THE OFFICE OF THE OMBUD FOR FINANCIAL SERVICES PROVIDERS

PRETORIA

CASE NUMBERS: FAIS 04955/12-13/FS1

In the matter between:

JOHANNA MAGDELENA DOROTHEA VAN DEN HEEVER **Complainant**

AND

DAWIE JOUBERT VERSEKERINGS MAKELAARS BK **First Respondent**

DAWIE JOUBERT **Second Respondent**

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

A. INTRODUCTION

[1] Complainant invested an amount of R300 000 in the now defunct Pickvest Highveld Syndication No. 21 Ltd investments (the Pickvest investment) and a further R300 000 in the now equally defunct Sharemax Property Syndication (the Sharemax

Kasteelpark, 2nd Floor, 546 Jochemus Street, Erasmuskloof, Pretoria
P O Box 74571, Lynnwood Ridge, 0040
Phone: (012) 762 5000; Fax: (012) 348 3447 / (012) 470 9097 Sharecall 086 066 3274
www.faisombud.co.za

investment). Both investments were made on the advice of the second respondent. It is no longer in dispute that complainant's capital, in respect of both investments, is lost with no prospect of recovering any portion thereof. Complainant filed a complaint and requests that her combined capital in an amount of R600 000 be recovered from the respondents.

[2] The first respondent is a licensed financial services provider (FSP) in terms of the Financial Advisory and Intermediary Services Act ("the Act") with licence number FSP 3368. Second respondent is the owner of the members interest in the first respondent close corporation and is also its key individual in keeping with the Act. Respondents responded to the complaint as well as to questions posed by this office during the course of investigating the complaint. In responding to the complaint and to this office, respondents were represented by their attorneys.

[3] Both parties are from Kroonstad and their details are on record in this office. For convenience I will refer to the respondents as "respondent" but will be more specific where the context requires me to do so.

B. THE COMPLAINT

[4] Complainant is 67 years old and at the end of July 2009 her husband passed away unexpectedly due to a heart attack. Her late husband had a life insurance and complainant wanted to find a suitable investment for the proceeds from his policy. Complainant's goal was to receive a monthly income from her investment so that she can continue to maintain her modest living standard and her brother-in-law referred her to respondent.

[5] She states that respondent called her several times a day to find out when she will come to make the investment. She informed respondent that what she had was all the funds available to her for her old age and that she could not afford to lose it.

[6] The first investment recommended by respondent was Pickvest alleging that the guaranteed interest was 12.5% per annum and that the capital was also guaranteed. On 4 September 2009 complainant, through respondent, invested R300 000 in Pickvest.

[7] Complainant's late husband's policy paid another amount and respondent approached her to make another investment through him. This time he recommended an investment in Sharemax The Villa. Complainant agreed to invest an amount of R300 000 in Sharemax as respondent explained it was the same as Pickvest. The Sharemax investment was made on 8 January 2010.

[8] For a few months everything went well and complainant received a monthly income of about R6400 per month, from both investments combined. Then one month, Sharemax failed to make interest payments and soon thereafter Pickvest also defaulted. She called respondent repeatedly and spoke to his secretary who told her that they are busy sorting everything out. Later Pickvest sent a letter informing her of revised interest rates which were substantially lower than the initially guaranteed rate of 12.5%.

[9] Complainant called on respondent's office and spoke to him. He told her that "it was high time that your children begin to take care of you". For a while complainant did not

pursue matters in the hope that Sharemax can be rescued so that she may receive an income again.

[10] Complainant's daughter began assisting her financially by paying her municipal bills and buying groceries. Her health deteriorated and she became diabetic and required to use insulin daily. She also developed a condition on her spine which caused extreme pain. She needed an operation but was unable to afford one. She had to wait for a provincial hospital to find the time to accommodate her. She is still waiting. Complainant is financially destitute and decided to pursue a complaint against respondent.

[11] Complainant requires return of her capital of R600 000 as well as the outstanding, guaranteed, interest payments.

[12] On 31 August 2012 complainant wrote to respondent explaining that her financial position was dire. She reminded him in the letter that she took the trouble to make him understand that she could not afford to lose even one cent of her capital and that the funds were meant to provide her with a monthly income. She points out that the investments were made in the property syndications on his advice.

[13] In the same letter she informed respondent that she intends taking the matter to this office unless he can come up with an agreement within 14 days. On 6 September 2012 respondent responded in a letter. He acknowledged receipt of her letter and informed her that he referred her case to his insurer AON South Africa (Pty) Ltd and that their attorneys will be in contact with her.

Complainants Documents

[14] In support of her complaint, complainant attached a number of material documents. I will highlight certain aspects from these documents below. The documents are not disputed and also form part of the respondent's documents. Nor is it disputed that respondent was the source of all the documents.

Service Level Agreement

[15] This is an agreement that was entered into by the parties, on the same day that the Pickvest investment was made (4 September 2009). Respondent signed the agreement as did complainant. This is a pre-printed document which contains a number of blank spaces required to be filled by the client. This document was filled in by respondent as it appears to be his handwriting. The following are noteworthy observations:

a) The document begins by noting that its purpose is to effectively manage client's financial risks;

b) The complainant stated that her requirements comprise an investment of R300 000;

c) The contract confirms that in the event that client requires a specific service, a full financial needs analysis will not be done. The client further confirms that a needs analysis need not be carried out. The client agreed that there will therefore be limits to the appropriateness of the advice and that the onus was on client to decide or weigh if the advice given was appropriate, bearing in mind her financial needs;

d) Client confirms that the advisor will provide advice based on the information provided by client;

e) The contract confirms that commission of 6% will be paid by the product provider.

[16] There appears to be an attempt, by respondent, to contract out of the provisions of the Act and the General Code of Conduct for authorised FSP's and Representatives ("the Code"). It is not possible to contract out of applicable legislation, Codes and Notices. Even if complainant wanted a single investment of R300 000; the Act and Code requires respondent to provide financial advice in keeping with the legislation. In this case respondent had even in the absence of a financial needs analysis, been informed in no uncertain terms that the funds were meant to provide an income for retirement and that complainant could not afford to lose a single cent of it. It did not require a needs analysis to inform respondent that complainant had absolutely no tolerance for risk.

Investment Proposal

[17] A relevant document is one titled "Investment Proposal". This is also a pre-printed document with some blank spaces for client to fill. It is a Pickvest document and the blank spaces appear to have been filled in by respondent in his hand writing. The following is noteworthy:

a) The document begins by stating that in the light of the needs and risk analysis carried out and the broad discussion around the prospectus and Pickvest product, the client confirms what follows.

b) Client confirms that the main features of what an investment should provide for her is:

"1. Guaranteed income

2. Guaranteed capital

3. Interest that beats the inflation rate

4. Is willing to invest for five years."

c) Respondent confirms that he was instructed to provide a specific service regarding property syndications. It then states that to comply with client's needs the following product features are set out:

"1. Income is guaranteed at 12.5% per annum

2. Capital is guaranteed by a buy-back agreement

3. Interest rate easily beats inflation

4. The investment is in unlisted shares

5. The investment must be for five years."

[18] This document was also signed by the parties on 4 September 2009. Of significance is the following: Firstly, complainant did not give respondent a specific instruction to invest in property syndication, she merely trusted respondent to invest her only funds in a safe investment. Secondly, respondent merely handed a prospectus over to complainant. Thirdly, the Pickvest investment did not guarantee income, nor did it guarantee the capital. This was known to respondent. Fourthly, complainant, who knew nothing about investments and property syndication, could not possibly have requested an investment in unlisted shares. Fifthly, complainant did not have the capacity to understand how a buy-back scheme worked and how it guaranteed her capital, she could not possibly have selected this as a feature for her investment.

Advice Record of Mutual Understanding

[19] This document is yet another document produced by Pickvest which complainant signed on 4 September 2009. It is certainly not a record of advice as contemplated in Section 9 of the Code. The purpose of this document is clearly to protect Pickvest and is not a record of advice by the respondent setting out how he advised complainant

and in particular how he concluded, in the light of complainant's financial circumstances, that the Pickvest product was appropriate for her financial needs and tolerance for risk. The following is relevant:

a) The document commences, with a preamble, by confirming that the parties had agreed as follows:
   - That respondent had conducted a financial analysis based on complainant's instructions and answers to a risk questionnaire;
   - That respondent provided investment advice based on what complainant wanted;
   - That complainant accepted the advice;
   - That complainant instructed respondent to continue to make the investment; and
   - That the parties agreed to reduce to writing the main features of the advice and agreement.

   Then follows, *inter alia,* what was agreed as the terms and conditions of the investment solution:

b) It is recorded that there is a once off investment of R300 000, and the investment is in unlisted shares;

c) The object of the investment is recorded as being a medium to long term growth providing a reasonable level of monthly income for the complainant;

d) The capital will be paid into the trust account of attorneys Eugene Kruger and Co and will be administered by Pickvest;

e) The capital is "protected" by a buy-back agreement the income by a head lease as stated in the prospectus;

f) The investment is subject to fluctuations in the property market and this could have a negative impact on the value of the investment. That complainant understands this and accepts the risks;

g) That it is not possible to guarantee the capital and promised income;

h) Investors income is paid out of the syndication company's nett profits, minus necessary corporate expenses;

i) The document warns that this investment is difficult to sell as it is in unlisted shares. The company undertakes to assist investors to sell their shares at the cost of a market related commission;

j) Commission payable to the respondent is 6% of the capital which Pickvest will pay.

[20] There are a number of difficulties with this document. Respondent signed it knowing full well that it does not comply with complainant's instructions. The terms and conditions certainly do not guarantee an income of 12.5% per annum, nor does it guarantee that capital will be preserved. It also makes clear that there are risks that the promised income would not materialise and complainant accepts that risk. The capital is paid into a trust account, but complainant is notified by this document as well as in a letter from the attorneys that the funds will be administered by Pickvest. Neither this document nor any other document handed to complainant deals with Notice 459 and it is plain from a wording of the terms and conditions that Pickvest had absolutely no intention of complying with this notice. Respondent was aware of this and failed to explain the consequences to complainant when he was under a duty to do so. It is patently clear that these documents contradict one another. On the probabilities complainant did not read and understand them, I note that all the documents, many pages of complex terms, were signed by her and the respondent at the same time and

place. Respondent was under a duty to explain the contents to complainant in plain language. Respondent did not provide this office with any record of advice which states that he gave his client an explanation in plain language and that she understood that she was investing in a high-risk investment. Respondent is compelled by the Code to keep such record of advice. On respondent's own version, had he explained the risks to complainant that neither her capital nor her income was guaranteed, she would not have invested.

Application Form

[21] The next document is the application form for shares in Pickvest. This application takes the form of a contract between complainant and Pickvest, where the complainant agrees to purchase shares which Pickvest is authorised to market in terms of the prospectus. Then follows an acknowledgement that the complainant received a copy of the prospectus and was able to understand its contents.

There is no evidence that complainant actually read and understood the prospectus. In fact, she states that she did not read it but relied on respondent. Nor can it be disputed that she was incapable of reading and understanding the contents thereof. She was possessed of a Standard six education and had no experience of finance and financial products.

[22] This document then deals with how investors' funds will be handled. The agreement notes that the money will be deposited in an attorney's trust account. Then the contract states that the promoter is authorised to instruct the attorneys to invest the funds in terms of Section 78 (2A) of the Attorneys Act.

In the same paragraph, the contract states that the funds will remain in such investment until the company (Pickvest Highveld Syndication No. 21 Ltd) takes

occupation of any of the properties described in the prospectus. This is completely misleading and contrary to Notice 459. The Notice provides that the funds may be transferred out of trust to the company upon the latter taking ***transfer*** of the property. The Notice does not authorise the syndication company to take transfer of the funds upon occupation of the property, only upon transfer. There was a duty on respondent to have advised complainant that Pickvest was in contravention of Notice 459 and that her funds did not enjoy the protection and benefit of a trust account. There is no record that he had done so. On the probabilities, had respondent discharged that duty, complainant would not have invested in Pickvest.

We know for a fact that investors funds were not invested in terms of Section 78 (2A) and were immediately paid out to Pickvest. The investor enjoyed no security and the payment into a trust account merely created an illusion that the funds were safe.

[23] Again, this contract confirms that complainant did not read and understand the contents of the prospectus.

[24] This document was also signed on 4 September 2009.

Quotation

[25] This document is a quotation for an investment in HS 21 in an amount of R300 000. The quotation, possibly prepared by respondent or even Pickvest, sets out the expected returns over a period of 5 years. What strikes one immediately is that the projected income is set at 12.5% per annum for each of the 5 years. This quote was presented to complainant by respondent who represented that a return of 12.5% was guaranteed. Yet one will find no such promise, guarantee nor undertaking from

Pickvest in any of the documents signed by complainant. As pointed out above, Pickvest points out that there is a risk that the promised income may not materialise.

Important Information

[26] This document is titled “important information”. It begins by stating that the “projected” income will be paid monthly, the rate is 12.5%.

Again, this is not a guarantee of an income at this rate. It is merely a projected income. We know for a fact that after the investment was made, complainant received a letter from Pickvest stating that due to market conditions, there will be a reduction in the interest rate. In fact, there was a substantial reduction.

Risk Assessment

[27] This is an important document. Its title is significant; “Risk Analysis in respect of Product Information”. This is a Pickvest document comprising a number of questions with a choice of a “yes” or “no” answer in tick boxes. I have read the six questions and it is clear that they relate to product information and have absolutely nothing to do with the complainant’s financial risk profile. For instance, the obvious question is missing: “Can you afford to lose any part of your capital?”; or “Are you aware that this is a high-risk investment?”

[28] It also appears that it was not complainant who ticked off the boxes, it was probably the respondent.

[29] I must also add that there are other documents which were handed to complainant, but were not signed and merely left in blank.

Assets and Liabilities

[30] Complainant made a disclosure of her assets and liabilities. The sum total of the value of her assets was R475 000. She was in temporary employment, close to retirement, earning R3500 per month. This surely informed respondent that this was a client of very modest means who was unable to replace lost capital. Respondent did not explain why, in the circumstances, he advised her that Pickvest, and later Sharemax, were appropriate and suitable investments for her needs. Respondent was also aware that complainant had no pension fund nor any other investments to sustain herself. The proceeds from her late husband's policies was all she had.

[31] Respondent, in his answers to questions put to him by this office, still believed that the Pickvest and Sharemax investments were appropriate for complainant as the latter wanted to "sustain a certain lifestyle". What this lifestyle was is not explained and is a blatant attempt by respondent to mislead. It is not in dispute; complainant lived very modestly and was left destitute when the investments failed. Respondent also believed that the Pickvest and Sharemax products answered complainants need for "high monthly return and capital growth as a hedge against inflation". Every investor requires higher returns, that is no reason to place their funds into high risk investments. Respondent does not dispute that Sharemax was a "risk capital investment" (the prospectus states as much) still he believed that these highly risky investments were suitable for someone with a nett worth of only R475 000. Respondent, typical of many brokers, refers to the investments as "single need investments". There is no such thing in the Act and the Code. Respondent was still obliged to comply with the Act and Code. A person who was worth only R475 000 cannot be regarded as anything other than a conservative investor with no capacity to

replace lost capital. Any reasonably competent FSP would have realised that complainant was not suitable for risk capital investments. This is an indication of negligent conduct on the part of respondent.

[32] "Risk capital investments" by their very nature, are not suitable for anyone with complainant's financial profile. Risk capital refers to funds allocated to speculative activity and used for high-risk, high-reward investments. Risk capital is the funds that are expendable in exchange for the opportunity to generate outsized gains. Investors must be willing to lose all of their risk capital and it should only account for 10% or less of a typical investor's portfolio equity. I must assume that the respondent, as highly qualified as he was, was aware of this. His advice to invest complainant's funds into risk capital investments was nothing short of negligent.

Needs Analysis and Risk Profile

[33] This is another document for a needs analysis and risk profile of complainant. Again, this is a pre-printed set of questions which required a selection from multiple choice answers. This document also does not effectively make an assessment of complainant's risk profile as most of the questions are not pertinent to this issue.

[34] However, some information is worth noting. As her main objective in investing, complainant stated that she required a monthly income and capital preservation. She stated that she expected an interest rate or return of 12.5% per annum. It must be remembered that complainant had no idea what her investment was expected to earn. The figure of 12.5% came from a promise made by respondent. At the end of this document, respondent conveniently omitted to state what complainants risk profile was. Clearly, she was a conservative investor who had no appetite for risk.

The Loss

[35] Complainant received a letter from Pickvest dated 30 March 2011 which informed her, *inter alia*, that due to various problems with lessees and cancellations, the interest rate will be reduced from 12.5% to 6.5%. This reduction came without warning and dealt a blow to complainant's fragile finances.

[36] On the 14 September 2011, things got worse, complainant received a letter informing her that HS 21 Ltd was being placed under business rescue. Payments of interest stopped and eventually HS 21 was liquidated and complainant lost her capital.

An Informed Decision

[37] One of the objectives of the Code is to ensure that investors are fully informed about the financial product they intend to invest in, so that they may make an informed decision. The Code placed a duty on respondent to fully inform complainant about the Pickvest and Sharemax investments. I note that complainant simultaneously signed all the documentation on the same date in a single consultation or visit by respondent. It was simply not possible that Respondent could have given complainant a full explanation and a full and frank disclosure of all the facts about Pickvest and Sharemax during this one visit. This was a complex investment involving head-leases and buy-back agreements, well beyond the capacity of complainant. The latter merely wanted a monthly income and capital preservation. This is what respondent guaranteed her and, having placed her trust in him, she signed all the documents. Neither Pickvest nor Sharemax gave any guarantees and they remained highly risky investments that were certainly not suitable for complainants needs and tolerance for

risk. As I will show below, respondent failed to comply with the requirements of the Code and put complainant in an investment not suitable for her needs.

C. RESPONDENTS RESPONSE

[38] Respondent filed a declaration coupled with supporting documents in response to the complaint. In addition, in response to a set of questions presented to respondent, the latter filed a supplementary declaration. I deal with both responses below.

Respondents Declaration

[39] Respondent presented this office with comprehensive responses. This included:

a) a declaration presented in response to the complaint;

b) a letter from his attorneys challenging this Office's finding regarding the nature of the Sharemax model; (here I pause to observe that this is not an issue if respondent admits that it is a risky investment where complainant can lose her income and capital) and

c) a supplementary declaration answering a series of questions submitted by this Office.

I have taken cognisance of these documents, together with all the annexures thereto, and this is evident throughout this determination.

The Declaration in Response

[40] It is a matter of routine for respondent's attorneys 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;

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

c) Thirdly, that this office does not have jurisdiction to determine this complaint; as the complaint falls within Section 27 (3) (a) (i) of the Act.

[41] 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 Board of Appeal and nor 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 is 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 will take too long, become unaffordable to most complainants and will require this office to find resources it does not have. Both parties are treated fairly and the High court has already ruled that the processes of this office do not deprive the parties of a fair hearing nor is it 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.**

c) The third point is without merit and cannot succeed. This complaint is not struck by Section 27 (1) (3) (a) of the Act. Respondents submissions are vague and lacking in detail in that no chronology is provided in order for this office to refuse to deal with this matter in terms of this subsection. The operative date is not the date of the investment, being the 4 September 2009, but the date on which complainant ought reasonably to have become aware of the problem with respondent's advice. That date was the date when her monthly payments stopped. It is not disputed that by August 2010, both Pickvest and Sharemax defaulted on monthly payments to their respective investors. She then waited to see if the problem will be rectified by the promoters. This did not happen and in September 2011 Pickvest was placed under business rescue. On the 13 September 2012, she lodged the complaint. Her complaint was made well within the three-year period.

[42] In the paragraphs that follow, I will refer to paragraph numbers, where necessary, from respondent's declaration for ease of reference.

[43] Respondent knew complainant and her late husband and must have known that they were people of very modest means and that complainants only available funds was the proceeds of two policies her husband had taken out, and which paid out after his untimely death.

[44] Respondent admits that complainant instructed him to find a "suitable investment for her funds". She was relying on respondent's advice and placed her trust in him to find her a suitable investment.

[45] On respondent's own version, they met for the first time, to discuss investment on 4 September 2009. On the same date, the Pickvest investment was made by complainant. The point being made is that respondent relied on complainant's own reading and understanding of the Pickvest investment. It is impossible for complainant (with her standard 6 education and no experience of financial investments) to read and understand the Pickvest prospectus, read and understand the many and voluminous documents she signed and be in a position to make an informed decision; all in a matter of a few hours, if even that. Complainant's version is that she did not read the prospectus and this is the most probable version.

[46] In paragraph 18 respondent states that he advised complainant that:

a) From a risk point of view, this was an acceptable investment, as the investments were supported by underlying properties;

b) Pickvest gave a guaranteed income of 12.5% and;

c) Pickvest guaranteed, through a buy-back, complainant's capital.

All of the above is not true and, on respondent's own version, he read and understood the prospectus. The Pickvest prospectus did not provide any such guarantees, in fact it warned investors that they could lose their capital and the income was not guaranteed. On respondent's own version, he did not tell complainant about this risk. Nor did he inform her that HS21 did not own any properties. He had effectively misled complainant.

[47] In paragraph 20 he claims to have explained the prospectus to her "in detail". Yet he contradicted what the prospectus actually stated. He knowingly misled complainant.

In paragraph 22 he states that after their discussion, complainant immediately decided to invest in Pickvest. What this confirms is that she did not have any opportunity to read and understand the prospectus. The prospectus made it clear that this was a high-risk investment. The form she signed stated that the Pickvest investment constituted *risk capital*.

[48] In paragraph 24 respondent admits that he was aware of the need to "spread risk" therefore he chose to invest in Sharemax. Ironically, he invested her funds in an equally risky investment and failed to disclose this to complainant.

The meeting for the Villa investment was on 8 January 2010. Again, the investment was made on the same date, complainant could not have read and understood the prospectus and read and understood voluminous documents to sign, all on the same day and in a matter of hours.

[49] In paragraph 25 respondent admits to advising complainant that the Sharemax investment structure "*was very much similar to the Pickvest investment*". This was misleading as the two investments are certainly not similar at all. The only similarity being that both investments warn the investor that each is a high-risk investment.

[50] In paragraph 26.4 respondent admits that the prospectus warns that investors could lose all their capital. This is contrary to complainant's requirement that she wanted capital preservation and respondent knew she was not in a position to risk her capital.

[51] In paragraph 32 respondent states that complainant does not complain about his conduct but only complains about product performance. His point being that therefore this does not amount to a complaint against him and must not be entertained by this office. This is not true, complainant's complaint is clear in its terms, although she wrote it as a lay person. Her complaint is not about product performance but about the loss of her income and capital. She complains that the loss was the result of respondent's advice and wants him to compensate her for the loss.

[52] In paragraph 34 respondent states that he carried out due diligence:

a) That companies were reputable because they were registered with CIPRO, this is nonsensical. Such registration tells one nothing about the reputation and financial standing of a company.

b) Respondent submits that both prospectuses complied with Notice 459. This is incorrect. Both prospectuses actually tell the investor that the companies had no intention to comply and did not comply with the notice. Significantly, respondent's own expert, Mr. Swanepoel, confirms that Sharemax did not comply with Notice

459, but justifies it on the basis that the Notice did not apply to Sharemax. This office disagrees as there can be no legal dispute that the Sharemax scheme was subject to Notice 459. This shows that respondent was either misleading his client or that he was out of his depth and did not know, in either event his conduct was negligent.

c) Respondent sets out a number of formalities which Pickvest and Sharemax complied with and claims to have carried out due-diligence. What was actually required of respondent was for him to fully understand the investment scheme, in particular to weigh the risks in the schemes, in order to properly advise his clients.

d) Respondent fails to state that he was satisfied that these were high risk investments. If he did not understand this about Pickvest and Sharemax, then he was incompetent and should have consulted someone who knew. He was negligent. See **Durr v ABSA Bank.**

[53] In paragraph 37 respondent relies on being registered with Masthead and suggests that Masthead was satisfied with these investments. Respondent does not state that Masthead warned him that these were high risk, risk capital investments where investors could lose their funds and income was not guaranteed. An aspect ignored by respondent; he was negligent in not finding out more about the risks before selling the product to conservative risk averse investors.

[54] Respondent's comment that this office is influenced by negative media reports around Pickvest and Sharemax is unfounded. This office makes comment about these investments based on what the prospectuses state. This office is independent and is not influenced by media statements.

[55] In paragraph 41 respondent deals with an important issue; respondent states that he could not have foreseen that the SARB will intervene, which caused the collapse. It was never established as a fact that the Reserve Bank's intervention was the cause of the collapse with regard to both Pickvest and Sharemax. The directors of these companies, as well as a number of their brokers, latched onto the actions of the SARB and turned this into an excuse for the collapse of the investments. The truth is that these were highly risky investments and collapsed because the business and funding models were unsustainable. These investments were doomed to collapse even if the SARB did not intervene. It must also be noted that the SARB did not shut these companies down nor did it prevent them from trading. However, once the media published the SARB's intervention, Sharemax and Pickvest were unable to attract new investments. The whole scheme relied on a steady stream of new investors; whose funds were used to pay interest to the existing investors and to continue funding development. It is not disputed that Sharemax and Pickvest paid investors immediately whilst not having any independent income nor any assets.

[56] Respondent obfuscates the real issues here. These were high risk investments when the investments were made. Respondent does not have to foresee how or why they collapsed. The point is that a risk materialized, respondent was expected to foresee the risk that actually materialized. The matter was not beyond his control, he was negligent in advising complainant to invest in such high-risk investments. But for such negligent advice, complainant would not have invested and would not have lost all her funds.

[57] It is not true that Pickvest continues to pay interest. First, they reduced the amount paid, then payments were missed, after which no payments were received. Nor is there any prospect of complainant recovering any part of her capital and arrear interest payments.

[58] Respondent, in paragraph 44, claims to have closely followed the media after July 2010. He also claims to have kept his clients informed. This is significant that he only read the media reports after the investments collapsed. If respondent, as a reasonably competent FSP, closely followed media reports, including financial media reports, he would have come across many articles and reports questioning the Sharemax and Pickvest investments. These reports began to emerge in 2006 and continued to make an appearance consistently. Surely a prudent FSP would have been careful about marketing these products and would have, as was his duty, made a full and frank disclosure to his clients. It is not in dispute that respondent did not draw complainant's attention to the negative media reports before the investments were made.

[59] Respondent submitted that it is premature to consider compensation because investors could still recover their funds. This is not true. This office does not know of any investor who recovered their capital and arrear interest payments. Sharemax and Pickvest were liquidated. There is no prospect that Frontier Asset Management will make any payments to investors.

[60] I consider respondent's submission in Paragraph 48 to be important; he submits that no decision concerning his alleged negligence can be made unless it is established whether or not Sharemax and Pickvest models were legal and what caused them to default in making payments to investors. There is no merit in this submission.

Respondent's negligence is not based on the legality of the investments but on whether or not such high-risk investments were suitable for complainant. This enquiry must be made bearing in mind, on respondent's own version, that he was aware that there was a risk of losing all the capital. Nor is the cause of the failure of these companies relevant to the respondent's negligence.

[61] In paragraphs 50 to 53 respondent in effect challenges the constitutionality of the processes in this office. Respondent relies on section 34 of Constitution. This issue was already decided in the High Court in favour of this office and respondent's submissions were 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.**

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 deflected 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 pertain to respondents conduct in advising complainant to put all her available funds into Sharemax and Pickvest.

[62] I am compelled to briefly deal with a submission made by respondent in paragraph 64. Respondent states that there may be a perception that it is equitable to allocate risk of failed investments onto an FSP because he/she must have professional

indemnity cover. I reject this submission as this office resolves disputes based on the facts and the law. Perceptions are not relevant, nor is respondent's insurance cover or lack thereof relevant to the issues before me.

[63] Respondent's submission that this office is not obliged to keep records of its investigations. This office maintains a record of the proceedings and practices transparency. When matters are referred to the Tribunal, this Office is required to file such record and the proceedings in this office are not off the record and respondent has been provided with all the documentation, including correspondence, from the moment the complaint is filed. No decision is made based on facts that are unknown to complainant and respondent.

[64] This office does not perform any disciplinary functions. Respondent is misdirected. This office's purpose is to consider and dispose of complaints in a procedurally fair, informal, economical and expeditious manner. This office also does not order compensation for a mere breach of the Code. The respondents conduct must also, in the circumstances, be negligent. Such conduct can also amount to a breach of contract.

[65] Respondents submissions in paragraph 74 is entirely irrelevant to this complaint. The issue here is the respondents conduct in advising complainant and it has nothing to do with the blameworthiness of any other party. The submissions in paragraph 74 have been dealt with by the erstwhile FSB Appeal Board and the courts.

[66] 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).**

Neither can respondent complain that he was deprived of the opportunity to call expert witnesses. In fact, respondent filed expert opinions which, as appears elsewhere in this determination, were properly considered and weighed.

[67] Finally, I am compelled to comment about respondent's scandalous allegations that this office is not independent and is influenced by the FSCA. The allegation is made merely on the basis that the FSCA intends to conduct investigations into misconduct on the part of Sharemax. Then follows allegations of bias. This determination was not made with access to secret information from the FSCA (formerly FSB). The record of the process is in the possession of respondent and that is all that was used to deal with this determination. There is also an unfounded attack on the integrity of the FSB (FSCA) that it wields influence over this office and influences the decisions of this office. This is denied in the strongest terms and respondent is reckless in making it.

[68] Respondent's response is concentrated on the following:

a) An attack on the processes of this office;
b) Attacks on the integrity of this office, with unfounded accusations of bias;
c) Lengthy explanations of the Sharemax model and why it was a perfectly legal investment;

d) Speculation about the cause of the collapse of Sharemax; and

e) Attempts at justifying respondent's advice to complainant.

[69] The majority of respondent's responses, and they are extremely and unnecessarily lengthy and repetitive, amounts to plain obfuscation. Respondent's strategy is to document bomb this office and to deflect attention from the actual issues at hand.

[70] Even if the Sharemax and Pickvest syndications were legal, and this Office does not concede that they were legal, they remained highly risky investments. They remained financial products not suitable for widows, pensioners and aging persons who are in their twilight years. This office need not even pronounce on the legality of the investments in order to determine this complaint.

[71] Respondent presents lengthy explanations from experts as to the legality and viability of Sharemax investments, yet he cannot explain how and, in particular, why he selected these products as being suitable for complainant. Neither does he dispute that complainant instructed him that she required a monthly income and capital preservation, this is confirmed in the documents described above and signed by respondent. Nor does respondent deny that he guaranteed her an interest rate of 12.5 % and guaranteed her capital; this too is recorded and signed by respondent. Yet respondent cannot explain why he gave these guarantees when neither Sharemax nor Pickvest gave such guarantees. In the absence of any rational explanation, the only conclusion to be drawn is that respondent, in giving these guarantees, was misleading the complainant into investing her money by putting her funds at risk.

[72] The fundamental issues here are the following: in giving complainant 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.

[73] By all accounts, Pickvest and Sharemax were risky investments. Even respondents' experts do 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.

[74] It cannot be disputed that respondent advised complainant to invest in these investments. Nor is it in dispute that these were high risk investments. The 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?

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; it is the suitability of the investment for complainant and her financial circumstances that is in issue.

The Questions

[75] As part of investigating the complaint, this office forwarded a set of questions to respondent pertaining to the investments recommended and the advice provided, this

was done in terms of Section 27 (4) of the Act. Respondent provided this office with a comprehensive answer supported by documents and expert opinion. Below I present a discussion and findings emanating from respondent's responses.

Qualifications and Explanation

[76] Respondent was licensed by the FSCA under categories 1.8 and 1.10 which authorised him, in his own right, to market the Sharemax and Pickvest products. On respondent's version he was highly qualified and capable of understanding the Sharemax and Pickvest prospectuses. He was also able to, and did, explain the product to complainant in plain language.

[77] However, respondent did not produce any record of advice to confirm this. Complainant denies that she received an explanation in plain language. I also note from the record of documents that all the forms for Pickvest and Sharemax were signed on the same date at the same time. According to respondent complainant also received and read, and understood, the Pickvest and Sharemax prospectus. If respondent explained all the forms and the prospectus to complainant, before the decision to invest was made by her, it would have taken the best part of a day, if not more. Complainant disputes this and informed this office that Respondent did not take her through the prospectus, but merely left a copy with her after the application to invest and other documents were signed.

[78] Similarly, respondent claims to have explained the Sharemax investment and prospectus to complainant. According to complainant, all respondent told her about Sharemax, was that it was the same as Pickvest. We know that the two investments were not the same. The only similarity being that they were both high risk investments.

Complainant denies that an explanation of the prospectus was given. Her version is that respondent merely left a copy of the prospectus with her after she invested.

Trading History

[79] Respondent admits that the investment was made in a company that had no trading history. However, respondent explains that he was actually referring to the trading history of Sharemax over a period of 10 years. The flaw in this explanation is that Sharemax Zambezi and Sharemax The Villa, were altogether different to the other syndications promoted by Sharemax and were in fact more risky as investments. The Villa and Zambezi model was not used before and the scale of the investment dwarfs any other syndication promoted by Sharemax in the past. There is no evidence that this was explained to complainant.

Interest Payments

[80] Relevant to this complaint is the respondent's duty, in terms of the Code, to make full and frank disclosure of the material details of the product to complainant. This must include an explanation of how Sharemax was going to pay the generous returns it promised, and in particular, that interest was not being paid out of the client's own funds.

[81] In his response respondent merely repeated what was stated in the prospectus. In plain language, the prospectus stated that investor funds will be used to make an unsecured loan to the developer to fund the building. The developer will then pay Sharemax interest on the loan and from such interest investors will be paid. There is no explanation, anywhere, as to how the developer (builder in plain language) was going to pay the interest if not from the investors own money which it just received as a loan.

Note that firstly, the Sale of Business Agreement between Sharemax and the developer (Capicol) was never attached to the prospectus nor does this office know of any investor who received a copy thereof either from Sharemax or their broker or financial advisor. Paragraph 26.1 of the Villa prospectus states that "*Copies of schedules A to N will be available for inspection"* at Sharemax's offices in Waterkloof. Respondent does not say that he called on Sharemax and inspected the Sale of Business Agreement before he began selling the product. Secondly, the developer's financial statements were never made available to investors, nor to the brokers. Respondent does not state that he received such statements and was satisfied that Capicol was creditworthy. Thirdly, the prospectus in paragraph 19.10 contradicts respondent. This paragraph reads as follows:

" 19.10 All application monies received in terms of this offer will be administered in trust by the Attorneys and retained by the Bank in a separate interest bearing bank account opened and controlled by the Attorneys for each and every applicant in terms of Section 78(2A) of the Attorneys Act 1979 (the applicant by completing the application form consents to such investment being made) either:

19.10.1

19.10.2 (both of which deal with cancellation of the investment)

19.10.3 in respect of successful applications until the minimum subscription was received and the immovable property has been transferred to The Villa."

[82] On respondent's own version, he knew that this was not true as the funds never remained long enough in trust to earn any significant interest and were immediately paid over to Sharemax who immediately paid it over to the developer, with the consequence that neither the Attorneys nor Sharemax had any control over the funds. Worse still, the money was paid over to the developer before The Villa took transfer of

the property. There is no record that this was explained to complainant. If she knew this, she would certainly not have invested in Sharemax. Respondent was also obliged to explain that Sharemax was not going to comply with Notice 459.

Compliance with Section 8 of the Code

[83] Respondent was requested to explain how he complied with Section 8 of the Code in determining that these investments were suitable for complainant. Firstly, respondent states that he did comply with this Section. However, there is no record that he did. Respondent admits that he did not do a financial analysis. But he did have enough information, on his own version, to enable a reasonably competent FSP to work out that risk capital investments in property syndication was entirely unsuitable for complainant. Secondly, having admitted to not carrying out a financial analysis, he justifies this by referring to the two investments as “single need” investments. There is no reference to this type of investment in the Act, Code and in Section 8. The exception in section 8 (4) does not apply to this investment. Respondent had to comply with Section 8 and satisfy himself that these high-risk investments were suitable for complainant. He also states that complainant did not want to invest in a bank as the returns were too low and she may have to use her capital. Even if this was the case, there was no justification for investing in a product where she risked losing all of her capital.

Trust Account

[84] Respondent had to respond to a series of questions regarding payment of the Capital into an attorney’s trust account. It is not in dispute that the funds were paid out before transfer of the property took place and was made available to Sharemax to deal with the funds at their discretion, there was no safety for the funds. Respondent admits that

the funds were paid out of trust almost immediately and used by Sharemax and Pickvest to fund the development and other expenses.

[85] The key issue here was whether respondent actually explained this to complainant. Respondent's answer is significant. He states emphatically that this was explained to complainant. How? He merely relies on complainant's own reading of the prospectus. As for complainant, she states that she merely received copies of the prospectuses and did not read and understand them before she made the investments. The fact that she signed a document confirming receipt of the prospectus, does not mean that she read and understood it. In addition, it must have been obvious to respondent that complainant did not have the capacity to read and understand these lengthy and complex documents.

[86] Therefore, I find that respondent failed to comply with Section 8 of the Code as he advised complainant to invest in two products that were highly risky and not suitable for her needs.

Annexures to Prospectus

[87] Respondent was directed to paragraph 26.1.3 of the Sharemax prospectus and he was asked to indicate if he requested and read the documents mentioned therein. In particular, one of the documents is the Sale of Business Agreement (SBA). This document, together with other documents, were omitted from the prospectus to which they were supposed to be annexed. His response is significant, respondent admits to not having obtained these documents, not even the SBA. This is a crucial document and goes to the heart of the Sharemax scheme.

[88] Respondents explanation is that the document was explained to him in a training seminar on the product. He never saw this document. He states further that in the light of the explanation he received, he thought it was not necessary to request it and read it. He also relies on the prospectus which he claims explains the document. The problem with this is that complainant did not receive any training about the product and relied entirely on her FSP, the respondent.

[89] It is not true that the prospectus covered all the material information about the SBA. For example, respondent is silent on the fact that the SBA authorised a payment of commission to a company called Brandberg in an amount of 3% of the investors' capital. There was absolutely no legal basis for this payment. Brandberg was a Sharemax front and they merely helped themselves to a further 3% of the capital. This was not revealed in the prospectus. This is material information which respondent had to convey to complainant. It is common cause that he did not. There can be no doubt that if complainant was aware of this, she would not have invested. A reasonably competent FSP would have read the SBA and would have asked for explanations and would have made a full disclosure to client. This was material to the investment and was required by complainant to make an informed decision. Respondent negligently failed to do so.

[90] Again, respondent can only rely on the prospectus, paragraph 17.4. Here the prospectus explains that the directors of Sharemax have no interest in Brandberg and explain that Brandberg is an estate Agent which "introduced" the Villa to Capicol, the developer and they will "share" in the commission. The prospectus is entirely vague about this. Sharemax enjoyed a relationship with Capicol and there was no need for any agent to claim a commission for introducing the parties. Besides, when the Villa

investment started, Sharemax had a similar SBA with Capicol in respect of the Zambezi investment. Respondent admits to not asking any questions, believing this to be a "usual" agreement.

Deductions

[91] It is not disputed that 10% was deducted from the investment to pay broker commission of 6% and Sharemax kept 4%. Respondent states that this was made clear in the application form and quotes paragraph 15 thereof. It is noteworthy that paragraph 15 points out that whilst 6% of the capital was paid out of investor funds, Sharemax will "*eventually*" pay the commissions. In effect Sharemax was in fact paying commission out of investor funds with a promise to eventually repay the funds. The cumulative commissions **per prospectus** amounted to R27 million which Sharemax undertook to pay back to investors. This is information every investor needed to know and it had to be part of the full and frank disclosure respondent had to make to complainant. Complainant denies this was explained to her or drawn to her attention. Respondent admits he did not explain this to her; but relies on the fact that complainant read the prospectus and understood. He therefore accepted that complainant was aware of the deductions from her capital.

[92] It is certainly irresponsible of respondent to merely rely on the complainants reading and understanding of the prospectuses. Firstly, she denies reading the prospectuses; secondly, respondent fails to explain or disclose when he delivered the respective prospectuses to complainant, how long before the application forms were signed and how much time complainant was given to read and understand the documents. On complainant's version, she did not read either of the prospectuses and placed her trust

in respondent. Thirdly, even if complainant received the documents, she was incapable of reading and understanding these lengthy and complex documents.

[93] The probabilities favour complainant's version that she did not read and understand the prospectuses and placed her faith in respondent.

Appreciation of Risk

[94] Respondent was asked by this office about his appreciation of risks in the Sharemax investment. He readily admits "*I would not regard Sharemax investment as safe, as it clearly contained elements of risk, as set out in the prospectus".* He admits further*; "the projections could not materialize and the investors could in fact lose their capital."* It is then inexplicable that, being aware of the risks, he still deemed the investment to be suitable for an ageing person with a nett worth of R475 000. He invested R600 000 of complainant's available funds (all the money she owned) in two high risk investments.

[95] Respondent unconvincingly tries to justify his advice by pointing out Sharemax's previous record over a 10-year period. However, on his own version, all Sharemax syndications prior to Zambezi and the Villa were altogether different to Zambezi and The Villa and such record was irrelevant to the present investment. The previous syndications involved purchasing developed property which was transferred into a property-owning company controlled by Sharemax. Here Sharemax did not own any assets. Respondent admits that there was also no rental income from which Sharemax paid investors. Again, respondent did not personally explain this to complainant, but relies on her own reading of the prospectus.

[96] If respondent read and understood the prospectus, and he admits that he did, he would know that this was a risky investment. Yet he advised complainant to invest.

He also relied on the complainant's own reading of the prospectus to satisfy herself about the risks in the investment. Respondent failed to explain how he satisfied himself that **she** read and understood the prospectuses. There is no independent record of this. He had a duty to do so.

Complainant did not have the capacity to even begin to understand these complex documents, she placed her trust in the hands of her FSP, the respondent.

Expert Opinion

[97] Respondent relies on the assistance of two experts, Mr Cohen and Mr Swanepoel. In addition, respondent submits that this office cannot deal with issues around respondent's conduct as an FSP and whether or not he was negligent, without consulting experts of our own. I need to deal with this submission immediately.

[98] Respondent submits that on the issue of negligence, this office erred in not engaging the services of an expert in order to establish what a reasonably competent financial services provider (FSP) would do in similar circumstances. It was not necessary, on the facts of this case, for this office to engage the services of an expert. I point out the following:

a) First of all, this office did not require the services of an expert regarding the negligent conduct of an FSP. This office has sufficient capacity to undertake such an inquiry; nor was it ever intended that this office should turn to expert assistance whenever there was a dispute regarding financial services.

b) Financial services, its regulation and codes of conduct, is not an area where this office is incapable of forming an opinion unassisted or to come to an independent conclusion. This office is also possessed of the necessary knowledge and skills in this area. In this regard I refer to a decision of the Tribunal in **Transport Sector Retirement Fund v The Pension Funds Adjudicator and others Case No PFA32/2020** where Harms JA, in paragraph 21, described the PFA as "an expert body". Similarly, this office is an expert body and a specialist tribunal.

c) We point out that expert witnesses are not the judges of fact in relation to which they express an opinion. On the issue of the negligence of an FSP, the facts must first be established by this office and only then, if necessary, an expert can be consulted.

d) The function of an expert is to assist this office to reach a conclusion on matters on which this office itself does not have the necessary knowledge to decide. The issues in this complaint do not require this office to seek the opinion of an expert.

e) The standards to be expected from an FSP in the position of the respondent do not require the opinion of an expert. Those standards are well documented in the FAIS Act and the Code. It is then a matter of fact as to whether or not there was compliance with the Code.

[99] Respondent then submits that this office's findings are in conflict with expert opinions submitted to this office. This is a reference to two opinions viz those of Mr Anton Swanepoel and Mr Derek Cohen. This office, for reasons repeatedly stated in various determinations, discredited both these experts on the merits of their respective opinions. They were not discredited in favour of another expert. This office has the capacity and the skills to weigh and evaluate expert opinions without having to call on other experts or to engage experts from outside this office. Nor can the respondent refer

this office to a judgement where Swanepoel's opinion was accepted. I also point out that neither of these experts said anything about Pickvest.

[100] It is Swanepoel's opinion that Sharemax collapsed as a result of the unforeseen intervention of the South African Reserve Bank (the SARB). In particular he opines that a reasonably competent FSP cannot be expected to have foreseen that the SARB will intervene. This is entirely irrelevant, even if it was true. Sharemax did not collapse due to the SARB intervention, its collapse was inevitable as the business model used provided for the payment of commissions, administrative costs, interest to investors and cost of development of the shopping malls from investor funds. It was never in dispute that Sharemax owned no assets and did not have any independent means of funding the development. The scheme was heading for an inevitable collapse.

[101] However, the consequence of the SARB intervention is irrelevant to this complaint. The issue was whether or not respondent's advice to invest in Sharemax was appropriate after respondent took into account complainant's financial profile and financial needs. The Sharemax investment was an investment in risk capital, not suitable, by any standard, for a person of complainant's 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. Nor do respondent's experts disagree that these were high risk investments. 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.

[102] It is further not in dispute that the complainant did not understand this investment. Respondent points out that the prospectus was explained in full and that complainant

was happy with the Pickvest and Sharemax products. But on respondent's own version, complainant was happy with the investment because she was investing in property and that her income of 12.5% and the preservation of her capital was guaranteed by respondent. It is not disputed that the Sharemax investment was not an investment in property. It was an investment into unlisted shares and debentures, a far riskier proposition than an investment in property. As I point out elsewhere, respondent relies on complainant's own reading and understanding of the prospectuses. The Sharemax prospectus is a 41-page document written in a complex manner and it is highly unlikely that a 56-year-old with a standard six education, with no experience of finance and financial planning, would have understood it. To illustrate this point, if complainant understood the prospectus, she would have known that all her funds were to be used to advance an unsecured loan to the developer and were not going to be safely kept in an attorney's trust account pending transfer of the property. Had she understood this, on the probabilities, she would never have invested.

[103] But the more important point to be made is that respondent failed to explain why he, as a licensed FSP, believed this investment was suitable for complainant's needs. Neither does respondent provide a record of advice where all of these risks were explained to complainant; and that the latter understood them. A reasonably qualified or competent FSP would not have advised this complainant to invest everything she had in a high-risk investment. Therein lies the negligent conduct and it is conduct that went unexplained. In fact, respondent persisted that his advice to complainant to place all her funds in, not one but two, property syndications was appropriate for complainant's needs.

[104] Respondent seems to have forgotten that one of the experts engaged by his own attorney, Mike Schussler, described the investment as very high risk where one should not invest more than 5% to 20% of one's available funds. Personal Finance (1st quarter 2006) advised as follows: "*Ensure that you place no more than five percent of your investments in a single property syndication. And do not invest more than 20% of your savings in property syndications."* Confirming Schussler's opinion. Here respondent invested 100% of complainants available funds in two property syndications.

[105] Surely, one would expect a reasonably competent FSP to know this. Advising a widow to place all her funds into two property syndications was negligent. Besides, respondent with a category 1.8 and 1.10 license can be expected to know this and advise complainant accordingly and in her best interests.

[106] In this regard I refer to what Harms J stated in the **C S Makelaar** decision:

"Each property syndication scheme must be assessed on its own merits and demerits ***and with reference to the risk profile of the client.*** *Terms such as low, moderate and high are relative and should be gauged in the circumstances of the case.* ***It is the duty of the FSP to inform the client of inherent risks in the particular product.*** *The client may be prepared to accept the risk which many are, who are looking for a higher return and the possibility of special growth."*

Here there is no record that respondent explained the risks to complainant. In fact, on his own version, he relied on complainant's own reading of the prospectuses to understand the risks.

I now make brief reference to submissions made by the two experts, Cohen and Swanepoel.

D Cohen

[107] This opinion was not helpful. Most of the opinion concentrates on why the Sharemax model was legal. As I have stated, the legality of Sharemax and Pickvest schemes need not be decided. Whether these investments were “Ponzi schemes” or not, need not be decided. Cohen admits that the investment was risky, but having said that he does not deal specifically with the facts of this case and in particular the conduct of respondent.

[108] Cohen is also misdirected in a number of respects:

a) He attempts to compare the Sharemax scheme to property loan stock companies (PLS) and real estate investment trusts (REITS). This is unhelpful as it is irrelevant because Sharemax was neither a PLS nor a REITS. For instance, REITS is a company that owns, operates or finances income-producing properties. Sharemax did not do this. It is common cause now that Sharemax used investor funds to finance the development costs as well as cost of paying returns and commissions.

b) Cohen admits that Sharemax used investor funds to finance the building of a, as yet, nonexistent shopping mall. The prospectus, in any event, states as much. Cohen’s opinion is that Sharemax did not have to rely only on investor funds and that it could have accessed alternate financing, such as through a bank. However, he states that after the SARB intervened, the banks did not want to offer facilities to Sharemax. The truth is that, when the SARB intervened, Sharemax already owed the developer and investors more money than what the property was worth, and we must consider that at that stage the property had not yet been transferred to the promoter, Sharemax. Cohen failed to point that out. The fact remains, Sharemax relied on a steady stream of new investments to stay in business. Willie Botha, CEO of Sharemax stated that money for The Villa was being raised from

investors and paid over to the developer, Capicol (News 24/Fin 24). This is characteristic of a pyramid scheme. Thus, when new investment slowed down, the whole scheme crashed immediately and there is no evidence that Sharemax had any alternative means to fund the development.

c) Both Cohen and Swanepoel point to the prospectus stating that, as security for investors funds, a bond would be registered over the property belonging to the developer. This is misleading as they were both well aware of the fact that; firstly, the bond was never registered and secondly, such a registration was meaningless as the sum total of Sharemax's debts (including what it owed to investors) far exceeded the value of the property with its unfinished developments. Neither Cohen nor Swanepoel asked the most relevant question; did respondent explain this funding model to complainant? Respondent, himself, merely relied on complainants own reading of the prospectuses and does not dispute that he did not explain to complainant what was to become of her funds. That was negligent conduct.

d) A further criticism of Cohen and Swanepoel is that both of them insist that investors were paid interest out of the attorney's trust account (Section 78(2A)). There are a number of flaws in this: firstly, that interest, if there was any, belonged to the investors and could not be used to satisfy any of Sharemax's obligations; secondly, the prospectus informs that, after the cooling off period, investors funds were going to be paid out of trust to Sharemax, the funds did not remain in the trust account long enough; thirdly, even if there was a pool of funds in trust, the interest rate earned (between 6% and 8%) could not possibly be enough to pay investors between 12.5% and 14% . Besides the attorneys, Weavind and Weavind, never accounted for the interest earned in their trust account and merely paid the whole amount to Sharemax.

A Swanepoel

[109] Swanepoel is not a credible expert, not insofar as it relates to Sharemax, as he has in the past promoted Sharemax and acted for them. This is easily manifested in his opinion as some of his views are bizarre and not supported by the facts and the law.

[110] A further flaw in the opinion is that it bears no reference to respondent's conduct in advising complainant. The opinion talks about the duty of FSPs in general terms and considers, in general terms, what a reasonably competent FSP was expected to do. In this regard Swanepoel agrees with the judgement in **Durr v ABSA Bank.** He also expresses the view that FSPs with a Category 1.8 and Category 1.10 license are regarded as competent to manage investments in securities and debentures. Respondent had such a licence and still managed to advise complainant to invest in altogether unsuitable investments. This too is proof of negligence.

[111] Swanepoel submits that Sharemax's historical performance was impressive and relevant. That is not the case as Zambezi and The Villa were completely different and were far more risky than previous syndications. Previous investments were in developed property producing an income whereas Zambezi and Villa were not the same in that the properties had no development and no independent source of income.

[112] In paragraph 37 of his opinion Swanepoel states that a reasonable FSP would consider an investment in The Villa as being a group of persons pooling their resources to buy an income producing property. This is misleading. That may be true for Sharemax's previous syndications but not for The Villa. The prospectus makes it clear that Sharemax had no property and no development producing an income. Investor funds were going into funding the development which was very far from earning any income.

Investors were not investing in “brick and mortar”, Sharemax merely created an illusion that they were.

[113] Significantly, Swanepoel admits that, with regard to The Villa, investors funds were going to be lent to a developer. His view is that, for a reasonably qualified FSP, the only issue was security for the funds so lent to the developer. Swanepoel opines that this was well catered for as the prospectus provided for a bond over the property. As I explained above, Swanepoel does not state the facts; firstly, the property belonged to the developer and was never transferred to Sharemax; secondly, the bond was *to be* registered. We know that no bond was registered in favour of the promoter in order to provide security for the loan funded by investors. One would expect a reasonably qualified FSP to check if a bond was registered and to satisfy himself that his clients funds were secure in the event of default by the developer. It is not disputed that respondent failed to do so and failed to advise his client of the risks. This is negligent conduct.

[114] Paragraph 42 of the opinion is bizarre. Swanepoel correctly puts his finger on the problem after being directed by this office. Paragraph 19.10 of the prospectus provides that all investor funds will be held in an attorney’s trust account until transfer is taken of the developed property (this is compliance with Notice 459). However, this is contradicted by the prospectus in paragraph 10.3 where the investor is informed that their funds will be used to advance a loan, of R2.9 billion, to the developer before transfer is taken. This is a material discrepancy which investors must know and receive an explanation. It is not disputed that respondent did not see this discrepancy nor did he draw complainant’s attention to it. Swanepoel has two explanations, firstly that Notice 459 had to “be adapted” and secondly the discrepancy was a “cut and paste”

error. How such a material error escaped the very experienced people in Sharemax, not to mention their even more experienced attorneys defies any credible explanation. Incidentally this error was repeated in all of the prospectuses for Zambezi and The Villa, totalling many billions of Rands. To make matters worse, Swanepoel consulted two people in this regard, Willie Botha and a partner from Weavind and Weavind, hardly the most objective people. They were both conflicted.

Regarding Notice 459, it had to be complied with, it provides for no circumstances where it can be "adapted".

[115] Paragraph 49 of the opinion is significant. Here Swanepoel deals with Section 7 of the Code which provides that an investor is entitled to full and frank disclosure of all the relevant information about the product. Swanepoel's view is that the requirements of Section 7 are met "*by providing a prospectus to a prospective client who is capable to understand its contents*" (emphasis added). Swanepoel ventures no views about a 56-year-old lady with a standard six education as being capable of understanding the prospectus. Complainant denies she even read the prospectuses, but even if she did, she certainly did not have the capacity to understand. Respondent was negligent in merely presenting the prospectus and leaving it for the client to read and understand, he did not comply with the code and his conduct was negligent.

[116] As Harms J correctly pointed out, in a passage from the **CS Makelaars** case quoted above, Zambezi and Villa were different in that whilst the other syndications involved acquisition of existing developed properties already earning an income, Zambezi and The Villa were different in that the properties had no development and no independent source of income. This difference, notwithstanding the **CS Makelaars** judgement, somehow escaped the attention of Respondent. There is no record, not even on his

own version, of respondent explaining this material difference to complainant. Something he was obliged to do as a licensed FSP.

[117] The experts do not say that this investment was appropriate for complainant, nor do they say that respondent did not act negligently as he was within the standards of a reasonably qualified FSP.

[118] This office does not accept the opinions of the experts that the cause of the Sharemax collapse was the unforeseen intervention of the SARB. The collapse was inevitable as the scheme was unsustainable. This is ably demonstrated by two facts: firstly, Sharemax allegedly completed the Zambezi Retail Park mall. Yet, after the completion, Sharemax still owed the developer a substantial amount of money and had not taken transfer of the property. Sharemax, in relation to Zambezi, was unable to issue out further prospectuses. Sharemax also, at that time owed the developer R526 million for work done on the Villa, while at the same time having to make monthly payments of 12% on capital to investors. The whole scheme was doomed to fail as it was already insolvent. Secondly, the experts say that the developer and Sharemax had alternative means of raising funds, apart from the investors' money, yet they allowed the scheme to collapse without successfully sourcing alternative financing. However, I point this out to demonstrate why this office does not accept the opinions of respondent's experts.

[119] The consequences of the SARB intervention is irrelevant to this complaint. The issue was whether or not respondent's advice to invest in Sharemax and Pickvest was appropriate after respondent took into account complainant's financial profile and financial needs. The Pickvest and Sharemax investments was an investment *in risk capital*, not suitable, by any standard, for a person of complainant's 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.

Negligence

[120] 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) understands that he is obliged to comply with the Code in providing financial advice;

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

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

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

f) understands that he is obliged to ensure and actually places his client in a position to make an informed decision; and

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

[121] Respondent states that he explained the risks in the Pickvest and Sharemax products to complainant, however he is extremely vague about the details. There is no record of advice that documents the risks explained to complainant.

[122] 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 prospectuses. Yet he failed to tell complainant the following:

a) Neither the preservation of her capital nor her monthly returns were guaranteed;

b) That the investments were considered risk capital;

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

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

e) That her 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 neither Pickvest nor Sharemax complied with the requirements of Notice 459;

g) That neither Pickvest nor Sharemax had independent financial resources from which to pay agents commission and interest on the capital; and

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

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

Application of Law

[124] 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 client 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 Pickvest and Sharemax products;

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

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

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

[126] Further, this office as well as the Board of Appeal has consistently found that there existed a contract between FSP and client. It was 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 was in breach of this term. A consequence of this breach was the loss of complainant's capital.

[127] 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.

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

a) Carried out diligent research to become familiar with the nature of the Pickvest and Sharemax products he intended to sell;

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 prospectuses and the annexures thereto and explain it to complainant in plain language;

d) Made a point of understanding how Pickvest and 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 prospectuses). Significantly, respondent had a duty to explain this to complainant;

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 complainant;

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 (in respect of Sharemax) 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 prospectuses).

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

[129] 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 complainant of the right to make an informed decision.

[130] 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 a 56-year-old, about to retire person, to invest all her

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.

[131] 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. That 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. The reasonable foreseeability must become even more clear 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 Pickvest and Sharemax

investments. The respondent was aware of these risks; but nevertheless, advised complainant to invest her funds.

[132] Respondent's conduct fell short of a reasonably competent FSP and Respondent was the factual and legal cause of complainant's loss.

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

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.

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

D. THE ORDER

[134] The following order is made:

1. In respect of the Pickvest investment:

   a) The complaint is upheld;

   b) The respondents are ordered to pay to complainant an amount of R300 000, jointly and severally;

   c) 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.

2. In respect of the Sharemax investment:

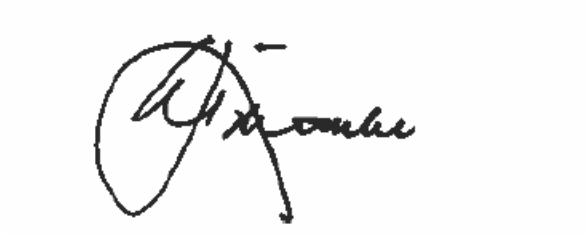
   a) The complaint is upheld;

   b) The respondents are ordered to pay to complainant an amount of R300 000, jointly and severally;

   c) 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), 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