliance company, it does not carry out product approval. It is always the duty of registered FSPs to consider the risks as well as the benefits of the investments

they market. Whether a product is suitable for client is not what Masthead is concerned with.

**Independence**

[37] Respondent's attorney habitually makes baseless allegations of bias against this office. These allegations are not supported by any facts and I dismiss those allegations. This office remains independent and treats everyone equally and fairly.

**Legality of the Sharemax Model**

[38] The issue raised by respondent is that no finding of negligence on his side can be made unless it is established whether or not the Sharemax model was legal. This is not correct, respondent's negligence relates to his conduct in presenting Sharemax as a suitable investment for complainants, bearing in mind the latters' financial and risk profiles. The undisputed fact is that the Sharemax investment was high risk at the time he recommended it. It is equally not disputed that respondent was aware that complainants had no tolerance for risk and desired capital preservation and a monthly income. The question then is; what would a reasonably competent FSP, in the same circumstances, have advised. Would a reasonably competent FSP have selected Sharemax as a suitable investment for complainants?

[39] Respondent's submission is that the Sharemax collapse was triggered by the intervention of the SARB; which intervention he was not expected to have reasonably foreseen.

[40] The consequences of the SARB intervention are irrelevant to this complaint. The issue is whether or not respondent's advice to invest in Sharemax was appropriate after respondent took into account complainants' financial profile and financial needs. The

Sharemax investment was an investment *in risk capital*, not suitable, by any standard, for consumers of complainants' financial profile who had absolutely no appetite for risk. It is not in dispute that this was a risky investment, it says as much in the prospectus. As is the case with risk capital investments, there was always a risk that the complainant's capital will be lost. The exact reason for the loss need not be anticipated or foreseen at the time of giving the advice.

[41] In this regard I refer to a comprehensive determination by this office in:
**Johanna Van Den Heever v Dawie Joubert Makelaars and another FAIS 04955-12/13.**
For reasons stated in that determination, respondent's submissions are dismissed.

**Process and Procedure**

[42] This is yet another routine attack on the process and procedure in this office. Firstly, the constitutionality of the process in this office is questioned and secondly that the process and procedures are not suited to determining a dispute of this nature. Respondent relies on section 34 of the Constitution. This issue was already decided in the High Court in favour of this office and respondent's submissions are dismissed. See**: Deeb Risk and others v The Ombud for Financial Services and others Case no 38791/2011 Gauteng Provincial Division Baqwa J judgement date – 07/09/2012.**

[43] Respondent also submits that the nature of this dispute and remedy is such that only a court of law can determine it. This is not correct; this office is an independent and impartial tribunal as contemplated in Section 34 of the Constitution. It is capable of dealing with this complaint according to its powers and functions set out in the Act.
Again, I am not going to be derailed by various technical points about the constitutionality of the processes in this office and it is not necessary for me to decide these points. The

high court has already decided these points. The issues here pertain to respondents conduct in advising complainants to put all their available funds into Sharemax.

[44] Then the submission is made that there exist irreconcilable disputes of fact between the parties, to the extent that this office cannot resolve the dispute. There are some differences in the respective versions of the parties. But they are not material to the extent that the dispute is incapable of being resolved absent oral evidence. As I pointed out throughout this determination, the material findings of fact were made on the undisputed evidence coupled with respondent's own version. This is a well-known method of resolving disputes without hearing oral evidence; see **Plascon Evans v Van Riebeeck Paints 1983 (3) SA 623 (A) and Stellenbosch Farmers Winery v Stellenvale Winery 1957 (4) SA 234 (C).**

[45] It is apparent from this determination that I carefully considered all of the facts and submissions presented by respondent, he was treated fairly and was not prejudiced by the processes of this office.

**Technical Objections**

[46] Respondent's declaration contains a number of technical objections to the processes and procedures in this office. The submissions are a "copy and paste" from the declaration served on this office in respect of the Van Den Heever determination. I dealt with the respondent's objections in the Van den Heever determination; and for reasons stated therein, I dismiss respondent's objections to the processes and procedures in this office.

## D. THE ISSUES

[47] The fundamental issues here are the following: in giving complainants financial advice:

a) Did respondent comply with the provisions of the Act and Code;

b) If respondent failed to comply, was his conduct and advice, in the circumstances, negligent;

c) If respondents conduct was negligent, did that negligence result in loss to complainant.

[48] By all accounts, the Sharemax investment was high risk. Even respondent does not suggest that these products were safe for pensioners who relied on their savings and who were unable to lose any portion of their capital.

[49] It cannot be disputed that respondent advised complainant to invest in these investments. Neither is it in dispute that these were high risk investments. The further issues then are:

a) Were these investments suitable for complainants needs;

b) What motivated respondent to give this advice;

c) Did respondent place complainant in a position to make an informed decision; and

d) Was there negligence on the part of respondent in providing the advice?

[50] For purposes of this determination, a finding need not be made that Sharemax was a "Legal or illegal investment". The legality of the investment is not the test neither is it an issue; it is the suitability of the investment for complainants and their financial circumstances that is in issue.

**Negligence**

[51] A reasonably competent FSP, at the time of providing financial advice to client, can be expected to do the following:

a) ensure that he read and understood the Code;

b) understand that he is obliged to comply with the Code in providing financial advice;

c) understand the nature of the financial product/s he is recommending to client;

d) understand the product so that he is in a position to explain it to client in plain language;

e) accept that he is obliged to make a full and frank disclosure of all the available information about the product;

f) understand that he is obliged to ensure that his client will be in a position to make an informed decision; and

g) accept that he must recommend a product that is suitable for client bearing in mind the latter's financial circumstances and tolerance for risk.

[52] Respondent states that he explained the risks in the Sharemax product to complainants, however he is extremely vague about the details. There is no record of advice that documents the risks explained to complainants.

[53] Respondent's conduct in not explaining the risks is exacerbated by the fact that he had received training in the products and had even read and understood the prospectus. Yet he failed to tell complainants the following:

a) Neither their capital nor monthly income were guaranteed;

b) That the investments were considered risk capital;

c) That in fact they were not investing in property, Sharemax did not own any property and the shopping mall was still being built;

d) Their funds were not going to enjoy the safety of a trust account, but were going to be paid out to the promoters who were going to use it at their discretion;

e) That their funds were being lent to a developer to construct the building, before the promoter took transfer of the property and that the loan was not subject to any security;

f) That Sharemax was not going to comply with the requirements of Notice 459;

g) That Sharemax had no independent financial resources from which to pay agents commissions and interest on the capital to investors; and

h) That their interest was going to be effectively paid from their own capital and from the investments of other investors.

[54] None of the above was a secret, this information appears in the prospectus and was available to respondent at the time when he gave complainants advice to invest. Respondent admits to have read the prospectus. There can be no doubt that had this information been disclosed to complainants, they would not have invested. Respondent failed to comply with the Code and negligently advised complainants to invest their modest pension in Sharemax.

**Application of Law**

[55] Bearing in mind the facts found to be proved and the conclusions to be drawn from them, the following findings can be made:

a) Respondent failed to act honestly, fairly, with due skill, care and diligence;

b) Respondent failed to act in the interests of his clients and by his conduct compromised the integrity of the financial services industry. Respondent contravened section 2 of The Code;

c) Respondent failed to provide full and frank disclosure of all the material information about the Sharemax product;

d) Respondent failed to enable complainants to make an informed decision. Respondent contravened section 7 (1) (a) of The Code; and

e) Respondent failed to seek relevant information from complainants and failed to provide appropriate advice. Respondent failed to identify a product that was appropriate to complainants' risk profile and financial needs. Respondent contravened section 8 (1) (a), (b) and (c) of The Code.

[56] The fact that respondent was in breach of the Act and The Code does not mean that he is automatically liable for complainants' loss. There is a breach of contract as well as a claim in delict.

[57] Further, this office as well as the Board of Appeal has consistently found that there existed a contract between FSP and client. It is an express, alternatively implied term of the contract that Respondent, in carrying out his obligations, will comply with the provisions of the Act and The Code. For reasons already stated, respondent acted in breach of this term. A consequence of this breach was the loss of complainants' capital.

[58] In a number of recent judgements in the high court, it was found that complainants claim is one in delict based on negligence. Once it is established that the respondent gave financial advice, two questions arise:

a) did the respondent comply with his legal duties towards the client; and

b) whether in terms thereof the respondent acted wrongfully and negligently.

[59] A reasonably competent FSP in the position of respondent would have done the following:

a) Carried out a diligent research to become familiar with the nature of the Sharemax product he intended to market;

b) Would have found out that The Villa promotion was completely different to all the other property syndications Sharemax had promoted in the past;

c) As a basic step he was expected to read and understand the prospectus and the annexures thereto and explain it to complainants in plain language;

d) Made a point of understanding how Sharemax intended to pay his commission and investors returns bearing in mind that the latter owned no assets and enjoyed no trading history and did not have any independent means of making these payments (these facts are stated in the prospectus). Significantly, respondent had a duty to explain all this to complainants;

e) Would have noticed that contrary to what was initially stated in the prospectus, it then informs that investor funds will not be kept in trust but will be paid out to the developer at the discretion of the promoter (this too is stated in the prospectus), this had to be explained to complainants;

f) Respondent knew that investor funds were going to be lent to the developer at an interest rate of 14% and that there was no security for the loan (stated in the prospectus), he was under a duty to inform complainant about this;

g) Would have called for and read the Sale of Business Agreement between the promoter and the developer (the agreement is in the schedules and annexures to the prospectus). Had he done so respondent would also have found out that 3% of the investor's capital was being paid out as "agents commission", 10% was deducted by the promoter as administrative fees. The developer then paid the promoter 14% interest on the loan; a further 14% taken out of the capital. A reasonably competent FSP would have worked out that after 27% of the capital was deducted, investors were still going to be paid 12% interest on 100% of their capital. This was certainly not sustainable (these facts are stated in the prospectus). Respondent failed to inform complainant of this;

h) Would have noticed that the shares will not be easy to dispose of, the promoter offered no assistance in disposing of the shares and the onus was placed on the investor to find a buyer (also stated in the prospectus).

Clearly by failing to draw complainant's attention to the above information, respondent failed in his legal duties to his client.

[60] The respondent also acted wrongfully and negligently; he was under a legal duty to make a disclosure of these facts to complainant. Respondent acted negligently in not making full and frank disclosure thereby depriving complainants of the right to make an informed decision.

[61] Respondent must be judged by the standard of a reasonably competent FSP in the same circumstances. Then the inquiry must progress to the next question: would a reasonably competent FSP have advised complainant differently? It is overwhelmingly clear that a reasonably competent FSP would have read and understood the prospectus and would not have advised pensioners to invest all their available funds in a manifestly high-risk investment where there was a prospect of losing all the capital. The SCA in **Durr v ABSA Bank**, Schutz JA stated as follows:

*"The reasonable person has no special skills and lack of skill or knowledge is not per se negligence. It is, however, negligent to engage voluntarily in any potentially dangerous activity unless one has the skill and knowledge usually associated with the proper discharge of the duties connected with such an activity."*

"Liability *in delict arises from wrongful and negligent acts or omissions. In the final analysis the true criterion for determining negligence is whether in the particular circumstances of the conduct complained of falls short of the standard of the reasonable person."*

Respondents conduct fell short of this standard and was the factual and legal cause of complainant's loss.

[62] Accordingly, and in the circumstances, the respondent was under a legal duty of care to comply with his obligations. An omission to comply, in the circumstances, amounts to a negligent breach of the duty of care. A reasonably competent FSP, at the time of providing advice, should reasonably be expected to foresee that in the event of a breach of the aforesaid legal duty of care client will suffer harm and that the harm will be the possible loss of client's capital. The precise or exact manner in which the harm occurred need not be foreseeable, the general manner of its occurrence had to be reasonably foreseeable. For example, advice to invest in a risky investment must result in a reasonable foreseeability that the investment could be lost in the near future. It is not a question of performance of the product but the realisation of existing risks in the product.

[63] The reasonable foreseeability must become even clearer where the product provider actually warns the FSP of the risks in the product. As in this matter, the prospectus and disclosure documents stated the risks in the Sharemax investments. The respondent was aware of these risks; but nevertheless, advised complainants to invest their funds.

Respondent's conduct fell short of a reasonably competent FSP and respondent was the factual and legal cause of complainants' loss.

See **Sea Harvest Corporation (Pty) Ltd and Another v Duncan Dock Cold Storage (Pty) Ltd and Another 2000 (1) SA 827 (SCA).**

[64] I refer to the following decisions:

**OOSTHUIZEN v CASTRO AND ANOTHER 2018 (2) SA 529 (FS)**

**CENTRIQ INSURANCE COMPANY LTD v OOSTHUIZEN AND ANOTHER 2019 (3) SA 387 (SCA)** – approved of the Castro judgement.

**ATWEALTH (PTY) LTD AND OTHERS v KERNICK AND OTHERS 2019 (4) SA 420 (SCA) at p529.**

[65] For all of the reasons stated above, I find that respondent acted negligently and such negligence was the cause of complainant's loss.

## E. THE ORDER

[66] The following order is made:

1. In respect of first complainant:

    a) The complaint is upheld;

    b) The respondent is ordered to pay to complainant an amount of R45 000;

    c) Interest on the amount of R45 000 at the rate of 7%, seven days from the date of this order to date of final payment.

2. In respect of second complainant:

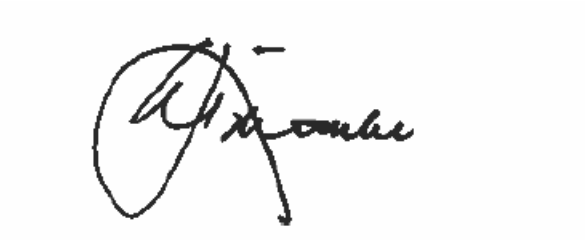
    d) The complaint is upheld;

    e) The respondent is ordered to pay to complainant an amount of R300 000;

    f) Interest on the amount of R300 000 at the rate of 7%, seven days from the date of this order to date of final payment.

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

**DATED AT PRETORIA ON THIS THE 8th DAY OF FEBRUARY 2021.**



**ADV NONKU TSHOMBE**

**OMBUD FOR FINANCIAL SERVICES PROVIDERS**